

SHINHAN FINANCIAL GROUP CO LTD

Form 20-F

June 30, 2006

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**As filed with the Securities and Exchange Commission on June 30, 2006**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**Form 20-F**

(Mark One)

**o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

**OR**

**p ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**For the fiscal year ended December 31, 2005**

**OR**

**o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**For the transition period from to  
OR**

**o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934**

**Date of event requiring this shell company report**

**Commission File Number: 001-31798**

**Shinhan Financial Group Co., Ltd.**

*(Exact name of registrant as specified in its charter)*

**N/A**

*(Translation of registrant's  
name into English)*

**The Republic of Korea**

*(Jurisdiction of incorporation  
or organization)*

**120, 2-Ga, Taepyung-Ro, Jung-Gu  
Seoul 100-102, Korea**

*(Address of principal executive offices)*

**Securities registered or to be registered pursuant to Section 12(b) of the Act:**

**Title of Each Class:**

**Name of Each Exchange on Which Registered:**

Common stock, par value Won 5,000 per share  
American depositary shares

New York Stock Exchange\*  
New York Stock Exchange

\* Not for trading, but only in connection with the listing of American depositary shares on the New York Stock Exchange, pursuant to the requirements of the Securities and Exchange Commission.

**Securities registered or to be registered pursuant to Section 12(g) of the Act:**

None

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:**

None

**Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the last full fiscal year covered by this Annual Report:** 347,597,116 shares of common stock, par value of Won 5,000 per share

**Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act:** Yes  No

**If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934:** Yes  No

**Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):**

Large accelerated filer  Accelerated filer  Non-accelerated filer

**Indicate by check mark which financial statement item the registrant has elected to follow:** Item 17  Item 18

**If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2) of the Exchange Act:** Yes  No

**(APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PAST FIVE YEARS)**

**Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court:** Yes  No

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**EXPLANATORY NOTE**

On August 19, 2003, we acquired 80.04% of the outstanding common shares of Chohung Bank. In December 2003, our ownership increased to 81.15% following our additional capital injection of W200 billion. In June 2004, we acquired the remaining 18.85% of the outstanding shares of Chohung Bank that we previously did not own through a cash tender offer followed by a small-scale share swap pursuant to Korean law. See Item 4. Information on the Company The Merger of Shinhan Bank and Chohung Bank . We delisted Chohung Bank from the Stock Market Division of the Korea Exchange on July 2, 2004. Effective as of April 3, 2006, we merged Shinhan Bank, our other principal banking subsidiary, into Chohung Bank, integrated their operations and renamed the merged bank as Shinhan Bank. Our consolidated financial statements as of and for the year ended December 31, 2003 include Chohung Bank as of and for the period from September 1, 2003 to December 31, 2003. Unless otherwise indicated, the income statement information and other data relating to the results of operations of Chohung Bank in 2003 refer to the results of operations of Chohung Bank for the period from September 1, 2003 to December 31, 2003. However, since we did not merge or integrate the operations of Chohung Bank into Shinhan Bank as of and for the year ended on December 31, 2005, we have presented information about Chohung Bank separately from information about the rest of our group.

**CERTAIN DEFINED TERMS, CONVENTIONS AND CURRENCY OF PRESENTATION**

All references to Korea or the Republic contained in this document mean The Republic of Korea. All references to the government mean the government of The Republic of Korea. The Financial Supervisory Service is the executive body of the Financial Supervisory Commission . References to MOFE are to the Ministry of Finance and Economy. The terms we, us and our mean Shinhan Financial Group Co., Ltd. ( Shinhan Financial Group ) and/or its consolidated subsidiaries as the context requires or unless the context otherwise requires. The terms Shinhan , SFG or the Group mean Shinhan Financial Group and/or its consolidated subsidiaries unless the context otherwise requires. The terms Shinhan Bank and SHB refer to Shinhan Bank on a consolidated basis, unless otherwise specified or the context otherwise requires. The terms Chohung Bank , Chohung and CHB refer to Chohung Bank on a consolidated basis, unless otherwise specified or the context otherwise requires.

Our fiscal year ends on December 31 of each year. All references to a particular year are to the year ended December 31 of that year.

In this document, unless otherwise indicated, all references to Won or W are to the currency of the Republic, and all references to U.S. Dollars , Dollars , \$ or US\$ are to the currency of the United States of America. Unless otherwise indicated, all translations from Won to Dollars were made at W1,010.00 to US\$1.00, which was the noon buying rate in The City of New York for cable transfers in Won per US\$1.00 as certified for customs purposes by the Federal Reserve Bank of New York (the Noon Buying Rate ) in effect on December 31, 2005. On June 23, 2006, the Noon Buying Rate was W955.80 = US\$1.00. No representation is made that the Won or U.S. Dollar amounts referred to in this report could have been or could be converted into Dollars or Won, as the case may be, at any particular rate or at all.

Unless otherwise indicated, the financial information presented in this document has been prepared in accordance with accounting principles generally accepted in the United States of America ( U.S. GAAP ).

Any discrepancies in any table between totals and the sums of the amounts listed are due to rounding.

**FORWARD LOOKING STATEMENTS**

This document includes forward-looking statements , as defined in Section 27A of the U.S. Securities Act, as amended, and Section 21E of the U.S. Securities Exchange Act of 1934, as amended (the Exchange Act ), including statements regarding our expectations and projections for future operating performance and business prospects. The words believe , expect , anticipate , estimate , project and similar words used in connection with any discussion of future operating or financial performance identify forward-looking

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statements. In addition, all statements other than statements of historical facts included in this document are forward-looking statements.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we can give no assurance that such expectations will prove to be correct. All forward-looking statements are management's present expectations of future events and are subject to a number of factors and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. This document discloses, under the caption

Item 3. Key Information Risk Factors and elsewhere, important factors that could cause actual results to differ materially from our expectations ( Cautionary Statements ). Included among the factors discussed under the caption

Item 3. Key Information Risk Factors are the followings risks related to our business, which could cause actual results to differ materially from those described in the forward-looking statements: the risk of adverse impacts from an economic downturn; increased competition; market volatility in securities and derivatives markets, interest or foreign exchange rates or indices; other factors impacting our operational plans; or legislative or regulatory developments.

We caution you not to place undue reliance on the forward-looking statements, which speak only as of the date of this document.

All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the Cautionary Statements.

**Table of Contents****ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**  
**DIRECTORS AND SENIOR MANAGEMENT**

The names and positions of our directors and executive officers are set forth below. The business address of all of our directors and executive officers is our registered office at 120, 2-Ga Taepyung-Ro, Jung-Gu, Seoul 100-102, Korea.

**Executive Directors**

<b>Name</b>	<b>Position</b>
<i>Eung Chan Ra</i>	Chairman of the Board of Directors and Head of the Board Steering Committee
<i>In Ho Lee</i>	President and Chief Executive Officer and a member of the Board Steering Committee
<i>Young Hwi Choi</i>	Executive Director

**Non-Executive Directors**

<b>Name</b>	<b>Position</b>
<i>Young Seok Choi</i>	Non-Executive Director; Audit Committee member
<i>Yong Woong Yang</i>	Non-Executive Director
<i>Il Sup Kim</i>	Outside Director; Head of Audit Committee; Compensation Committee member
<i>Sang Yoon Lee</i>	Outside Director; Board Steering Committee member, Audit Committee member; Compensation Committee member
<i>Yoon Soo Yoon</i>	Outside Director; Risk Management Committee member; Compensation Committee member
<i>Shee Yul Ryoo</i>	Outside Director; Board Steering Committee member; Risk Management Committee member, Compensation Committee member
<i>Byung Hun Park</i>	Outside Director, Board Steering Committee member
<i>Young Hoon Choi</i>	Outside Director
<i>Si Jong Kim</i>	Outside Director; Audit Committee member
<i>Philippe Reynieix</i>	Outside Director; Risk Management Committee member
<i>Haeng Nam Chung</i>	Outside Director
<i>Myoung Soo Choi</i>	Outside Director

Non-executive directors are directors who are not our employees and do not hold executive officer positions in us. Outside directors are non-executive directors who also satisfy the requirements set forth under the Korea Securities and Exchange Act of 1976 to be independent of our major shareholders, affiliates and the management.

**Table of Contents****Executive Officers**

In addition to the executive directors who are also our executive officers, we currently have the following executive officers.

<b>Name</b>	<b>Position</b>
<i>Jae Woo Lee</i>	Chief Operating Officer; Managing Director of General Affairs Team, Public Relations Team and Human Resources Team
<i>Byung Jae Cho</i>	Chief Financial Officer; Managing Director of Finance Planning Team, Risk Management Team and Investor Relations Team
<i>Jin Won Suh</i>	Chief Strategy Officer; Managing Director of Strategic Planning Team, Information & Technology Planning Team and Future Strategy & Management Team
<i>Jae Woon Yoon</i>	Group Synergy Officer; Managing Director of Synergy Management Team, Joint Procurement Team and Audit & Compliance Team

**ADVISERS**

Certain legal matters in connection with the American depositary shares will be passed upon for us by Simpson Thacher & Bartlett LLP, our United States counsel, at 425 Lexington Avenue, New York, New York, and by Horizon Law Group, our Korean counsel, at The Korea Chamber of Commerce & Industry Building 11 F, 45 4-ga, Namdaemun-ro, Jung-gu, Seoul 100-743, Korea.

**INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRMS**

Our independent auditors for the consolidated financial statements prepared under accounting principles generally accepted in the United States of America, or U.S. GAAP, were as follows.

<b>Name</b>	<b>Period</b>	<b>Address</b>	<b>Membership in Professional Bodies</b>
Samil PricewaterhouseCoopers	For the year ended December 31, 2003	Kukje Center Building 15th Floor 191 Hangangro 2ga, Yongsan-gu, Seoul, Korea	Korean Institute of Certified Public Accountants
KPMG Samjong Accounting Corp.	For the years ended December 31, 2004 and 2005	Star Tower 10th Floor 737 YeokSam-dong, KangNam-gu, Seoul 135-984 Korea	Korean Institute of Certified Public Accountants

**ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE**

Not applicable.

**Table of Contents****ITEM 3. KEY INFORMATION****SELECTED FINANCIAL DATA****Selected Consolidated Financial and Operating Data under U.S. GAAP**

The selected consolidated financial data set forth below for the years ended December 31, 2001, 2002, 2003, 2004 and 2005 and as of December 31, 2001, 2002, 2003, 2004 and 2005 have been derived from our consolidated financial statements which have been prepared in accordance with U.S. GAAP.

You should read the following data with the more detailed information contained in Item 5. Operating and Financial Review and Prospects and our consolidated financial statements included in Item 18. Financial Statements. Historical results do not necessarily predict the future.

**Consolidated Income Statement Data****Year Ended December 31,**

	2001	2002	2003	2004	2005	2005
<b>(In billions of Won and millions of US\$, except per common share data)</b>						
Interest and dividend income	W 3,694	W 3,735	W 5,331	W 7,712	W 7,488	\$ 7,413
Interest expense	2,439	2,305	2,998	4,138	4,014	3,974
Net interest income	1,255	1,430	2,333	3,574	3,474	3,439
Provision (reversal) for credit losses	405	246	965	135	(183)	(182)
Noninterest income	632	1,037	1,118	2,092	2,702	2,675
Noninterest expense	828	1,302	1,937	3,152	3,662	3,625
Income tax expense	223	320	248	764	942	933
Minority interest	(1)	10	26	153	16	16
Income before extraordinary item and effect of accounting change	432	589	275	1,462	1,739	1,722
Extraordinary gain	64			28		
Cumulative effect of a change in accounting principle, net of taxes				(23)		
Net income	W 496	W 589	W 275	W 1,467	W 1,739	\$ 1,722
<b>Net income per common share (in currency unit):</b>						
Net income basic(1)	W 1,948	W 2,246	W 1,024	W 4,875	W 5,190	\$ 5.14
Net income diluted(2)	1,663	2,243	984	4,347	4,882	4.83
Weighted average common shares outstanding-basic (in thousands of common shares)	254,680	262,480	262,987	292,465	333,424	
Weighted average common shares outstanding-diluted (in thousands of common shares)	299,215	262,812	279,745	337,479	356,140	

Notes:

- (1) Basic earnings per share are calculated by dividing the net income available to common stockholders by the weighted average number of common shares issued and outstanding for the period.
- (2) Diluted earnings per share are computed in a manner consistent with that of basic earnings per share, while giving effect to the potential dilution that could occur if convertible securities, options or other contracts to issue common stock were converted into or exercised for common stock. We have two categories of potentially dilutive common shares: (i) shares issuable on exercise of stock option and (ii) shares issuable on conversion of preferred shares.

**Table of Contents****Consolidated Balance Sheet Data**

As of December 31,

2001      2002      2003      2004      2005      2005

(In billions of Won and millions of US\$, except per common share data)

<b>Assets</b>												
Cash and cash equivalents	W	580	W	282	W	1,897	W	2,444	W	2,434	\$	2,410
Restricted cash		678		1,365		3,662		3,301		3,644		3,608
Interest-bearing deposits		255		125		409		220		627		621
Call loans and securities purchased under resale agreements		1,816		576		1,898		1,591		1,499		1,485
Trading assets:												
Trading securities and other		858		926		2,857		4,639		3,573		3,538
Derivatives assets		98		139		520		1,678		934		925
Securities:												
Available-for-sale securities		7,087		8,737		18,099		18,108		22,480		22,257
Held-to-maturity securities		6,038		4,408		3,605		3,099		2,963		2,934
Loans (net of allowance for loan losses of W720 billion in 2001, W996 billion in 2002, W3,631 billion in 2003, W2,311 billion in 2004 and W1,512 billion in 2005)		32,997		44,139		91,791		94,868		104,447		103,413
Customers liability on acceptances		1,566		928		2,365		2,012		1,879		1,860
Premises and equipment, net		530		828		2,003		1,848		1,876		1,858
Goodwill and intangible assets		4		219		1,676		1,660		2,957		2,928
Security deposits		390		466		966		968		1,078		1,067
Other assets		2,205		1,648		4,601		7,072		4,724		4,676
<b>Total assets</b>	<b>W</b>	<b>55,102</b>	<b>W</b>	<b>64,786</b>	<b>W</b>	<b>136,349</b>	<b>W</b>	<b>143,508</b>	<b>W</b>	<b>155,115</b>	<b>\$</b>	<b>153,580</b>

**Liabilities and Stockholders Equity****Liabilities:**

<b>Deposits:</b>												
Interest-bearing	W	31,036	W	35,886	W	82,161	W	79,934	W	83,278	\$	82,454
Non-interest-bearing		1,184		1,163		1,328		2,746		3,143		3,112
Trading liabilities		119		131		513		1,758		1,048		1,038
Acceptances outstanding		1,566		928		2,365		2,012		1,879		1,860
Short-term borrowings		5,759		6,994		11,204		10,954		11,968		11,850
Secured borrowings		4,088		4,706		6,316		6,308		7,502		7,427
Long-term debt		4,876		8,235		21,218		23,617		26,172		25,913
Future policy benefit										4,778		4,730
		3,562		3,193		6,555		9,713		7,089		7,019

## Accrued expenses and other liabilities

Total liabilities	52,190	61,236	131,660	137,042	146,857	145,403
Minority interest	2	288	583	66	80	79
Redeemable convertible preferred stock			711	736	368	364
<b>Stockholders equity:</b>						
Common stock	1,462	1,462	1,472	1,596	1,795	1,779
Additional paid-in capital	1,041	1,048	1,073	1,658	2,407	2,383
Retained earnings	638	1,077	1,189	2,456	3,953	3,914
Accumulated other comprehensive income, net of taxes	164	70	58	158	(100)	(99)
Less: treasury stock, at cost	(395)	(395)	(397)	(204)	(245)	(243)
Total stockholders equity	2,910	3,262	3,395	5,664	7,810	7,734
Total liabilities, minority interest, Redeemable Convertible Preferred Stock and stockholders equity	W 55,102	W 64,786	W 136,349	W 143,508	W 155,115	\$ 153,580

**Table of Contents****Dividends**

	<b>Year Ended December 31,</b>				
	<b>2001(1)</b>	<b>2002(2)</b>	<b>2003(2)</b>	<b>2004(2)</b>	<b>2005(2)</b>
	<b>(In Won and US\$, except ratios)</b>				
<b>U.S. GAAP:</b>					
Cash dividends per share of common stock:					
In Korean Won	W 750	W 600	W 600	W 600	W 750
In U.S. dollars	\$ 0.63	\$ 0.50	\$ 0.50	\$ 0.50	\$ 0.74
Cash dividends per share of preferred stock					
In Korean Won	N/A	N/A	N/A	W 135.12	W 365.34
In U.S. dollars	N/A	N/A	N/A	\$ 0.13	\$ 0.36
Stock dividends per share of common stock					
<b>Korean GAAP:</b>					
Cash dividends per share of common stock:(3)					
In Korean Won	W 600	W 600	W 600	W 600	W 750
In U.S. dollars	\$ 0.50	\$ 0.50	\$ 0.50	\$ 0.50	\$ 0.74
Dividend ratio(4)	12.00%	12.00%	12.00%	12.00%	15.00%
Cash dividends per share of preferred stock:					
In Korean Won	N/A	N/A	N/A	W 857	W 1,183
In U.S. dollars	N/A	N/A	N/A	\$ 0.83	\$ 1.17
Dividend ratio(4)	N/A	N/A	N/A	17.14%	23.66%
Stock dividends per share of common stock					

*N/A = not available.*

*Notes:*

- (1) Represents, under U.S. GAAP, dividends declared on common stock of Shinhan Bank for the year ended December 31, 2000 and, under Korean GAAP, dividends accrued in the period to which such dividends relate for the year ended December 31, 2001.
- (2) Represents dividends declared on the common stock of Shinhan Financial Group for the year ended December 31, 2002, 2003, 2004 and 2005.
- (3) Represents, under Korean GAAP, for each year ended December 31, 2001 and 2002, dividends accrued on the common stock of Shinhan Financial Group for such year, and, for each year ended December 31, 2003, 2004 and 2005, dividends declared on common stock of Shinhan Financial Group in such year. In connection with our holding company restructuring in 2001, common stock of Shinhan Bank was exchanged for common stock of Shinhan Financial Group on a 1:1 ratio.
- (4) Dividends declared and paid as a percentage of par value of W5,000 per common share of Shinhan Financial Group.

**Table of Contents****Selected Statistical Information***Profitability Ratios*

	Year Ended December 31,				
	2001	2002	2003	2004	2005
	(Percentages)				
Net income as a percentage of:					
Average total assets(1)	0.94%	0.94%	0.29%	1.01%	1.16%
Average stockholders equity(1)(2)	16.14	15.99	8.83	31.44	29.80
Including Redeemable Convertible Preferred Stock(3)	N/A	N/A	8.15	27.22	27.08
Including Redeemable Convertible Preferred Stock and Redeemable Preferred Stock(3)	N/A	N/A	8.24	22.73	19.98
Dividend payout ratio(4)	38.91	25.59	57.20	15.87	15.99
Net interest spread(5)	2.28	2.39	2.48	2.63	2.64
Net interest margin(6)	2.66	2.58	2.65	2.78	2.70
Efficiency ratio(7)	43.88	52.78	56.13	55.63	59.29
Cost-to-average assets ratio(8)	1.57	2.08	2.01	2.18	2.45
Equity to average asset ratio(9):	5.84	5.89	3.24	3.22	3.91
Including Redeemable Convertible Preferred Stock(3)	N/A	N/A	3.51	3.72	4.30
Including Redeemable Convertible Preferred Stock and Redeemable Preferred Stock(3)	N/A	N/A	4.04	4.83	5.39

N/A = Not applicable.

Notes:

- (1) Average balances are based on (a) daily balances for Shinhan Bank, Chohung Bank and Jeju Bank and (b) quarterly balances for other subsidiaries.
- (2) Does not include the Redeemable Preferred Stock or the Redeemable Convertible Preferred Stock described below.
- (3) As consideration for our acquisition of Chohung Bank, in August 2003, we issued to the Korea Deposit Insurance Corporation (i) 46,583,961 shares of our Redeemable Preferred Stock, with an aggregate redemption price of W842,517,518,646 and (ii) 44,720,603 shares of our Redeemable Convertible Preferred Stock, with an aggregate redemption price of W808,816,825,858, which were convertible into shares of our common stock. In November 2005, Korea Deposit Insurance Corporation converted 22,360,302 shares of these shares of our Redeemable Convertible Preferred Stock into 22,360,302 shares of our common stock, representing 6.22% of our total issued shares (or 5.86% of our total issued shares on a fully diluted basis) of our common stock. In April 2006, Korea Deposit Insurance Corporation sold to BNP Paribas S.A. and other institutional investors all of our common shares held by it. As of the date hereof, Korea Deposit Insurance Corporation does not hold any share of our common stock but still holds 22,360,301 shares of Redeemable Convertible Preferred Stock, representing 6.22% of the total issued shares (or 5.86% of the total issued shares on a fully diluted basis) of our common stock. Korea Deposit Insurance Corporation is entitled to convert such shares into our common stock beginning in August 2006. Pursuant to the terms of the Redeemable Preferred Stock issued to Korea Deposit Insurance Corporation, we are required to redeem such shares in five equal annual installments commencing three years from the date of

issuance. These Redeemable Preferred Stock are treated as debt under U.S. GAAP. Pursuant to the terms of our Redeemable Convertible Preferred Stock, we are required to redeem the full amount of such shares outstanding five years from the date of issuance to the extent not converted into our common shares. Each share of our Redeemable Convertible Preferred Stock is convertible into one share of our common stock. The dividend ratios on our Redeemable Preferred Stock

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and Redeemable Convertible Preferred Stock are 4.04% and 2.02%, respectively. In August 2003, we also raised W900 billion in cash through the issuance of 6,000,000 shares of Redeemable Preferred Stock, all of which were sold in the domestic fixed-income market through Strider Securitization Specialty Co., Ltd., a special purpose vehicle. These redeemable preferred shares have terms that are different from the redeemable preferred shares issued to Korea Deposit Insurance Corporation. We are required to redeem these preferred shares issued to the special purpose vehicle in three installments in 2006, 2008 and 2010. See Item 4. Information on the Company The Merger of Shinhan Bank and Chohung Bank Liquidity and Capital Resources and Item 10. Additional Information Articles of Incorporation Description of Capital Stock Description of Redeemable Preferred Stock .

- (4) Represents the ratio of total dividends declared on common stock as a percentage of net income.
- (5) Represents the difference between the yield on average interest-earning assets and cost of average interest-bearing liabilities.
- (6) Represents the ratio of net interest income to average interest-earning assets.
- (7) Represents the ratio of noninterest expense to the sum of net interest income and noninterest income, a measure of efficiency for banks and financial institutions. Efficiency ratio may be reconciled to comparable line-items in our income statements for the periods indicated as follows:

	<b>Year Ended December 31,</b>				
	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
	<b>(In billions of Won, except percentages)</b>				
Non-interest expense(A)	W 828	W 1,302	W 1,937	W 3,152	W 3,662
<i>Divided by</i>					
The sum of net interest income and noninterest income(B)	1,887	2,467	3,451	5,666	6,176
Net interest income	1,255	1,430	2,333	3,574	3,474
Noninterest income	632	1,037	1,118	2,092	2,702
Efficiency ratio ((A) as a percentage of(B))	43.88%	52.78%	56.13%	55.63%	59.29%

- (8) Represents the ratio of noninterest expense to average total assets.
- (9) Represents the ratio of average stockholders' equity (not including the Redeemable Preferred Stock or the Redeemable Convertible Preferred Stock) to average total assets.

**Asset Quality Ratios**

	<b>As of December 31,</b>				
	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
	<b>(In billions of Won, except percentages)</b>				
Total loans	W 33,665	W 45,052	W 95,295	W 97,080	W 105,848
Total allowance for loan losses	720	996	3,631	2,311	1,512
Allowance for loan losses as a percentage of total loans	2.14%	2.21%	3.81%	2.38%	1.43%
Total non-performing loans(1)	W 530	W 518	W 1,844	W 1,750	W 1,594

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Non-performing loans as a percentage of total loans	1.57%	1.15%	1.94%	1.80%	1.51%
Non-performing loans as a percentage of total assets	0.96%	0.80%	1.35%	1.22%	1.03%
Impaired loans(2)	W 1,492	W 1,263	W 3,488	W 2,646	W 2,285
Allowance for impaired loans	385	480	1,349	885	704
Impaired loans as a percentage of total loans	4.43%	2.80%	3.66%	2.73%	2.16%
Allowance for impaired loans as a percentage of impaired loans	25.80%	38.00%	38.68%	33.47%	30.81%

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- (1) Non-performing loans are defined as loans, whether corporate or consumer, that are past due more than 90 days.
- (2) Impaired loans include loans that are classified as substandard or below according to the asset classification guidelines of the Financial Supervisory Commission, loans that are past due for 90 days or more and loans that qualify as troubled debt restructurings under U.S. GAAP.

**Capital Ratios**

	<b>As of December 31,</b>				
	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
	<b>(Percentages)</b>				
Requisite capital ratio(1)	134.43%	130.93%	118.41%	129.41%	132.81%
Total capital adequacy ratio for Shinhan Bank(2)	11.99	10.92	10.49	11.94	12.23
Tier I capital adequacy ratio(2)	8.24	6.81	6.34	7.45	8.16
Tier II capital adequacy ratio(2)	3.75	4.11	4.15	4.49	4.07
Total capital adequacy ratio for Chohung Bank(3)	10.43	8.66	8.87	9.40	10.94
Tier I capital adequacy ratio(3)	5.91	4.61	4.47	4.99	6.52
Tier II capital adequacy ratio(3)	4.52	4.05	4.40	4.41	4.42
Adjusted equity capital ratio of Shinhan Card(4)	N/A	10.86	13.78	16.48	17.68
Solvency ratio for Shinhan Life Insurance(5)	204.5	238.9	224.7	265.7	232.1

N/A = not applicable.

*Notes:*

- (1) We were restructured as a financial holding company on September 1, 2001 and became subject to minimum capital requirements as reflected in the requisite capital ratio. Under the guidelines issued by the Financial Supervisory Commission applicable to financial holding companies, we, at the holding company level, are required to maintain a minimum requisite capital ratio of 100%. Requisite capital ratio represents the ratio of net aggregate amount of our equity capital to aggregate amounts of requisite capital (all of which are described in Item 4. Information on the Company Supervision and Regulation Principal Regulations Applicable to Financial Holding Companies Capital Adequacy ). This computation is based on our consolidated financial statements prepared in accordance with Korean GAAP.
- (2) Shinhan Bank's capital adequacy ratios are computed in accordance with the regulations issued by the Financial Supervisory Commission, which was revised as of December 31, 2002 to take into account market risk as well as credit risk. The capital ratios as of December 31, 2002 were calculated using these revised guidelines. Under these guidelines, Shinhan Bank is required to maintain a minimum capital adequacy ratio of 8%. Applying the previous calculation, which only takes into account credit risks, Shinhan Bank's total capital adequacy ratio as of December 31, 2002, 2003, 2004 and 2005 were 10.91%, 10.59%, 11.96% and 12.27%, respectively. This computation is based on Shinhan Bank's consolidated financial statements prepared in accordance with Korean GAAP. See Item 4. Information on the Company Supervision and Regulation Principal Regulations Applicable to Banks Capital Adequacy.
- (3) Chohung Bank's capital adequacy ratios are computed in accordance with the regulations issued by the Financial Supervisory Commission, which was revised as of December 31, 2002 to take into account market risk as well as

credit risk. The capital ratios as of December 31, 2002 were calculated using these revised guidelines. Under these regulations, Chohung Bank is required to maintain a minimum capital adequacy ratio of 8%. Applying the previous calculation, which only takes into account credit risks,

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Chohung Bank's total capital adequacy ratio as of December 31, 2002, 2003, 2004 and 2005 was 8.64%, 8.89%, 9.39% and 10.94%, respectively. This computation is based on the Chohung Bank's consolidated financial statements prepared in accordance with Korean GAAP. See Item 4. Information on the Company - Supervision and Regulation - Principal Regulations Applicable to Banks - Capital Adequacy.

- (4) Represents the ratio of total adjusted shareholders' equity to total adjusted assets and is computed in accordance with the guidelines issued by the Financial Supervisory Commission for credit card companies. Under these regulations, Shinhan Card, which was established on June 4, 2002, is required to maintain a minimum adjusted equity capital ratio of 8%. This computation is based on Shinhan Card's nonconsolidated financial statements prepared in accordance with Korean GAAP.
- (5) Solvency ratio is the ratio of Solvency Margin to Standard Amount of Solvency Margin and is computed in accordance with the regulations issued by the Financial Supervisory Commission for life insurance companies. Under these regulations Shinhan Life Insurance is required to maintain a minimum solvency ratio of 100%. Based on the calculation, Shinhan Life Insurance's solvency ratio as of March 31, 2006 was 230.8%.

**EXCHANGE RATES**

The following table sets forth, for the periods and dates indicated, certain information concerning the Noon Buying Rate in Won per US\$1.00.

<b>Year Ended December 31,</b>	<b>At End of Period</b>	<b>Average(1)</b>	<b>High</b>	<b>Low</b>
		<b>(Won per US\$1.00)</b>		
2000	1,267.00	1,130.90	1,267.00	1,105.50
2001	1,313.50	1,292.00	1,369.00	1,234.00
2002	1,186.30	1,250.31	1,332.00	1,160.60
2003	1,192.00	1,192.08	1,262.00	1,146.00
2004	1,035.10	1,139.30	1,195.10	1,035.10
2005	1,010.00	1,023.75	1,059.80	997.00
2006 (through June 23)	955.80	962.29	1,002.90	927.40
January	958.90	981.44	1,002.90	958.90
February	970.90	969.84	976.30	962.00
March	971.40	974.71	981.95	966.80
April	942.80	952.60	970.40	939.60
May	945.30	940.82	951.50	927.40
June (through June 23)	955.80	953.75	961.80	942.70

*Note:*

- (1) The average of the Noon Buying Rates over the relevant period.

We have translated certain amounts in Korean Won, which appear in this document, into dollars for convenience. This does not mean that the Won amounts referred to could have been, or could be, converted into dollars at any particular rate, the rates stated above, or at all. All translations from Won to dollars are based on the Noon Buying Rate in effect on December 31, 2005, which was W1,010.00 to US\$1.00. The exchange rates used for convenience translations differ from the actual rates used in the preparation of our consolidated financial statements.

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**RISK FACTORS**

*An investment in the American depositary shares representing our common shares involves a number of risks. You should carefully consider the following information about the risks we face, together with the other information contained in this document, in evaluating us and our business.*

**Risks Relating to Competition**

***Competition in the Korean banking industry, in particular in the small- and medium-sized enterprises banking, retail banking and credit card operations, is intense, and we may experience declining margins as a result.***

We compete principally with other national commercial banks in Korea but also face competition from a number of additional sources including regional banks, development banks, specialized banks and foreign banks operating in Korea, as well as various other types of financial institutions, including credit card companies, securities companies and asset management companies. Over the past few years, regulatory reforms and liberalization of the Korean financial markets have led to increased competition among financial institutions in Korea. As the reform of the financial sector continues, foreign financial institutions, many with greater resources than we have, have entered the Korean market. There can be no assurance that we will be able to compete successfully with other domestic and foreign financial institutions or that increased competition will not have a material adverse effect on our financial condition or operating results.

The Korean commercial banking industry has undergone dramatic changes recently as a number of significant mergers and acquisitions in the industry have taken place. There may be additional consolidation in the Korean commercial banking industry, including Korea's regional banks in particular. In November 2001, Kookmin Bank and Housing & Commercial Bank, two of the strongest banks in Korea, merged to form Kookmin Bank. The newly merged bank is significantly larger and has more financial resources than us. Also in 2001, Woori Bank restructured itself as a financial holding company and significantly realigned its businesses and products to compete with other larger banks in Korea. Furthermore, a number of significant mergers and acquisitions in the industry have taken place in Korea over the last few years. In 2002, there was a merger of Hana Bank and Seoulbank. In 2003, Lone Star acquired a controlling interest in Korea Exchange Bank. In 2004, Citibank acquired KorAm Bank through a tender offer and subsequently renamed it Citibank Korea. In 2005, Standard Chartered Bank acquired Korea First Bank. In addition, in 2006, Kookmin Bank has entered into a definitive agreement to acquire Korea Exchange Bank from Lone Star pending regulatory approval. At present, these and other banks resulting from mergers or acquisitions may have more financial resources or more experience in providing certain banking or financial services than us. Increased competition and continuing consolidation in the Korean banking industry may lead to decreased margins. There can be no assurance that we will be able to compete successfully with such banks.

Over the past several years, virtually all Korean banks have adopted a strategy of reducing large corporate exposure and increasing small- and medium-sized enterprises, retail and credit card exposure. As a result, substantially all commercial banks and financial institutions in Korea have focused their business on, and engaged in aggressive marketing campaigns and made significant investments in, these sectors. The growth and profitability of our small- and medium-sized enterprises and retail banking activities and credit card operations may decline as a result of growing market saturation in these sectors, increased interest rate competition, pressure to lower the fee rates applicable to these sectors and higher marketing expenses. In particular, it will be more difficult for our bank subsidiaries to secure new small- and medium-sized enterprise customers, retail and credit card customers with the credit quality and on credit terms necessary to achieve our business objectives.

An important focus of our business is to increase our fee income in order to diversify our revenue base, in anticipation of greater competition and declining lending margins. To date, except for credit card fees, securities brokerage fees and trust account management fees, we have not generated significant fee revenues. Our focus on generating fee revenue also involves the development of fee business from bancassurance and investment trust management. We recognize, however, that other banks and financial institutions in Korea

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have recently recognized the same trends and are beginning to focus on increasing their fee income, in particular from bancassurance and investment trust.

Successful acquisition of these fee generating businesses by our competitors may result in increased competition in the area of investment trust business. Recently, Woori Securities has acquired LG Investment & Securities, Hana Bank has acquired Daehan Investment & Securities, and Dongwon Financial Holding has acquired Korea Investment & Securities.

Intense competition in the fee-based business will require us to create a new market and innovative products and services in a highly competitive environment. Our failure to do so could adversely affect our future results of operations.

In addition, the impending sale of the controlling equity stake in LG Card, currently the largest credit card company in Korea in terms of asset size which has been in debt restructuring since November 2003, by its creditors committee may significantly change the competitive environment for providers of credit card services in Korea, including us. The sale will take the form of an auction to multiple bidders, and we are currently participating in this auction as one of the bidders. See Developments adversely affecting the business and liquidity of credit card companies in Korea, including LG Card, may result in losses in respect of our exposure to such companies. Failure by us to win the bid to acquire the controlling equity stake of LG Card and/or the acquisition of such stake of LG Card by one of our leading competitors in the banking business could adversely affect our competitive position in the credit card business as well as other related businesses and limit our future growth.

***We are highly dependent on short-term funding sources that are susceptible to price competition, which dependence may adversely affect our operations.***

Most of our funding requirements, principally those of Shinhan Bank and Chohung Bank, are met through short-term funding sources, primarily in the form of customer deposits, which are subject to significant price competition. As of December 31, 2005, approximately 90.69% of our total deposits had current maturities of one year or less or were payable on demand. In the past, a substantial portion of such customer deposits has been rolled over upon maturity or otherwise maintained with us, and such short-term deposits have been a stable source of funding over time. For example, of Shinhan Bank's total time deposits outstanding as of December 31, 2005 with remaining maturities of four months or less, approximately 54.46% were rolled over or otherwise maintained with Shinhan Bank. Of Chohung Bank's total time deposits maturing during the four months ended December 31, 2005, approximately 57.01% were rolled over or otherwise maintained with Chohung Bank. No assurance can be given, however, that such stable source of funding will continue, including as a result of intense price competition. If a substantial number of depositors fail to roll over deposited funds upon maturity or withdraw such funds from us, our liquidity position could be materially adversely affected, and we may be required to seek more expensive sources of short-term and long-term funds to finance our operations.

**Risks Relating to Our Banking Business**

***We have significant exposure to small- and medium-sized enterprises including smaller enterprises, which may result in a deterioration of our asset quality to this segment and have an adverse impact on us.***

Our loans to small- and medium-sized enterprises meeting the definition of such enterprises under the Basic Act on Small- and Medium-sized Enterprises and its Presidential Decree increased from W38,055 billion as of December 31, 2003 to W38,713 billion as of December 31, 2004 and to W39,943 billion as of December 31, 2005. These balances represent 40.0%, 39.9% and 37.7%, respectively, of our total loan portfolio as of December 31, 2003, 2004 and 2005. For a definition of small- and medium-sized enterprises, see Item 4. Information on the Company Business Overview Our Principal Activities Corporate Banking Services Small- and medium-sized Enterprises Banking. Non-performing loans to small- and medium-enterprises as described above were W605 billion as of December 31, 2003, W1,005 billion as of

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December 31, 2004 and W1,015 billion as of December 31, 2005, representing 1.59%, 2.60% and 2.54% of our total loans to small- and medium-sized enterprises as of December 31, 2003, 2004 and 2005.

Since 2002, the industry-wide delinquency ratios for loans to small- and medium-sized enterprises have been rising under Korean GAAP. According to data compiled by the Financial Supervisory Service, the delinquency ratio (net of charge-offs, which has also increased significantly) for loans by Korean banks to small- and medium-sized enterprises increased from 1.9% as of December 31, 2001 to 3.2% as of May 31, 2004, the record-high to date, and decreased to 1.5% as of December 31, 2005. The delinquency ratio for loans to small- and medium-sized enterprise is calculated as the ratio of (1) the outstanding balance of such loans in respect of which either principal payments are overdue by one day or more or interest payments are overdue by 14 days or more (if prior interest payments on a loan were made late on more than three occasions, in which case the loan is considered delinquent if interest payments are overdue by one day or more) to (2) the aggregate outstanding balance of such loans. Under Korean GAAP, Shinhan Bank's delinquency ratio for such loans increased from 1.75% as of December 31, 2003 to 1.80% as of December 31, 2004 and decreased to 1.44% as of December 31, 2005 and Chohung Bank's delinquency ratio for such loans decreased from 3.49% as of December 31, 2003 to 2.21% as of December 31, 2004 and to 1.70% as of December 31, 2005. In 2003, 2004 and 2005, under Korean GAAP, Shinhan Bank charged off loans to small- and medium-sized enterprises of W36 billion, W101 billion and W82 billion, respectively, while Chohung Bank charged off loans to small- and medium-sized enterprises of W73 billion, W255 billion and W118 billion, respectively. In addition, Chohung Bank did not sell any of its loans to small- and medium-sized enterprises of in 2003, but sold W357 billion in 2004 and W175 billion in 2005 under Korean GAAP. Shinhan Bank did not sell any of its loans to small- and medium-sized enterprises in 2003, but sold W146 billion in 2004 and W126 billion in 2005 under Korean GAAP. Absent these charge-offs and loan sales, the delinquency ratios would have been higher.

We have increased significant exposure to the real estate, leasing and service industry as it presented significant growth opportunities in recent years. Our loans to the real estate, leasing and service industry increased from W6,132 billion, or 11.34% of total corporate loans (Shinhan Bank and Chohung Bank combined), as of December 31, 2003, to W7,691 billion, or 14.08% of total corporate loans, as of December 31, 2004, and to W9,434 billion, or 16.30% of total corporate loans, as of December 31, 2005. In addition, our loans to the hotel and leisure industry (consisting principally of hotels, motels and restaurants) as of December 31, 2003, 2004 and 2005 aggregated W1,977 billion, W2,082 billion and W2,114 billion, respectively, or 3.66%, 3.81% and 3.65%, respectively, of total corporate loans. The real estate, leasing and service industry and the hotel and leisure industry experienced significant difficulties in 2004 resulting in higher delinquencies and impairment. As of December 31, 2005, under Korean GAAP, the delinquency ratios for loans to the real estate, leasing and service industry were 1.73% for Chohung Bank and 1.00% for Shinhan Bank, in each case net of charge-offs and loan sales. As of December 31, 2005, under Korean GAAP, the delinquency ratios for loans to the hotel and leisure industry were 3.30% for Chohung Bank and 1.88% for Shinhan Bank, in each case net of charge-offs and loan sales. A continued deterioration in asset quality of loans to these industry sectors may materially and adversely affect our financial condition and results of operations.

The small- and medium-sized enterprise lending business is still the focus of intense competition among large commercial banks and the opportunities for us to expand our business with more established small- and medium-sized enterprises have been reduced. We have in recent years selectively increased our customer base to include relatively smaller enterprises, including small unincorporated businesses and sole proprietorships. We believe that lending to these customers have presented an opportunity for growth but also increased our credit risk exposure relative to our existing customers in this segment. Continued weakness in the Korean and global economies, among other things, will adversely affect the financial condition of small- and medium-sized enterprises and may impair their ability to service their debt, including our loans to such customers.

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***We may not be able to sustain the high rate of growth in our mortgage and home equity lending. In addition, we cannot assure that the asset quality of our mortgage and home equity loans, in particular the long-term mortgage and home equity loans, will not deteriorate.***

Over the past three years, mortgage and home equity lending was the largest contributor to the growth of our lending business. Our mortgage and home equity lending grew from W20,517 billion as of December 31, 2003 to W22,180 billion as of December 31, 2004 and to W25,840 billion as of December 31, 2005. Such increase represents 20.5% and 41.74% of the overall increase in our loan portfolio during 2004 and 2005, respectively. Of our total consumer loan portfolio, 49.8%, 52.24% and 53.88% was attributable to mortgage and home equity lending as of December 31, 2003, 2004 and 2005, respectively. The growth of such lending is significantly dependent on, among other things, competitive conditions, real estate prices, interest rate levels and government policies affecting these markets. The Korean government enacted a number of changes to laws governing retail lending volumes, including the lowering of maximum loan-to-value ratio of mortgage and home equity loans to 60%, and in certain cases to 40%. In recent years, the Korean government has issued several policy-driven regulations to suppress the increasing real estate prices in certain zones of the Seoul Metropolitan area that are in high demand, including the further reduction of maximum loan-to-value ratio applicable to mortgage and home equity loans for real estate in those regulated zones, which may result in a general decline in the real estate prices in Korea. Due to the factors discussed above, there can be no assurance that significant growth of our mortgage and home equity lending business will continue.

Consistent with practices in the Korean banking sector, a substantial majority of our mortgage and home equity loans have maturity of one to three years and are renewable based on our credit decisions. Since early 2004, however, we have begun offering longer-term mortgage and home equity loans with maturities of ten to 30 years similar to those offered in the United States. As of December 31, 2005, we had W11,451 billion of such long-term mortgage and home equity loans outstanding, for which we established an allowance for loan losses of W5 billion. This relatively low amount of allowance for loan losses compared to the amount of the long-term mortgage and home equity loans were primarily due to the fact that these loans are oversecured and are made subject to the condition of relatively low loan-to-value ratios. For mortgage and home equity loans, we establish allowances based on loss factors taking into consideration historical performance of the portfolio, previous loan loss history and charge-off information. Due to the limited history of extending these longer term mortgage and home equity loans, we cannot assure you that the allowances we have established against these loans will be sufficient to cover all future losses arising from these loans in the future. Although we adjust the loss factors derived from the migration analysis as appropriate to reflect the impact of any current conditions on loss recognition that has not been adequately captured by our historical analysis, no assurance can be given that we may adequately do so in time or at all.

***A decline in the value of the collateral securing our loans and our inability to realize full collateral value may adversely affect our credit portfolio.***

Borrowers' house, other real estate and other securities secure substantial portions of our loans. As of December 31, 2005, the secured portion of Won-denominated loans of Shinhan Bank amounted to W29,578 billion, or 66.66% of such loans, and the secured portion of Won-denominated loans of Chohung Bank amounted to W18,231 billion, or 51.94% of such loans, under Korean GAAP. No assurance can be given that the collateral value may not materially decline in the future. Until recently, it was Shinhan Bank's general policy to lend up to 50%-70% of the appraised value of collateral, which appraisal value we believe was, in general, lower than the market value. Chohung Bank's policy is to lend up to the estimated recovery value of the collateral, which Chohung Bank calculates based on the value of collateral published by the courts as recovered through court-approved auctions and further adjusted to take into account the existence of any lien or other security interest that is prior to Chohung Bank's security interest. We believe that such estimated recovery value of the collateral is, in general, lower than the market value. However, downturns in the real estate market as well as decreases in the value of securities collateral in the past have resulted in a number of loans whose principal amount exceeds the value of the underlying collateral at times. Declines in the value of securities and/or real estate prices in Korea that result in shortfalls in collateral values compared to loan amounts would require us to increase loan loss provisions and may have a material adverse effect on us. For a

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description of our collateral valuation policy, see Item 4. Information on the Company Description of Assets and Liabilities Risk Management Credit Risk Management of Shinhan Bank Credit Evaluation and Approval Consumer Loans and Item 4. Information on the Company Business Overview Our Principal Activities Retail Banking Services Consumer Lending Activities .

Foreclosure on collateral generally requires a written petition to a Korean court. Such application, when made, may be subject to delays and administrative requirements that may result in a decrease in the recovery value of such collateral. Foreclosure proceedings under laws and regulations in Korea typically take from seven months to one year from initiation to collection depending on the nature of the collateral. In addition, there can be no assurance that we will be able to realize the full value of such collateral as a result of, among other factors, delays in foreclosure proceedings, defects in the perfection of collateral, fraudulent transfers by borrowers and general declines in collateral value due to oversupply of properties that are placed in the market.

***We may experience a further deterioration of the credit quality of our credit card and other consumer lending portfolios.***

Our total consumer portfolio is comprised of three principal product types, namely mortgage and home equity loans, credit cards and other consumer loans (which include principally unsecured consumer loans). In recent years, credit card and other consumer lending, including lending to small unincorporated businesses, in Korea experienced significant growth as a result of government policies and a greater focus on these sectors by commercial banks and credit card companies. This growth, however, led to industry-wide declines in overall credit quality, with increased delinquencies, provisions and charge-offs, as a result of, among other things, weak economic conditions as well as an increase in unemployment. The unemployment rate in Korea was 3.8% as of December 31, 2003 and 3.8% as of December 31, 2004, and decreased to 3.5% as of December 31, 2005.

In response to the events described above, including as part of our continued efforts to reduce or charge-off delinquent credit card loans, the amount of credit card loans has decreased from W6,112 billion as of December 31, 2003 to W4,732 billion as of December 31, 2004 and to W4,242 billion as of December 31, 2005. Our other consumer loans, on the other hand, have continued to increase from W14,580 billion as of December 31, 2003, to W15,546 billion as of December 31, 2004 and to W17,875 billion as of December 31, 2005. While our delinquency ratio for total consumer loans decreased from 3.95% in 2003 to 1.70% in 2005, the credit card and other consumer loan sectors may still experience credit quality problems and there can be no assurance that these problems will not have a material adverse effect on our results of operations.

In addition, due to the rapid increase in consumer debt in Korea in recent years, the Korean government has adopted a series of regulations designed to restrain the rate of growth in, and delinquencies of, cash advances, credit card loans and credit card usage generally and to strengthen the reporting of, and compliance with, credit quality indexes. In March 2002, the Financial Supervisory Commission imposed sanctions, ranging from warnings and administrative fines to partial business suspensions, on substantially all Korean credit card issuers as a result of alleged unlawful or unfair practices discovered during its industry-wide inspection. In March 2002, Chohung Bank was given a warning by the Financial Supervisory Commission for issuing credit cards to underaged customers. In late 2002, the Korean government enacted a number of changes to the laws governing the reporting by credit card issuers, including increasing the minimum allowance required, stated as a certain percentage of outstanding balance, and revising the calculation of delinquency ratios applicable to credit cards, which are performed on a Korean GAAP basis as described in Item 5. Operating and Financial Review and Prospects Reconciliation with Korean Generally Accepted Accounting Principles . The Korean government may adopt further regulatory changes in the future that affect the credit card industry, which in turn may adversely affect our credit card operations. See Item 4. Information on the Company Business Overview Our Principal Activities Credit Card Services . We believe that the Korean government will continue to announce regulatory changes restricting the growth of consumer loans. These regulations may significantly reduce the level of our consumer lending and credit card operations that we engage and maintain in the future. The growth and profitability of our consumer lending and credit card operations may suffer materially as a result of these enforcement activities and regulations and proposed regulations.



**Table of Contents*****Developments adversely affecting the business and liquidity of credit card companies in Korea, including LG Card, may result in losses in respect of our exposure to such companies.***

Adverse developments in the credit card industry in recent years such as industry-wide increases in delinquencies and resulting increases in provisioning for loan losses have had a negative impact on investors' perception of credit card companies in the Korean corporate debt market, thereby significantly limiting the ability of credit card companies to obtain financing through issuances of debt securities. As a result, Korean credit card companies recently experienced significant financial and liquidity difficulties. According to a press release issued by the Financial Supervisory Commission, the average industry-wide delinquency ratio (defined as ratio of credit card balances that are delinquent for more than 30 days over total outstanding balances, including delinquent balances rewritten as credit card loans) of credit card companies in Korea was approximately 10.05% as of December 31, 2005 and 8.77% as of March 31, 2006. Although such delinquency ratio was reported to have decreased from 28.28% as of December 31, 2003, the level of delinquencies experienced by the credit card industry in Korea still remains relatively high. As of December 31, 2005, we held debt and equity securities issued by credit card companies (including through asset-backed securitization) in the aggregate principal amounts of W787 billion and W195 billion, respectively, in our investment portfolio.

As of December 31, 2005, we had loans outstanding to credit card companies in the aggregate principal amount of W610 billion. These loans, excluding loans extended to LG Card, are considered performing in accordance with our internal credit rating methodology and therefore we have not recognized a specific loan loss allowance against these loans. See Item 4. Information on the Company Description of Assets and Liabilities Loans Loan Concentrations Exposures to the Credit Card Industry. To the extent that financial and liquidity difficulties experienced by credit card companies are not resolved on a timely basis, the asset quality of our exposure to credit card companies may become significantly impaired, resulting in losses that are materially adverse to our financial condition and results of operations and capital adequacy.

In particular, LG Card, currently Korea's largest credit card company, experienced significant liquidity and asset quality problems in 2003 and has been engaged in a workout since November 2003. As part of this workout program, the creditor banks of LG Card (including Shinhan Bank and Chohung Bank) have taken a number of steps, including providing a W2 trillion credit facility (with respect to W1 trillion of which facility, maturity has been extended until December 2006), engaging in several rounds of debt-to-equity swaps and agreeing to substantial capital write-downs. Recently, the creditors committee of LG Card, led by Korea Development Bank, has been attempting to sell a controlling equity stake in LG Card in the form of an auction to multiple bidders. We are currently participating in this auction as one of the bidders with a view to acquiring control in LG Card.

As of December 31, 2005, our total exposure to LG Card was W364 billion, including W136 billion of loans, W33 billion of debt securities and W195 billion of equity securities. We made an allowance for loan losses of W0.7 billion for the loans. As a result of the satisfactory progress on scheduled debt restructuring of LG Card, in 2005, we recorded reversal of loan loss provisions of W12 billion but also recognized securities impairment losses of W7 billion, resulting in a net gain of W5 billion in respect of our exposures to LG Card. In connection with the LG Card rescue plan, Shinhan Bank transferred W10 billion of exposure in its performance-based trust account to the bank account in January 2004 and Chohung Bank also transferred W30 billion of exposure in its performance-based trust account to the bank account in February 2004, resulting in an increase in our total exposure to LG Card. These exposures were included in our credit exposure that was converted into equity in connection with the rescue plan of LG Card as described above.

The value of underlying collateral, our pro rata entitlement thereto and the allowances we have established or will establish against our exposures to LG Card and other Korean credit card companies may not be sufficient to cover all future losses arising from these exposures. Following the debt-to-equity conversions in respect of our exposures to LG Card, we may experience further losses if the market value of the LG Card equity securities we own falls below their recorded book value.

In addition, in the case of credit card companies that are in or in the future enter into workout, restructuring, reorganization or liquidation proceedings, our recoveries from those companies may be limited.



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We may, therefore, experience future losses with respect to these exposures. Furthermore, to the extent that our investment portfolio include in the future beneficiary certificates representing interests in investment trusts whose assets include securities issued by troubled credit card companies and the value of securities issued by credit card companies declines as a result of their financial difficulties or otherwise, we may experience losses on our investment securities.

***We have significant exposure to the largest Korean business conglomerates, known as chaebols, and, as a result, recent and any future financial difficulties of chaebols may have an adverse impact on us.***

As a result of the unfavorable financial and economic conditions in Korea, a number of chaebols have experienced and continue to experience financial difficulties. We have significant exposure to chaebols and large corporate borrowers. Of our twenty largest corporate exposures as of December 31, 2005, seven are companies that are members of the 29 largest chaebols in Korea. If the quality of the exposures extended by us to chaebols declines, we would require additional loan loss provisions in respect of loans and would record impairment losses in respect of securities, which would adversely affect our financial condition, results of operations and capital adequacy.

In particular, we have significant exposure to SK Networks, which experienced financial difficulties after disclosure of its accounting irregularities and is currently in a workout program. If this program is not satisfactorily resolved, it may have a material adverse effect on us. As of December 31, 2005, our total exposure outstanding to SK Networks (formerly, SK Global) alone was W670 billion, or 0.47% of our total exposure, consisting of W326 billion in loans, W7 billion in debt securities, W240 billion in equity securities and W97 billion in guarantees and acceptances. Of our total loans outstanding to SK Networks, W24 billion was secured. For the unsecured loans of W302 billion, we made allowance for loan losses of W20 billion. With respect to the guarantees and acceptances outstanding, we made allowances of W6 billion.

All of the indebtedness of SK Networks and its overseas subsidiaries held by Korean financial institution creditors was resolved either through an exchange for 43% of the principal amount in promissory notes and 5% of the principal amount in the form of bonds with warrants or in accordance with the Memorandum. Under the Memorandum, all of the indebtedness of SK Networks held by the Korean financial institution creditors was converted into shares of common stock, Redeemable Preferred Stock and mandatory convertible bonds of SK Networks. As a result of this corporate restructuring, we owned 9.54% of common shares of SK Networks (or 9.87% of total equity ownership in SK Networks including the Redeemable Preferred Stock) as of December 31, 2005.

We also have exposures to other companies belonging to the SK Group. As of December 31, 2005, our total exposure outstanding to SK Corporation, the controlling company of the SK Networks, was W398 billion, or 0.28% of our total exposure, consisting of W141 billion in loans, W43 billion in debt securities, W132 billion in equity securities, and W82 billion in guarantees and acceptances. We classify loans and guarantees and acceptances to other SK Group companies, including SK Corporation, as non-impaired in accordance with our internal credit rating methodology and therefore no specific allowance is made against these loans or guarantees and acceptances. Our management believes the general allowance of W0.9 billion against the non-impaired element of the corporate loan portfolio in total is sufficient to cover any incurred losses within this portfolio, including those loans to companies within the SK Group, including SK Corporation and excluding SK Networks. For a more detailed discussion of our exposure to the SK Group as of December 31, 2005, see Item 4. Information on the Company Description of Assets and Liabilities Loans Loan Concentrations Exposures to SK Group Companies .

In addition, we have significant exposures to former Ssangyong Group companies, a number of which have been experiencing financial difficulties. In 1998, Daewoo Motors acquired Ssangyong Motors from the former Ssangyong Group, on condition that certain of the then existing liabilities of Ssangyong Motors be retained by the former Ssangyong Group. In connection with this transaction, nine member companies of the Ssangyong Group assumed in the aggregate W1.8 trillion, which subsequently resulted in significant increases in interest expense for such companies, further aggravated by a sharp increase in interest rates during the financial crisis of the late 1990 s. Several of the Ssangyong Group companies, including Ssangyong

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Corporation, Ssangyong Cement Industrial and Ssangyong Engineering & Construction, have experienced significant financial and liquidity difficulties as a result and were subsequently placed under workout programs by their respective creditors. In particular, Chohung Bank is the largest creditor to Ssangyong Corporation and, as such, is the lead creditor bank under the workout program applicable to Ssangyong Group companies. Ssangyong Cement exited the workout in November 2005, and the controlling equity interest in Ssangyong Corporation was sold to Morgan Stanley Private Equity Holdings AB in April 2006. As of December 31, 2005, our total exposure to Ssangyong Corporation and Ssangyong Cement Industrial amounted to W221 billion and W174 billion, respectively, for which we have raised allowances for loan losses of W1.3 billion, or 0.6%, and W0.2 billion, 0.1%, respectively. Of our total loans and guarantees and acceptances to the Ssangyong Group, W172 billion was classified as impaired. We cannot assure you that the allowances we have established against our exposures to the former Ssangyong Group companies will be sufficient to cover all future losses arising from these exposures. For a more detailed discussion of our exposure to the former Ssangyong Group as of December 31, 2005, see Item 4. Information on the Company Description of Assets and Liabilities Loans Loan Concentrations Exposures to Ssangyong Group Companies .

In addition, with respect to those companies that are in or in the future enter into workout or liquidation proceedings, we may not be able to make any recoveries against such companies. We may, therefore, experience future losses with respect to those loans, which may have a material adverse impact on our financial condition, results of operations and capital adequacy.

***Future financial difficulties of chaebols may adversely affect the credit quality of our small- and medium-sized enterprise customers who serve chaebols.***

Many of the more established small- and medium-sized enterprises, which have been a key focus of our corporate banking activities, have close business relationships with chaebols, primarily as suppliers and subcontractors. Recently, many chaebols have moved and continue to move their production plants or facilities or business operations to China and other countries with lower labor costs and other expenses, which will lead to less business opportunities for small- and medium-sized enterprises resulting in a material adverse impact on their financial condition and results of operations, including their ability to service their debt as they come due. Financial difficulties experienced by our small- and medium-sized enterprises customers, and our less established customers in particular, may have an adverse impact on our financial condition and results of operations.

***We have exposure to companies that are currently or may in the future be put in restructuring, and we may suffer losses as a result of additional loan loss provisions required and/or the adoption of restructuring plans with which we do not agree.***

As of December 31, 2005, our loans to companies that were under troubled debt restructurings amounted to W990 billion, or 0.94% of our total loans, and our allowances for losses on these loans amounted to W179 billion, or 18.1% of such loans. As of the same date, our guarantees and acceptances to companies that were under troubled debt restructurings amounted to W247 billion, or 3.57% of our total guarantees and acceptances, and our allowance for such guarantees and acceptances amounted to W14 billion, or 5.7% of such guarantees and acceptances. These allowances may not be sufficient to cover all future losses arising from our exposure to these companies. Furthermore, pursuant to the Corporate Restructuring Promotion Act which was abolished as of December 31, 2005, in the event that any of our borrowers became subject to corporate restructuring procedures, we could be forced to restructure our credits pursuant to restructuring plans approved by other creditor financial institutions holding 75% or more of the total outstanding debt (and 75% or more of the total outstanding secured debt, if the restructuring plan included the restructuring of existing secured debt) of the borrower, or to dispose of our credits to other creditors on unfavorable terms. Although the Corporate Restructuring Promotion Act was abolished and is no longer effective, the National Assembly is currently in discussion as to reviving such law and accordingly, a law similar to the Corporate Restructuring Promotion Act may be adopted in the future and subject us to similar restraints.

**Table of Contents*****The recent announcement by the Korean National Tax Service relating to the tax treatment of certain deposit products may adversely affect our financial condition and results of operations.***

Beginning in 2002, commercial banks in Korea, including Shinhan Bank and Chohung Bank, offered to their customers deposit products that utilize Korean Won and Japanese Yen swaps to maximize the return for such customers. According to the terms of these deposit products, deposits made by customers in Korean Won are converted into Japanese Yen and repaid in Japanese Yen at maturity. The repayment amount is then converted back into Korean Won. While these deposit products typically carry a low interest rate, ranging from 0.05% to 0.30% per annum, the actual return to the customers was higher as a result of foreign exchange gains. These deposit products are attractive to customers, in particular high net worth customers, since the gains from foreign exchange were deemed not to be interest subject to income tax. However, in 2005, the Korean National Tax Service announced that foreign currency deposits disguised as derivative products would be subject to tax and tax withholding and issued a recommendation that the banks should refile its tax returns to include the unwithheld amounts. Eight of the commercial banks in Korea, who are subject to this adverse tax treatment, have announced their intention to challenge the foregoing decision by the Korean National Tax Service while complying with the Tax Service's information requests.

The commercial banks had marketed these deposit products to their customers on the basis that such deposit products were exempt from income tax or tax withholding. We believe that few, if any, of these customers have reported the gains from such deposit products as interest income subject to taxation in their tax returns. According to the Korean National Tax Service, these deposit customers are also responsible for including the income received from these deposits in their final individual tax returns relating to comprehensive financial taxable income. However, depending on the amount of income received from these products, the individual customers may be subject to (i) a higher tax rate on all of his or her taxable income, (ii) a fine for failing to properly report the interest income in an amount equal to 20% of the unreported amount, and (iii) a fine for failing to pay tax on such interest income in an amount equal to interest applied at a rate of 10.95% per annum to such unpaid tax amount. No assurance can be given that aggrieved customers will not bring claims against these commercial banks, including Shinhan Bank and Chohung Bank, if their tax liabilities are increased as a result of the foregoing events.

Beginning in September 2005, we have been subject to a tax audit by the Korean National Tax Service. In May 2006, based upon its tax audit of us and other relevant banks, the Korean National Tax Service reached a decision to impose additional taxes (including interest thereon) of W36 billion on Shinhan Bank. This decision did not include a judgment on deposits utilizing the Korean Won and Japanese Yen swaps as described above, but such judgment is expected soon. In anticipation of an adverse tax ruling against these deposit products utilizing Korean Won and Japanese Yen swaps, we have determined, on a voluntary basis, to indemnify our customers for their increased tax liability to the extent resulting from their investment in these deposit products, including any additional tax liability that our customers may have against the Korean National Tax Service for gifts tax from the benefit of this indemnity. We currently estimate that we may be subject to maximum additional tax-related liability, including the liability from the indemnity to our customers, of W85 billion as of December 31, 2005. Accordingly, we recorded a total charge to our income of W78 billion in the year ended December 31, 2005, consisting of additional tax expenses of W29 billion and provision for other losses of W49 billion. In addition, we also recorded W7 billion as deferred tax assets on our balance sheet as of December 31, 2005.

***The loss of deposit accounts maintained by Korean courts with Chohung Bank may adversely affect Chohung Bank's financial position and results of operations.***

Chohung Bank believes that it holds the largest amount of deposits made by litigants and applicants in connection with legal proceedings in Korean courts or by persons involved in disputes. Although Chohung Bank has been involved in this business for more than forty years and has acquired certain competitive advantages and entry barriers in connection therewith, no assurance can be given that Chohung Bank will be able to maintain its competitiveness in this area. The Korean Supreme Court in 1994 opened to other banks the opportunity to establish new sub-branches or branches in newly opened court houses. The Supreme Court may open up competitive bidding to the entire network of sub-branches and branches taking court deposits. If



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the Supreme Court decides to select a bank for court deposits at all courts through competitive bidding, there can be no assurance that Chohung Bank will be selected. Because court deposits are a low-cost source of funding and Chohung Bank had total court deposits of W4,205 billion, W4,329 billion and W5,002 billion as of December 31, 2003, 2004 and 2005, respectively, which accounted for 10.8%, 11.2% and 12.9% of total Won deposits of Chohung Bank as of the same periods, the loss of such business may adversely affect Chohung Bank's financial condition and results of operations.

***Any deterioration in the asset quality of our guarantees and acceptances will likely have a material adverse affect on our financial condition and results of operations.***

In the normal course of our banking activities, we make various commitments and incur certain contingent liabilities in the form of guarantees and acceptances. Certain guarantees issued or modified after December 31, 2002 that are not derivative contracts have been recorded on our consolidated balance sheet at their fair value at inception. Other guarantees are recorded as off-balance sheet items in the footnotes to our financial statements and those guarantees that we have confirmed to make payments on become acceptances, which are recorded on the balance sheet. We had aggregate guarantees of W5,079 billion, and acceptances of W1,879 billion as of December 31, 2005. We provide an allowance for losses with respect to guarantees and acceptances as of each balance sheet date. We provided allowances for losses of W36 billion in respect of the guarantees and W15 billion in respect of acceptances as of December 31, 2005. If we experience significant asset quality deterioration in our guarantees and acceptances exposures, no assurance can be given that such allowances will be sufficient to cover any actual losses resulting in respect of these liabilities, or that the losses we incur on guarantees and acceptances will not be larger than those experienced on corporate loans.

**Risks Relating to Our Strategy**

***As a holding company, we are dependant on receiving dividends from our subsidiaries in order to pay dividends on our common shares.***

We are a financial holding company with minimal operating assets other than the shares of our subsidiaries. Our source of funding and cash flow is dividends from, or disposition of our interests in, our subsidiaries or our cash resources, most of which are currently the result of borrowings. Since our principal asset is the outstanding capital stock of Shinhan Bank and Chohung Bank, our ability to pay dividends on our common shares will mainly depend on dividend payments from Shinhan Bank, Chohung Bank and other subsidiaries.

Under the Korean Commercial Code, dividends may only be paid out of distributable income, an amount which is calculated by subtracting the aggregate amount of a company's paid-in capital and certain mandatory legal reserves from its net assets, in each case as of the end of the prior fiscal year;

Under the Bank Act, a bank also is required to credit at least 10% of its net profit to a legal reserve each time it pays dividends on distributable income until such time when this reserve equals the amount of its total paid-in capital; and

Under the Bank Act and the requirements promulgated by the Financial Supervisory Commission, if a bank fails to meet its required capital adequacy ratio or otherwise subject to the management improvement measures imposed by the Financial Supervisory Commission, then the Financial Supervisory Commission may restrict the declaration and payment of dividend by such a bank.

Shinhan Bank is considered well-capitalized under the Bank Act and the Financial Supervisory Commission requirements. As a result of its merger with Chohung Bank which had accumulated deficit, however, the distributable profits of Shinhan Bank (which represents retained earnings less certain reserves) decreased significantly in 2006. Accordingly, we cannot assure you that Shinhan Bank will continue to meet the criteria under the regulatory guidelines, in which case it may stop paying or reduce the amount of dividends paid to us.

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***We may fail to fully realize the anticipated benefits of the merger of Shinhan Bank and Chohung Bank.***

We aim to capitalize over time on the combined strengths of Shinhan Bank and Chohung Bank in terms of market share, product and service mix, customer base and cost efficiencies. Our ability to achieve these benefits, in particular following the merger of the two banks in April 2006, is subject to risks and uncertainties, some of which are beyond our control, including:

difficulties in operating the integrated information technology system, electronic banking systems, risk management and other systems;

difficulties in harmonizing the two corporate cultures;

difficulties in integrating the currently separate labor unions of the former Chohung Bank and Shinhan Bank; and

difficulties in retaining and attracting customers that overlapped between Chohung Bank and Shinhan Bank prior to the merger.

***We may need to raise additional capital, and adequate financing may not be available to us on acceptable terms, or at all.***

We may seek additional capital in the near future to fund the growth of our operations, including through mergers and acquisitions, including but not limited to our targeted acquisition of LG Card, to provide financial support for our subsidiaries, including funds needed to address liquidity difficulties, to meet minimum regulatory capital adequacy ratios and to enhance our capital levels. We may not be able to obtain additional debt or equity financing, or if available, it may not be in amounts or on terms commercially acceptable to us, it may impose conditions on our ability to pay dividends or grow our business or it may impose restrictive financial covenants on us. If we are unable to obtain the funding we need, we may be unable to continue to implement our business strategy, enhance our financial products and services, take advantage of future opportunities or respond to competitive pressures, all of which could have a material adverse effect on our financial condition and results of operations.

***We may not succeed in improving customer service through the introduction of performance-based compensation.***

Our ability to increase our market share in the retail, small- and medium-sized enterprise and credit card segments will depend in part upon our ability to attract and maintain customers through high-quality services. We intend to enhance the quality of our customer service by increasing employee performance measured against the level of customer satisfaction and customer response to our products and services and the quality of the assets and revenues generated. To do so, it may involve the introduction of performance-based compensation. Virtually all employees interfacing with our customers are members of our labor union subject to contracts that do not currently provide for performance-based compensation. To the extent we attempt to implement performance-based compensation, we may face strong resistance from our labor union. Failure of the union to accept or cooperate fully with our new programs may materially adversely affect the implementation of this aspect of our strategy.

**Risks relating to our other businesses**

***We may incur significant losses from our investment and, to a lesser extent, trading activities due to market fluctuations.***

We enter into and maintain large investment positions in the fixed income markets, primarily through our treasury and investment business. We describe these activities in Item 4. Information on the Company Business Overview Our Principal Activities Treasury and Securities Investment . We also maintain smaller trading positions, including securities and derivative financial instruments as part of our banking operations. In each of the product and business lines in which we enter into these kinds of positions, part of our business entails making assessments about financial market conditions and trends. The revenues and profits

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we derive from many of our positions and related transactions are dependent on market prices. When we own assets such as debt securities, market price declines, including as a result of fluctuating market interest rates, can expose us to losses. If prices move in a way we have not anticipated, we may experience losses. Also, when markets are volatile, characterized by rapid changes in price direction, the assessments we have made may prove to lead to lower revenues or profits, or losses, on the related transactions and positions.

***Protracted market declines can reduce liquidity in the markets, making it harder to sell assets and leading to material losses.***

In some of our businesses, protracted market movements, particularly price declines in assets, can reduce the level of activity in the market or reduce market liquidity. These developments can lead to material losses if we cannot close out deteriorating positions in a timely way. This may especially be the case for assets that are not traded on stock exchanges or other public trading markets, such as corporate debt securities issued by Korean companies, including credit card companies, and derivatives contracts, which may have values that we calculate using models other than publicly-quoted prices. For instance, the market value of debt securities in our portfolio as reflected on our balance sheet is determined by references to suggested prices posted by Korean rating agencies. These valuations, however, may differ significantly from the actual value that we may realize in the event we elect to sell these securities. As a result, we may not be able to realize the full marked-to-market value at the time of any such sale of these securities and thus may incur additional losses. Monitoring the deterioration of prices of assets like these is difficult and could lead to losses we did not anticipate.

***We may generate lower revenue from brokerage and other commission- and fee-based business.***

Market downturns are likely to lead to a decline in the volume of transactions that we execute for our customers and, therefore, to a decline in our non-interest revenues. In addition, because the fees that we charge for managing our clients' portfolios are in many cases based on the value of performance of those portfolios, a market downturn that reduces the value of our clients' portfolios or increases the amount of withdrawals would reduce the revenues we receive from our securities brokerage, trust account management and other asset management services. Even in the absence of a market downturn, below-market performance by our securities, trust account or asset managers may result in increased withdrawals and reduced inflows, which would reduce the revenue we receive from these businesses.

***Our Internet banking services are subject to security concerns relating to the commercial use of the Internet.***

We provide Internet banking services to our retail and corporate customers, which require sensitive customer information, including passwords and account information, to be transferred over a secure connection on the Internet. However, connections on the Internet, although secure, are not free from security breach. No assurance can be given that security breach in connection with our Internet banking service will not occur in the future, which may result in significant liability to our customers and third parties and materially and adversely affect our business.

***We may experience disruptions, delays and other difficulties from our information technology systems.***

We rely on our information technology systems for our daily operations including billing, effecting online and offline banking transactions and record keeping. In connection with the merger of Shinhan Bank and Chohung Bank, we are currently in the process of integrating the information technology systems of the two banks and to launch an upgraded and integrated information technology platform of the new bank by October 2006. We may experience disruptions, delays or other difficulties from our information technology systems, which may have an adverse effect on our business and adversely impact our customers' confidence in us.

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***We are subject to operational risks which our current risk management system may not detect in time or at all.***

Operational risk is risk that is difficult to quantify and subject to different definitions. In addition to internal audits and inspections, the Financial Supervisory Service conducts general annual audits of operations at Shinhan Financial Group and also performs general annual audits of our operations. The Financial Supervisory Service also performs special audits as the need arises on particular aspects of our operations such as risk management, credit monitoring and liquidity. In the ordinary course of these audits, the Financial Supervisory Service routinely issue warning notices where it determines that a regulated financial institution or such institution's employees have failed to comply with the applicable laws or rules, regulations and guidelines of the Financial Supervisory Service. We have in the past received, and expect in the future to receive, such notices and we have taken and will continue to take appropriate actions in response to such notices.

In April 2005, the Financial Supervisory Service found that Chohung Bank's employees had embezzled approximately W40 billion of Chohung Bank's funds over a period of five months. Chohung Bank recovered approximately W4 billion of the embezzled fund. As a remedial measure, the Financial Supervisory Service issued a warning to Chohung Bank as well as its president and the statutory auditor for supervisory negligence and ordered Chohung Bank to sign a memorandum of understanding to improve its internal controls and took several remedial measures, including increasing staffing at our back office, strengthening periodic monitoring and improving internal control procedures related to fund transfer documentation.

In addition, during a periodic audit in November 2005, the Financial Supervisory Service discovered that one of Chohung Bank's employees, in collaboration with an employee of Kookmin Bank, issued counterfeit certificates of deposits in the course of embezzling over a period of seven months an aggregate of approximately W445 billion of customer funds deposited at the two banks, of which amount W20 billion was deposited with Chohung Bank. The Financial Supervisory Service suspended for three months the operation of the branches of the two banks directly involved with the incident and issued warnings against the presidents and statutory auditors of Chohung Bank and Kookmin Bank (including a disciplinary warning against the president of Chohung Bank) for negligent supervision. In response to this incident, Chohung Bank took several remedial measures to strengthen compliance procedures and improve the execution of the existing internal control systems.

No assurance can be given, however, that these remedial measures would be sufficient to prevent similar or more adverse operational risks from materializing.

**Risks Relating to Government Regulation and Policy**

***We operate in a legal and regulatory environment that is subject to change, which may have an adverse effect on our business, financial condition and results of operations.***

The legal and regulatory framework for the Korean banking industry has continued to undergo significant reforms recently. Historically, regulations of the Korean government included, among other things, establishing lending rates and deposit rates for banks. Regulations also dictated the extent of competition through restrictions on new entrants and on the growth of existing banks, including the opening of new branches. Regulatory reform of the Korean banking industry to date has removed controls on all lending rates and all deposit rates and provided for increased prudent supervision of the financial sector by the Korean government. We believe that the Korean government intends to continue to deregulate the financial sector, by allowing market forces to have a larger role in guiding the development of the industry. However, with respect to setting liquidity and capital adequacy standards, the Government has revised its regulations to implement stricter standards for commercial banks and credit card companies. We expect the regulatory environment in which we operate to continue to change. There can be no assurance that any future changes will not have an adverse effect on our business, financial condition or results of operations.

In addition, currently different types of financing business are regulated by individual acts that relate to the type of financing business, such as the Bank Act, the Insurance Business Act, the Securities Exchange Act, the Act on Business of Operating Indirect Investment and Asset and Futures Trading Act. However, the

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Korean government is preparing for a combined financial act, which will comprehensively regulate securities and futures, operation of indirect investment asset, trust and any other financing businesses other than banking and insurance businesses in order to allow investment bank type of financial organization to be established to comprehensively manage such businesses other than banking and insurance. If such regulation is enacted, competition may be fierce among existing banks, insurance companies, securities companies and other financial organizations, and may lead to significant changes in the current Korean financial market which can have an adverse effect on our business, financial conditions or results of operations.

***Structural reforms in the Korean economy and its financial sector may have a substantial impact on our business.***

In response to the financial and economic downturn in Korea in 1997 and 1998, the Korean government announced and implemented a series of comprehensive policy packages to address structural weaknesses in the Korean economy and its financial sector. One of these policy packages involved mergers and restructurings of a number of banks. We expect that these comprehensive policy packages will continue to have a substantial impact on our business. The government has indicated that it may advocate further mergers or restructurings involving other commercial banks and financial institutions in the Korean financial sector. Such mergers or restructurings may create larger banks and financial institutions that may pose a competitive threat and in turn have an adverse impact on our business, financial condition and results of operations.

***The Financial Supervisory Commission may impose supervisory measures if it deems us or our operating subsidiaries to be financially unsound.***

If the Financial Supervisory Commission deems our financial condition, including the financial conditions of our operating subsidiaries, to be unsound or if our operating subsidiaries or we fail to meet the applicable requisite capital ratio or the capital adequacy ratio, as the case may be, set forth under Korean law, the Financial Supervisory Commission may order, among others, at the level of the holding company or that of its subsidiary, capital increases or reductions, stock cancellations or consolidations, transfers of business, sales of assets, closures of branch offices, mergers with other financial institutions, or suspensions of a part or all of our business operations. If any of such measures is imposed on us or on our operating subsidiaries by the Financial Supervisory Commission as a result of poor financial condition or failure to comply with minimum capital adequacy requirements or for other reasons, such measures may have a material adverse effect on our business and the price of our common shares and/or American depositary shares.

***The Korean government may encourage lending to and investment in certain types of borrowers in furtherance of government initiatives, and we may take this factor into account.***

The Korean government has encouraged and may in the future encourage lending to or investment in the securities of certain types of borrowers and other financial institutions in furtherance of government initiatives. The Korean government, through its regulatory bodies such as the Financial Supervisory Commission, has in the past announced lending policies to encourage Korean banks and financial institutions to lend to or invest in particular industries or customer segments, and, in certain cases, has provided lower cost funding through loans made by the Bank of Korea for further lending to specific customer segments, such as the small- and medium-sized enterprises. The Korean government has in this manner encouraged commercial banks to step in to provide credit card companies with additional liquidity. While all loans or securities investments will be reviewed in accordance with our credit review policies or internal investment guidelines and regulations, we, on a voluntary basis, may factor the existence of such policies and encouragements into consideration in making loans or securities investments. However, the ultimate decision whether to make loans or securities investments remains with us and is made based on our credit approval procedures and our risk management system, independently of government policies.

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**Risks Relating to Korea and the Global Economy**

***Unfavorable financial and economic conditions in Korea and worldwide may have a material adverse impact on our asset quality, liquidity and financial performance.***

We are incorporated in Korea, and substantially all of our operations are located in Korea. As a result, we are subject to political, economic, legal and regulatory risks specific to Korea. Financial turmoil in Asia in the late 1990s adversely affected the Korean economy and in turn Korean financial institutions. In addition, investors' reactions to developments in one country can have adverse effects on the securities of companies in other countries, including Korea. In addition, the economic indicators in 2003, 2004 and 2005 have shown mixed signs of recovery and uncertainty, and future recovery or growth of the economy is subject to many factors beyond our control.

Developments that could hurt Korea's economy in the future include, among other things:

failure of restructuring of *chaebols* and accounting irregularities of and regulatory proceedings against *chaebols*, together with its negative effect on the Korean financial markets and on the small- and medium-sized enterprises market;

failure of restructuring of large troubled companies, including LG Card and other troubled credit card companies and financial institutions;

volatility in foreign currency reserve levels, commodity prices (including oil prices), exchange rates (including continued weakness of the U.S. dollar and/or the appreciation of the Korean Won against foreign currencies), interest rates and stock markets;

increased reliance on exports to service foreign currency debts, which could cause friction with Korea's trading partners;

adverse developments in the economies of countries to which Korea exports goods and services (such as the United States, China and Japan), or in emerging market economies in Asia or elsewhere that could result in a loss of confidence in the Korean economy;

the continued emergence of China, to the extent its benefits (such as increased exports to China) are outweighed by its costs (such as competition in export markets or for foreign investment and relocation of the manufacturing base from Korea to China);

social and labor unrest or declining consumer confidence or spending resulting from lay-offs, increasing unemployment and lower levels of income;

uncertainty and volatility in real estate prices arising, in part, from the Korean government's policy-driven tax and other regulatory measures;

a decrease in tax revenues and a substantial increase in the Korean government's expenditures for unemployment compensation and other social programs that together could lead to an increased government budget deficit;

political uncertainty or increasing strife among or within political parties in Korea, including as a result of the increasing polarization of the positions of the ruling progressive party and the conservative opposition; and

a deterioration in economic or diplomatic relations between Korea and its trading partners or allies, including such deterioration resulting from trade disputes or disagreements in foreign policy.

Deterioration in the Korean economy can also occur as a result of deterioration in the global economic conditions. Recent developments in the Middle East, including the war in Iraq and its aftermath, higher oil prices and the

continued weakness of the economy in parts of the world have increased the uncertainty of world economic prospects in general and continue to have an adverse effect on the Korean economy. Any future deterioration of the Korean economy could have an adverse effect on us and the market price of our common shares or our American depositary shares.

**Table of Contents*****Tensions with North Korea could have an adverse effect on us and the price of our common stock and our American depositary shares.***

Relations between Korea and North Korea have been tense over most of Korea's history. The level of tension between the two Koreas has fluctuated and may increase or change abruptly as a result of current and future events, including ongoing contacts at the highest levels of the governments of Korea and North Korea and increasing hostility between North Korea and the United States. In December 2002, North Korea removed the seals and surveillance equipment from its Yongbyon nuclear power plant and evicted inspectors from the United Nations International Atomic Energy Agency, and has reportedly resumed activity at its Yongbyon power plant. In January 2003, North Korea announced its intention to withdraw from the Nuclear Non-Proliferation Treaty, demanding that the United States sign a non-aggression pact as a condition to North Korea dismantling its nuclear program. In August 2003, representatives of Korea, the United States, North Korea, China, Japan and Russia held multilateral talks in an effort to resolve issues relating to North Korea's nuclear weapons program. While the talks concluded without resolution, participants in the August meeting indicated that further negotiations may take place in the future and, in February 2004, six party talks resumed in China. In June 2004, the third round of the six-party talks resumed in China, which ended with an agreement by the parties to hold further talks by the end of September 2004, which failed to take place as planned. In February 2005, North Korea declared that it had developed and was in possession of nuclear weapons. It also announced its indefinite withdrawal from further six-party talks. However, in July 2005, fourth round of six-party talks resumed and concluded in September 2005 at which time a joint statement was released that reaffirmed the parties' commitment to peace and stability in the Korean peninsula. Soon thereafter, a fifth round of six-party talks concluded in November 2005. However, prior to the next six-party talks, the U.S. accused North Korea of money laundering activities through Banco Delta Asia in Macau and producing and distributing counterfeit U.S. dollars. The U.S. pressured Banco Delta Asia to abandon its ties with North Korea. In May 2006, it was reported that the Korea Energy Development Organization ( KEDO ) project designed to replace North Korea's existing nuclear power facilities with a light water reactor would be terminated. These events led to another stalemate in the negotiations with North Korea, which is still continuing. Any further increase in tensions, resulting for example from a break-down in contacts or an outbreak in military hostilities, could hurt our business, results of operations and financial condition and could lead to a decline in the price of our common stock and our American depositary shares.

***Korea's new legislation allowing class action suits related to securities transactions may expose us to additional litigation risk.***

Effective January 1, 2005, a new law enacted on January 20, 2004 allows class action suits to be brought by shareholders of companies listed on the Korea Exchange, including ours, for losses incurred in connection with the purchase and sale of securities and other securities transactions arising from (i) false or inaccurate statements provided in registration statements, prospectuses, business reports and audit reports; (ii) insider trading and (iii) market manipulation. In March 2005, this law was amended to provide for a grace period for class action suits based on (i) of the above in order to afford the companies an opportunity to correct any prior false or inaccurate statements until the release of their audited financial statements for the fiscal year ended December 31, 2006. During this grace period, companies will be immune from any class action suits arising from (i) of the above. The new law permits 50 or more shareholders who collectively hold 0.01% or more of the shares of a company at the time when the cause of such damages occurred to bring a class action suit against, among others, the issuer and its directors and officers. It is uncertain how the courts will apply this law, however, as this law has been enacted only recently. Litigation can be time-consuming and expensive to resolve, and can divert valuable management time and attention from the operation of a business. We are not aware of any basis for such suit being brought against us, nor, to our knowledge, are there any such suits pending or threatened. Any such litigation brought against us could have a material adverse effect on our business, financial condition and results of operations.

**Table of Contents*****Labor unrest may adversely affect the Korean economy and our operations.***

During 1998 and 1999, there were large-scale protests and labor strikes in Korea. In July 2000, the Korean Financial Industry Union, which represents the employees of over 30 financial institutions, urged its members to participate in a strike to express their opposition to mergers of the banks and the possibility of further layoffs, when the Korean government announced its plan to implement the second phase of restructuring the Republic's banks, including the promulgation of a law which allows the formation of financial holding companies. The strike subsequently was cancelled after the Korean government and the union leaders reached an agreement under which the Korean government would not require mandatory bank mergers. Any future labor unrest could adversely affect our operations, as well as the operations of many of our customers and their ability to repay their loans, and could affect the financial conditions of Korean companies in general, depressing the prices of securities on the Korea Exchange, the value of unlisted securities and the value of the Won relative to other currencies. Such developments would likely have an adverse effect on our financial condition, results of operations and capital adequacy.

Our acquisition of Chohung Bank faced opposition from the labor union of Chohung Bank, which engaged in a strike in mid-June 2003, which interrupted Chohung Bank's operations for five days and caused temporary liquidity problems, until the union entered into an understanding with our management to cooperate. Following execution of the acquisition agreements, the labor union of Chohung Bank opposed the selection of Chohung Bank's new CEO, who was a former executive of Chohung Bank, and attempted to prevent the recommendation committee for the CEO of Chohung Bank from meeting to approve the appointment. Subsequently, the labor union withdrew their objection. Following the merger of Shinhan Bank and Chohung Bank on April 3, 2006, the labor union of the former Chohung Bank continues to exist in addition to the labor union of Shinhan Bank. Currently, there is no deadline for integrating the two unions. Disagreements between the labor union of the former Chohung Bank on the one hand and the labor union of Shinhan Bank or our management on the other regarding the process and direction of the integration following the merger of Shinhan Bank and Chohung Bank or the integration of the two unions and actions taken to delay or disrupt the process could have a material adverse effect on our ability to realize the anticipated benefits of the merger of Shinhan Bank and Chohung Bank and have an adverse effect on our combined results of operations and the price of our common shares or American depositary shares.

**Risks Relating to Our American Depositary Shares*****There are restrictions on withdrawal and deposit of common shares under the depositary facility.***

Under the deposit agreement, holders of shares of our common stock may deposit those shares with the depositary bank's custodian in Korea and obtain American depositary shares, and holders of American depositary shares may surrender American depositary shares to the depositary bank and receive shares of our common stock. However, under current Korean laws and regulations, the depositary bank is required to obtain our prior consent for the number of shares to be deposited in any given proposed deposit which exceeds the difference between (1) the aggregate number of shares deposited by us for the issuance of American depositary shares (including deposits in connection with the initial and all subsequent offerings of American depositary shares and stock dividends or other distributions related to these American depositary shares) and (2) the number of shares on deposit with the depositary bank at the time of such proposed deposit. We have consented to the deposit of outstanding shares of common stock as long as the number of American depositary shares outstanding at any time does not exceed 20,216,314. As a result, if you surrender American depositary shares and withdraw shares of common stock, you may not be able to deposit the shares again to obtain American depositary shares.

***The value of your investment may be reduced by future sales of our common stock or our American depositary shares by the Korea Deposit Insurance Corporation or BNP Paribas, by other stockholders or holders of American depositary shares or by us.***

Korea Deposit Insurance Corporation owns 22,360,301 shares of our Redeemable Convertible Preferred Stock representing 6.22% of the total issued shares (or 5.86% of the total issued shares on a fully diluted basis)

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of our common stock. Korea Deposit Insurance Corporation is entitled to convert such shares into our common stock beginning in August 2006. Following the conversion of the Redeemable Convertible Preferred Shares owned by Korea Deposit Insurance Corporation in April 2006, 90.0% of which was purchased by BNP Paribas and the remaining 10.0% was sold in the market, BNP Paribas currently owns approximately 9.38% of our total issued shares (or 8.83% of our total issued shares on a fully diluted basis after taking into account 22,360,301 shares of the Redeemable Convertible Preferred Shares currently owned by Korea Deposit Insurance Corporation). Currently, we do not know when, how, or what percentage of, our Redeemable Convertible Preferred Shares will be converted by Korea Deposit Insurance Corporation and when, how or what percentage of our shares Korea Deposit Insurance Corporation will dispose of upon conversion or BNP Paribas will dispose of our shares, or to whom such shares will be sold. As a result, we cannot currently predict the impact of such sales on us.

***In certain cases, we must obtain the consent of the Korea Deposit Insurance Corporation to declare and pay dividends on our shares or our American depositary shares. If Korea Deposit Insurance Corporation declines to give such consent, holders of American depositary shares may be adversely affected.***

Pursuant to the terms of the Investment Agreement, we are required to obtain the consent of the Korea Deposit Insurance Corporation, to the extent permitted under applicable law, in order to declare and pay dividends on our common shares in excess of W750, representing 15% of par value (W5,000), if our net income under Korean GAAP is below W800 billion in a given fiscal year and any of the Redeemable Preferred Stock and Redeemable Convertible Preferred Stock are outstanding. Failure to obtain the consent of the Korea Deposit Insurance Corporation in such instances may lead to payment of dividends at a level that is lower than expected and may adversely affect the price of our common shares and our American depositary shares and further adversely affect the interest of our shareholders, including the holders of our American depositary shares.

***Ownership of our shares is restricted under Korean law.***

Under the Financial Holding Companies Act, any single shareholder (together with certain persons in a special relationship with such shareholder) may acquire beneficial ownership of up to 10% of the total issued and outstanding shares with voting rights of a bank holding company controlling national banks such as us. In addition, any person, except for a non-financial business group company (as defined below), may acquire in excess of 10% of the total voting shares issued and outstanding of a financial holding company which controls a national bank, provided that a prior approval from the Financial Supervisory Commission is obtained each time such person's aggregate holdings exceed 10% (or 15% in the case of a financial holding company controlling regional banks only), 25% or 33% of the total voting shares issued and outstanding of such financial holding company. The Korean government and the Korea Deposit Insurance Corporation are exempt from this limit. Furthermore, certain non-financial business group companies (i.e., (i) any same shareholder group with aggregate net assets of all non-financial business companies belonging to such group of not less than 25% of the aggregate net assets of all members of such group; (ii) any same shareholder group with aggregate assets of all non-financial business companies belonging to such group of not less than W2 trillion; or (iii) any mutual fund in which a same shareholder group identified in (i) or (ii) above owns more than 4% of the total shares issued and outstanding of such mutual fund) may not acquire beneficial ownership in us in excess of 4% of our outstanding voting shares, provided that such non-financial business group companies may acquire beneficial ownership of up to 10% of our outstanding voting shares with the approval of the Financial Supervisory Commission under the condition that such non-financial business group companies will not exercise voting rights in respect of such shares in excess of the 4% limit. See Item 4. Information on the Company Supervision and Regulation Principal Regulations Applicable to Financial Holding Companies Restriction on Financial Holding Company Ownership. To the extent that the total number of shares of our common stock that you and your affiliates own together exceeds these limits, you will not be entitled to exercise the voting rights for the excess shares, and the Financial Supervisory Commission may order you to dispose of the excess shares within a period of up to six months. Failure to comply with such an order would result in a fine of up to W50 million.

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***Holders of American depositary shares will not have preemptive rights in certain circumstances.***

The Korean Commercial Code and our articles of incorporation require us, with some exceptions, to offer shareholders the right to subscribe for new shares in proportion to their existing ownership percentage whenever new shares are issued. If we offer any rights to subscribe for additional shares of our common stock or any rights of any other nature, the depositary bank, after consultation with us, may make the rights available to you or use reasonable efforts to dispose of the rights on your behalf and make the net proceeds available to you. The depositary bank, however, is not required to make available to you any rights to purchase any additional shares unless it deems that doing so is lawful and feasible and:

a registration statement filed by us under the US Securities Act of 1933, as amended, is in effect with respect to those shares; or

the offering and sale of those shares is exempt from or is not subject to the registration requirements of the US Securities Act.

We are under no obligation to file any registration statement with the U.S. Securities and Exchange Commission. If a registration statement is required for you to exercise preemptive rights but is not filed by us, you will not be able to exercise your preemptive rights for additional shares and you will suffer dilution of your equity interest in us.

***Your dividend payments and the amount you may realize upon a sale of your American depositary shares will be affected by fluctuations in the exchange rate between the Dollar and the Won.***

Investors who purchase the American depositary shares will be required to pay for them in U.S. dollars. Our outstanding shares are listed on the Korea Exchange and are quoted and traded in Won. Cash dividends, if any, in respect of the shares represented by the American depositary shares will be paid to the depositary bank in Won and then converted by the depositary bank into Dollars, subject to certain conditions. Accordingly, fluctuations in the exchange rate between the Won and the Dollar will affect, among other things, the amounts a registered holder or beneficial owner of the American depositary shares will receive from the depositary bank in respect of dividends, the Dollar value of the proceeds which a holder or owner would receive upon sale in Korea of the shares obtained upon surrender of American depositary shares and the secondary market price of the American depositary shares.

***If the government deems that certain emergency circumstances are likely to occur, it may restrict the depositary bank from converting and remitting dividends in Dollars.***

If the government deems that certain emergency circumstances are likely to occur, it may impose restrictions such as requiring foreign investors to obtain prior government approval for the acquisition of Korean securities or for the repatriation of interest or dividends arising from Korean securities or sales proceeds from disposition of such securities. These emergency circumstances include any or all of the following:

sudden fluctuations in interest rates or exchange rates;

extreme difficulty in stabilizing the balance of payments; and

a substantial disturbance in the Korean financial and capital markets.

The depositary bank may not be able to secure such prior approval from the government for the payment of dividends to foreign investors when the government deems that there are emergency circumstances in the Korean financial markets.

***Holders of American depositary shares may be required to pay a Korean securities transaction tax upon withdrawal of underlying common shares or the transfer of American depositary shares.***

Under Korean tax law, a securities transaction tax (including an agricultural and fisheries special surtax) is imposed on transfers of shares listed on the Korea Exchange, including our common shares, at the rate of

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0.3% of the sales price if traded on the Korea Exchange. According to a tax ruling recently issued by Korean tax authorities, securities transaction tax of 0.5% of the sales price could be imposed on the transfer of American depositary shares unless American depositary shares are listed or registered on the New York Stock Exchange, NASDAQ National Market or other foreign exchanges that may be designated by the Ministry of Finance and Economy, and transfer of American Depositary shares takes place on such exchange. At this time, it is unclear as to when the Korean government will begin to enforce the imposition of such securities transaction tax. See Item 10. Additional Information Taxation Korean Taxation .

**Other Risks*****We do not prepare interim financial information on a U.S. GAAP basis.***

We, including our subsidiaries such as Shinhan Bank and Chohung Bank, are not required to and do not prepare interim financial information on a U.S. GAAP basis. U.S. GAAP differs in significant respects from Korean GAAP, particularly with respect to the establishment of provisions and loan loss allowance and determination of the scope of consolidation. See Item 5. Operating and Financial Review and Prospects Selected Financial Information under Korean GAAP and Reconciliation with Korean Generally Accepted Accounting Principles . As a result, provision and allowance levels reflected under Korean GAAP in our results for the three months ended March 31, 2005 and 2006 may differ significantly from comparable figures under U.S. GAAP for these and future periods.

***We are generally subject to Korean corporate governance and disclosure standards, which differ in significant respects from those in other countries.***

Companies in Korea, including us, are subject to corporate governance standards applicable to Korean public companies which differ in many respects from standards applicable in other countries, including the United States. As a reporting company registered with the Securities and Exchange Commission and listed on the New York Stock Exchange, we are, and in the future will be, subject to certain corporate governance standards as mandated by the Sarbanes-Oxley Act of 2002. However, foreign private issuers, including us, are exempt from certain corporate governance requirements under the Sarbanes-Oxley Act or under the rules of the New York Stock Exchange. For significant differences, see Item 6. Directors, Senior Management and Employees Corporate Governance . There may also be less publicly available information about Korean companies, such as us, than is regularly made available by public or non-public companies in other countries. Such differences in corporate governance standards and less public information could result in less than satisfactory corporate governance practices or disclosure to investors in certain countries.

***You may not be able to enforce a judgment of a foreign court against us.***

We are corporations with limited liability organized under the laws of Korea. Substantially all of our directors and officers and other persons named in this document reside in Korea, and all or a significant portion of the assets of our directors and officers and other persons named in this document and substantially all of our assets are located in Korea. As a result, it may not be possible for holders of the American depositary shares to effect service of process within the United States, or to enforce against them or us in the United States judgments obtained in United States courts based on the civil liability provisions of the federal securities laws of the United States. There is doubt as to the enforceability in Korea, either in original actions or in actions for enforcement of judgments of United States courts, of civil liabilities predicated on the United States federal securities laws.

**Table of Contents****ITEM 4. INFORMATION ON THE COMPANY****HISTORY AND DEVELOPMENT OF SHINHAN FINANCIAL GROUP****Introduction**

We are the largest financial holding company in Korea on the basis of total assets, total deposits and stockholders equity. We were formed in 2001 as the holding company for Shinhan Bank and related financial services companies. On August 19, 2003, we acquired 80.04% of Chohung Bank and plan to merge its operations with those of Shinhan Bank after a three-year transition period. In June 2004, we acquired the remaining 18.85% of the outstanding shares of Chohung Bank that we previously did not own through a cash tender offer followed by a small-scale share swap pursuant to Korean law. As of December 31, 2005, based on asset size published by the Financial Supervisory Commission, Shinhan Bank was the fourth largest bank in Korea, with total assets of W75,642 billion (US\$74,893 million) and Chohung Bank was the sixth largest bank in Korea, with total assets of W66,610 billion (US\$65,950 million). Following the merger of Shinhan Bank and Chohung Bank, the newly merged Shinhan Bank currently is the second largest bank in Korea in terms of total assets. From this expanded platform, we serve all major components of the corporate and retail banking and financial services markets. In the corporate sector, we serve the large corporate community, established and developing small- and medium- sized enterprises as well as certain small unincorporated businesses. In the retail sector, we provide mortgages and home equity finance as well as general unsecured consumer lending to retail customers ranging from high net worth customers to the mass retail market. As of December 31, 2005, prior to the split-merger of the credit card operations of Chohung Bank into Shinhan Card, Shinhan Card and Chohung Bank had credit card operations with approximately 3,467,000 and approximately 2,494,000 cardholders, respectively. Through our banking and non-banking subsidiaries, we engage in a comprehensive range of related financial services including securities brokerage, investment banking, investment trust management and insurance. We have also entered into joint ventures with BNP Paribas, our shareholder, in the areas of investment trust management and bancassurance to bring an international perspective to these operations.

Following the merger of Shinhan Bank and Chohung Bank, we currently operate the second largest nationwide branch network in Korea with 451 branches in the Seoul and its metropolitan area, 351 branches in Kyunggi Province and six major cities in Korea and 160 branches throughout the rest of the country. As of December 31, 2005, Shinhan Bank and Chohung Bank combined (not taking into account overlap in customers) had over 266,000 corporate deposit customers and over 15.5 million retail deposit customers with an aggregate average deposit of W86,421 billion. This combined customer base provides us with a large, stable and cost effective core funding base, and access to an established corporate and retail customer base to whom we can market the full range of our financial products and services.

**History and Organization**

On September 1, 2001, we were formed as a financial holding company under the Financial Holding Companies Act, by acquiring all of the issued shares of the following companies from the former shareholders in exchange for shares of our common stock:

Shinhan Bank, a nationwide commercial bank;

Shinhan Securities Co., Ltd., a securities brokerage company;

Shinhan Capital Co., Ltd., a leasing company; and

Shinhan Investment Trust Management Co., Ltd., an investment trust management company.

Shinhan Bank and Shinhan Securities were previously listed on the Korea Stock Exchange and Shinhan Capital was previously registered with Korea Securities Dealers Association Automated Quotation, or KOSDAQ, whereas Shinhan Investment Trust Management was privately held. On September 10, 2001, we listed the common stock of our holding company on the Korea Stock Exchange See Item 9 The offer and Listing Market Price Information and Trading Market Korea Securities Market .



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In December 2001, we concluded an agreement with our strategic partner and our largest shareholder, the BNP Paribas Group, pursuant to which BNP Paribas purchased a 4.00% equity interest in us. In September 2003, BNP Paribas increased its equity interest in us to 4.61%. As a result of the issuance of additional shares of our common stock in connection with transactions involving our acquisition of minority shares in our subsidiaries and the additional over-the-counter acquisition by BNP Paribas of 20,124,272 shares of our common stock from Korea Deposit Insurance Corporation in April 2006, BNP Paribas is currently our largest shareholder with ownership of 9.38% of our total issued common shares (or 8.83% of our total issued shares on a fully-diluted basis after taking into account 22,360,301 shares of the Redeemable Convertible Preferred Stock currently owned by Korea Deposit Insurance Corporation).

In April 2002 and July 2002, we acquired an aggregate of 62.4% equity stake in Jeju Bank, a regional bank incorporated in 1969 to engage in commercial banking and trust businesses.

During 2002, through a series of transactions, we acquired 31.7% of common stock (or 30.7% of voting equity securities) of Good Morning Securities. Subsequently, we merged Shinhan Securities into Good Morning Securities and renamed it Good Morning Shinhan Securities Co., Ltd. As of December 31, 2002, following the foregoing transactions, we effectively owned 60.5% of Good Morning Shinhan Securities. In December 2004, Good Morning Shinhan Securities became our wholly-owned subsidiary after we acquired the remaining shares of Good Morning Shinhan Securities. In January 2005, Good Morning Shinhan Securities was delisted from the Korea Exchange.

On June 4, 2002, the credit card division of Shinhan Bank was spun off and established as our wholly-owned subsidiary, Shinhan Card Co., Ltd. Effective as of April 3, 2006, the credit card division of Chohung Bank was split off and merged into Shinhan Card.

Shinhan Credit Information Co., Ltd. was established on July 8, 2002 as our wholly-owned subsidiary, which engages in the business of debt collection and credit reporting.

On August 9, 2002, we signed a joint venture agreement with BNP Paribas Asset Management, the asset management arm of BNP Paribas, in respect of Shinhan Investment Trust Management. On October 24, 2002, we sold to BNP Paribas Asset Management 3,999,999 shares of Shinhan Investment Trust Management, representing 50% less one share, which was subsequently renamed Shinhan BNP Paribas Investment Trust Management Co., Ltd.

On October 1, 2002, SH&C Life Insurance Co., Ltd., a bancassurance joint venture, was established under a related joint venture agreement with Cardif S.A., the bancassurance subsidiary of BNP Paribas.

On August 19, 2003, we acquired 80.04% of common shares of Chohung Bank, a nationwide commercial bank in Korea. See The Merger of Shinhan Bank and Chohung Bank. In December 2003, we acquired an additional 1.11% of common shares of Chohung Bank. In June 2004, we acquired the common shares of Chohung Bank that we previously did not own, which were 135,548,285 shares, or 18.85% of total common shares of Chohung Bank outstanding as of December 31, 2003, through a cash tender offer followed by a small-scale share swap under Korean law. As a result, we own 100% of Chohung Bank as of the date hereof. The common shares of Chohung Bank were delisted from the Stock Market Division of the Korea Exchange on July 2, 2004. The merger of Shinhan Bank and Chohung Bank occurred effective as of April 3, 2006, with Chohung Bank becoming the legal surviving entity. The newly merged bank then changed its name to Shinhan Bank.

In December 2005, in a series of related transactions, we acquired 100% of Shinhan Life Insurance, an insurance company, through a small scale share exchange mechanism provided under applicable Korean law, pursuant to which we issued 17,528,000 new shares of our common stock to the shareholders of Shinhan Life Insurance in exchange for all outstanding common stock of Shinhan Life Insurance held by them for an aggregate purchase price of W612 billion, or W15,300 per share. As part of this share exchange, Shinhan Bank exchanged 5,524,772 shares of common stock of Shinhan Life Insurance previously held by it into 2,420,955 shares of our common stock and Good Morning Shinhan Securities exchanged 464,800 shares of common stock of Shinhan Life Insurance previously held by it into 203,675 shares of our common stock. Similarly, as part of this transaction, Shinhan Life Insurance also exchanged 9,000 shares of its common

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stock, which Shinhan Life Insurance acquired as a result of the exercise of appraisal rights by dissenting shareholders of Shinhan Life Insurance, into 3,943 shares of our common stock. All of such shares of our common stock received by Shinhan Life Insurance were sold in the market on December 29, 2005. As of December 31, 2005, we had 11,610,197 treasury shares of our common stock, which were held by Chohung Bank, Shinhan Bank and Good Morning Shinhan Securities. Of such treasury shares, 1,708,050 shares were granted to the employees of the newly merged Shinhan Bank in April 2006 and 916,580 shares were sold in the market in June 2006. As of the date hereof, 8,985,567 treasury shares of our common stock are held by Shinhan Bank which must be disposed of by June 2007 in accordance with the Financial Holding Company Act of Korea. Under the Financial Holding Company Act of Korea, the voting rights on our treasury shares are subject to certain restrictions and the treasury shares must be sold within six months of acquisition with certain exceptions.

We also own the following subsidiaries that were subsidiaries of Chohung Bank and whose names were changed as of April 3, 2006, the date of the merger of Shinhan Bank and Chohung Bank.

SH Asset Management, previously known as Chohung Investment Trust Management Co., Ltd., was established in 1988 and engages in investment management services. In 1997, the company changed its name from Chohung Investment Management Co., Ltd. to Chohung Investment Trust Management Co., Ltd. and, on April 3, 2006, to SH Asset Management Co., Ltd. As of December 31, 2005, its capital stock amounted to W45 billion of which Chohung Bank owned 79.77 %.

Shinhan Asia Limited, formerly known as Chohung Finance Ltd., is engaged in various merchant banking activities in Hong Kong. As of December 31, 2005, its capital stock amounted to US\$15 million, of which Shinhan Bank owns 99.99%.

Shinhan Bank America was formerly known as CHB America Bank, a wholly-owned subsidiary of Chohung Bank in the United States. On April 3, 2006, it became a wholly-owned subsidiary of Shinhan Bank in connection with the merger of Shinhan Bank and Chohung Bank. It offers full banking services to Korean residents in New York and in California. As of December 31, 2005, CHB America Bank's capital stock amounted to US\$14 million.

Shinhan Bank Europe GmbH, formerly known as Chohung Bank (Deutschland) GmbH was established in 1994 as a wholly-owned subsidiary of Chohung Bank in Germany. On April 3, 2006, it became a wholly-owned subsidiary of Shinhan Bank. As of December 31, 2005, its capital stock amounted to EUR 15,339 thousand.

Shinhan Vina Bank, formerly known as Chohung Vina Bank, was established in November 2000 as a joint venture between Chohung Bank and Vietcom Bank, and engages in banking activities in Vietnam. Its capital stock as of December 31, 2005 was US\$20 million, of which Shinhan Bank currently owns 50%.

In December 2004, we established Shinhan Private Equity Inc. as our wholly-owned subsidiary with initial paid-in-capital of W10 billion. In August 2005, Shinhan Private Equity established Shinhan NPS PEF 1st as its subsidiary. Shinhan Private Equity owns 5% and Shinhan Financial Group owns 36.7% of Shinhan NPS PEF 1st.

On November 24, 2005, we liquidated e-Shinhan, which provides Internet-based financial services, in order to improve efficiency by focusing our resources on our growing non-banking operations.

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As of the date hereof, we have eleven direct and nine indirect subsidiaries. The following diagram shows our organization structure as of the date hereof:

With the exception of Shinhan Finance Limited and Shinhan Asia Limited, which are incorporated in Hong Kong, Shinhan Bank America and Good Morning Shinhan Securities USA Inc., which are incorporated in the United States, Good Morning Shinhan Securities Europe Ltd., which is incorporated in London, United Kingdom, Shinhan Bank Europe GmbH which is incorporated in Germany, and Shinhan Vina Bank, which is incorporated in Vietnam, all of our other subsidiaries are incorporated in Korea.

Our legal name is Shinhan Financial Group Co., Ltd. and commercial name is Shinhan Financial Group. Our registered office and principal executive offices are located at 120, 2-Ga, Taepyung-Ro, Jung-gu, Seoul 100-102, Korea. Our telephone number is 82-2-6360-3000. Our agent in the United States, Shinhan Bank, New York branch, is located at 32<sup>nd</sup> Floor, 800 Third Avenue, New York, NY 10022, U.S.A. Our agent's telephone number is (212) 371-8000.

**Our Strategy**

Since our holding company establishment in 2001, we have actively realigned our market position in an ever-changing environment of the Korean banking and financial industry. In particular, with our acquisition of Chohung Bank in 2003, we have emerged as the second largest financial institution in terms of assets and distribution network in Korea. With the acquisition of Chohung Bank, we currently believe that we have completed our reconfiguration of our corporate structure in the area of commercial banking.

Our vision is to enhance shareholder value by securing a solid position as the leading provider of total financial solutions in Korea by achieving global standards in corporate governance, operational efficiencies and integration of process and services. To this end, we are focusing, in the medium-term, on the successful completion of the integration of our banking operations to create total financial solutions by providing a full range of financial products and services to meet the needs of both corporate and retail customers. To achieve this vision, we are implementing and will continue to implement the following strategies:

*Creating synergies within our holding company structure.* Since our reconfiguration into a holding company structure in 2001, we have focused on achieving synergy through cross-selling of products and services. Shinhan Bank, Good Morning Shinhan Securities and Shinhan Life Insurance are assuming the roles of primary distribution channel while the rest of our non-bank subsidiaries are focusing on developing competitive products and services. Examples of our principal products for cross-selling in the retail segment include bancassurance, credit cards, beneficiary certificates and Financial Network Accounts, which are integrated accounts for banking, brokerage and insurance services. In the corporate segment, Good Morning Shinhan Securities provide to corporate customers of Shinhan Bank financial services including underwriting of initial public offerings, asset securitization, M&A advisory and issuance of debt or equity securities.

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*Enhancing the core competency of our operating subsidiaries.* In order to provide the highest quality products and services from each of our banking and financial businesses, we intend to focus on enhancing the core competency of each of our operating subsidiaries by taking the following initiatives:

in commercial banking, we have sought to achieve economies of scale by acquiring Chohung Bank, enabling us to, among other things, capitalize on greater mass market penetration and large corporate portfolio as a complement to Shinhan Bank's greater emphasis on small-and medium-sized enterprises and high net worth individuals.

in securities brokerage services, we have sought to achieve economies of scale and enhance brand image through our acquisition of Good Morning Securities.

in credit cards, we have focused on and will continue to focus on improved credit initiation through higher credit scoring requirements, risk management through continued credit scoring reviews and improved collection results through coordinated call centers and increased collection staff, as well as enhanced marketing. Upon the merger of Shinhan Bank and Chohung Bank in April 2006, we split off the credit card services division of Chohung Bank and merged it into Shinhan Card. Following such split-merger, Shinhan Card is expected to have W4 trillion in assets, W25 trillion in total credit card use (excluding corporate cards) and 5.9 million customers. In terms of the amount of the total credit card use, Shinhan Card currently ranks fourth among credit card service providers (including banks) following the split-merger. In addition, as opportunity arises, we may pursue growth through acquisitions, including the acquisition of LG Card that we are currently targeting.

in insurance, we have sought to achieve economies of scale by acquiring Shinhan Life Insurance in December 2005 in addition to SH&C Life Insurance, which joined the group in 2002, enabling the development and distribution of more diversified insurance products and services to meet the growing needs of our customers.

in areas where we lack core competency as compared to the leading global financial institutions, we will continue to expand our relationships through affiliations and business cooperation with world class financial institutions such as BNP Paribas and Macquarie.

*Establishing and Consolidating the One Portal Network.* In order to provide total financial solutions to our customers on a real-time basis, we are continuing to develop our one portal network. The one portal network refers to the ability of a corporate or retail customer to have access to our total financial solutions through any single point of contact with our group. In furtherance of this strategy, we have been implementing and will continue to implement the following initiatives:

integrating our physical and online distribution channels to offer products and services developed by all of our operating subsidiaries and businesses, including as follows:

making banking, securities brokerage, insurance and other services available at each branch;

enabling online cross access between commercial banking and our online securities brokerage service; and

integrating the customer service call centers for our commercial banking, credit card and securities brokerages services.

focusing on retail and corporate customers with total financial solutions designed to meet their respective needs and utilizing specialized branches to provide convenient access and trained employees to offer and provide relevant products and services, including as follows:

in retail banking, utilizing private banking centers to provide high net worth customers convenient access to total financial solutions that link banking to brokerage services, asset management and insurance; as well as penetrating the mass market penetration by enhancing brand and customer loyalty through focus on cross selling of products and strengthened customer relationship management;

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in corporate banking, expanding and enhancing the capabilities of our large corporate and small-and medium-sized enterprises specialist branch network and leveraging our increased large corporate customer base to provide total financial solutions that combine banking and non-banking financial products, such as asset backed securities, structured finance, M&A advice; syndication and equity derivatives, acting more as a financial advisor for larger, well established small-and-medium-sized enterprises by providing underwriting, rights offerings and offering related investment banking services in addition to lending, deposit and foreign exchange products and services and focusing on investment in corporate debt securities and initial public offerings for smaller businesses;

developing and promoting integrated financial products customized to meet the needs and demands of our customer segments, such as Financial Network Accounts that combine banking services and securities brokerage services or that combine credit card services and securities brokerage services and Safe Loans that combine banking services and insurance services.

enhancing customer loyalty by offering an All Plus Points System that combines customers banking, securities and credit card activities in a single report from which certain customer benefits are awarded.

developing joint products and services and joint sales support and enhancing cross-selling by sharing customer information through integrated data-warehousing and customer relationship management systems.

*Achieving Cost Efficiency from our Holding Company Structure.* We intend to achieve cost efficiency and to achieve maximum benefit from our holding company structure by:

preventing overlapping investments in solution development, information technology related investments, new investments in distribution channels, hiring and training of employees; and

identifying and realizing synergies such as combined information technology systems, call centers and shared customer services, distribution channels and new products and services;

*Introducing a Performance-based Culture.* In order to promote a customer oriented group culture, we intend to measure and reward employee performance in relation to the level of customer satisfaction reflected in customer response to our products and services, including products and services offered as part of our cross-selling efforts, and the quality of the assets and revenues generated.

**Table of Contents****THE MERGER OF SHINHAN BANK AND CHOHUNG BANK****History of Our Acquisition of Chohung Bank**

Through the acquisition of Chohung Bank, our Board of Directors sought primarily to achieve greater scale and market share, and secure stronger distribution channels to fulfill the advantages of our holding company model. Prior to the acquisition, Shinhan Bank was the fifth largest bank in Korea in terms of assets as of December 31, 2002. The acquisition of Chohung Bank placed us second in terms of assets. With these substantially enhanced resources, we constitute a broad-based nationwide financial services platform that enjoys a leadership position in the retail, corporate and small- and medium-sized enterprise banking sectors, as well as enhances our position in related financial services segments, including credit card, securities brokerage and investment trust management services. The acquisition has also enhanced our ability to optimize funding costs with a larger core deposit base and greater leverage in product sourcing. Through the acquisition, our Board of Directors also sought over time to benefit from synergies associated with combining and integrating the resources of Shinhan Bank and Chohung Bank, including combined information technology platforms, branch specialization, banking product and service development and the expansion and development of related financial services such as bancassurance and investment banking.

On August 19, 2003, we acquired 543,570,144 shares of common stock of Chohung Bank from Korea Deposit Insurance Corporation, which shares represent 80.04% of the outstanding shares of Chohung Bank. Korea Deposit Insurance Corporation had acquired the Chohung Bank shares in connection with a capital injection in 1999 during the Korean financial crisis. Our acquisition of these shares of Chohung Bank was the culmination of a lengthy process pursuant to which we were selected as the preferred bidder in January 2003 following which we entered into negotiations with Korea Deposit Insurance Corporation over a six-month period with respect to the price and terms of the acquisition.

The definitive terms of the acquisition were reflected in the Stock Purchase Agreement and the Investment Agreement, each dated July 9, 2003. The purchase price for the Chohung Bank shares consisted of (i) a maximum cash amount of W1,718,800,548,296, of which W900,000,000,000 was paid at the closing, with the W652,284,172,800 being due two years after the closing, subject to reduction if certain loan portfolio quality conditions existing as of December 31, 2002 under Korean GAAP are not maintained, and W166,516,375,496 being due two years after the closing, subject to reductions relating to the accuracy of representations and warranties contained in the Stock Purchase Agreement, (ii) 46,583,961 shares of our Redeemable Preferred Stock and (iii) 44,720,603 shares of our Redeemable Convertible Preferred Stock convertible into 12.28% of our common shares as of December 31, 2004. For the terms of these preferred stocks, see Item 10. Additional Information Articles of Incorporation Description of Capital Stock Description of Redeemable Preferred Stock .

The loan portfolio quality adjustment to the cash portion of the acquisition price referred to above was based on the Korean GAAP performance of Chohung Bank's portfolios of certain large corporate loans, including corporate loans sold with recourse to the Korea Asset Management Corporation, and credit card loans. Any loan loss provisions, net charge-offs or other losses or costs associated with such adjustments and with adjustments associated with accuracy of representations and warranties referred to above were reflected in the ordinary course on our consolidated income statement prepared under Korean GAAP. Any cash payments made when the amounts payable to Korea Depository Insurance Corporation can be estimated with reasonable certainty will be reflected on our consolidated balance sheet as additional goodwill from the acquisition. As of December 31, 2005, we recorded liabilities of W20,461,370,553 on the consolidated balance sheet which increased goodwill by the same amount.

W166,516,375,496, which was due two years after the closing subject to adjustments associated with accuracy of representations and warranties referred to above, was paid in 2005 and an adjustment in the corresponding amount was made to the goodwill in 2004. As for W652,284,172,800 due two years after the closing subject to reduction if certain loan portfolio quality conditions existing as of December 31, 2002 under Korean GAAP were not maintained, W220,713,909,507 was determined to be the final amount payable. Of this amount, W200,252,538,954 was paid in 2005 and W20,461,370,553 was paid in 2006, and a corresponding

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amount was added to the goodwill in 2005. The earnout amount will be determined following the adjustment period for the fiscal year 2006.

The Stock Purchase Agreement also provided for the resignation of the board of directors and officers of Chohung Bank and the election of persons specified by us, all of which has taken place and a new management and board of directors of Chohung Bank were formed. Pursuant to the terms of the Investment Agreement, so long as Korea Deposit Insurance Corporation holds 4.0% or more of the outstanding shares of our common stock resulting from conversion of our Redeemable Convertible Preferred Stock, Korea Deposit Insurance Corporation has the right to nominate one outside director. In March 2006, Korea Deposit Insurance Corporation exercised this right and appointed Myoung Soo Choi as our outside director. In addition, we have the right to exercise all voting rights that Korea Deposit Insurance Corporation may have with respect to the enfranchised Redeemable Preferred Stock and our Redeemable Convertible Preferred Stock as well as our common shares issuable to Korea Deposit Insurance Corporation upon conversion of our Redeemable Convertible Preferred Stock provided that, so long as Korea Deposit Insurance Corporation owns more than 4.0% of our outstanding shares of common stock resulting from conversion of the shares of our Redeemable Convertible Preferred Stock, we are required to obtain the consent of Korea Deposit Insurance Corporation prior to voting on the following matters: (i) any matters which require a special resolution or unanimous resolution of the shareholders under the Korean Commercial Code; (ii) approval of any dividend payment on our common shares; and (iii) appointment or dismissal of any outside director nominated by Korea Deposit Insurance Corporation.

Pursuant to the terms of the Investment Agreement, we are required to obtain the consent of the Korea Deposit Insurance Corporation, to the extent permitted under applicable law, in order to declare dividends on our common shares in excess of W750, if our net income under Korean GAAP is below W800 billion in any given fiscal year while any share of our Redeemable Preferred Stock and Redeemable Convertible Preferred Stock is outstanding.

In December 2003, our ownership of Chohung Bank increased to 81.15% following our additional capital injection of W200 billion into Chohung Bank. In June 2004, we acquired the common shares of Chohung Bank that we previously did not own, which were 135,548,285 shares, or 18.85% of total common shares of Chohung Bank outstanding as of December 31, 2003, through a cash tender offer followed by a small-scale share swap under Korean law. We delisted the common shares of Chohung Bank from the Korea Exchange on July 2, 2004. In April 2006, we consummated the merger of Shinhan Bank and Chohung Bank as further described below in [The Merger of Shinhan Bank and Chohung Bank](#).

**The Merger of Shinhan Bank and Chohung Bank**

To provide integration leadership during the initial phases of the integration, in September 2003, a joint management committee was established consisting of the CEO and the responsible Senior Executive Vice President at our holding company level, the CEOs and the responsible Senior Executive Vice Presidents of both Shinhan Bank and Chohung Bank and other members of our senior management, including those of our other subsidiaries as appropriate from time to time. Under the supervision of this joint management committee, and upon outside consulting, including review of global best practice to improve fairness and objectivity in our decision-making process, the merger of Shinhan Bank and Chohung Bank was implemented through two group-wide initiatives called [One Bank](#) and [New Bank](#) projects.

The [One Bank](#) initiative focused on achieving near-term synergies and operational efficiencies in advance of the physical and systems integration, such as in the areas of sharing retail distribution channels, joint proposals and credit policies for large-scale loans and joint investor relations and public relations. The day-to-day implementation of the [One Bank](#) initiative was handled by a joint work group established with working level employees participating from the holding company, Shinhan Bank and Chohung Bank, further broken down into task force teams and smaller work groups depending on the various areas of integration.

The [New Bank](#) initiative focused more on longer-term integration and upgrading of the merged bank's services platform. The areas of focus include upgrading retail service models, establishing the one portal channel network, business process reengineering, developing an integrated credit risk management system and



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upgrading our information technology systems. The day-to-day implementation is being handled by six upgrade project teams.

After both banks had substantially completed the implementation of these integration initiatives, on December 30, 2005, the respective board of directors of the two banks approved the terms of the merger (the Merger) as set out in the Merger Agreement by and between Chohung Bank and Shinhan Bank dated December 30, 2005 (the Merger Agreement). The board of directors of Chohung Bank also approved the terms of the spin-off of its credit card business and the merger of this business into Shinhan Card (the Split-Merger). For purposes of the Split Merger, Chohung Bank and Shinhan Card entered into a Split-Merger Agreement on December 30, 2005 (the Split-Merger Agreement). The respective meetings of the shareholders of Shinhan Bank and Chohung Bank were held on February 15, 2006 to approve the Merger and, in the case of Chohung Bank, also the Split-Merger. The creditor protection procedures under the Act on the Structural Improvement of the Financial Industry commenced on February 17, 2006 and terminated on February 27, 2006. The Merger and the Split Merger were approved by the Financial Supervisory Commission of Korea.

Pursuant to the terms of the Merger Agreement, effective on April 3, 2006, Shinhan Bank was merged into Chohung Bank with Chohung Bank being the surviving legal entity. In connection with the Merger, each share of common stock of Shinhan Bank was exchanged for 3.867799182 shares of common stock of Chohung Bank. Immediately after the Merger, Chohung Bank changed its name to Shinhan Bank.

Pursuant to the terms of the Split-Merger Agreement, effective on April 3, 2006, Chohung Bank's credit card business was spun-off and merged into Shinhan Card. In connection with the Split-Merger, 41,207,856 shares of common stock of Shinhan Card were issued to us in exchange for 42,008,463 shares of common stock of Chohung Bank and Shinhan Card assumed assets amounting to W1,967 billion, together with certain liabilities amounting to W1,797 billion relating to the credit card business of Chohung Bank. As a result of the Split-Merger, 42,008,463 shares of common stock of Chohung Bank were retired, resulting in a reduction in its shareholders' equity of approximately W210 billion.

The integration and merger of Shinhan Bank and Chohung Bank is subject to risks, uncertainties and difficulties. The newly merged Shinhan Bank may fail to consummate the integration of the two banks as currently contemplated or may not be able to achieve the intended benefits of the merger and integration at a level desired by us. See Risk Factors - Risks Relating to our Acquisition and Integration of Chohung Bank.

**Relationship with the Labor Unions**

Our acquisition of Chohung Bank encountered opposition from both the labor union and the senior management of Chohung Bank during the stages of negotiation. Beginning in mid-June 2003, the labor union of Chohung Bank undertook actions, including a strike, opposing our acquisition of Chohung Bank. In connection with the finalization of the Stock Purchase Agreement, our management, together with the managements of Korea Deposit Insurance Corporation and Chohung Bank, reached a written understanding with the labor union of Chohung Bank. Labor related issues relating to Chohung Bank will be resolved through consultation. The understanding contemplated that a merger of Shinhan Bank and Chohung Bank may take place three years after the closing and that during the transition period (i) the chief executive officer of Chohung Bank will be drawn from a pool of candidates with backgrounds at Chohung Bank and will, as such, manage Chohung Bank within the holding company structure, (ii) Chohung Bank and Shinhan Bank will have equal representation on the integration committee to be established two years after the acquisition and equal representation as senior executive officers of Shinhan Financial Group, and (iii) forcible lay-offs will not take place, employee compensation will be harmonized and seniority will be discussed. Upon completion of the merger, employee redundancy policy will be retained and, where feasible, branch redundancies will be avoided. This understanding was broadly consistent with our strategy and timetable for combining the resources of the two banks and was designed to enhance the support and cooperation of Chohung Bank's employees in the process. Neither of the labor unions of the two banks objected to the Merger or the Split Merger and, to date, we have not experienced any significant difficulties in our relationships.

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with the respective labor unions of Shinhan Bank and Chohung Bank since our acquisition of Chohung Bank, including in connection with the Merger. We expect the newly merged Shinhan Bank to retain two labor unions for the foreseeable future.

**Liquidity and Capital Resources**

As consideration for our purchase of Chohung Bank shares, at closing, we (i) paid to Korea Deposit Insurance Corporation cash of W900 billion, (ii) issued to Korea Deposit Insurance Corporation 46,583,961 shares of our Redeemable Preferred Stock, with a redemption price of W842,517,518,646 and (iii) issued to Korea Deposit Insurance Corporation 44,720,603 shares of our Redeemable Convertible Preferred Stock convertible into our shares of common stock with a redemption price of W808,816,825,858. In August 2003, we raised W900 billion in cash through the issuance of 6,000,000 shares of Redeemable Preferred Stock, all of which were sold in the domestic fixed-income market through Strider Securitization Specialty Co., Ltd., a special purpose vehicle. These redeemable preferred shares have terms that are different from the preferred shares issued to Korea Deposit Insurance Corporation. We are required to redeem these preferred shares issued to the special purpose vehicle in three installments in 2006, 2008 and 2010.

Pursuant to the terms of our Redeemable Preferred Stock issued to Korea Deposit Insurance Corporation, we are required to redeem such shares in five equal annual installments commencing three years from the date of issuance and, pursuant to the terms of our Redeemable Convertible Preferred Stock, we are required to redeem the full amount of such shares outstanding five years from the date of issuance to the extent not converted into our common shares. Each share of the Redeemable Convertible Preferred Stock is convertible into one share of our common stock. The dividend ratios on our Redeemable Preferred Stock and Redeemable Convertible Preferred Stock are 4.04% and 2.02%, respectively. See Item 10. Additional Information Articles of Incorporation Description of Capital Stock Description of Redeemable Preferred Stock .

The following table sets forth the contractual scheduled maturities by type of preferred stock issued by us in connection with our acquisition of Chohung Bank.

	<b>Due August</b>					
	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>Total</b>
	<b>(In millions of Won)</b>					
Redeemable preferred stock issued to KDIC	W 168,503	W 168,503	W 168,504	W 168,504	W 168,504	W 842,518
Redeemable preferred stock issued in the market through a special purpose vehicle	525,000		365,000		10,000	900,000
Redeemable convertible preferred Stock(1)			404,408			404,408
<b>Total</b>	<b>W 693,503</b>	<b>W 168,503</b>	<b>W 937,912</b>	<b>W 168,504</b>	<b>W 178,504</b>	<b>W 2,146,926</b>

*Note:*

- (1) In November 2005, Korea Deposit Insurance Corporation ( KDIC ) converted 22,360,302 shares of Redeemable Convertible Preferred Stock into 22,360,302 shares of our common stock, representing 6.22% of the total issued shares (or 5.86% of the total issued shares on a fully diluted basis) of our common stock. The figures herein assumes no further conversion of the Redeemable Convertible Preferred Stock into our common stock.

Pursuant to laws and regulations in Korea, we may redeem our preferred stock to the extent of our retained earnings of the previous fiscal year, net of certain reserves as determined under Korean GAAP. At this time, we expect that cash from our future operations should be adequate to provide us with sufficient capital resources to enable us to redeem our preferred stock pursuant to the scheduled maturities as described in the table above. In the event there is a short-term shortage of liquidity to make the required cash payments for redemption as a result of, among other things, failure to receive dividend payments from our operating

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subsidiaries on time or as a result of significant expenditures resulting from future acquisitions, we plan to raise cash liquidity through the issuance of long-term debt in the Korean fixed-income market in advance of the scheduled maturity on our preferred stock. To the extent we need to obtain additional liquidity, we plan to do so through the issuance of long-term debt and the use of our other secondary funding sources. See Item 5. Operating and Financial Review and Prospects – Liquidity and Capital Resources .

As consideration for our acquisition of Chohung Bank, in August 2003, we issued to the Korea Deposit Insurance Corporation (i) 46,583,961 shares of our Redeemable Preferred Stock, with an aggregate redemption price of W842,517,518,646 and (ii) 44,720,603 shares of our Redeemable Convertible Preferred Stock, with an aggregate redemption price of W808,816,825,858, which were convertible into shares of our common stock. In November 2005, Korea Deposit Insurance Corporation converted 22,360,302 shares of our Redeemable Convertible Preferred Stock into 22,360,302 shares of our common stock, representing 6.22% of our total issued shares (or 5.86% of our total issued common stock on a fully diluted basis). In April 2006, Korea Deposit Insurance Corporation sold to BNP Paribas S.A. and other institutional investors all of our common shares held by it. As of the date hereof, Korea Deposit Insurance Corporation does not hold any share of our common stock but still holds 22,360,301 shares of Redeemable Convertible Preferred Stock, representing 6.22% of the total issued shares (or 5.86% of the total issued shares on a fully diluted basis) of our common stock.

**Capital Adequacy**

As of March 31, 2006, the date before the merger of Shinhan Bank and Chohung Bank, the capital adequacy ratios were 12.55 and 10.77 for Shinhan Bank and Chohung Bank, respectively. As of the same date, the Tier I ratios were 8.36 and 6.91 for Shinhan Bank and Chohung Bank, respectively.

**Table of Contents****BUSINESS OVERVIEW**

Unless otherwise specifically mentioned, the following business overview is presented on a consolidated basis under U.S. GAAP.

In the overview of our business that follows, we provide you with information regarding our branch network and other distribution channels and a detailed look at our principal group activities.

**Our Branch Network and Distribution Channels**

Through branches maintained at various levels of our subsidiaries, we offer a variety of financial services to retail and corporate customers. The following table presents the geographical distribution of our domestic branch network, according to our principal subsidiaries with branch networks, as of December 31, 2005.

	Shinhan Bank		Chohung Bank		Jeju Bank	Good	Shinhan	Shinhan	Shinhan	Total
	Retail	Corporate	Retail	Corporate		Morning Shinhan Securities		Card(1)		
Seoul and metropolitan	162	48	189	44	1	35	5	48	532	
Kyunggi Province	75	15	74	15		10	3	12	204	
Six major cities:	48	16	78	15	1	18	5	27	208	
Incheon	17	5	18	3		2	1	7	53	
Busan	11	5	24	4	1	5	1	7	58	
Kwangju	5	1	6	2		2	1	5	22	
Taegu	6	3	13	3		4	1	3	33	
Ulsan	4	1	7	1		2		1	16	
Taejon	5	1	10	2		3	1	4	26	
Sub-total	285	79	341	74	3	63	13	87	944	
Others	28	10	107	15	29	14	3	30	236	
Total	313	89	448	89	32	77	16	117	1,180	

Note:

(1) Represents sales offices focusing on attracting new customers.

**Banking Branch Network**

As of December 31, 2005, Shinhan Bank had 402 branches in Korea. Shinhan Bank's branch network is designed to focus on providing one-stop banking services tailored to one of the three customer categories: retail customers, small- and medium-sized enterprises customers and large corporate customers. Under the customer oriented branch network, branch officers operate under the sole and independent supervision of their respective division profit centers, providing one-stop banking services tailored to their respective customer groups. Of the 402 total domestic branches, three branches specialize in serving large corporations, 86 branches concentrate on small-and medium-sized enterprises and 313 branches focus on retail customers.

As of December 31, 2005, Chohung Bank had an extensive nation-wide branch network with a total of 537 branches in Korea. With key branches located in high traffic locations such as airports, hospitals and other public facilities, we believe that the former branch network of Chohung Bank provided, and will provide following integration with Shinhan Bank, its former customers with convenience and efficiency that enabled Chohung Bank to

secure a significant source of stable funding at competitive rates. Of the 537 total branches, six branches specialize in serving large corporations, 83 branches concentrate on small- and medium enterprises and 448 branches focus on retail customers.

We believe that targeting specific service areas and offering differentiated services to each group of customers will improve our profitability and productivity.

**Table of Contents***Retail Banking Branches*

In Korea, many retail transactions are conducted in cash or with credit cards, and conventional checking accounts are generally not offered or used as widely as in other countries. As a result, an extensive retail branch network plays an important role for Korean banks as customers generally handle most transactions through bank branches.

Shinhan Bank's 162 retail branches are principally located near Seoul and its metropolitan area to target and service high net worth individuals. Chohung Bank had an extensive nationwide network of 448 retail branches covering all regions of Korea, which also offered credit card-related services in addition to conventional consumer lending.

Chohung Bank traditionally focused on retail banking. To focus more on profitability, it developed and implemented what was referred to as "deepening customer relationship branches" or DCR branches, which had separate layouts from conventional branches and provided easier access and differentiated services to high net worth customers. As of December 31, 2005, Chohung Bank had 263 DCR branches located primarily in strategic locations in major Korean cities.

Our private banking relationship managers are representatives who, within target customer groups, assist clients in developing individual investment strategies. We believe that our relationship managers help us foster enduring relationships with our clients. Private banking customers also have access to our retail branch network and other general banking products we offer through our retail banking operations.

*Corporate Banking Branches*

In order to service corporate customers and attract high-quality borrowers, in particular from the small- and medium-sized enterprises sector, Shinhan Bank has developed a relationship management system within its domestic branch network and strengthened its marketing capability. Shinhan Bank's relationship managers help us foster enduring relationships with our corporate customers, the small- and medium-sized enterprises in particular. As of December 31, 2005, Shinhan Bank had 86 corporate banking branches with these relationship management teams focusing on serving its small- and medium-sized enterprises customers. Shinhan Bank expects its headquarters to be much better positioned to effect policies and business strategies throughout its branch network. This should lead to greater efficiency and better services being provided to these customers. Shinhan Bank has three corporate branches solely dedicated to large corporate customers, all of which are located in Seoul, Korea.

In August 2002, in order to service quality corporate customers, in particular from the small- and medium-sized enterprises sector, Chohung Bank spun off the corporate sections from its existing branches and created separate corporate banking branches. As of December 31, 2005, Chohung Bank had 89 corporate banking branches, consisting of six large corporate branches and 83 small- and medium-sized enterprises branches. These corporate banking branches operate independently from the retail banking branches and form a separate corporate banking branch network. Each corporate banking branch has its own general manager and is dedicated solely to large corporate customers.

*Self-Service Terminals*

In order to complement our branch network, we have established an extensive network of automated banking machines, which are located in branches and in unmanned outlets. These automated banking machines consist of ATMs, cash dispensers and passbook printers. As of December 31, 2005, Shinhan Bank had 866 cash dispensers and 1,585 ATMs, and Chohung Bank had 829 cash dispensers and 3,662 ATMs. We have actively promoted the use of these distribution outlets in order to provide convenient service to customers, as well as to maximize the marketing and sales functions at the branch level, reduce employee costs and improve profitability. We believe that the use of our automated banking machines has increased in recent years. In 2005, automated banking machine transactions accounted for approximately 17.1% of total deposit and withdrawal transactions of Shinhan Bank and 28.1% of those of Chohung Bank.

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The following table sets forth information, for the periods indicated, regarding the number of transactions and the fee revenue of our ATMs and cash dispensers.

	For the Year Ended December 31,					
	2003		2004		2005	
<b>Shinhan Bank:</b>						
ATMs and cash dispensers		2,373		2,459		2,751
Number of transactions (millions)		107		105		111
Fee revenue (billions of Won)	W	20	W	20	W	20
<b>Chohung Bank:</b>						
ATMs and cash dispensers		4,655		4,397		4,395
Number of transactions (millions)		281		262		205
Fee revenue (billions of Won)	W	42	W	34	W	33

*Electronic Banking*

Since launching Korea's first internet banking service in July 1999, Shinhan Bank has been widely acknowledged in the print and electronic media as the internet banking leader among Korean commercial banks. Shinhan Bank's internet banking services are more comprehensive than those available at the counter, including such services as 24 hour account balance posting, real-time account transfer, overseas remittance and loan requests. Consistent with the fact that Korea has the highest internet supply rate in the world and an active e-business market, internet banking has continued to grow at a rapid pace. In 2005, internet banking transactions made up 17.0% of total banking transactions of Shinhan Bank. In the case of loans, in particular, an average of approximately 3,946 requests are made per month. Among the electronic banking service customers of Shinhan Bank in 2005, approximately 1,550,769 were retail customers and 105,427 were corporate customers.

In March 2004, we launched the Mobile Banking service, which enables customers to make speedy, convenient and secure banking transactions using IC chip-installed mobile phones. As of December 31, 2005, Shinhan Bank had 40,377 M Banking subscribers who used the service for approximately 3.9 million transactions per year amounting to W900,399 million, and Chohung Bank had 55,542 M Banking subscribers who used the service for approximately 7.1 million transactions amounting to W785,140 million.

Chohung Bank launched its electronic banking services in May 1993, allowing customers to transfer funds, make account inquiries and receive account statements by telephone and facsimile. Chohung Bank provided a 24-hour phone banking service which facilitated money transfers and account inquiries as well as Chohung Bank's efforts to market its products and services through the phone. Chohung Bank's internet banking system, launched in July 1999, enabled customers to transfer funds more conveniently than under the existing phone banking system. In 2005, internet banking transactions made up 18.6% of total banking transactions of Chohung Bank. In the case of loans, in particular, an average of approximately 4,272 requests were made per month. Among the electronic banking service customers of Chohung Bank in 2005, approximately 1,301,125 were retail customers and 94,645 were corporate customers.

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The following table sets forth information, for the periods indicated, on the number of users and transactions and the fee revenue of the above services provided to our retail and corporate customers.

	<b>For the Year Ended December 31,</b>		
	<b>2003</b>	<b>2004</b>	<b>2005</b>
<b>Shinhan Bank:</b>			
<b>Telephone banking(1):</b>			
Number of users(2)	1,109,552	1,398,827	1,685,031
Number of transactions (in thousands)	39,670	36,646	41,608
<b>Internet banking(1):</b>			
Number of users(2)	1,023,195	1,339,571	1,656,196
Number of transactions (in thousands)(3)	306,667	359,160	403,869
Total fee revenue (millions of Won)	W 18,325	W 29,884	W 26,693
<b>Chohung Bank:</b>			
<b>Telephone banking(1):</b>			
Number of users(2)	2,670,658	720,492	976,606
Number of transactions (in thousands)(3)	120,931	108,745	82,349
<b>Internet banking(1):</b>			
Number of users	2,417,415	2,472,415	1,395,770(4)
Number of transactions (in thousands)(3)	141,196	166,937	298,452
Total fee revenue (millions of Won)	W 35,052	W 45,007	W 43,953

*Notes:*

- (1) Includes customers simultaneously using both telephone banking and internet banking.
- (2) Includes customers using services of both Shinhan Bank and Chohung Bank.
- (3) Includes balance transfers.
- (4) The decrease in the number of internet banking users of Chohung Bank was due primarily to Chohung bank's efforts during 2005 to close non-active user accounts (meaning accounts that were not used for six months or more).

E-banking functions primarily as a cost-saving method, rather than a profit-generating platform. Accordingly, substantially all of electronic banking transactions do not generate fee income as many transactions, such as balance inquiries, consultations with customer representatives or transfers of money within our banking institutions, are not charged fees. This is especially the case for phone banking services where a majority of the transactions are balance inquiries or consultations with customer representatives. Firm banking services, which are electronic banking services offered to corporate customers, have also contributed to reducing expenditures on operations and administrative costs.

In line with our strategy to provide high quality and comprehensive customer service, we are in the process of establishing a group-wide integrated call center designed to provide comprehensive customer service and marketing.

**Table of Contents***Overseas Branch Network*

The table below sets forth Shinhan Bank's overseas banking subsidiary and branches as of December 31, 2005.

<b>Business Unit</b>	<b>Location</b>	<b>Year Established or Acquired</b>
<i>Subsidiaries</i>		
Shinhan Finance Limited	Hong Kong SAR, China	1990
<i>Branches</i>		
Tokyo	Japan	1988
Osaka	Japan	1986
Fukuoka	Japan	1997
New York	U.S.A.	1989
London	United Kingdom	1991
Ho Chi Minh City	Vietnam	1995
Shanghai	China	2003
Qingdao	China	2005

The table below sets forth Chohung Bank's overseas banking subsidiaries and branches as of December 31, 2005.

<b>Business Unit</b>	<b>Location</b>	<b>Year Established or Acquired</b>
<i>Subsidiaries</i>		
Chohung Finance Ltd., Hong Kong(1)	Hong Kong SAR, China	1982
Chohung Bank (Deutschland) GmbH(2)	Germany	1994
CHB America Bank(3)	U.S.A.	2003
Chohung Vina Bank(4)	Vietnam	2000
<i>Branches</i>		
Tokyo	Japan	1981
Singapore	Singapore	1990
Tianjin	China	1994
Mumbai	India	1996

*Notes:*

- (1) Renamed as Shinhan Asia Ltd. following the merger of Shinhan Bank and Chohung Bank on April 3, 2006.
- (2) Renamed as Shinhan Bank Europe GmbH following the merger of Shinhan Bank and Chohung Bank on April 3, 2006.
- (3) Created as a result of a merger of Chohung Bank of New York and California Chohung Bank in March 2003. CHB America Bank has offices in New York City, New York and Los Angeles, California; renamed as Shinhan Bank America following the merger of Shinhan Bank and Chohung Bank on April 3, 2006.
- (4) Renamed as Shinhan Vina Bank following the merger of Shinhan Bank and Chohung Bank on April 3, 2006.

The principal activities of overseas branches and subsidiaries of Shinhan Bank, including those of the former Chohung Bank, are providing trade financing and local currency funding for Korean companies and Korean nationals in the overseas markets and providing foreign exchange services in conjunction with our headquarters. On a limited

basis, these overseas branches and subsidiaries also engage in investment and trading of securities of foreign issuers.

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***Credit Card Distribution Channels***

As part of our strategy to focus on cross-selling of credit card products and services to our banking customers, we generally market our credit card products and services to our customers through our established retail distribution channels, primarily through retail and corporate banking branch network of Shinhan Bank (including that of the former Chohung Bank), including automated transaction machines. In addition, as of December 31, 2005, Shinhan Card had 16 sales offices nationwide, which primarily focus on attracting new credit card customers.

***Securities Brokerage Distribution Channels***

Our securities brokerage services is conducted principally through Good Morning Shinhan Securities. As of December 31, 2005, Good Morning Shinhan Securities had 77 branches nationwide and two overseas subsidiaries based in New York and London to service our customers in this business.

Approximately 61.0% of our brokerage branches are located in the Seoul metropolitan area with a focus to attract high net worth individual customers and also to achieve synergy with our retail and corporate banking branch network. In the corporate sector in particular, we continue to explore new opportunities through cooperation between Good Morning Shinhan Securities and Shinhan Bank and Chohung Bank.

***Insurance Sales and Distribution Channels***

We sell and provide our insurance services primarily through Shinhan Life Insurance and SH&C Life Insurance. SH&C Life Insurance specializes in bancassurance products, which it distributes solely through our bank branches. In contrast, Shinhan Life, in addition to distributing bancassurance products through our bank branches, also distributes a wide range of life insurance products through its own branch network, an agency network of financial planners and telemarketers as well as through the Internet. As of December 31, 2005, Shinhan Life Insurance had 112 branches and five customer support centers. These branches are staffed by financial planners, telemarketers and account managers to meet the various needs of our insurance and lending customers. Our customer support centers provide lending services to our insurance customers as well as other customers, and also handle insurance payments.

***Our Principal Activities***

Our principal group activities consist of deposit-taking activities from our retail and corporate customers, which provide us with funding necessary to offer a variety of commercial banking, securities brokerage, investment banking and other financial services.

The comprehensive financial services that we provides are:

Commercial banking services, consisting of the following:

Retail banking services;

Corporate banking services, comprised of two divisions:

Small- and medium-sized enterprises banking; and

Large corporate banking;

Credit cards services;

Treasury and securities investment

Other banking services

Securities brokerage services

Insurance Services

Life insurance services

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Bancassurance

Other insurance services

Reinsurance for life insurance and other insurance services

Asset management services, including brokerage and trading of various securities, related margin lending and deposit and trust services, and other asset management to the extent permitted by law

Other services, including leasing and equipment financing, investment trust management, regional banking, investment banking advisory and loan collection and credit reporting.

In addition to the above business activities, we have a corporate center at the holding company level to house those functions that support the cross-divisional management in our organization.

***Deposit-Taking Activities***

We offer many deposit products that target different customer segments with features tailored to each segment's financial profile and other characteristics. Our deposit products principally include the following:

*Demand deposits*, which either do not accrue interest or accrue interest at a lower rate than time or savings deposits. Demand deposits allow the customer to deposit and withdraw funds at any time and, if they are interest bearing, accrue interest at a fixed or variable rate depending on the period and the amount of deposit. Retail and corporate demand deposits constituted approximately 10.1% of our total deposits as of December 31, 2004 and paid average interest of 1.33% in 2004, and approximately 8.1% of our total deposits as of December 31, 2005 and paid an average interest of 1.90% in 2005.

*Time deposits*, which generally require the customer to maintain a deposit for a fixed term during which the deposit accrues interest at a fixed rate or variable rate based on certain financial indexes, including the Korea Composite Stock Price Index (KOSPI). If the amount of the deposit is withdrawn prior to the end of the fixed term, the customer will be paid a lower interest rate than that originally offered. The term for time deposits typically ranges from one month to five years. Retail and corporate time deposits constituted approximately 47.7% of our total deposits as of December 31, 2004 and paid average interest of 3.83% in 2004, and approximately 42.7% of our total deposits as of December 31, 2005 and paid average interest of 3.69% in 2005.

*Mutual installment deposits*, which generally require the customer to make periodic deposits of a fixed amount over a fixed term during which the deposit accrues interest at a fixed rate. If the amount of the deposit is withdrawn prior to the end of the fixed term, the customer will be paid a lower interest rate than that originally offered. The term for installment deposits typically ranges from six months to five years. Mutual installment deposits constituted approximately 2.9% of our total deposits as of December 31, 2004 and paid average interest of 4.54% in 2004, and approximately 1.8% of our total deposits as December 31, 2005 and paid average interest of 4.16% in 2005.

*Savings deposits*, which allow the customer to deposit and withdraw funds at any time and accrue interest at an adjustable interest rate, which is lower than time or installment deposits. Currently, interest on savings deposits ranges from zero to 3.05%. Saving deposits constituted approximately 29.5% of our total deposits as of December 31, 2004 and paid average interest of 1.24% in 2003, and approximately 31.4% of our total deposits as of December 31, 2005 and paid average interest of 0.96% in 2005.

*Marketable deposits*, consisting of certificates of deposit, cover bills and bonds sold under repurchase agreements that have maturities ranging from 30 days to two years. Interest rates on marketable deposits are determined based on the length of the deposit and prevailing market interest rates. Certificate of deposits are sold on a discount to their face value, reflecting the interest payable on the certificate of deposit. Under U.S. GAAP, cover bills sold are reflected as short-term borrowings and bonds sold under repurchase agreements are reflected under

secured borrowings.

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*Foreign currency deposits*, which accrue interest at an adjustable rate and are available to Korean residents, nonresidents and overseas immigrants. Shinhan Bank offers foreign currency demand and time deposits and checking and passbook accounts in 20 currencies and Chohung Bank offers such accounts in 20 foreign currencies. Deposits in foreign currency constituted approximately 5.81% of our total deposits as of December 31, 2004 and paid average interest of 0.60% in 2004, and approximately 4.41% of our total deposits as of December 31, 2005 and paid average interest of 1.77% in 2005.

We also offer deposits which provide the holder with preferential rights to housing subscriptions under the Housing Construction Promotion Law, and eligibility for mortgage loans. These products include:

*Housing subscription time deposits*, which are special purpose time deposit accounts providing the holder with a preferential right to subscribe for new private apartment units under the Housing Construction Promotion Law. This law is the basic law setting forth various measures supporting the purchase of houses and the supply of such houses by construction companies. If a potential home-buyer subscribes for these deposit products and holds them for a certain period of time as set forth in the Housing Construction Promotion Law, such deposit customers obtain the right to subscribe for new private apartment units on a priority basis under this law. Such preferential rights are neither transferable nor marketable in the open market. These products accrue interest at a fixed rate for one year and at an adjustable rate after one year, which are consistent with other time deposits. Deposit amounts per account range from W2 million to W15 million depending on the size and location of the dwelling unit. These deposit products target high and middle income households.

*Housing subscription installment savings deposits*, which are monthly installment savings programs providing the holder with a preferential subscription right for new private apartment units under the Housing Construction Promotion Law. Such preferential rights are neither transferable nor marketable in the open market. These deposits require monthly installments of W50,000 to W500,000, have maturities between three and five years and accrue interest at fixed rates depending on the term, which are consistent with other installment savings deposits. These deposit products target low- and middle-income households.

For information on our deposits in Korean Won based on the principal types of deposit products we offer, see Item 4. Information on the Company Description of Assets and Liabilities Funding Deposits .

The following table sets forth the number of the deposit customers of Shinhan Bank and Chohung Bank by category as well as the number of domestic branches as of the dates indicated.

	As of December 31,		
	2003	2004	2005
(In thousands, except branches)			
<b>Shinhan Bank:</b>			
Retail deposit customers(1)	5,551	5,934	6,436
Active retail deposit customers(2)	1,621	1,753	1,727
Corporate deposit customers	101	113	121
Domestic branches	354	372	402
<b>Chohung Bank:</b>			
Retail deposit customers(1)	9,239	10,361	9,063
Active retail deposit customers(3)	2,619	2,563	2,932
Corporate deposit customers	138	142	145
Domestic branches	557	533	537

Notes:

(1)

Based on the classification for the purpose of customer management, retail deposit customers include individual deposit customers, foreigners, sole proprietorships and certain small- and medium-sized enterprises deposit customers classified as retail customers depending on a number of factors, including

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those small- and medium-sized enterprises to whom a credit of less than W1 billion has been extended and who are sole proprietors.

- (2) For Shinhan Bank, represents customers (i) whose average monthly account balance is W300,000 or more or (ii) who is 20 years of age or more, has an average loan balance during the year, and accordingly is required to maintain a deposit account with Shinhan Bank to service payment of interest on, and principal of, such loans.
- (3) For Chohung Bank, represents customers whose aggregate of outstanding balances of all accounts as of December 31 of each year was W100,000 or more.

We offer varying interest rates on our deposit products depending on the rate of return on our interest earning assets, average funding costs and interest rates offered by other nationwide commercial banks.

We believe that, as of December 31, 2005, Chohung Bank held the largest amount of deposits made by litigants in connection with legal proceedings in Korean courts or by persons involved in disputes. In Korea, a debtor may discharge his obligation by depositing the subject of performance with the court for the creditor if a creditor refuses to accept payment of debt or is unable to receive it, or if the debtor cannot ascertain without any negligence who is entitled to the payment. Also, in instances in which there has been a preliminary attachment of real property, the property owner may deposit in cash the amount being claimed by such preliminary attachment holder in escrow with the court, in which case the court will remove such lien or attachment. Chohung Bank performed such court deposit services since 1958, and developed an infrastructure of equipment, software and personnel for such business. Following the merger, Shinhan Bank provides such court deposit services, which services may also be provided by other regional banks beginning in July 2006. Such deposits in the past have carried interest rates, which were generally lower than market rates (on average approximately 2% per annum). Such deposits totaled W4,205 billion, W4,329 billion and W5,002 billion as of December 31, 2003, 2004 and 2005, respectively.

The Monetary Policy Committee of the Bank of Korea imposes a reserve requirement on Won currency deposits of commercial banks which currently ranges from 1% to 5%, based generally on the term to maturity and the type of deposit instrument. See Item 4. Information on the Company Supervision and Regulation Principal Regulations Applicable to Banks Liquidity . The Monetary Policy Committee also regulates maximum interest rates that can be paid on certain deposits. Under the Korean government's finance reform plan issued in May 1993, controls on deposit interest rates have been gradually reduced. Currently, only maximum interest rates payable on demand deposits are subject to regulation by the Bank of Korea.

The Depositor Protection Act provides for a deposit insurance system where the Korea Deposit Insurance Corporation guarantees to depositors the repayment of their eligible bank deposits. The deposit insurance system insures up to a total of W50 million per depositor per bank. See Item 4. Information on the Company Supervision and Regulation Principal Regulations Applicable to Banks Deposit Insurance System .

***Retail Banking Services***

*Overview*

We provide retail banking services primarily through Shinhan Bank (and prior to the merger of the two banks, through Shinhan Bank and Chohung Bank), and, to a significantly lesser extent, through Jeju Bank, a regional commercial bank. The consumer loans of Shinhan Bank amounted to W22,874 billion (not including credit cards) as of December 31, 2005, and those of Chohung Bank amounted to W18,204 billion (not including credit cards) as of December 31, 2005.

Retail banking services include mortgage, small business and consumer lending as well as demand, savings and fixed deposit-taking, checking account services, electronic banking and ATM services, bill paying services, payroll and check-cashing services, currency exchange and wire fund transfer. We believe that the provision of modern and efficient retail banking services is important both in maintaining our public profile and as a source of fee-based income. We believe that our retail banking services and products will become

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increasingly important in the coming years as the domestic and regional banking sectors further develop and become more diverse.

Retail banking of Shinhan Bank has been and will continue to remain one of our core businesses. Shinhan Bank's strategy in retail banking is to provide prompt and comprehensive services to retail customers through increased automation and improved customer service, as well as a streamlined branch network focused on sales. The retail segment places an emphasis on targeting high net worth individuals. As of December 31, 2005, Shinhan Bank had approximately 45,055 high net worth customers with deposits of W100 million or more.

Chohung Bank leveraged its customer information database to actively market and cross-sell to, as well as focus more resources on, its most profitable customers. In addition, Chohung Bank, through its Product Development Division, offered a wider variety of products differentiated and targeted towards differentiated customer segments with a greater focus on the high margin, high net worth individuals. As of December 31, 2005, Chohung Bank had approximately 35,720 high net worth customers with deposits of W100 million or more.

*Consumer Lending Activities*

We offer various consumer loan products, consisting principally of household loans, which target different segments of the population with features tailored to each segment's financial profile and other characteristics, including each customer's profession, age, loan purpose, collateral requirements and the length of time a borrower has been our customer. Household loans consist principally of the following:

*Mortgage and home equity loans*, mostly comprised of mortgage loans which are loans to finance home purchases and are generally secured by the home being purchased; and

*Other consumer loans*, which are loans made to customers for any purpose (other than mortgage and home equity loans) and the terms of which vary based primarily upon the characteristics of the borrower and which are either unsecured or secured or guaranteed by deposits or a third party.

As of December 31, 2005, mortgage and home-equity loans and other consumer loans accounted for 59.11% and 40.89%, respectively, of our consumer loans (excluding credit cards).

For secured loans, including mortgage and home equity loans, Shinhan Bank's policy is to lend up to 50%-70% of the appraisal value of the collateral, by taking into account the value of any lien or other security interest that is prior to our security interest (other than petty claims). Chohung Bank's policy is to lend up to the estimated recovery value of the collateral, which Chohung Bank calculated based on the average value of collateral published by courts as recovered through court-approved auctions during the previous year and further adjusted to take into account the existence of any lien or other security interest that is prior to Chohung Bank's security interest. As of December 31, 2005, the loan-to-value ratios of mortgage and home equity loans, under Korean GAAP, of Shinhan Bank and Chohung Bank were approximately 48.52% and 53.05%, respectively.

Due to the rapid increase in mortgage and home equity loans in Korea, in 2005 and 2006, the Financial Supervisory Commission implemented stringent regulations and guidelines that are designed to suppress the increase of loans secured by housing. These regulations include restrictions on banks' maximum loan-to-value ratios, guidelines with respect to appraisal of collateral, internal control and credit approval policy requirements with regard to housing loans as well as provisions designed to discourage commercial banks or other financial institutions from instituting incentive-based marketing and promotion of housing loans. In addition to the existing regulations and guidelines, from the second half of 2005 to the first quarter of 2006, the Financial Supervisory Commission implemented additional guidelines to reduce mortgage and home equity loans and stabilize the real estate market, including (i) restricting the number of extensions on loans secured by the borrower's apartment to one, (ii) reducing the maximum loan-to-value ratio for loans secured by the borrower's apartment in highly speculated areas, (iii) forbidding to extend mortgage or home equity loans to minors and (iv) (applying each of the debt-to-income ratio the loan-to-value ratio to 40% in respect of loans by banks and insurance companies for the purpose of assisting the purchase of apartments located in highly

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speculated areas with a purchase price of less than W600 million. We believe that Government regulations relating to the real estate market will also reduce the rate of growth in the mortgage and home equity markets.

As of December 31, 2005, substantially all of our mortgage and home equity loans were secured by residential property.

In Korea, contrary to general practices in the United States, it is a common practice in Korea for construction companies in Korea to require buyers of new homes (particularly apartments under construction) to make installment payments of the purchase price well in advance of the title transfer of the home being purchased. In connection with this common practice, we provide advance loans, on an unsecured basis for the time being, to retail borrowers where the use of proceeds is restricted to financing of home purchases. A significant portion of these loans are guaranteed by third parties, which may include the construction company receiving the installment payment, until construction of the home is completed. Once construction is completed and the titles to the homes are transferred to the borrowers, which may take several years, these loans become secured by the new homes purchased by these borrowers. As of December 31, 2003, we had approximately W634 billion of such unsecured loans, classified as mortgage and home equity loans and representing approximately 3.1% of our total mortgage and home equity loans. Recognizing the unsecured nature of such loans, we classified such loans as other consumer loans as of December 31, 2004. As of December 31, 2004 and 2005, we had approximately W824 billion and W1,340 billion, respectively, of such unsecured loans to construction companies, classified as other consumer loans.

The following table sets forth the portfolio of our consumer loans.

	As of December 31,					
	2003		2004		2005	
(In billions of Won, except percentages)						
Consumer loans(1)						
Mortgage and home-equity	W	20,517	W	22,180	W	25,840
Other consumer		14,580		15,546		17,874
Percentage of consumer loans to total gross loans		36.8%		38.9%		41.3%

*Notes:*

(1) Before allowance for loans losses and excludes credit card accounts.

*Pricing*

The interest rates on consumer loans made by Shinhan Bank (and Chohung Bank prior to the merger) are either periodic floating rates (which is based on a base rate determined for three-month, six-month or twelve-month periods derived using our internal transfer price system, which reflects our cost of funding in the market, further adjusted to account for our expenses related to lending and profit margin) or fixed rates that reflect our cost of funding, as well as our expenses related to lending and profit margin. Fixed rate loans are currently limited to maturities of three years and offered only on a limited basis. For unsecured loans, both types of rates also incorporate a margin based on, among other things, the borrower's credit score as determined during our loan approval process. For secured loans, credit limit is based on the type of collateral, priority with respect to the collateral and loan to value. We can adjust the price to reflect the borrower's current and/or expected future contribution to our profitability. The applicable interest rate is determined at the time a loan is extended. If a loan is terminated prior to its maturity, the borrower is obligated to pay us an early termination fee of approximately 0.5% to 1.5% of the loan amount in addition to the accrued interest, depending on the timing, the nature of the credit and the amount.

As of December 31, 2005, Shinhan Bank's three-month, six-month and twelve-month base rates were approximately 4.08%, 4.37% and 4.77%, respectively, and Chohung Bank's three-month, six-month and twelve-month base rates were approximately 4.08%, 4.68% and 4.68%, respectively. As of December 31, 2005, Shinhan Bank's fixed

rates for home equity loans with a maturity of one year, two years and three years were 7.8%, 8.1% and 8.4%, respectively, and Shinhan Bank's fixed rates for other consumer loans with a maturity of

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one year ranged from 8.75% to 12.75%, depending on the consumer credit scores of its customers, while Chohung Bank's fixed rates for home equity loans with a maturity of one year, two years and three years were 7.00%, 7.36% and 7.54%, respectively, and Chohung Bank's fixed rates for other consumer loans with a maturity of one year ranged from 9.00% to 13.00%, depending on the consumer credit scores of its customers.

As of December 31, 2005, approximately 57.96% of our consumer loans were priced based on a floating rate and approximately 42.05% were priced based on a fixed rate. As of the same date, approximately 63.39% of our consumer loans with maturity of over one year were priced based on a floating rate and approximately 36.61% were priced based on a fixed rate.

*Private Banking*

Historically, we have focused on customers with higher net worth. Our retail banking services provide a private banking service to our high net worth customers who seek personal advice in complex financial matters. Our aim is to help enhance the private wealth and increase the financial sophistication of our clients by offering them portfolio/fund management services, tax consulting services and real estate management service. To date, our fee revenues from these activities have not been significant.

We believe that we were one of the first banks to initiate private banking in Korea. We opened our first Private Banking Center in Seoul in 2002 to serve the needs of high net worth customers, in particular those customers with deposits of W1 billion or more, and we currently have seven private banking centers both of which are located in Seoul metropolitan area. While we believe that the market for private banking services in Korea is still at an early stage of development, in connection with our strategy to target high net worth retail customers, we established a separate private banking department in 2003 to further develop and improve our services in this area. With the launch of our New Bank initiative, our private banking department was spun off from its original organization and was elevated to the Private Banking Group. As of May 2006, we operate twelve Private Banking Centers nationwide, including eight in Seoul, one in the suburbs of Seoul and three in other cities located in other regions in Korea. Through these efforts, we believe that our private banking service marked the year 2005 with notable growth. The combined customer base grew to 1,830 people and assets under management increased 47% from W3.2 trillion in 2004 to W4.7 trillion in 2005.

*Corporate Banking Services**Overview*

We provide corporate banking services, primarily through Shinhan Bank (and also through Chohung Bank prior to the merger), to small- and medium-sized enterprises and, to a lesser extent, to large corporations, including corporations that are affiliated with chaebols. We also lend to government-controlled companies.

The following table sets forth the balances and percentage of our total lending attributable to each category of our corporate lending business as of the dates indicated.

	<b>As of December 31,</b>					
	<b>2003</b>		<b>2004</b>		<b>2005</b>	
	<b>(In billions of Won, except percentages)</b>					
Small- and medium-sized enterprises loans(1)	W 38,055	40.0%	W 38,713	39.9%	W 39,943	37.7%
Large corporate loans(2)	16,031	16.8	15,909	16.4	17,948	16.9
<b>Total corporate loans</b>	<b>W 54,086</b>	<b>56.8%</b>	<b>W 54,622</b>	<b>56.3%</b>	<b>W 57,891</b>	<b>54.6%</b>

Notes:

- (1) Represents the principal amount of loans extended to corporations meeting the definition of small- and medium-sized enterprises under the Basic Act on Small- and Medium-sized Enterprises and its Presidential Decree. Certain loans to sole proprietorships are included under retail lending.
- (2) Includes loans to government-controlled companies.

**Table of Contents***Small- and Medium-sized Enterprises Banking*

The small- and medium-sized enterprise loans of Shinhan Bank amounted to W21,669 billion as of December 31, 2005 and those of Chohung Bank amounted to W14,869 billion as of December 31, 2005. Under the Basic Act on Small and Medium-sized Enterprises and its Presidential Decree, small- and medium-sized enterprises are defined as companies which (i) do not have employees and assets exceeding the number or the amount, as the case may be, specified in accordance with their types of businesses in the Presidential Decree and (ii) do not belong to a conglomerate as defined in the Monopoly Regulations and Fair Trade Act. As of December 31, 2005, we had approximately 97,346 small- and medium-sized enterprises loan customers, consisting of approximately 48,055 customers with Shinhan Bank and 49,291 customers with Chohung Bank (not taking into account any overlap between the two sets of customers). Shinhan Bank's small- and medium-sized enterprises business has historically focused on larger and well-established small- and medium-sized enterprises in Korea that prepared financial statements audited by independent auditors. This focus is based on our belief and historical observation that the larger and, in many cases, more sound businesses tend to engage independent auditors and strengthen investor confidence. Chohung Bank traditionally focused on large corporate and retail banking and, as a result, its small- and medium-sized enterprises lending portfolio increased during recent years with a focus on higher profit, higher risk customers who are comparatively smaller than Shinhan Bank's customers.

As of December 31, 2005, our corporate banking operation was the largest among Korean banks, with 16.2% of the market share, in terms of the total amount of Won-denominated loans to small- and medium-sized enterprises (other than affiliates of the thirty largest conglomerates in Korea) that are audited by certified public accountants. Of such loans, W11,073 billion were made by Shinhan Bank to 2,901 corporate customers, representing 19.13% of our total outstanding Won-denominated corporate loans, and W7,267 billion were made by Chohung Bank to 2,576 corporate customers, representing 12.55% of our total outstanding Won-denominated corporate loans.

Our small- and medium-sized enterprises banking business has traditionally been and will remain one of our core businesses. However, the small- and medium-sized enterprise business is currently the focus of intense competition among large commercial banks and the opportunities for us to expand our business with more established small- and medium-sized enterprises have been reduced. During recent years, most of the nationwide banks have shifted their focus to or increased their emphasis on this type of lending, as opportunities in the large corporate and retail sectors diminished. While we expect competition in this sector to intensify, we believe that our established customer base, quality brand image and experienced lending staff will provide an opportunity to maintain steady growth in this environment.

We believe that Shinhan Bank, which has traditionally focused on small- and medium-sized enterprises lending, possesses the necessary elements to succeed in the small- and medium-sized enterprises market, including its marketing capabilities (which we believe have provided Shinhan Bank with significant brand loyalty) and its credit rating system for credit approval. To maintain or increase its market share of small- and medium-sized enterprises lending, Shinhan Bank has:

- positioned itself based on accumulated expertise. We believe Shinhan Bank has a better understanding of the credit risks embedded in this market segment and to develop loan and other products specifically tailored to the needs of this market segment;

- begun operating a relationship management system to provide targeted and tailored customer service to small- and medium-sized enterprises. Shinhan Bank has 89 corporate banking branches with relationship management teams. These relationship management teams market products and review and approve smaller loans that pose less credit risks; and

- begun to focus on cross-selling loan products with other products. For example, when Shinhan Bank lends to small- and medium-sized enterprises, it also explores opportunities to cross-sell consumer loans or deposit products to the employees of those companies or to provide financial advisory services.

Chohung Bank in recent years identified small- and medium-sized enterprise lending as its principal areas of growth and increased its small- and medium-sized enterprises customer base to include relatively



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smaller enterprises, such as small unincorporated businesses and sole proprietorships. While lending to these customers has resulted in growth of Chohung Bank's corporate lending portfolio, it also increased its credit risk exposure relative to its other existing customers.

Since 2003, the industry-wide delinquency ratios for loans to small- and medium-sized enterprises have been rising. According to data compiled by the Financial Supervisory Service, the delinquency ratio (net of charge-offs, which has also increased significantly) for Won-denominated loans by Korean banks to small- and medium-sized enterprises increased from 1.5% as of December 31, 2003 to 2.19% as of December 31, 2005. The delinquency ratio for loans to small- and medium-sized enterprise is calculated as the ratio of (1) the outstanding balance of such loans in respect of which either principal payments are overdue by one day or more or interest payments are over due by 14 days or more (if prior interest payments on a loan were made late on more than three occasions, in which case the loan is considered delinquent if interest payments are overdue by one day or more) to (2) the aggregate outstanding balance of such loans. Shinhan Bank's delinquency ratio, calculated under Korean GAAP, for such loans increased from 1.75% as of December 31, 2003 to 1.80% as of December 31, 2004 and decreased to 1.44% as of December 31, 2005 and to 1.42% as of March 31, 2006. Chohung Bank's delinquency ratio, calculated under Korean GAAP, for such loans decreased from 3.49% as of December 31, 2003 to 2.21% as of December 31, 2004 to 1.70% as of December 31, 2005 and to 2.06% as of March 31, 2006. In particular, Shinhan Bank's delinquency ratios, calculated under Korean GAAP, for Won-denominated loans to small- and medium-sized enterprises that do not prepare audited financial statements were 2.46% as of December 31, 2003, 1.95% as of December 31, 2004 and 1.95% as of December 31, 2005. Such delinquency ratios for Chohung Bank were 4.86% as of December 31, 2003, 2.74% as of December 31, 2004 and 1.45% as of December 31, 2005. Shinhan Bank's delinquency ratios for loans to small unincorporated businesses and sole proprietorships were 1.56% as of December 31, 2003, 2.07% as of December 31, 2004, 1.64% as of December 31, 2005 and 1.62% as of March 31, 2006. Such delinquency ratios for Chohung Bank were 3.03% as of December 31, 2003, 2.00% as of December 31, 2004, 1.64% as of December 31, 2005 and 2.23% as of March 31, 2006. These delinquencies may rise further in 2006 compared to 2003, 2004 and 2005. The current focus of our small- and medium-sized enterprise lending business is to improve the asset quality and maintain the profitability of our loans to small- and medium-sized enterprises.

*Large Corporate Banking*

Large corporate customers consist primarily of member companies of chaebols and financial institutions. Large corporate loans of Shinhan Bank amounted to W9,113 billion as of December 31, 2005, and those of Chohung Bank amounted to W8,203 billion as of December 31, 2005. As a late entrant into the Korean commercial banking industry, large corporate banking has not been a core business of Shinhan Bank and its focus of business in this customer sector has been on investments in corporate debt securities and fee-based businesses rather than conventional lending activities. On the other hand, Chohung Bank, the oldest commercial bank in Korea that we acquired in 2003, traditionally focused on large corporate customers as its core corporate banking business.

In recent years, our Corporate & Investment Banking Group has begun providing investment banking services. We provide services as an arranger, trustee and liquidity provider for asset-backed securities. We also participate in and administer syndicated loans and project financings. We provide advisory services in the area of social overhead capital projects such as highway, port, power and water and sewage projects, as well as equity and venture financing, real estate financing and mergers and acquisitions advice.

*Corporate Lending Activities*

Our principal loan products for corporate customers are working capital loans and facilities loans. Working capital loans, which include discounted notes and trade financing, are, in general, loans used for general working capital purposes. Facilities loans are provided to finance the purchase of equipment and the establishment of manufacturing won-denominated plants. As of December 31, 2005, working capital loans and facilities loans amounted to W33,474 billion and W4,682 billion, respectively, representing 87.73% and 12.27% of our total Won-denominated corporate loans under Korean GAAP. Working capital loans generally have a

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maturity of one year, but may be extended on an annual basis for an aggregate term of three years in the case of unsecured loans and five years in the case of secured loans. Facilities loans, which are generally secured, have a maximum maturity of ten years.

Loans to corporations may be unsecured or secured by real estate, deposits or guaranty certificates. As of December 31, 2005, under Korean GAAP, secured loans and guaranteed loans (including loans secured by guaranty certificates issued by credit guarantee insurance funds) accounted for 52.19% and 10.34%, respectively, of Shinhan Bank's Won-denominated loans to small- and medium-sized enterprises. Among the secured loans, approximately 89.43% were secured by real estate. As of December 31, 2005, under Korean GAAP, secured loans and guaranteed loans (including loans secured by guaranty certificates issued by credit guarantee insurance funds) accounted for 41.61% and 12.64%, respectively, of Chohung Bank's Won-denominated loans to small- and medium-sized enterprises. Among the secured loans, approximately 79.20% were secured by real estate.

When evaluating the extension of loans to corporate customers, we review the corporate customer's creditworthiness, credit scoring, value of any collateral or third party guarantee. The value of any collateral is defined using a formula that takes into account the appraised value of the property, any prior liens or other claims against the property and an adjustment factor based on a number of considerations including, with respect to property, the average value of any nearby property sold in a court-supervised auction during the previous year. We revalue any collateral when a secured loan is renewed or if a trigger event occurs with respect to the loan in question.

As of December 31, 2005, in terms of outstanding loan balance, 39.4% of our corporate loans were extended to borrowers in the manufacturing industry, 14.3% were to borrowers in the retail and wholesale industry, 16.3% were to the borrowers in the real estate, leasing and service industry, 5.5% were to borrowers in the construction industry, and 6.2% were extended to borrowers in the finance and insurance industry. Beginning in 2004, loans to corporate borrowers in the real estate, leasing and service industry and the hotel and leisure industry, which are principally small- and medium-sized enterprises, began experiencing an increase in delinquencies as well as deterioration in credit quality. Under Korean GAAP, delinquency ratio for Won-denominated loans to the real estate, leasing and service industry was 1.73% for Chohung Bank and 1.00% for Shinhan Bank as of December 31, 2005, in each case net of charge-offs and loan sales. Under Korean GAAP, delinquency ratio for Won-denominated loans to the hotel and leisure industry was 3.30% for Chohung Bank and 1.88% for Shinhan Bank as of December 31, 2005, in each case net of charge-offs and loan sales. Shinhan Bank's Won-denominated corporate loans classified as substandard or below under the guidelines of the Financial Supervisory Commission decreased from W557 billion as of December 31, 2003 to W289 billion as of December 31, 2005 and Chohung Bank's Won-denominated corporate loans classified as substandard or below were W233 billion as of December 31, 2005, as compared to W588 billion as of December 31, 2003, in each case net of charge-offs and loan sales.

*Pricing*

We establish the price for our corporate loan products of Shinhan Bank (and prior to the merger, also Chohung Bank) based principally on their respective cost of funding and the expected loss rate based on a borrower's credit risk. As of December 31, 2005, 58.15% of Shinhan Bank's corporate loans with outstanding maturities of one year or more had interest rates that were not fixed but were variable in reference to Shinhan Bank's market rate and 16.65% of Chohung Bank's corporate loans with outstanding maturities of one year or more had interest rates that were not fixed but were variable in reference to Chohung Bank's market rate.

*Shinhan Bank*

Shinhan Bank generally determines pricing of its corporate loans as follows:

Interest rate = (Shinhan Bank's periodic market floating rate *or* reference rate) *plus* transaction cost *plus* a credit spread *plus* risk premium *plus or minus* a discretionary adjustment rate.

Depending on the situation and Shinhan Bank's agreement with the borrower, Shinhan Bank may use either its periodic market floating rate or the reference rate as the base rate in calculating its pricing. As of

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December 31, 2005, Shinhan Bank's periodic market floating rates (which are based on a base rate determined for three-month, six-month, one-year, two-year, three-year or five-year periods derived using Shinhan Bank's market rate system) were 4.08% for three months, 4.37% for six months, 4.77% for one year, 5.13% for two years, 5.31% for three years and 5.60% for five years. As of the same date, Shinhan Bank's reference rate was 8.60%.

Transaction cost is added to reflect the standardized transaction cost assigned to each loan product and other miscellaneous costs, including contributions to the Credit Guarantee Fund and education taxes.

The credit spread is added to the periodic floating rate to reflect the expected loss from a borrower's credit rating and the value of any collateral or payment guarantee. In addition, we add a risk premium that is measured by the unexpected loss that exceeds the expected loss from the credit rating assigned to a particular borrower.

A discretionary adjustment rate is added or subtracted to reflect the borrower's current and/or future contribution to Shinhan Bank's profitability. In the event of additional credit provided by way of a guarantee of another, the adjustment rate is subtracted to reflect such change in the credit spread. In addition, depending on the price and other terms set by competing banks for similar borrowers, we may reduce the interest rate Shinhan Bank charges to compete more effectively with other banks.

*Chohung Bank*

Chohung Bank generally determined pricing of its corporate loans as follows:

Interest rate = Funds transfer pricing *plus* operating cost (or transaction cost) *plus* loan policy margin *plus* a credit spread *plus* a periodic spread *plus* risk premium *plus* estimated margin *plus or minus* a discretionary adjustment rate.

Fund transfer pricing represents inter-segment lending rates published by Chohung Bank's Treasury & Investment Division and varies depending on the type of loans.

Transaction cost is added to reflect the standardized transaction cost assigned to each loan product and other miscellaneous indirect costs, including contributions to the Credit Guarantee Fund and education taxes.

Loan policy margin is determined by loan policy to compensate for the opportunity cost of the capital and achieve competitiveness among peer banks in consideration of, among others, loan type, transaction risk and proper margin.

The credit spread is added to reflect the expected loss from the value of any collateral or payment guarantee.

The periodic spread is added to reflect the expected loss from the length of the maturity.

The risk premium is added, which is measured by the unexpected loss that exceeds the expected loss from the credit rating assigned to a particular borrower.

Estimated margin is added to reflect targeted profitability based on expected losses.

A discretionary adjustment rate is added or subtracted to reflect the borrower's current and/or future contribution to Chohung Bank's profitability. In the event of additional credit provided by way of a guarantee of another, the adjustment rate is subtracted to reflect such change in the credit spread. In addition, depending on the price and other terms set by competing banks for similar borrowers, we may reduce the interest rate Chohung Bank charged to compete more effectively with other banks.

*Electronic Corporate Banking*

Shinhan Bank launched its electronic corporate banking services connecting its corporate customers through dedicated subscriber lines in 1991. Shinhan Bank has since developed its electronic corporate banking services to offer to corporate customers a web-based total cash management service through Shinhan Bizbank. Shinhan Bizbank supports all types of banking transactions from basic transaction history inquiries

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and fund transfers to opening letters of credit and trade finance. Products and services related to cash management include payment management, collection management, sales settlement service, acquisition settlement service, B2B settlement service, sweeping and pooling. By offering such information technology-related products and services such as purchase cards, loans for purchasing goods, e-biz loans, and a B2B settlement service, Shinhan Bank is able to continue to reinforce its image as one of the leaders in electronic corporate banking. Through the enhancement of Shinhan Bizbank and its cash management service, we intend to improve the support service system related to customer cash management. Shinhan Bizbank's services were being used by approximately 105,427 corporations as of December 31, 2005 and, in 2005, its number of transactions and aggregate transaction amount were approximately 14,094,880 and W519,222 billion, respectively.

Chohung Bank launched its electronic corporate banking through e-FMS in January 2002. e-FMS offers not only cash management services, including payment management, but also B2B settlement service and enterprise resources planning service. Enterprise resource planning service includes accounting, human resources, salary payments, procurement, sales settlement service and production management and also offers cashflow management and tax management to its corporate customers. Chohung Bank's e-FMS users were approximately 94,645 corporations as of December 31, 2005 and, in 2005, its number of transactions and aggregate transaction amount were approximately 19,304,174 and W369,221 billion, respectively.

***Credit Card Services******Overview***

As of December 31, 2005, our total credit card balance outstanding was W4,242 billion, or 4.01% of our total loans outstanding as of the same date, which consists of W1,923 billion with Shinhan Card and W2,278 billion with credit card operations of Chohung Bank.

On June 4, 2002, Shinhan Bank spun-off its credit card business into Shinhan Card Co., Ltd., a monoline credit card subsidiary. Despite the spin-off, Shinhan Bank continues to manage a substantial portion of our credit card operations, including the collections and receiving and processing of applications, pursuant to an agency agreement between the two subsidiaries.

Prior to the merger of Shinhan Bank and Chohung Bank in April 2006, Chohung Bank had an active credit card business division. Chohung Bank was a member of BC Card Co., Ltd. (BC Card), which is owned by 11 consortium banks with Chohung Bank holding 14.85% equity interest in BC Card. BC Card issues credit cards under the names of the member banks, substantially all of which are licensed to use MasterCard, Visa or JCB. This allows holders of BC Card to use their cards at any establishment which accepts MasterCard, Visa or JCB, as the case may be.

Upon the merger of the two banks in April 2006, we split off the credit card services division of Chohung Bank and merged it into Shinhan Card.

Following such split-merger, Shinhan Card is expected to have W4 trillion in assets, W25 trillion in total credit card use (excluding corporate cards) and 5.9 million customers ranking fourth among credit card service providers (including banks) in terms of the total credit card use.

The use of credit cards in Korea has increased dramatically in recent years as the Korean economy and consumer spending recovered from the financial and economic difficulties of late 1990's and also as a result of government initiatives designed to promote the use of credit cards, such as providing tax benefits to businesses that accept credit cards and tax deductions for consumers up to certain amounts charged to credit cards. However, as credit card delinquencies in Korea have begun to increase since mid-2002, concerns have been raised regarding the rapid growth in credit card usage and significant deterioration in asset quality of the Korean credit card industry. Throughout 2002 and during the first half of 2003, the Financial Supervisory Commission strengthened regulations designed to address these concerns relating to the credit card industry. See Item 3. Key Information Risk Factors Risks Relating to Our Banking Business Government regulation of our consumer and credit card operations has increased significantly which may materially and adversely affect our credit card and consumer operations, and Supervision and Regulation .

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*Products and Services*

We offer a variety of credit card products and services that target select customer profiles and focus on:  
offering cards that provide additional benefits such as frequent flyer miles and reward program points that can be redeemed by the customer for complementary services, prizes and cash;

offering gold cards, platinum cards and other preferential members cards which have higher credit limits and provide additional services in return for higher annual membership fees;

acquiring new customers through strategic alliances and cross-marketing with wholesalers and retailers;

encouraging increased use of credit cards by existing customers through special offers for dormant customers;

introducing new features to preferred customers, such as revolving credit cards, travel services and insurance;

developing fraud detection and security systems to prevent the misuse of credit cards and to encourage the use of credit cards over the Internet; and

issuing smart cards and preparing for a cardless business environment in which customers can use credit cards to make purchases by phone or over the Internet.

Cardholders have several options for repayment of balances as follows:

general purchases of goods and services on credit, which are repayable on a lump-sum basis at the end of a monthly billing cycle;

installment purchases, which require payment approximately within 18 to 48 days after purchase and are repayable on an even-payment installment basis over a period of time ranging from two months to three years and generally accrue interest;

cash advances, which are repayable on a lump-sum basis at the end of a monthly billing cycle and generally accrue interest effective annual rates of approximately 9.8% to 26.8% for Shinhan Card and 18.0% to 26.97% for Chohung Bank; and

payments on a revolving payment basis, which allow customers to roll over their balance into a revolving basis with fixed minimum percentage or amount of the total outstanding balance.

Credit card loans may be secured or unsecured, have initial maturities of one year and currently accrue interest at the effective annual rates of approximately 15.5% to 20.0% in the case of Chohung Bank and approximately 9.8% to 21.8% in the case of Shinhan Card.

Income from the credit card business consists of annual fees paid by cardholders, installment purchase fees, cash advance fees, interest on late and deferred payments and fees paid by merchants, with fees from merchants and cash advance fees constituting the largest source. Merchant discount fees, which are processing charges on the merchants, can be up to 4.5% of the purchased amount depending on the merchant used, with the average charge being 2.34% for Shinhan Card and 2.44% for Chohung Bank in 2005.

Although the revolving credit system is more common in the United States and many other countries, this payment system is still in early stages of development in Korea. Credit card holders in Korea are required to pay for their purchases within approximately 18 to 48 days of purchase depending on their payment cycle and, except in the case of installment purchases where the charged amounts are repaid in installments, typically during the following three to six months. Credit card accounts that remain unpaid after this period are deemed to be delinquent accounts. We charge penalty interest on delinquent accounts and closely monitor such accounts. For purchases made by installments, we charge interest on unpaid amounts at rates that vary according to the terms of repayment.

In certain cases, credit card companies in Korea, including Shinhan Card (and Chohung Bank prior to the split-merger of its credit card division into Shinhan Card), have been allowed to rewrite delinquent credit

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card balances for purchase and cash advance as credit card loans. Each of Shinhan Card and Chohung Bank rewrites a small number of card balances as a means of maximizing collection related to a relatively small number of borrowers who are suffering from temporary financial difficulties where it believes it is probable that all or substantially all principal and interest will ultimately be recovered. Prior to the split-merger, Shinhan Card offered the borrower the option of either repaying the rewritten balance either on a monthly installment basis over five years or as a term loan due at the end of one year while credit card customers of Chohung Bank could apply for entry into the rewritten loan program when the loan balance is past due one month or more. Following the split-merger, Shinhan Card currently provides two repayment programs: (1) the installment repayment program, under which a cardholder with an account which has been delinquent for less than four months repays at least 90% of the original amount owed within a period chosen by such cardholder (provided that the period is between two to 36 months); and (2) the re-aged loan program, under which a qualified cardholder with a guarantor or security repays the full original principal amount, whereas a cardholder without a guarantor or security repays at least 90% of the original full amount owed, in both instances within a maximum period of five years. Except in limited circumstances, borrowers applying for entry into this program in general are required to secure one or more guarantors meeting certain asset and credit quality criteria. If approved, Chohung Bank rewrote card balances including past due interest into card loans and amends the maturity and the repayment terms accordingly. In general, rewritten credit card loans are due at the end of one year. Shinhan Card segregates, and prior to the merger, Chohung Bank segregated, this portfolio for performance measurement and monitoring purposes due to the higher credit risk. The balance of rewritten loans of Shinhan Card were W27 billion, W9 billion and W4 billion as of December 31, 2003, 2004 and 2005 respectively, against which we recognized an allowance of W8 billion, W2 billion and W1 billion, respectively. The balance of rewritten loans of Chohung Bank were W680 billion, W495 billion and W269 billion as of December 31, 2003, 2004 and 2005, respectively, against which Chohung Bank made an allowance of W160 billion, W180 billion and W99 billion, respectively. See Financial and Statistical Information below. The balance of such rewritten loans has been decreasing since both Shinhan Card provides, and prior to the merger, Chohung Bank provided, rewritten loans on a very limited basis.

*Customers and Merchants*

As we believe that internal growth through cross-selling can only be limited, we also seek to enhance our market position by selectively targeting new customers with high net worth and good creditworthiness through the use of a sophisticated and market-oriented risk management system. Credit card applicants are screened and appropriate credit limits are assessed according to internal guidelines based on our credit scoring system.

The following table sets forth the number of customers and merchants of Shinhan Card and Chohung Bank's credit card business as of the dates indicated.

	As of December 31,		
	2003	2004	2005
	(In thousands, except percentages)		
<b>Shinhan Card:</b>			
Number of credit card holders	2,773	3,002	3,467
Personal accounts	2,678	2,905	3,370
Corporate accounts	95	97	96
Active ratio(1)	56.6%	50.7%	63.8%
Number of merchants	2,112	2,513	2,934
<b>Chohung Bank:</b>			
Number of credit card holders	3,205	2,819	2,494
Personal accounts	3,138	2,756	2,434
Corporate accounts	66	63	60

Active ratio(1)	53.9%	50.9%	56.4%
Number of merchants(2)	2,091	2,165	2,225

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(1) Represents the ratio of accounts used at least once within the last six months to total accounts as of year end.

(2) Represents the number of merchants of BC Card's merchant network.

As of December 31, 2005, Shinhan Card had approximately 3,467,000 card customers, which represents an increase of approximately 465,000 customers from approximately 3,002,000 as of December 31, 2004. Of all the customers outstanding as of December 31, 2005, the number of platinum and gold card members, whose higher creditworthiness entitles them to certain benefits, was approximately 1,469,000. As of December 31, 2005, Chohung Bank had approximately 2,494,000 credit card customers, which represents a decrease of approximately 325,000 customers from approximately 2,819,000 as of December 31, 2004 primarily as a result of the reduction in the number of delinquent credit card customers.

The number of Shinhan Card's merchants also increased to approximately 2,934,000 as of December 31, 2005 from approximately 2,513,000 as of December 31, 2004 while the number of merchants that use the services of Chohung Card's credit card division also increased from approximately 2,165,000 as of December 31, 2004 to approximately 2,225,000 as of December 31, 2005.

Chohung Bank developed an independent card processing system that allowed Chohung Bank to process future billings for the existing BC Cards on its own, demonstrating Chohung Bank's focus on cutting costs.. Chohung Bank also participated in a nationwide debit card program with 30 other banks. In connection with this business, as of December 31, 2005, Chohung Bank charged service establishment commissions of 1.5% on average on amounts purchased using the debit card.

*Financial and Statistical Information*

The following table sets forth certain financial and statistical information relating to the credit card operations of Shinhan Card and Chohung Bank as of the dates or for the period indicated.

**As of or for the Year Ended December 31,**

	2003		2004		2005	
	Shinhan Card	Chohung Bank(1)	Shinhan Card	Chohung Bank(1)	Shinhan Card	Chohung Bank(1)
<b>(In billions of Won, except percentages)</b>						
<b>Interest income:</b>						
Installments	W 42	W 133	W 40	W 84	W 49	W 64
Cash advances	164	354	30	212	111	181
Card loans(2)	35	93	34	97	30	60
Annual membership	5	6	2	5	9	4
Revolving(3)	7	113	6	71	6	49
Late payments	21	5	6	11	18	15
<b>Total</b>	<b>W 274</b>	<b>W 704</b>	<b>W 118</b>	<b>W 480</b>	<b>W 223</b>	<b>W 373</b>
<b>Credit card fees:</b>						
Merchant fees(4)	W 176	W 195	W 146	W 200	W 188	W 211
Other fees	4	23	8	2	10	5
<b>Total</b>	<b>W 180</b>	<b>W 218</b>	<b>W 154</b>	<b>W 202</b>	<b>W 198</b>	<b>W 216</b>



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	2003		2004		2005	
	Shinhan Card	Chohung Bank(1)	Shinhan Card	Chohung Bank(1)	Shinhan Card	Chohung Bank(1)
<b>(In billions of Won, except percentages)</b>						
<b>Charge volume:(5)</b>						
General purchases	W 3,695	W 5,484	W 4,835	W 5,519	W 6,255	W 6,039
Installment purchases	1,143	2,505	1,247	2,099	1,650	2,003
Cash advances	6,805	12,585	4,355	6,875	3,488	5,564
<b>Total</b>	<b>W 11,643</b>	<b>W 20,574</b>	<b>W 10,437</b>	<b>W 14,493</b>	<b>W 11,393</b>	<b>W 13,606</b>
<b>Outstanding balance (at year end):(6)</b>						
General purchases	W 395	W 455	W 456	W 538	W 539	W 528
Installment purchases	455	786	292	563	333	497
Cash advances	725	1,025	474	653	423	575
Revolving purchases	39	484	158	200	89	199
Card loans	329	745	233	529	255	289
Others	489	185	376	213	284	190
<b>Total</b>	<b>W 2,432</b>	<b>W 3,680</b>	<b>W 1,989</b>	<b>W 2,696</b>	<b>W 1,923</b>	<b>W 2,278</b>
Average balance	W 2,212	W 4,957	W 2,186	W 3,288	W 1,916	W 2,618
<b>Delinquent balances:(7)</b>						
From 1 day to 1 month	W 173	W 376	W 67	W 109	W 49	W 92
<b>Over 1 month:</b>						
From 1 month to 3 months	W 80	W 150	W 35	W 71	W 17	W 31
From 3 months to 6 months	71	172	38	44	18	29
Over 6 months						
<b>Sub-total</b>	<b>151</b>	<b>322</b>	<b>73</b>	<b>115</b>	<b>35</b>	<b>60</b>
<b>Total</b>	<b>W 324</b>	<b>W 698</b>	<b>W 140</b>	<b>W 224</b>	<b>W 84</b>	<b>W 152</b>
<b>Delinquency ratios:(8)</b>						
From 1 day to 1 month	7.11%	10.22%	3.37%	4.04%	2.53%	4.04%
<b>Over 1 month:</b>						
From 1 month to 3 months	3.29%	4.08%	1.76%	2.63%	0.87%	1.34%
From 3 months to 6 months	2.92	4.67	1.91	1.63	0.95	1.30
Over 6 months(9)						

Sub-total		6.21		8.75		3.67		4.27		1.82		2.64
Total		13.32%		18.97%		7.04%		8.33%		4.36%		6.68%
Rewritten loans(10)	W	25	W	680	W	9	W	495	W	4	W	269
Gross charge-offs	W	290	W	1,304	W	223	W	649	W	94	W	227
Recoveries		32		58		20		35		25		47
Net charge-offs	W	258	W	1,246	W	203	W	614	W	69	W	180
Gross charge-off ratio(11)		13.11%		26.31%		10.20%		19.74%		4.92%		8.66%
Net charge-off ratio(12)		11.66%		25.14%		9.29%		18.67%		3.62%		6.87%

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*Notes:*

- (1) Represents the credit card business of Chohung Bank, consisting of both BC Card and Forever Card, which we acquired in 2003. Effective as of April 3, 2006, the credit card division of Chohung Bank was split off and merged into Shinhan Card.
- (2) Card loans consist of loans that are provided on either a secured or unsecured basis to cardholders upon prior agreement. Payment of principal, fees and interest on such a loan can be due either in one payment or in installments after a fixed period.
- (3) Revolving purchases were introduced in October 1998 for certain creditworthy credit card customers (e.g., customers who have not been delinquent for more than three times in the past one year) of Shinhan Card and in March 25, 2000 for certain creditworthy credit card customers of Chohung Bank.
- (4) Merchant discount fees consist of merchant membership and maintenance fees, charges associated with prepayment by Shinhan Card or Chohung Bank (on behalf of customers) of sales proceeds to merchants, processing fees relating to sales and membership applications.
- (5) Represents the aggregate cumulative amount charged during the year.
- (6) Represents amounts before allowance for loan losses.
- (7) Includes the unbilled balances of installment purchases.
- (8) Represents the ratio of delinquent balances to outstanding balances for the year.
- (9) Our charge-off policy for Shinhan Card (and Chohung Bank prior to the split-merger of its credit card division into Shinhan Card) has been to charge off all credit card balances which are 180 days past due.
- (10) Represents delinquent credit card balances for purchase and cash advance which have been rewritten as credit card loans, thereby reducing the balance of delinquent accounts.
- (11) Represents the ratio of gross charge-offs for the year to average balance for the year.
- (12) Represents the ratio of net charge-offs for the year to average balances for the year.

*Supervisory Statistical Information prepared in accordance with Korean GAAP*

Due to the rapid increase in consumer debt in Korea in recent years, the Korean government has adopted a series of regulations designed to restrain the rate of growth in, and delinquencies of, cash advances, credit card loans and credit card usage generally and to strengthen the reporting of, and compliance with, credit quality indexes. The Financial Supervisory Commission and the Financial Supervisory Service have announced a number of changes to the rules governing the reporting of credit card balances, as well as the procedures governing which persons may receive credit cards. In addition, the Korean government has also revised the calculation formula for capital adequacy ratios and delinquency ratios applicable to credit card companies, imposing sanctions against credit card companies with capital adequacy ratios of 8% or below and/or delinquency ratios of 10% or above. These computations are all based on financial information prepared in accordance with Korean GAAP, as required by regulatory guidelines, which differs significantly from U.S. GAAP. As of December 31, 2003, 2004 and 2005, under Korean GAAP, Shinhan Card's delinquent balances (defined as credit card accounts delinquent for over 30 days) were W266 billion, W121 billion and W57 billion, respectively, representing delinquency ratios (defined as the ratio of delinquent balances to outstanding balances) of 11.01%, 6.03% and 2.96%, respectively. As of December 31, 2003, 2004 and

2005, calculated on the same basis, Chohung Bank's delinquent credit card balances, were W274 billion, W97 billion and W51 billion, respectively, representing delinquency ratios of 7.42%, 3.60% and 2.25%, respectively. In certain cases, credit card companies in Korea have been allowed to rewrite delinquent credit card balances for purchase and cash advance as credit card loans, thereby reducing the balance of delinquent accounts. Delinquent credit card balances that were rewritten as loans as of December 31, 2003, 2004 and 2005, under Korean GAAP, were W27 billion, W10 billion and W4 billion, respectively, for Shinhan Card and W682 billion, W497 billion and W270 billion, respectively, for Chohung Bank. Net charge-offs for Shinhan Card, under Korean GAAP, during 2003, 2004 and 2005 were W260 billion, W212 billion and W88 billion, respectively, representing net charge-off ratios (defined as the ratio of net charge-offs for the year to average balances for the year) of 10.10%, 9.70% and 5.07%, respectively. Net charge-offs for Chohung Bank, under

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Korean GAAP, during 2003, 2004 and 2005 were W1,266 billion, W625 billion and W180 billion, respectively, representing net charge-off ratios (defined as the ratio of net charge-offs for the year to average balance for the year) of 10.07%, 9.88% and 6.90%, respectively. As of December 31, 2005, Shinhan Card's adjusted equity capital ratio was 17.68%. Credit card business of Chohung Bank is not subject to such adjusted equity capital ratio requirement.

*Recent Regulatory Changes*

Under the Specialized Credit Financial Business Act, as amended on June 16, 2004, and other related regulations, the formula for calculating capital adequacy ratios for each credit card company was revised to increase the proportion of adjusted total assets by including certain risk-weighted asset-backed securitization assets which may incur contingent liability. In addition, the Financial Supervisory Service changed the standards for calculating the delinquency ratios by including delinquent balances that were rewritten as credit card loans in the calculation of such ratios as if such underwriting of rewritten loans had not occurred (referred to as substantial delinquency ratio herein). This resulted in credit card companies and credit card businesses of commercial banks reporting higher delinquency ratios in 2004 as compared to prior years, despite the improvement in asset quality of credit card assets. On a pro forma basis, the substantial delinquency ratios for the Korean credit card industry as announced by the Financial Supervisory Service were 28.28% as of December 31, 2003, 25.12% as of June 30, 2004, 18.25% as of December 31, 2004, 13.27% as of June 30, 2005, 10.05% as of December 31, 2005 and 8.77% as of March 31, 2006.

Further, in July 2004, the Financial Supervisory Service required each credit card company with a substantial delinquency ratio of 10% or more to enter into a memorandum of understanding with the Financial Supervisory Service specifying the credit card company's proposed plan to reduce its substantial delinquency ratio to less than 10% by the end of 2006 in accordance with the Specialized Credit Financial Business Act. Since the substantial delinquency ratio of Shinhan Card was less than 10%, Shinhan Card did not enter into such a memorandum of understanding.

*Personal Workout and Debt Forgiveness Program*

In an effort to resolve the problems caused by consumer credit delinquencies, the Korean government established Hanmaum Financial Company and the Credit Counseling & Recovery Service on May 20, 2004. Hanmaum Financial Company is a so-called bad bank, a type of private asset management company that acquires non-performing assets from banks and other financial institutions for the purpose of providing long-term financial aid to certain qualified delinquent consumers who apply for this program to enable them to pay off their financial debts. After restructuring delinquent debts of approximately 170,000 consumers, Hanmaum Financial Company was wound down. The Korean government established a second bad bank known as Himangmoah in May 2005 to aid the delinquent consumers who did not benefit from Hanmaum Financial Company despite being qualified to do so. The second bad bank provides relief by collecting 3% of the debt amount in advance, allowing delinquent cardholders to repay their delinquent debts within eight years. The second bad bank raises its funds to purchase the delinquent debts from financial institutions through a special purpose company in an asset-backed securitization transaction. The second bad bank distributes the debt amount collected in excess of the initial purchase price to the selling financial institutions. At this time, we cannot accurately predict the number of applicants and amounts subject to the second bad bank program. To the extent the second bad bank achieves less-than-expected level of collection of, and recovery on, non-performing assets, commercial banks and credit card companies, including Shinhan Bank, Chohung Bank and Shinhan Card, may realize less gains from recoveries.

Unlike the bad bank program that provides loans directly to consumers, the Credit Counseling & Recovery Service has adopted an individual workout program. For delinquent consumers who are deemed to be capable of repaying their debts, the Credit Counseling & Recovery Service will, pursuant to an agreement with the creditor financial institution, provide opportunities to repay in installments, provide repayment grace periods, reduce debt amounts, or extend the maturity date of the debts. Currently, approximately 185 financial institutions, including banks and insurance companies, are parties to the Credit Recovery Support Agreement, pursuant to which such financial institutions, have agreed to provide such support described above to those

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consumers who meet the following qualifications: (i) income exceeding minimum living expenses promulgated by the Ministry of Health and Welfare of Korea, (ii) debt not exceeding W500 million in total amount, and (iii) official records being on file at Korea Federation of Banks as to the default status of debt. Each application for credit recovery is reviewed by the Credit Counseling & Recovery Service and approval of each application requires the approval by creditors representing at least one-half of the unsecured debt amount and at least two-thirds of the secured debt amount.

In September 2004, a court-administered individual workout program was adopted under the Individual Debtor Recovery Act. Under this program, a qualified individual debtor may file a petition for an individual workout program with a competent court. Subject to the court's approval, the debtor may repay the debt over a period of less than five years (or from three to eight years for those debtors who filed before the effective date of the Debt Recovery and Bankruptcy Act and continue to be subject to the Individual Debtor Recovery Act) and will be exempted from other debts without declaring bankruptcy. To qualify, an individual delinquent debtor must have less than W500 million in debt (in the case of unsecured debt) or W1 billion in debt (in the case of secured debts), and must have regular and reliable income or have the potential to earn recurring income on an ongoing basis.

The Debtor Recovery and Bankruptcy Act, promulgated on March 31, 2005 and effective as of April 1, 2006, consolidated all existing bankruptcy-related laws in Korea, namely, the Corporate Reorganization Act, the Composition Act, the Bankruptcy Act and the Individual Debtor Recovery Act. See Description of Assets and Liabilities Credit Exposures to Companies in Workout, Court Receivership and Composition .

***Treasury and Securities Investment***

Through relevant departments at the newly merged Shinhan Bank, we engage in treasury and securities investment business, which involves, among other things, the following activities:

treasury;

securities investment and trading;

derivatives trading; and

international business.

***Recent Regulatory Changes***

The formation and operation of private equity funds were permitted as of October 5, 2004 under the Act on Business of Operating Indirect Investment and Asset. The purpose of a private equity fund is to provide diverse investment opportunities for qualified investors and to utilize funds in the market place for mergers and acquisitions or corporate restructuring. In April 2006, the Government amended the Presidential Decree of the Act on Business of Operating Indirect Investment and Asset and regulations thereunder in order to facilitate the formation and operation of private equity funds by lowering the required minimum equity investment, relaxing the mandatory investment ratio, allowing the value of the purchased shares of listed companies to be estimated by the purchase price of such shares reflecting control premium as well as its market price and allowing private equity funds to invest in non-performing loans. The key provisions of the Act on Business of Operating Indirect Investment and Asset relating to private equity funds are as follows:

A private equity fund is a limited partnership company that is incorporated in accordance with the Korean Commercial Code, which has not less than one general partner and not less than one limited partner.

The minimum value of the equity investment by limited partners is W1 billion for an individual investor or W2 billion for a legal entity.

Details of the private equity fund, such as its objective, name, location, term of existence, information concerning partners, a summary of the operation, shall be registered with the Financial Supervisory Service.



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A private equity fund shall apply 50% of its assets (provided that, if the Fund (as defined under the Framework Act on Fund Management) is a partner and its method of contribution is other than as capital commitment, such contribution shall be excluded from the calculation of assets), within two years after capital injection by the partners, to (1) an investment in excess of 10% of the total number of shares issued by the target company, (2) an investment that makes it possible for the private equity fund to exercise *de facto* control over major corporate governance matters including appointments and dismissals of officers, (3) an investment in Investment Securities (as defined under the Act on Business of Operating Indirect Investment and Asset) issued by SOC Investment Companies (as defined under the Promotion of Social Overhead Capital Investment Act) or (4) an investment in securities or equities of Investment Purpose Companies (as defined under the Act on Business of Operating Indirect Investment and Asset) under the Act on Business of Operating Indirect Investment and Asset. In addition, a private equity fund shall hold the acquired shares for at least six months following the date of investment.

As a special rule, if a private equity fund meets the above requirements for investment, for ten years from the date on which such requirements are met, (1) the provisions governing holding companies as provided in the Monopoly Regulation and Fair Trade Act shall not apply and (2) the private equity fund shall not be deemed a financial holding company as provided in the Financial Holding Companies Act.

In May 2005, the amendment to the Presidential Decree of the Act on Business of Operating Indirect Investment and Asset allowed a direct or indirect subsidiary of a financial holding company to invest as a limited partner in a private equity fund which is another direct or indirect subsidiary of the same financial holding company. Prior to such amendment, under the Financial Holding Companies Act, a direct or indirect subsidiary of a financial holding company was prohibited from acquiring the shares of another subsidiary of the same financial group.

In addition, pursuant to the amendment of the Presidential Decree of the Act on Business of Operating Indirect Investment and Asset and regulations thereunder in April 2006, in an effort to relax the regulatory barriers to the business of operating indirect investment, when the asset management companies operate indirect investment assets, such companies are allowed to engage in trading certain derivatives or borrowing Investment Securities (as defined under the Act on Business of Operating Indirect Investment and Asset), and the maximum limit by such companies to invest in notes issued by government-invested organization and in foreign loans has increased.

*Treasury*

At Shinhan Bank, the Treasury Department provides funds to all of its business operations and ensures the liquidity of Shinhan Bank's operation and, at Chohung Bank, the Treasury & International Group provided funds to all of its business operations and ensures the liquidity of its banking operation. To secure long-term stable funds, we use fixed and floating rate notes, debentures, structured financing, and other advanced funding methods. As for overseas funding, we constantly explore the feasibility of raising funds in currencies other than the U.S. dollar, such as Japanese Yen and the Euro. In addition, Shinhan Bank makes (and prior to the merger, Chohung Bank made) call loans and borrow call money in the short-term money market. Call loans are short-term lending among banks and financial institutions in either Korean Won or foreign currencies, in amounts exceeding W100 million, with maturities of 30 days or less. Typically, call loans have maturities of one day.

*Securities Investment and Trading*

We invest in and trade securities for our own account in order to maintain adequate sources of liquidity and generate interest and dividend income and capital gains. Our trading and investment portfolios consist primarily of Korean treasury securities and debt securities issued by Korean government agencies, local governments or certain government-invested enterprises and debt securities issued by financial institutions. Our equity securities consist of equities listed on the Stock Market and KOSDAQ Market of Korea

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Exchange. For a detailed description of our securities investment portfolio, see Description of Assets and Liabilities Investment Portfolio .

Prior to the merger, Chohung Bank focused on reducing risks in its securities investment portfolio. Chohung Bank had limited its investment in equity securities and discontinued its trading in equity securities in 2000 to contain its exposure to market risk.

*Derivatives Trading*

We provide and trade a range of derivatives products. The derivatives products that we offer, through Shinhan Bank (and prior to the merger, also through Chohung Bank), include:

Interest rate swaps and futures relating to Korean Won interest rate risks and LIBOR risks, respectively;

Cross-currency swaps largely for Korean Won against U.S. dollars, Japanese Yen and Euros;

Foreign currency forwards, swaps and options;

Credit derivatives; and

KOSPI 200 indexed equity options.

Shinhan Bank's trading volume in terms of notional amount was W90,696 billion, W102,226 billion and W179,762 billion in 2003, 2004 and 2005, respectively, and Chohung Bank's trading volume in terms of notional amount was W117,946 billion, W151,482 billion and W186,761 billion in 2003, 2004 and 2005, respectively. Such derivative operations have focused on addressing the needs of our corporate clients to hedge their risk exposure and back-to-back derivatives entered into to hedge our risk exposure that results from such client contracts.

We also enter into derivative trading contracts to hedge the interest rate and foreign currency risk exposure that arise from our own assets and liabilities. Many of these nontrading derivative contracts, however, do not qualify for hedge accounting under U.S. GAAP and are accordingly accounted for as trading derivatives in the financial statements. In addition, on a limited basis, we engage in proprietary trading of derivatives within our regulated open position limits. See Description of Assets and Liabilities Derivatives .

*International Business*

We are also engaged in treasury and trading and securities investment in international capital markets, principally engaged in foreign currency denominated securities trading, foreign exchange trading and services, trade-related financial services, international factoring services and foreign retail banking operations through our overseas branches and subsidiaries. Due to the volatility in the Asian capital markets since the economic and financial crisis of the late 1990's, we had reduced our international capital markets activities and our international securities investment portfolio. We currently plan to resume these activities.

*Other Banking Services*

The revenue-generating activities in other banking services of Shinhan Bank (and prior to the merger, also of Chohung Bank) consist primarily of their respective trust account management services. As a result, our discussion in this subsection will focus on our trust account management services.

*Trust Account Management Services*

*Overview*

Our trust account management services offer trust accounts managed by the banking operations of Shinhan Bank (or, prior to the merger, Chohung Bank) consisting primarily of money trusts. In Korea, a money trust is a discretionary trust over which (except in the case of a specified money trust) we have

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investment discretion (subject to applicable law) and is commingled and managed jointly for each type of trust account. The specified money trusts are established on behalf of customers who give us specific directions as to the investment of trust assets. Trust account customers are typically individuals seeking higher rates of return than those offered by bank account deposits. Because there are fewer regulatory restrictions on trust accounts than on bank account deposits, including no deposit reserve requirements, we have historically been able to offer higher rates of return on trust account products than on bank account deposits. Trust account products, however, generally require higher minimum deposit amounts compared with comparable bank account deposit products. Assets of the trust accounts are invested primarily in securities and loans, except that a greater percentage of the assets of the trust accounts are invested in securities compared to the bank accounts because trust accounts generally require more liquid assets due to their limited funding source compared to bank accounts. As a result of the recent low interest environment, we have not been able to offer attractive rates of return on our trust account products.

Under Korean law, assets accepted in trust accounts are segregated from other assets of the trustee bank and are not available to satisfy the claims of the depositors or other creditors of such bank. Accordingly, trust accounts are accounted for and reported separately from the bank accounts. See *Supervision and Regulation*. Trust accounts are regulated by the Trust Act, the Trust Business Act and the Act on Business of Operating Indirect Investment and Asset of Korea and most national commercial banks offer similar trust account products. We earn income from trust account management services, which is reflected in our accounts as net trust management fees. See *Item 5. Operating and Financial Review and Prospects Operating Results Noninterest Income*.

Under U.S. GAAP, generally, we have not consolidated trust accounts in our financial statements except for the Guaranteed Fixed Rate Trust Accounts or recognized the acquisition of such accounts in accordance with the purchase method of accounting due to the fact that these are not our assets but customer assets. As of December 31, 2003, 2004 and 2005, under Korean GAAP, Shinhan Bank had total trust assets of W14,472 billion, W14,099 billion and W15,386 billion, respectively, comprised principally of securities investments of W5,425 billion, W4,855 billion and W5,422 billion, respectively, and loans in the principal amount of W280 billion, W357 billion and W291 billion, respectively. Securities investments consisted of corporate bonds, government-related bonds and other securities, primarily commercial paper. As of December 31, 2003, 2004 and 2005 under Korean GAAP, equity securities constituted 5.9%, 6.0% and 4.3%, respectively, of our total trust assets. Loans made by trust accounts are similar in type to those made by our bank accounts, except that they are made only in Korean Won. As of December 31, 2003, 2004 and 2005, under Korean GAAP, approximately 84.6%, 65.1% and 68.5%, respectively, of the amount of loans from the trust accounts were collateralized or guaranteed. In making investment from funds received for each trust account, each trust product maintains investment guidelines applicable to each such product which sets forth, among other things, company, industry and security type limitations.

As of December 31, 2003, 2004 and 2005, under Korean GAAP, Chohung Bank had total trust assets of W4,262 billion, W4,634 billion and W6,289 billion, respectively, comprised principally of securities investments of W3,746 billion, W3,361 billion and W3,455 billion, respectively, and loans in the principal amount of W150 billion, W59 billion and W86 billion, respectively. Securities investments consisted of corporate bonds, government-related bonds and other securities, primarily commercial papers. As of December 31, 2003, 2004 and 2005, under Korean GAAP, equity securities constituted 10.5%, 10.1% and 7.0%, respectively, of our total trust assets. Loans made by trust accounts are similar in type to those made by our bank accounts, except that they are made only in Korean Won. As of December 31, 2003, 2004 and 2005, under Korean GAAP, approximately 39.9%, 84.3% and 93.0%, respectively, of the amount of loans from the trust accounts were collateralized or guaranteed. In making investment from funds received for each trust account, each trust product maintains investment guidelines applicable to such product which sets forth, among other things, issuer, industry and security type limitations.

The balance of the money trusts managed by our trust account business was W9,837 billion as of December 31, 2005 under Korean GAAP, showing an increase of 4.3% compared to W9,412 billion as of December 31, 2004, consisting of W6,175 billion with Shinhan Bank and was W3,662 billion with Chohung Bank.

**Table of Contents***Trust Products*

Our trust account management services offer individuals primarily two basic types of money trust accounts: guaranteed fixed rate trusts and variable rate trusts.

*Guaranteed Fixed Rate Trust Accounts.* Guaranteed fixed rate trust accounts offer customers a fixed-rate of return and guaranteed principal. We receive any amounts remaining after taking into account the guaranteed return and all expenses of the trust accounts, including provisions for valuation losses on equity securities, loan losses and special reserves. We maintain two types of guaranteed fixed rate trust accounts: general unspecified money trusts and development money trusts. Korean banks, including Shinhan Bank (and, prior to the merger, Chohung Bank), have been restricted from establishing new general unspecified money trusts since January 1, 1996, and development money trusts effective January 1, 1999. As a result, the size of general unspecified money trusts and development money trusts has decreased substantially and most of development money trusts matured by the end of 2001 and most of general unspecified money trusts matured by the end of 2002. As of December 31, 2003, 2004 and 2005, under Korean GAAP, Shinhan Bank's development money trusts amounted to W0.2 billion, W0.04 billion and W0.04 billion, respectively, and general unspecified money trusts amounted to an aggregate of W0.3 billion, W0.2 billion and W0.2 billion, respectively. As of December 31, 2005, under Korean GAAP, Chohung Bank's development trusts had no outstanding balance and general unspecified money trusts amounted to an aggregate of W9.1 billion. See Note 35 of our consolidated financial statements in Item 18. Financial Statements Notes to consolidated financial statements of Shinhan Financial Group .

*Variable Rate Trust Accounts.* Variable rate trust accounts are trust accounts for which we do not guarantee the return on the trust account but, in certain instances described below, the principal of the trust account is guaranteed. In respect of variable rate trust accounts, we are entitled to receive fixed rate of trust fees. We also receive fees upon the termination of trust accounts prior to their stated maturities. However, the recent trend has been to offer products with stated maturities that are significantly shorter than those offered in the past, resulting in lower fees from early termination.

We are required to set aside allowances for trust assets which are not marked to market and provide special reserves under Korean GAAP for principal guaranteed variable rate trust accounts in addition to guaranteed fixed rate trust accounts. Provisions for variable rate trust assets that are not marked to market are reflected in the rate of return to customers, and thus, have no impact on our income while provisions for guaranteed fixed rate trust accounts could reduce our income in case of a deficiency in the payment of the guaranteed amount. We provide special reserves with respect to guaranteed fixed rate and principal-guaranteed variable rate trust account credits by deducting the required amounts from trust fees for such trust accounts in accordance with the Trust Act and Trust Business Act.

Korean banks are currently allowed to guarantee the principal of the following types of variable rate trust account products: (i) existing individual pension trusts, (ii) new individual pension trusts, (iii) existing retirement pension trusts, (iv) new retirement pension trusts, (v) pension trusts and (vi) employee retirement benefit trusts.

*Payments from Bank Accounts to Guaranteed Fixed Rate Trust Accounts.* If income from a guaranteed fixed rate trust account is insufficient to pay the guaranteed amount, such deficiency must be satisfied from (i) first, special reserves maintained in such trust accounts, (ii) secondly, trust fees and (iii) lastly, funds transferred from the bank accounts of Shinhan Bank (or, prior to the merger, Chohung Bank), as the case may be. Chohung Bank recorded zero or a negligible amount of such obligations as of December 31, 2003, 2004 and 2005. Shinhan Bank made no such payments from its bank accounts to cover such deficiencies during 2003, 2004 and 2005, primarily due to a decrease in the balance of Shinhan Bank's guaranteed fixed rate trust accounts, which resulted from the legal prohibition against providing such accounts beginning in 1996 with respect to general unspecified money trusts and beginning in 1999 for development money trusts, as well as the improving economic condition in Korea. The decrease in the balance of Shinhan Bank's guaranteed fixed rate trust accounts, in turn, has generally translated into a decrease in non-performing credits. There can be no assurance, however, that such transfers will not be required in the future.

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*Distribution Channels and Marketing*

We distribute our trust products primarily through the branch network of our retail banking services. See Our Branch Network and Distribution Channels above.

*Recent Regulatory Developments*

Under the Act on Business of Operating Indirect Investment and Asset, which took effect on January 5, 2004, all banks engaged in the money trust business (except for specified money trust business) based on their approval received under the Trust Business Act must qualify as an asset management company by July 5, 2004 and will not be permitted to offer unspecified money trust products after such date (except under certain limited circumstances). Once a bank qualifies as an asset management company under the Act on Business of Operating Indirect Investment and Asset, such bank may continue to engage in the investment trust business as long as it is limited to investment trust products and does not include unspecified money trust products. As a result, we ceased offering unspecified money trust account products from our banking subsidiaries and instead began to offer products developed by our asset management business that fulfills the requirements as an asset management company.

***Securities Brokerage Services***

*Overview*

Through Good Morning Shinhan Securities, our securities brokerage subsidiary, we provide a full range of brokerage services, including investment advice and financial planning, to our retail customers as well as international and institutional brokerage services to our corporate customers. As of December 31, 2005, our market share was approximately 5.62% in the Korean equity brokerage market and is ranked seventh in the industry in terms of brokerage volume.

*Recent Regulatory Changes*

The Presidential Decree of the Securities and Exchange Act and regulations thereof, recently amended the scope of securities to include derivative securities (including, without limitation, credit linked derivative securities) and equity of limited partnerships such as private equity funds. Furthermore, securities company can provide trust account management services in accordance with the Trust Business Act. See Item 4. Information on the Company Supervision and Regulation Principle Regulation Applicable to Securities Companies. Good Morning Shinhan Securities is taking steps to provide the trust account management services.

*Products and Services*

We offer a variety of financial and advisory services through three main business groups of Good Morning Shinhan Securities, consisting of the Retail Business Division, the Institutional & International Client and Research Division and Capital Markets Division.

*Retail Business Division* provides equity and bond brokerage, investment advisory and financial planning services to retail customers, with a focus on high net worth individuals. In 2005, revenues generated by the Retail Business Division represented approximately 58.8% of total revenues of our Securities Brokerage Services in 2005. The Retail Business Division earns fees by managing client assets as well as commissions as a broker for our clients in the purchase and sale of securities. In addition, we generate net interest revenue by financing customers securities transactions and other borrowing needs through security-based lending and also receive commissions and other sales and service revenues through the sale of proprietary and third-party mutual funds.

*Institutional & International Client and Research Division* offers a variety of brokerage services, including brokerage of corporate bonds, futures and options, to our institutional and international customers. In addition, through our research center with more than 50 research analysts, we produce equity, bonds and derivatives research to serve both institutional and international investor clients.

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*Capital Markets Division* offers a wide array of investment banking services, including selling institutional financial products and trading equity and derivatives and, to a lesser extent, M&A advisory and underwriting, to our corporate customers.

***Other Services***

Through our other operating subsidiaries, we also provide leasing and equipment financing, investment trust management, regional banking and investment banking and advisory services. In addition, we have also established a bancassurance joint venture to offer life insurance and other insurance-related products and services following deregulation of this industry in September 2003. In December 2005, we also acquired a life insurance company to offer a diversified range of life insurance products in addition to bancassurance services. See *Life Insurance* below.

***Leasing and Equipment Financing***

We provide leasing and equipment financing services to our corporate customers through Shinhan Capital, our leasing subsidiary. Established as a leasing company in 1991, Shinhan Capital provides customers with leasing, installment financing and new technology financing.

As of December 31, 2005, Shinhan Capital's total assets were W1,401 billion, showing a W80 billion increase from the previous year. In particular, our operating assets increased from W1,061 billion in 2003 to W1,091 billion in 2004 and to W1,287 billion in 2005. We believe that our strength is in leasing of ships, printing machines, automobiles and other specialty items. We continue to diversify our revenue base from this business by expanding our services, as demonstrated by our acting as corporate restructuring company for financially troubled companies beginning in 2002 and financing provided to real estate projects and infrastructure investments. Shinhan Capital's profitability continued to improve and stabilize gradually over the past few years. Shinhan Capital's operating income increased from W145 billion in 2003 to W221 billion in 2004 and W222 billion in 2005, and its net income increased from W16 billion in 2003 to W23 billion in 2004 and W37 billion in 2005.

***Investment Trust Management Services***

In addition to personalized asset management services provided by our private banking and securities brokerage services, we also provide our customers with investment trust services through Shinhan BNP Paribas Investment Trust Management, our 50:50 joint venture with BNP Paribas, and through SH Asset Management, previously known as Chohung Investment Trust Management Co., Ltd. These companies offer a broad range of asset management products and services such as beneficiary certificates, mutual funds, closed-end funds and separately managed accounts to domestic institutional, high net worth and retail clients. As a joint venture with BNP Paribas Asset Management, Shinhan BNP Paribas ITMC intends to focus on providing products using the skills of BNP Paribas while SH Asset Management will focus on local market products.

The asset management industry in Korea is under transformation since the enactment of the *Act on Business of Operating Indirect Investment and Asset* in 2004 which deregulated many restrictions on investment assets and improved investors' rights in various ways. With improved corporate governance structure and transparency, more investors started to show interest on the asset management industry's products as an alternative form of investment. Such move, especially among retail customers, became possible as the interest rate continues to be low and the government adopted several measures to hold down real estate prices. Accordingly, Shinhan BNP Paribas Investment Trust Management's total assets under management grew from W6,071 billion as of the end of 2004 to W7,353 billion as of the end of 2005 and SH Asset Management, formerly known as Chohung Investment Trust Management Co., Ltd., from W6,427 billion as of the end of 2004 to W7,788 billion as of the end of 2005. Although competition among asset management companies in Korea has intensified, Shinhan BNP Paribas ITMC and SH Asset Management seek to maintain profitability by providing high quality services to local customers.

**Table of Contents***Regional Banking Services*

In April 2002, pursuant to a stock purchase agreement with Korea Deposit Insurance Corporation, we acquired a majority interest in Jeju Bank, which is engaged in providing commercial banking services on a regional basis, primarily on Jeju Island of Korea, through its network of 32 branches. As of December 31, 2005, Jeju Bank had total assets, total liabilities and total stockholders' equity of W2,051 billion, W1,932 billion and W119 billion, respectively.

*Investment Banking and Advisory Services*

In addition to the investment banking services provided by the Investment Banking Department of Shinhan Bank (and prior to the merger, also the Investment Banking Division of Chohung Bank) and the Capital Markets Division of Good Morning Shinhan Securities, we also provide a variety of investment banking and advisory services through Shinhan Macquarie Financial Advisory, our 51:49 joint venture with Macquarie Bank of Australia. The advisory services offered by Shinhan Macquarie Financial Advisory ( SMFA ) include project and infrastructure finance, capital and debt raisings, corporate finance advisory, structured finance, mergers and acquisitions, cross-border leasing and infrastructure and specialized fund management advisory services. Since its inception SMFA has grown to become one of the leading infrastructure-related financial advisory companies. During the year ended December 31, 2005, we derived total revenues of W24.5 billion from advisory activities.

*Bancassurance*

Since the deregulation of the Korean bancassurance market in September 2003, SH&C Life Insurance, our 50:50 joint venture with Cardif S.A., an insurance arm of the BNP Paribas Group, has developed various bancassurance products for our customers. In 2003 and 2004, the volume of bancassurance market grew significantly as the banks took aggressive steps to establish market shares, but this growth slowed in 2005 due to substantial market penetration. As a result of such steps, the total sales volume of the banks in Korea from initial insurance premium increased from W399 billion in 2003 to W2,255 billion in 2004 and to W2,395 billion in 2005, which represented approximately 47.8% of the total new sales volume of life insurance in Korea during 2005. Regulatory restrictions on the bancassurance products may be further liberalized in the future, which may lead to further growth of the bancassurance market. In response, the traditional insurance companies with low penetrations in the bancassurance business have collectively lobbied for new regulatory restrictions on bancassurance business, which may significantly affect the growth of the banks' revenue from the bancassurance business in 2006.

During the growth of the bancassurance industry in 2004, largely due to synergy effects from our group-wide marketing and sales channels, SH&C Life Insurance ranked fourth among companies in Korea offering bancassurance products in terms of the number of policies sold and recorded profit after two years of losses since its inception.

*Life Insurance*

Shinhan Life Insurance, a mid-tier insurance company with diversified distribution channels with balanced growth in the number of financial planners, telemarketers, account managers and bancassurance specialists, became our subsidiary on December 13, 2005. Shinhan Life Insurance has a leading telemarketing channel in the industry.

As of December 31, 2005, Shinhan Life Insurance's total assets were W5,129.3 billion, which increased from W4,056 billion as of December 31, 2004 and W3,205 billion as of December 31, 2003. Based on the insurance premium received during its fiscal year 2005, Shinhan Life Insurance ranked sixth among the 22 life insurance companies in Korea.

We expect the insurance premium received by Shinhan Life Insurance to increase as a result of growing demands for both investment-type and annuity-type products and potential synergy effects from interactions between Shinhan Life Insurance and our other subsidiaries.

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### *Loan Collection and Credit Reporting*

In order to centralize our loan collection, on July 8, 2002, we established Shinhan Credit Information Co. Ltd., our wholly-owned subsidiary engaged in credit collection and credit reporting. Shinhan Credit Information is capable of managing and collecting bad loans generated by our subsidiaries to improve our overall asset quality. We plan to expand Shinhan Credit Information's services to such areas as credit reporting, credit inquiry, credit card rating, civil application/petition services, lease and rental research and advisory and consulting services related to non-performing loan management. For the year ended December 31, 2005, our total revenues from this operation were W24 billion.

### *Internet Portal Financial Services*

In 2001, we established e-Shinhan Inc., a joint venture with The Boston Consulting Group to offer high-quality internet financial services. Through its portal site, *www.emoden.com*, e-Shinhan offers an integrated account aggregation service that enables the user to see all of his or her accounts at a glance, an electronic accounting service that keeps track of all the user's financial transactions, an investment clinic service and a financial supermarket service that helps users to choose the financial products that best meet their needs. To offer high quality financial portal service, we concluded business ties with Yodlee of the U.S., the world's leading account aggregation provider. At a shareholders meeting in August 2005, we resolved to liquidate e-Shinhan in light of the less-than-earlier volume in financial transactions attributable partly to the real-name regulatory requirements for online financial transactions, as well as the lower-than-expected brand recognition of e-Shinhan among the online customers in general. Following the liquidation of e-Shinhan in November 2005, we discontinued providing the following Internet-based electronic banking services: account consolidation, online bookkeeping, personalized financial management and corporate financial information portal management, among others. However, we do not believe the liquidation of e-Shinhan will have a material impact on the existing electronic banking services provided by our subsidiaries which are currently being provided at a competitive level. Furthermore, we believe our electronic banking services may be expanded by creating a financial network account that consolidates the different financial services provided by our subsidiaries and otherwise focuses on the potential synergy from linking the various services provided by our subsidiaries.

## **Information Technology**

We believe that a sophisticated information technology system is crucial in supporting our operations management and providing high quality customer service. We employ a total of approximately 1,070 employees and plan to spend approximately W560 billion in connection with updating and integrating our information technology system by the end of 2006.

In order to maximize synergy among our subsidiaries, we are currently continuing to build and implement a single enterprise information technology system known as "enterprise data warehouse" for our subsidiaries. In addition, we are currently continuing to upgrade the information technology systems for each of our subsidiaries to enhance the quality of our customer service specific to such subsidiary. We currently expect to complete the integration and upgrade of information technology system for our merged bank by the end of 2006. We are currently in the planning stage for the implementation of improved systems for our other subsidiaries, including Shinhan Card and Shinhan Life Insurance, with 2009 as the target completion date.

We plan to continue our efforts to improve our information technology systems by taking the following initiatives:

- building a customer-oriented system to provide customers with diversified and customized financial services;

- establishing a flexible platform which can quickly adapt to new financial products and services;

- introducing a group-wide strategic enterprise management system designed to facilitate swift managerial response;

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empowering the sales operation by a group-wide integrated enterprise data warehousing system and a group-wide integrated customer relationship management system, which are designed to provide us with comprehensive customer information, including transaction history, and thereby allow us to identify potential marketing and cross-marketing opportunities;

further upgrading our information system in respect of the New Basel Capital Accord (Basel II), the initial layout for which was completed in March 2006;

upgrading our information reporting system to enable us to monitor our internal control and to test its effectiveness and to enable us to comply with Section 404 of the Sarbanes-Oxley Act; and

developing IT functions to improve comprehensive back office functions, including deposit taking, lending and foreign exchange activities, at the branch office level.

Our information technology system for each of our subsidiaries is currently backed up on a real time basis. We have established a completely duplicative back-up IT system in different locations in Korea, depending on the subsidiary, to provide a back-up system in the event of any system failure of our primary information technology center located in the suburbs of Seoul. See Properties . We believe that, when the integration of the subsidiaries back-up systems is completed by the end of 2006 as currently planned, our information technology system at the group level will be able to fully resume operation within an hour even in the case of a complete disruption of the information technology system at our headquarters.

**Competition**

We compete principally with other national commercial banks in Korea, but also face competition from a number of additional entities, including regional banks, Korea's specialized banks and branches and subsidiaries of foreign banks operating in Korea, as well as various other types of financial service institutions, including savings institutions (such as mutual savings and finance companies and credit unions and credit cooperatives), investment institutions (such as securities brokerage firms, merchant banking corporations and asset management companies) and life insurance companies. Regulatory reforms in the Korean banking industry have increased competition among banks for deposits, generally leading to lower margins from lending activities. Prior to the beginning of the economic crisis in Korea in late 1997, there were 26 commercial banks, three development banks and four specialized banks. Due in part to the economic crisis, as of December 31, 1999, there were 17 commercial banks, two development banks and four specialized banks. Of these, two commercial banks were recapitalized by the Government. During 1999, four mergers were consummated and, in the first half of 2000, Korea First Bank sold its controlling interest to a foreign investor. In 2001, H&CB and Kookmin Bank merged to create the largest Korean bank in terms of assets. Also in 2001, Woori Bank restructured itself as a financial holding company and significantly realigned its businesses and products to compete with other larger banks in Korea. In December 2002, Hana Bank merged with Seoulbank. In 2003, Lone Star acquired a controlling interest in Korea Exchange Bank. In May 2004, Citibank, through its affiliate, completed a tender offer pursuant to which it purchased a substantial majority interest in KorAm Bank. In September 2004, KorAm Bank was renamed Citibank Korea. In April 2005, Standard Chartered Bank completed its acquisition of Korea First Bank, the seventh largest commercial bank in Korea in terms of asset size. In addition, in 2006, Kookmin Bank has entered into a definitive agreement to acquire Korea Exchange Bank from Lone Star pending regulatory approval. We believe that the financial industry in Korea, including banking, will continue to experience consolidation among institutions leading to increased competition in all areas in which we operate.

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As of December 31, 2005, Shinhan Bank and Chohung Bank were ranked fourth and sixth largest, respectively, in terms of total assets among Korean commercial banks based on information published by the Financial Supervisory Commission. Following the merger in April 2006, the newly merged Shinhan Bank is ranked second, after Kookmin Bank, in terms of total assets. In March and May 2005, Korea Deposit Insurance Corporation sold its controlling interests in Korea Investment Trust Company and Daehan Investment Trust Company, which had been acquired and recapitalized by the Korea Deposit Insurance Corporation on behalf of the Korean government due to the financial difficulties these companies were experiencing, to Dongwon Financial Holdings and Hana Bank, respectively. Dongwon Financial Holdings is the third financial holding company to be launched in Korea, and Hana Bank is currently the fourth largest commercial bank in Korea in terms of asset size. As a result, competition in the Korean financial and banking industry, in particular for high net worth and high profit customers, has intensified.

See Item 3. Key Information Risk Factors Risks Relating to Competition Competition in the Korean banking industry, in particular in the small- and medium-sized enterprises banking, retail banking and credit card operations, is intense, and we may experience declining margins as a result .

**Table of Contents****DESCRIPTION OF ASSETS AND LIABILITIES**

*Unless otherwise specifically mentioned or the context otherwise requires, the following description of assets and liabilities is presented on a consolidated basis under U.S. GAAP.*

**Loans**

As of December 31, 2005, our total gross loan portfolio was W105,848 billion, which represented an increase of 9.0% from W97,080 billion at December 31, 2004. The increase in the portfolio primarily reflects an increase in the mortgage and home equity loans and other commercial loans.

**Loan Types**

The following table presents our loans by type for the periods indicated. Except where specified otherwise, all loan amounts stated below are before deduction for loan loss allowances. Total loans reflect our loan portfolio, including past due amounts.

		As of December 31,				
		2001	2002	2003	2004	2005
		(In billions of Won)				
<b>Corporate</b>						
	Commercial and industrial(1)	W 13,459	W 15,800	W 35,617	W 35,653	W 35,728
	Other commercial(2)	6,748	9,352	17,378	17,988	21,409
	Lease financing	598	636	1,091	981	754
<b>Total</b>	<b>Corporate</b>	<b>20,805</b>	<b>25,788</b>	<b>54,086</b>	<b>54,622</b>	<b>57,891</b>
<b>Consumer</b>						
	Mortgages and home equity	7,253	11,539	20,517	22,180	25,840
	Other consumer(3)	3,537	4,962	14,580	15,546	17,875
	Credit cards	2,070	2,763	6,112	4,732	4,242
<b>Total</b>	<b>Consumer</b>	<b>12,860</b>	<b>19,264</b>	<b>41,209</b>	<b>42,458</b>	<b>47,957</b>
	<b>Total gross loans(4)</b>	<b>W 33,665</b>	<b>W 45,052</b>	<b>W 95,295</b>	<b>W 97,080</b>	<b>W 105,848</b>

**Notes:**

- (1) Consists primarily of working capital loans, general purpose loans, bills purchased, trade-related notes and inter-bank loans.
- (2) Consists primarily of privately placed bonds, credit facility drawdowns and purchases of commercial paper or notes at a discount from its customers with recourse.
- (3) Consists of general unsecured loans and loans secured by collateral other than housing to retail customers.
- (4) As of December 31, 2003, 2004 and 2005, approximately 71.9%, 89.4% and 90.6% of our total gross loans, respectively, were Won-denominated.

**Loan Concentrations**

On a consolidated basis, our exposure to any single borrower and exposure to any single group of companies belonging to the same conglomerate is limited by law to 20% and 25%, respectively, of the Net Total Equity Capital Credit under Korean GAAP (as defined in Supervision and Regulation ). In addition, each of Shinhan Bank s and Chohung Bank s exposure, on a non-consolidated basis, to any single borrower and exposure, on a non-consolidated basis, to any single group of companies belonging to the same conglomerate is limited by law to 20% and 25%, respectively, of each bank s total Tier I and Tier II capital under Korean GAAP.

**Table of Contents***Twenty Largest Exposures by Borrower*

As of December 31, 2005, our twenty largest exposures, consisting of loans, securities and guarantees and acceptances, totaled W24,446 billion and accounted for 17.08% of our total exposures. The following table sets forth, as of December 31, 2005, our total exposures to these top twenty borrowers.

Company	Loans	Loans	Equity Securities	Debt Securities	Guarantees and Acceptances	Total Exposure	Amounts of Impaired Loans and Guarantees and Acceptances
	in Won Currency	in Foreign Currency					
<b>(In billions of Won)</b>							
The Bank of Korea Ministry of Finance and Economy	W	W	W	W	6,100	W	6,100
Korea Deposit Insurance Corporation	33				3,805		3,838
Korea Development Bank					1,137		1,137
Kookmin Bank	46		13		732		791
Samsung Electronics Military Mutual Aid Association		584	180			22	786
SK Networks(1)	691						691
Industrial Bank of Korea	253	73	240		7	97	670
Samsung Card			2		668		670
Kia Motors	395	20			194	5	614
Korea Highway Corporation	49	368	1		103	34	555
Woori Bank					551		551
Korea Asset Management Corporation	1	4	1		538		544
Korea Exchange Bank			14		510		524
Hana Bank			3		467		470
Hyundai Motors		10			416		426
SK Corporation	21	282	20			94	417
National Agricultural Cooperative Federation	69	72	132		43	82	398
LG Electronics			21		368		389
		331	7		24	12	374
<b>Total</b>	<b>W 1,558</b>	<b>W 1,744</b>	<b>W 634</b>	<b>W 20,164</b>	<b>W 346</b>	<b>W 24,446</b>	<b>W 424</b>

*Note:*

(1) Includes its remaining offshore subsidiaries, SK Networks Hong Kong and SK Networks Europe.

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**Table of Contents***Exposure to Chaebols*

As of December 31, 2005, 7.83% of our total exposure was to the twenty-nine largest chaebols. The following table shows, as of December 31, 2005, our total exposures to the ten *chaebol* groups to which we have the largest exposure.

Chaebol	Loans		Equity Securities	Debt Securities	Guarantees and Acceptances		Total Exposure	Amounts of Impaired Loans and Guarantees and Acceptances
	in Won Currency	in Foreign Currency			and	Acceptances		
(In billions of Won)								
Samsung	W 506	W 970	W 357	W 218	W 191	W 2,242	W	
Hyundai Motors	576	826	25	240	251	1,918		
SK	482	255	406	87	230	1,460		424
LG	229	696	52	55	120	1,152		
Lotte	195	43	1	217	117	573		
Doosan	159	47	3		202	411		
Hyundai Heavy Industries	1	24	1		340	366		
LS	39	52	2	5	263	361		
Hanhwa	132	40	9	20	78	279		
Hyosung	63	108		48	43	262		
<b>Total</b>	<b>W 2,382</b>	<b>W 3,061</b>	<b>W 856</b>	<b>W 890</b>	<b>W 1,835</b>	<b>W 9,024</b>	<b>W</b>	<b>424</b>

*Exposure to LG Card*

LG Card, one of Korea's largest credit card companies, has experienced significant liquidity and asset quality problems in recent years. In November 2003, the creditor banks of LG Card (including Shinhan Bank and Chohung Bank) agreed to provide a new W2 trillion credit facility, secured by credit card receivables, to enable LG Card to resume cash operations. Our portion of this commitment was W216.7 billion, consisting of W113.7 billion for Shinhan Bank and W103 billion for Chohung Bank. The maturity of this credit facility was extended in March 31, 2005 to December 31, 2005, and it was repaid in four equal installments over the course of one year following December 31, 2005. Certain of LG Card's creditor banks (including our subsidiaries) also agreed to extend the maturity of a portion of LG Card's debt coming due in 2003 for one year, after the chairman of LG Group pledged his personal stake in LG Corporation, the holding company for the LG Group, LG Investment & Securities and LG Card as collateral to offset future losses of LG Card.

After the failure to auction LG Card to a buyer in December 2003, the principal creditors of LG Card tentatively agreed to a rescue plan in January 2004 under which the Korea Development Bank would acquire a 25% (subsequently adjusted to 26%) interest in LG Card and the other creditors would collectively acquire a 74% (subsequently adjusted to 73%) ownership interest following the completion of several debt-to-equity swaps contemplated for 2004. In addition, the creditors agreed to form a normalization steering committee for LG Card to oversee LG Card's business operations. An extraordinary shareholders' meeting of LG Card was held in March 2004 and a new chief executive officer as well as directors nominated by the normalization steering committee were elected. In February 2004, the creditors exchanged indebtedness of W954 billion (including our portion of

W77.5 billion) for shares constituting 54.8% of the outstanding share capital of LG Card. LG Group also funded an additional W800 billion to LG Card (in addition to a W200 billion capital contribution made in December 2003). In March 2004, the LG Group and the Korea Development Bank provided additional liquidity of W375 billion and W125 billion, respectively. In May 2004, LG Card completed a capital write-down of 97.7% of its outstanding common stock, which included the W954 billion converted into equity by the creditors in February 2004 (including our portion of W77.5 billion). In July 2004, the creditors also converted an additional W954 billion of indebtedness into equity of LG Card (including our portion of W77.5 billion) and W1.59 trillion of new loans extended to LG Card (including our portion of W154.4 billion) into equity of LG Card. In January 2005, the LG Group and the creditor banks converted an

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additional W1 trillion in the aggregate (including W25.3 billion for Shinhan Bank and W23.0 billion for Chohung Bank for our aggregate portion of W48.3 billion) into equity. In addition, the creditor banks also reduced the interest rate on existing credit facility of LG Card in the aggregate amount of W1 trillion from 7.5% per annum to 5.5% per annum and further extended the maturity of the credit facility to December 2006, subject to four equal quarterly installment repayments in 2006. In addition, the terms of the collateral for this facility was amended. Prior to this amendment, the creditor financial institutions were entitled to receive the cash inflows from collection on such collateral. LG Card was not required to maintain a minimum collateral ratio or to enhance its credit support through the provision of additional collateral. Thus, there was no guarantee against losses to the extent that collection results in a shortfall of the principal amount of the credit extended. As a result of the amendment, however, LG Card is entitled to the cash received from collection on condition that LG Card maintains a minimum collateral ratio of 105%. In March 2005, LG Card also completed a capital write-down of 81.8% of its outstanding common stock, which included the W2,417 billion of equity held by the creditors (including our portion of W216 billion). In April 2006, we submitted a letter of intent indicating our wish to participate in the bidding for the controlling equity stake in LG Card. Subsequently, we were selected as one of the potential bidders and as of the date of this offering circular, we are currently conducting due diligence to evaluate our bid for LG Card.

As of December 31, 2005, our total exposure to LG Card was W364 billion, including W136 billion of loans, W33 billion of debt securities and W195 billion of equity securities. We made an allowance for loan losses of W0.7 billion for the loans. As a result of the satisfactory progress on scheduled debt restructuring of LG Card, we recorded reversal of loan loss provisions of W12 billion and recognized securities impairment losses of W7 billion in respect of our exposures to LG Card. In connection with the LG Card rescue plan, Shinhan Bank transferred W10 billion of exposure in its performance-based trust account to the bank account in January 2004 and Chohung Bank also transferred W30 billion of exposure in its performance-based trust account to the bank account in February 2004, resulting in an increase in our total exposure to LG Card. These exposures were included in our credit exposure that was converted into equity in connection with the rescue plan of LG Card as described above.

The value of underlying collateral, our pro rata entitlement thereto and the allowances we have established or will establish against our exposures to LG Card may not be sufficient to cover all future losses arising from these exposures. Following the debt-to-equity conversions in respect of our exposures to LG Card, we may experience further losses if the market value of the LG Card equity securities we own falls below their recorded book value.

As of the date hereof, the creditors of LG Card held in the aggregate 103,287,662 shares, representing 82.39% of total issued and outstanding shares of LG Card of 125,369,403 shares, including 8,960,005 shares of LG Card, representing 7.14% of total issued and outstanding shares. In August 2005, the creditors of LG Card resolved to sell up to 90,364,299 shares, including 8,312,240 shares held by us, by way of an auction conducted by the creditors, with Korea Development Bank taking the lead role. The current plan is for the creditors to sell at least 51% to a successful bidder with a view to transferring control in LG Card to the purchaser. The proposed timetable for this auction is subject to change pending negotiations with multiple bidders. It is expected that a preliminary, preferred bidder(s) will be selected in the second half of 2006. We, together with our competitors in the Korean financial market, have participated in this auction to purchase control of LG Card.

*Exposures to the Credit Card Industry*

Recent adverse developments in the credit card industry such as industry-wide increases in delinquencies and resulting increases in provisioning for loan losses have had a negative impact on investors' perception of credit card companies in the Korean corporate debt market, thereby significantly limiting the ability of credit card companies to raise financing through issuances of debt securities. As a result, Korean credit card companies have been experiencing significant financial and liquidity difficulties.

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The following table shows, as of December 31, 2005, the breakdown of our total exposure to credit card companies.

Company	Debt Securities		Securities Issued Through Asset-Backed Securitization(1)		Equity Securities	Loans in Won Currency	Guarantees and Acceptances	Loans in Foreign Currency	Total
	W		W		W	W	W	W	
(In billions of Won)									
Samsung Card(2)	W	194	W	281	W	W 395	W 5	W 20	W 895
LG Card		2		31	195	136			364
Hyundai Card				150		20			170
Lotte Card		129				19			148
KDB Capital(3)						20			20
Total	W	325	W	462	W 195	W 590	W 5	W 20	W 1,597

*Notes:*

- (1) Securities issued by special purpose vehicles of credit card companies, established with credit card receivables as underlying assets. In general, these special purpose vehicles are entitled to credit or collateral support from such credit card companies.
- (2) Samsung Card recorded net loss of W1,301 billion in 2005, despite a turnaround beginning in the second half of 2005. In the first quarter of 2006, Samsung Card recorded net income of W76 billion.
- (3) KDB Capital is a subsidiary of Korea Development Bank, which is owned and controlled by the Korean government.

As of December 31, 2005, we had loans outstanding to credit card companies in the aggregate principal amount of W610 billion. Despite the recent financial difficulties of certain credit card companies, our loans to these credit card companies, except LG card, are considered performing in accordance with our internal credit rating methodology, and therefore we have not recognized a specific allowance for loan losses against these. In light of the improvement in the asset quality of the credit companies in general, we believe our general allowance of W1 billion against the performing element of the corporate loan portfolio in total is sufficient to cover any incurred losses within these specific loans.

In addition, our investment portfolio includes beneficiary certificates representing interests in investment trusts whose assets include securities issued by troubled credit card companies, including LG Card. Accordingly, to the extent that the value of securities issued by credit card companies declines as a result of their financial difficulties or otherwise, we may experience losses on our investment securities.

In the case of credit card companies that are in or in the future enter into workout, restructuring, reorganization or liquidation proceedings, our recoveries from those companies may be limited. We may, therefore, experience future losses with respect to these exposures.

*Exposures to SK Group Companies*

In the first quarter of 2003, accounting irregularities were discovered at SK Networks to which most commercial banks in Korea, including ourselves, had substantial exposure. These irregularities had concealed the weak financial condition of SK Networks over a period of several years. In March 2003, the principal creditor banks of SK Networks commenced formal workout procedures against SK Networks under the Corporate Restructuring Promotion Act of Korea. In October 2003, SK Networks and its overseas subsidiaries completed the final major step in the restructuring of indebtedness of SK Networks and its overseas subsidiaries, including the following:

the purchase by SK Networks of approximately US\$540 million of the US\$563 million of total indebtedness of its overseas subsidiaries held by non-Korean institutions in exchange for 43% of the

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principal amount in promissory notes and 5% of the principal amount in the form of bonds with warrants;

the purchase or inclusion in the restructuring plan of SK Networks of all of the approximately US\$126 million of indebtedness of its overseas subsidiaries held by Korean financial institutions; and

the entering into a Memorandum of Understanding on the Corporate Restructuring Implementation, or Memorandum, in respect of the restructuring of the approximately US\$2 billion of indebtedness to SK Networks.

All of the indebtedness of SK Networks and its overseas subsidiaries held by Korean financial institution creditors was resolved either through an exchange for 43% of the principal amount in promissory notes and 5% of the principal amount in the form of bonds with warrants or in accordance with the Memorandum. Under the Memorandum, all of the indebtedness of SK Networks held by the Korean financial institution creditors was converted into shares of common stock, Redeemable Preferred Stock and mandatory convertible bonds of SK Networks. SK Corp., which is the parent company of SK Networks, also converted approximately US\$760 million of its claims against SK Networks into the shares of common stock of SK Networks in connection with the Memorandum.

As a result of this corporate restructuring, we owned 9.54% of common shares of SK Networks (or 9.87% of total equity ownership in SK Networks including the Redeemable Preferred Stock) as of December 31, 2005.

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As of December 31, 2005, 1.02% of our total exposure was to the member companies of the SK Group. The following table shows, as of December 31, 2005, the breakdown of our total exposure by member companies of the SK Group.

Company	Loans	Loans	Equity	Debt	Guarantees	Total	Amounts
	in	in			and		of
	Won	Foreign	Securities	Securities	Acceptances	Exposure	Loans and
	Currency	Currency					Guarantees
							and
							Acceptances
(In billions of Won)							
SK Networks	W 253	W 73	W 240	W 7	W 97	W 670	W 424
SK Corporation	69	72	132	43	82	398	
K Power Co., Ltd.	59					59	
SK Telecom Co., Ltd.	1		33	20		54	
SK Chemical	10	18		3	21	52	
SK C&C Co., Ltd.	40				2	42	
SKC Co., Ltd.	5	11		15	2	33	
SK Gas Co., Ltd (Kim Se Kwang)	3	24				27	
SK Gas Co., Ltd.		27				27	
SK Shipping		19				19	
Walkerhill	6				8	14	
SK Construction					13	13	
Choongnam City Gas Co., Ltd.	7					7	
Daehan City Gas Co., Ltd.	7					7	
Pohang City Gas	6					6	
Pusan City Gas	5					5	
Dong Shin Pharm, Co., Ltd.		3			1	4	
Global Shipbuilding SA		4				4	
Champion Shipbuilding SA		4				4	
SK Telesys		1			2	3	
Chonnam City Gas Co., Ltd.	3					3	
InnoAce Co., Ltd.	2					2	
In2gen	2					2	
SK Sitech					2	2	
Infosec Co., Ltd.	1					1	
Kangwon Gas	1					1	
<b>Total</b>	<b>W 480</b>	<b>W 256</b>	<b>W 405</b>	<b>W 88</b>	<b>W 230</b>	<b>W 1,459</b>	<b>W 424</b>

As of December 31, 2005, our total exposure outstanding to SK Networks alone was W670 billion, or 0.47% of our total exposure, consisting of W326 billion in loans, W7 billion in debt securities, W240 billion in equity securities

and W97 billion in guarantees and acceptances. Of our total loans outstanding to SK Networks, W24 billion was secured. For the unsecured loans of W302 billion, we made allowance for loan losses of W20 billion. With respect to the guarantees and acceptances outstanding, we made allowances of W6 billion. As of December 31, 2005, we had no exposure outstanding to SG Wicus Corporation.

In addition, as of December 31, 2005, our total exposure outstanding to SK Corporation, the controlling company of the SK Group, was W398 billion, or 0.28% of our total exposure, consisting of W141 billion in loans, W132 billion in equity securities, W43 billion in debt securities and W82 billion in guarantees and acceptances. We classify loans and guarantees and acceptances to other SK Group companies, including SK Corporation, as performing in accordance with our internal credit rating methodology and therefore no

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specific allowance is made against these loans or guarantees and acceptances. Our management believes the general allowance of W0.9 billion against the performing element of the corporate loan portfolio in total is sufficient to cover any incurred losses within this portfolio, including those loans to companies within the SK Group, including SK Corporation and excluding SK Networks. See Item 3. Key Information Risk Factors Risks Relating to our banking business We have significant exposure to SK Networks which is experiencing financial difficulties that it concealed through accounting irregularities and which is in a workout program. If this program is not satisfactorily resolved, it may have a material adverse effect on us .

*Exposures to Ssangyong Group Companies*

In 1998, Daewoo Motors acquired Ssangyong Motors from the former Ssangyong Group, on condition that certain of the then existing liabilities of Ssangyong Motors be retained by the former Ssangyong Group. In connection with this transaction, nine member companies of the Ssangyong Group assumed in the aggregate liabilities of W1.8 trillion, which subsequently resulted in significant increases in interest expense for such companies, further aggravated by a sharp increase in interest rates during the financial crisis of the late 1990 s. Several of the Ssangyong Group companies, including Ssangyong Corporation, Ssangyong Cement Industrial and Ssangyong Engineering & Construction, have experienced significant financial and liquidity difficulties as a result and were subsequently placed under workout programs by their respective creditors.

As of December 31, 2005, 0.3% of our total exposure was to the member companies of the Ssangyong Group. The following table shows, as of December 31, 2005, the breakdown of our total exposure by member companies of the Ssangyong Group.

Company (1)	Loans		Equity Securities	Debt Securities	Guarantees and Acceptances		Total Exposure	Amounts of Impaired Loans and Guarantees and Acceptances
	in Won Currency	in Foreign Currency						
(In billions of Won)								
Ssangyong Corporation	W 3	W 91	W 49	W	W 78	W 221	W 172	
Ssangyong Cement Industrial	87		87			174		
Ssangyong Engineering & Construction		4	6	14	5	29		
Ssangyong Resources Development Co., Ltd.	2					2		
<b>Total</b>	<b>W 92</b>	<b>W 95</b>	<b>W 142</b>	<b>W 14</b>	<b>W 83</b>	<b>W 426</b>	<b>W 172</b>	

*Note:*

(1) Includes domestic and overseas subsidiaries of each company.

In July 2003, the committee of creditors participating in the workout program of Ssangyong Cement Industrial approved a plan to (i) extend new credits of W150 billion to provide additional liquidity, of which Chohung Bank s portion was W50 billion, all of which are entitled to priority in repayment as agreed by the creditors committee, (ii) debt-to-equity swap of W573 billion, in which we did not participate, and (iii) extend the maturity for repayment

of principal from December 2003 to December 2005. Ssangyong Cement exited the workout in November 2005. As of December 31, 2005, our total exposure to Ssangyong Cement Industrial amounted to W174 billion, of which W0 billion was classified as impaired. As of December 31, 2005, allowance for loan losses and guarantees and acceptances with respect to our loans and guarantees and acceptances to Ssangyong Cement Industrial was W0.2 billion.

In August 2003, the committee of creditors participating in the workout program of Ssangyong Corporation approved a plan to (i) conduct a 5-to-1 capital reduction of existing shares of Ssangyong Corporation (including minority share ownership and shares obtained through debt-to-equity swaps) and (ii) subsequently enter into an additional debt-to-equity swap of loans in the aggregate principal amount of approximately W121 billion, including W80 billion of our loans consisting of W80 billion from Chohung Bank

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and W0.4 billion from Shinhan Bank. As of December 31, 2005, our total exposure to Ssangyong Corporation (including its overseas offices in Hong Kong, Japan and Singapore) amounted to W221 billion. Of our total loans and guarantees and acceptances to Ssangyong Group, W172 billion was classified as impaired. As of December 31, 2005, allowance for loan losses and guarantees and acceptances with respect to our loans and guarantees and acceptances to Ssangyong Corporation and Ssangyong Cement Industrial was W2 billion and W0.2 billion, respectively.

In August 2005, eight members of the committee of creditors, including Shinhan Bank, selected Morgan Stanley Private Equity Holdings AB as the preferred bidder for the sale of 8,374,236 shares, or 75% of total issued and outstanding shares of Ssangyong Corporation, out of 9,887,150 such shares in the aggregate held by the creditors group. A memorandum of understanding was entered into in September 2005 and the definitive agreement for the sale was entered into in December 2005. The closing of this sale occurred in April 2006 at the aggregate sale price of W68 billion, of which W5 billion was placed in escrow to provide for an indemnity on certain representation and warranties provided by the selling creditors to the purchaser. Simultaneously with the closing, all of the credits previously extended in connection with Ssangyong Corporation's workout program, amounting to W357 billion, including W232 billion owing to Shinhan Bank, was repaid in full.

Except as described above, no material changes have occurred with respect to our exposures to the former Ssangyong Group companies since December 31, 2003. See Item 3. Key Information Risk Factors Risks Relating to our banking business We have significant exposure to the largest Korean commercial conglomerates, known as chaebols, and, as a result, recent and any future financial difficulties of chaebols may have an adverse effect on us.

*Loan Concentration by Industry*

The following table shows the aggregate balance of our corporate loans by industry concentration as of December 31, 2005 under US GAAP.

Industry	Aggregate Loan Balance		Percentage of Total Corporate Loan Balance
	(In billions of Won)		(Percentages)
Manufacturing	W	22,823	39.42%
Retail and wholesale		8,271	14.29
Real estate, leasing, and service		9,434	16.30
Construction		3,182	5.50
Hotel and leisure(1)		2,114	3.65
Finance and insurance		3,615	6.24
Transportation, storage and communication		2,511	4.34
Other service		5,854	10.11
Other		87	0.15
Total	W	57,891	100.00%

*Note:*

(1) Consists principally of hotels, motels and restaurants.

**Table of Contents***Loan Concentration by Size of Loans*

The following table shows the aggregate balances of our loans by outstanding loan amount as of December 31, 2005.

	<b>Aggregate Loan Balance</b>	<b>Percentage of Total Loan Balance</b>
	<b>(In billions of Won)</b>	<b>(Percentages)</b>
<b>Commercial and industrial</b>		
Up to W10 million	W 116	0.11%
Over W10 million to W50 million	1,756	1.66
Over W50 million to W100 million	2,220	2.10
Over W100 million to W500 million	10,045	9.48
Over W500 million to W1 billion	4,351	4.11
Over W1 billion to W5 billion	8,357	7.90
Over W5 billion to W10 billion	2,899	2.74
Over W10 billion to W50 billion	4,538	4.29
Over W50 billion to W100 billion	1,136	1.07
Over W100 billion	310	0.29
Sub-total	W 35,728	33.75%
<b>Other commercial</b>		
Up to W10 million	W 64	0.06%
Over W10 million to W50 million	481	0.45
Over W50 million to W100 million	546	0.52
Over W100 million to W500 million	3,077	2.91
Over W500 million to W1 billion	1,923	1.82
Over W1 billion to W5 billion	5,125	4.84
Over W5 billion to W10 billion	2,473	2.34
Over W10 billion to W50 billion	5,668	5.36
Over W50 billion to W100 billion	1,032	0.97
Over W100 billion	1,020	0.96
Sub-total	W 21,409	20.23%
<b>Lease financing</b>		
Up to W10 million	W 2	
Over W10 million to W50 million	15	0.01%
Over W50 million to W100 million	18	0.02
Over W100 million to W500 million	100	0.09
Over W500 million to W1 billion	50	0.05
Over W1 billion to W5 billion	214	0.20
Over W5 billion to W10 billion	125	0.12
Over W10 billion to W50 billion	230	0.22
Over W50 billion to W100 billion		
Over W100 billion		

Sub-total

W

754

0.71%

88

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	<b>Aggregate Loan Balance</b>	<b>Percentage of Total Loan Balance</b>
	<b>(In billions of Won)</b>	<b>(Percentages)</b>
<b>Mortgage and home equity</b>		
Up to W10 million	W 391	0.37%
Over W10 million to W50 million	6,817	6.44
Over W50 million to W100 million	7,662	7.24
Over W100 million to W500 million	10,222	9.65
Over W500 million to W1 billion	633	0.60
Over W1 billion to W5 billion	115	0.11
Over W5 billion to W10 billion		
Over W10 billion to W50 billion		
Over W50 billion to W100 billion		
Over W100 billion		
Sub-total	W 25,840	24.41%
<b>Other consumer</b>		
Up to W10 million	W 3,507	3.31%
Over W10 million to W50 million	5,088	4.81
5.00	2,598	2.45
Over W100 million to W500 million	5,109	4.84
Over W500 million to W1 billion	841	0.79
Over W1 billion to W5 billion	686	0.65
Over W5 billion to W10 billion	46	0.04
Over W10 billion to W50 billion	0	0.00
Over W50 billion	0	0.00
Over W100 billion	0	0.00
Sub-total	W 17,875	16.89%
<b>Credit cards</b>		
Up to W10 million	W 2,998	2.84%
Over W10 million to W50 million	995	0.94
Over W50 million to W100 million	89	0.08
Over W100 million to W500 million	120	0.11
Over W500 million to W1 billion	27	0.03
Over W1 billion to W5 billion	13	0.01
Over W5 billion to W10 billion	0	0.00
Over W10 billion to W50 billion	0	0.00
Over W50 billion to W100 billion	0	0.00
Over W100 billion	0	0.00
Sub-total	W 4,242	4.01%
<b>Total</b>	<b>W 105,848</b>	<b>100.00%</b>



**Table of Contents*****Maturity Analysis***

The following table sets out the scheduled maturities (time remaining until maturity) of our loan portfolio as of December 31, 2005. The amounts disclosed are before deduction of attributable loan loss reserves.

	<b>As of December 31, 2005</b>						
	<b>1 Year or Less</b>		<b>Over 1 Year but Not More Than 5 Years</b>		<b>Over 5 Years</b>		<b>Total</b>
<b>(In billions of Won)</b>							
<b>Corporate:</b>							
Commercial and industrial	W	30,361	W	4,666	W	701	W 35,728
Other commercial		14,280		6,099		1,030	21,409
Lease financing		422		325		7	754
<b>Total corporate</b>	<b>W</b>	<b>45,063</b>	<b>W</b>	<b>11,090</b>	<b>W</b>	<b>1,738</b>	<b>W 57,891</b>
<b>Consumer:</b>							
Mortgage and home equity	W	9,885	W	4,648	W	11,307	W 25,840
Other consumer		12,959		3,830		1,086	17,875
Credit cards		4,068		162		12	4,242
<b>Total consumer</b>	<b>W</b>	<b>26,912</b>	<b>W</b>	<b>8,640</b>	<b>W</b>	<b>12,405</b>	<b>W 47,957</b>
<b>Total gross loans</b>	<b>W</b>	<b>71,975</b>	<b>W</b>	<b>19,730</b>	<b>W</b>	<b>14,143</b>	<b>W 105,848</b>

We may roll over our working capital loans and consumer loans (which are not payable in installments) after we conduct our normal loan review in accordance with our loan review procedures. Working capital loans of Shinhan Bank may be extended on an annual basis for an aggregate term of three years for unsecured loans and five years for secured loans and consumer loans may be extended for additional terms of up to 12 months for an aggregate term of five years for unsecured loans and ten years for secured loans. Working capital loans of Chohung Bank may be extended on an annual basis for an aggregate term of five years and consumer loans are commonly extended for additional terms of up to 12 months for an aggregate term of ten years, regardless of whether such loans are secured or unsecured. Such loans have been classified as loans with maturity of one year or less in the tables above.

***Interest Rate Sensitivity***

The following table shows our loans by interest rate sensitivity as of December 31, 2005.

	<b>As of December 31, 2005</b>				
	<b>Due Within 1 Year</b>		<b>Due After 1 Year</b>		<b>Total</b>
<b>(In billions of Won)</b>					
Fixed rate loans(1)	W	34,605	W	15,892	W 50,497
Variable rate loans(2)		37,370		17,981	55,351
<b>Total gross loans</b>	<b>W</b>	<b>71,975</b>	<b>W</b>	<b>33,873</b>	<b>W 105,848</b>

*Notes:*

- (1) Fixed rate loans are loans for which the interest rate is fixed for the entire term. Includes W18,693 billion of loans due within one year and W11,088 billion of loans due after one year, which are priced based on one or more reference rates which may vary at our discretion. However, it is not our practice to change such reference rates during the life of a loan.
- (2) Variable or adjustable rate loans are for which the interest rate is not fixed for the entire term.

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For additional information regarding management of interest rate risk of each of Shinhan Bank and Chohung Bank, see Risk Management Market Risk Management of Shinhan Bank and Risk Management of Chohung Bank.

***Nonaccrual Loans and Past Due Accruing Loans***

Except in the case of repurchased loans, we generally do not recognize interest income on nonaccrual loans unless it is collected. Generally, the accrual of interest is discontinued on loans (other than repurchased loans) when payments of interest and/or principal become past due by one day. Interest is recognized on these loans on a cash received basis from the date the loan is placed on nonaccrual status. Loans (other than repurchased loans) are not reclassified as accruing until interest and principal payments are brought current.

We do not generally request borrowers to make immediate repayment of the whole outstanding principal balances and related accrued interest on nonaccrual loans whose interest payments are past due for one to 14 days in case of commercial loans and 1 to 30 days in case of consumer loans. Except where specified otherwise, the amount of such past due loans within the repayment grace period is excluded from the amount of non-accrual loans disclosed in this document and from the basis for related foregone interest calculation.

Interest foregone is the interest due on nonaccrual loans that has not been accrued in our books of account. For the year ended December 31, 2005 we would have recorded gross interest income of W186 billion, compared to W184 billion for the year ended December 31, 2004 and W110 billion for the year ended December 31, 2003 on loans accounted for on a nonaccrual basis throughout the year, or since origination for loans held for part of the year, had the loans been current with respect to their original contractual terms. The amount of interest income on those loans that was included in our net income for the years ended December 31, 2003, 2004 and 2005 were W48 billion, W142 billion and W117 billion, respectively.

The category accruing but past due one day includes loans which are still accruing interest but on which principal or interest payments are contractually past due one day or more. We continue to accrue interest on loans where the total amount of loan outstanding, including accrued interest, is fully secured by cash on deposits.

The following table shows, at the dates indicated, the amount of loans that are placed on a nonaccrual basis and accruing loans which are past due one day or more.

	<b>As of December 31,</b>				
	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
	<b>(In billions of Won)</b>				
<b>Loans accounted for on a nonaccrual basis</b>					
Corporate	W 834	W 741	W 1,536	W 1,681	W 1,475
Consumer	78	111	580	479	367
Credit cards	234	358	1,016	294	210
Sub-total	1,146	1,210	3,132	2,454	2,052
<b>Accruing loans which are contractually past due one day or more as to principal or interest</b>					
Corporate(1)	29	32	196	55	32
Consumer(2)	32	38	27	17	32
Credit cards				76	3
Sub-total	61	70	223	148	67
<b>Total</b>	<b>W 1,207</b>	<b>W 1,280</b>	<b>W 3,355</b>	<b>W 2,602</b>	<b>W 2,119</b>



**Table of Contents***Notes:*

- (1) Includes accruing loans which are contractually past due 90 days or more in the amount of W2 billion, W113 billion, W12 billion and W5 billion of corporate loans as of December 31, 2002, 2003, 2004 and 2005, respectively.
- (2) Includes accruing loans which are contractually past due 90 days or more in the amount of W10 billion, W7 billion, W6 billion and W7 billion of consumer loans as of December 31, 2002, 2003, 2004 and 2005, respectively.

***Troubled Debt Restructurings***

The following table presents, at the dates indicated, our loans which are troubled debt restructurings as defined under U.S. GAAP. These loans consist of corporate loans that have been restructured through the process of workout, court receivership and composition. See Credit Exposures to Companies in Workout, Court Receivership and Composition . These loans accrue interest at rates lower than the original contractual terms, or involve the extension of the original contractual maturity as a result of a variation of terms upon restructuring.

	<b>As of December 31,</b>				
	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
	<b>(In billions of Won)</b>				
Loans not included in nonaccrual and past due loans which are classified as troubled debt restructurings	W 360	W 145	W 1,179	W 916	W 735

For the year ended December 31, 2005, interest income that would have been recorded under the original contract terms of restructured loans amounted to W26 billion, out of which W22 billion was reflected as our interest income during 2005.

***Credit Exposures to Companies in Workout, Court Receivership and Composition***

Shinhan Bank's exposures in restructuring are managed and collected by our Corporate Restructuring Team. Chohung Bank's exposures in restructuring are managed and collected by Chohung Bank's Loan Recovery Division and, following the merger of the two banks, by Shinhan Bank's Corporate Credit Collection Department. As of December 31, 2005, 1.3% of our total exposure, or W1,875 billion, was under restructuring. The legal form of our restructurings is principally either workout, court receivership or composition.

***Workout***

Under the Corporate Restructuring Promotion Act, which became effective in September 2001, all creditors to borrowers that are financial institutions were required to participate in a creditors' committee. The Corporate Restructuring Promotion Act was mandatorily applicable to more than 420 financial institutions in Korea, which include commercial banks, insurance companies, asset management companies, securities companies, merchant banks, the Korea Deposit Insurance Corporation and the Korea Asset Management Corporation. Under this act, the approval of financial institution creditors holding not less than 75% of the total debt outstanding of a borrower approved such borrower's restructuring plan, including debt restructuring and provision of additional funds, which plan would be binding on all the financial institution creditors of the borrower, provided that any financial institution creditor that disagreed with the final restructuring plan approved by the creditors' committee would have the right to request the creditors' committee to purchase its claims at a mutually agreed price. In the event that the creditors' committee and the dissenting financial institution creditor failed to come to an agreement, a mediation committee consisting of seven experts would be set up to resolve the matter. There was a risk that these procedures might require us to participate in a plan that we did not agree with or might require us to sell our claims at prices that we did not believe were adequate. As the Corporate Restructuring Promotion Act expired on December 31, 2005 and no other

law replacing this Act or other law with the similar effect was enacted, the bill to extend the effective term of this Act until December 31, 2010 was presented to and is pending at the National Assembly of Korea. With  
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respect to any workout for which the lead creditor bank called for a meeting of the creditors' committee while the Corporate Restructuring Promotion Act was still effective, the procedures applicable to such creditors' committee and the related workout remain subject to the Corporate Restructuring Promotion Act until the suspension or conclusion of such workout.

The total amount currently undergoing workout as of December 31, 2005 was W1,612 billion, including W738 billion of loans and W874 billion of other exposures.

*Court Receivership and Composition*

The Debtor Recovery and Bankruptcy Act, promulgated on March 31, 2005 became effective as of April 1, 2006, which was designed to consolidate all existing bankruptcy-related laws in Korea, namely the Corporate Reorganization Act, the Composition Act, the Bankruptcy Act and the Individual Debtor Recovery Act.

Prior to the enactment of the Debtor Recovery and Bankruptcy Act, court receivership or corporate reorganization procedures under the Corporate Reorganization Act were court-supervised procedures to rehabilitate an insolvent company. The restructuring plan was adopted at a meeting of interested parties and was subject to approval of a court. In a court receivership, the management of the company was taken over by a court appointed receiver. Creditors were required to file their claims with the court and if they failed to do so, their claims were discharged at the end of the reorganization proceeding. Creditors were allowed to recover on their claims only in compliance with the reorganization plan.

Under the Composition Act, composition was also a court-supervised procedure to rehabilitate an insolvent company. The restructuring plan was adopted at a meeting of interested parties and was subject to approval of a court. However, in composition proceedings the existing management of the company continued to operate the debtor's business. Claims not filed with the court were not discharged at the end of a composition proceeding although the creditors were required to file their claims with the court if they wanted to exercise their voting rights at the meeting of interested parties. In addition, secured creditors were allowed to enforce their security interest outside the composition proceeding unless they waived their security interest and consent to the composition plan.

Under the Debtor Recovery and Bankruptcy Act, composition proceedings are abolished and recovery proceedings are introduced to replace the court receiverships. In a recovery proceeding, unlike the previous court receivership proceedings where the management of the debtor company was assigned to a court appointed receiver, the current chief executive officer of the debtor company may continue to manage the debtor company, provided that (i) neither fraudulent conveyance nor concealment of assets existed, (ii) financial failure of the debtor company was not due to the gross negligence of the chief executive officer, and (iii) no creditors' meeting was convened to request, based on reasonable cause, a court-appointed receiver to replace the existing chief executive officer. While court receivership proceeding was permitted only with respect to joint stock companies (*chushik-hoesa*), the recovery proceeding may be commenced by any insolvent debtor. In addition, in an effort to meet the global standards, international bankruptcy procedures are introduced in Korea, under which a receiver of a foreign bankruptcy proceeding may, upon receiving Korean court's approval of the ongoing foreign bankruptcy proceeding, apply for or participate in a Korean bankruptcy proceedings conducted in a Korean court. Similarly, a receiver in a domestic recovery proceeding or a bankruptcy trustee is allowed to perform its duties in a foreign country where an asset of the debtor is located to the extent the applicable foreign law permits.

However, any composition, corporate reorganization, bankruptcy and rehabilitation proceedings for individual debtors pending as of April 1, 2006, the effective date of the Debtor Recovery and Bankruptcy Act, continue to proceed in accordance with the respective applicable laws.

The total amount currently subject to court receivership as of December 31, 2005 was W148 billion, including W143 billion of loans and W5 billion of other exposures.

The total amount currently subject to composition proceedings as of December 31, 2005 was W115 billion, including W109 billion of loans and W6 billion of other exposures.

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Loans in the process of workout, court receivership or composition continue to be reported as loans on our balance sheet and are included as nonaccrual loans described in Nonaccrual Loans and Past Due Accruing Loans above since they are generally past due more than one day and interest generally does not accrue on such loans. Restructured loans that meet the U.S. GAAP definition of a troubled debt restructuring are included within Troubled Debt Restructurings described above. These are disclosed as loans or securities after the restructuring on our balance sheet depending on the type of instrument we receive.

The following table shows, as of December 31, 2005, our ten largest exposures that had been negotiated in workouts, composition or court receivership.

Company	Loans in Won Currency	Loans in Foreign Currency	Equity Securities	Debt Securities	Guarantees and Acceptances	Total Exposure(1)
(In billions of Won)						
SK Networks	W 253	W 73	W 240	W 7	W 97	W 670
LG Card	136		195	2		333
Ssangyong Corporation(2)	3	91	49		78	221
Hyundai Engineering & Construction(3)		8	56	32	62	158
Inchon Oil Refinery	98		5			103
Daewoo Electronics Corporation	38		28			66
Saehan Industries, Inc.	27	5	9		5	46
Hankook Ilbo	43					43
Daewoo Electronics Co., Ltd.	33					33
Dongbang Textile & Mart Co., Ltd.	3	10			13	26
<b>Total</b>	<b>W 634</b>	<b>W 187</b>	<b>W 582</b>	<b>W 41</b>	<b>W 255</b>	<b>W 1,699</b>

*Notes:*

- (1) Only includes the portion of total exposure identified by us as troubled debt restructuring and excludes amount of loans or other exposures to the same borrower that are not subject to workouts, composition or court receivership.
- (2) The sale of 8,374,236 shares, or 75.00%, of Ssangyong Corporation by the eight members of the creditor group to Morgan Stanley Private Equity Holdings AB for W8,091.31 per share, or W68 billion in the aggregate, was consummated in April 2006. As a result, in April 2006, Ssangyong Corporation graduated from the workout program.
- (3) In May 2006, Korea Exchange Bank, the lead creditor of Hyundai Engineering & Construction, announced Hyundai Engineering & Construction's graduation from its workout program. It is expected that the shares currently held by the creditors group will be up for sale in the second half of 2006.

**Potential Problem Loans**

As of December 31, 2005, we had W216 billion of loans which are current as to payment of principal and interest but carries serious doubt as to the ability of the borrower to comply with repayment terms in the near future. These

loans are classified as impaired and therefore included in our calculation of loan loss allowance under U.S. GAAP.

We have certain other interest-earning assets which, if they were loans, would be required to be disclosed as part of the nonaccrual, past due or troubled debt restructuring or potential problem loan disclosures provided above. As of December 31, 2005, we had zero book value for our debt securities on which interest was past due.

**Table of Contents*****Provisioning Policy***

We conduct periodic and systematic detailed reviews of our loan portfolios to identify credit risks and to evaluate the adequacy of the overall allowance for loan losses. Our management believes the allowance for loan losses reflects the best estimate of the probable loan losses incurred as of each balance sheet date.

Our loan loss allowance determined under U.S. GAAP consists of a specific allowance and a general allowance. The specific allowance is applied to corporate loans that are considered to be impaired and are either individually or collectively evaluated for impairment. The general allowance is applied to all other loans to reflect losses that have been incurred but not specifically identified.

***Loan Classifications***

For Korean GAAP and regulatory reporting purposes, each of our banking operations bases its provisioning on the following loan classifications that classify corporate and consumer loans, with the exception of credit card receivables which are classified based on the number of days past due, as required by the Financial Supervisory Commission.

**Loan Classification****Loan Characteristics**

Normal	Loans made to customers whose financial position, future cash flows and nature of business are deemed financially sound. No problems in recoverability are expected.
Precautionary	Loans made to customers whose financial position, future cash flows and nature of business show potential weakness, although there is no immediate risk of nonrepayment.
Substandard	Loans made to customers whose adverse financial position, future cash flows and nature of business have a direct effect on the repayment of the loan.
Doubtful	Loans made to customers whose financial position, future cash flows and nature of business are so weak that significant risk exists in the recoverability of the loan, to the extent the outstanding amount exceeds any collateral pledged.
Estimated loss	Loans where write-off is unavoidable.

***Corporate Loans***

We review all corporate loans annually for potential impairment through a formal credit review, however, our loan officers also consider the credits for impairment throughout the year should information be presented that may indicate an impairment event has occurred.

Under U.S. GAAP, a loan is impaired when, based on current information and events, it is probable that the creditor will be unable to collect all amounts due according to the contractual terms of the agreement. We use our loan classifications as a basis to identify impaired loans. We consider the following loans to be impaired loans for the purpose of determining our specific allowance:

loans classified as substandard or below according to the asset classification guidelines of the Financial Supervisory Commission;

loans that are 90 days or more past due; and

loans which are troubled debt restructurings as defined under U.S. GAAP.

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Specific loan loss allowances for corporate loans are established based on whether a particular loan is impaired. Smaller balance corporate loans are evaluated collectively for impairment as these loans are managed collectively.

*Loans individually identified for review and considered impaired*

Consistent with the internal credit risk monitoring policies, we evaluate larger-balance impaired loans (which are impaired loans in excess of W1 billion for all of our subsidiaries except Chohung Bank whose impaired loans are in excess of W2 billion) individually for impairment. Loan loss allowances for these loans are generally established by discounting the estimated future cash flows (both principal and interest) we expect to receive using the loan's effective interest rate. We consider the likelihood of all possible outcomes in determining our best estimate of expected future cash flows. Management consults closely with individual loan officers and reviews the cash flow assumptions used to ensure these estimates are valid.

Alternatively, for impaired loans that are considered collateral dependent, the amount of impairment is determined by reference to the fair value of the collateral. We consider the reliability and timing of appraisals and determine the reasonableness of fair value estimates, taking into account the time to value the collateral and current market conditions.

We may also measure impairment by reference to the loan's observable market price, however the availability of this information is not commonplace in Korea.

We establish a specific allowance when the discounted cash flow (or collateral value) is lower than the carrying amount of the loan. The specific allowance is equal to the difference between the discounted cashflow (or collateral value) amount and the related carrying amount of the loan.

*Loans collectively evaluated for impairment*

We also establish specific allowances for smaller-balance impaired corporate loans. These loans are managed on a portfolio basis and are therefore collectively evaluated for impairment since it is not practical to analyze or provide for our smaller loans on an individual, loan by loan basis.

The allowance is determined based on loss factors taking into consideration past performance of the portfolio, previous loan loss history and charge-off information.

These loss factors are developed through a migration model that is a statistical tool used to monitor the progression of loans through different classifications over a specific time period. We adjust these loss factors developed for other qualitative or quantitative factors that affect the collectibility of the portfolio as of the evaluation date including:

Prevailing economic and business conditions within Korea and foreign jurisdictions in which we operate;

Industry concentrations;

Changes in the size and composition of the relevant underlying portfolios; and

Changes in lending policies and procedures, including underwriting standards and collection, charge-offs, and recovery practices.

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The following table sets out, at the dates indicated, our loan loss allowances as a percentage of outstanding loans allocable to our impaired corporate borrowers based on their loan classification.

	As of December 31,		
	2003	2004	2005
	(Percentages)		
Normal	2.35%	1.87%	2.42%
Precautionary	23.72	8.25	7.92
Substandard	33.01	27.79	22.41
Doubtful	68.63	83.15	47.60
Estimated loss	90.11	92.58	87.19

*Loans not specifically identified as impaired*

We establish a general allowance for non-impaired corporate loans to reflect losses incurred within the portfolio which have not yet been specifically identified. The general allowance is also determined based on loss factors developed through a migration model and are adjusted, as appropriate using similar criteria as above.

*Leases*

For leases, we follow a similar approach to corporate loans collectively evaluated for impairment and establish allowances based on loss factors developed through a migration model and adjusted for specific circumstances related to individual borrowers of the leased asset.

*Consumer loans*

Consumer loans are segmented into the following product types for the purposes of evaluation of credit risk:

Mortgages;

Home equity loans;

Other consumer loans (consisting of unsecured and secured consumer loans); and

Credit cards.

*Mortgages, home equity loans and other consumer loans*

For loan losses on mortgages, home equity loans and other consumer loans, we also establish allowances based on loss factors taking into consideration historical performance of the portfolio, previous loan loss history and charge-off information.

We adjust the loss factors derived from the migration analysis as appropriate to reflect the impact of any current conditions on loss recognition that has not been adequately captured by our historical analysis. These include:

Changes in economic and business conditions such as levels of unemployment and house prices;

Change in the nature and volume of the portfolio, including any concentrations of credits; and

The effect of external factors such as regulatory or government requirements.

*Credit Cards*

We establish an allowance for the credit card portfolio using a roll-rate model. A roll-rate model is a statistical tool used to monitor the progression of loans based on aging of the balance and established loss

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rates. The actual loss rates derived from this model are used to project the percentage of losses within each aging category based on performance over an established period of time.

The expected percentage of loss reflects estimates of both default probability within each loan aging bucket and severity of loss. All loans in excess of six months past due are charged off. We adjust our loan loss rate for severity of loss when considering historical recovery of charged off credits when establishing the allowance.

We further segment our credit card portfolio and perform separate roll-rate analyses for card balances, card loans and rewritten card loans to reflect the different risks and characteristics of these portfolios.

We adjust the results from the roll-rate analysis as appropriate to reflect the impact of any current conditions on loss recognition that has not been adequately captured by our historical analysis. These include:

Delinquency levels of cardholders;

Current government involvement within the credit card industry (such as the 2001 Government Amnesty Program);

Key retail performance indicators (such as ratios of household debt to disposable income and household liabilities to financial assets).

The actual amount of incurred loan losses may vary from the estimate of incurred losses due to changing economic conditions or changes in industry or geographic concentrations. We have procedures in place to monitor differences between estimated and actual incurred loan losses, which include detailed periodic assessments by senior management of both individual loans and credit portfolios and the models used to estimate incurred loan losses in those portfolios.

**Loan Aging Schedule**

The following table shows our loan aging schedule (excluding accrued interest) as of the dates indicated.

As of December 31,	Current		Past Due up to 3 Months		Past Due 3-6 Months		Past Due More Than 6 Months		Total Amount	
	Amount	%	Amount	%	Amount	%	Amount	%		
<b>(In billions of Won, except percentages)</b>										
2001	W 32,648	96.98	W 487	1.45	W 144	0.43	W 386	1.14	W 33,665	
2002	43,962	97.58	572	1.27	121	0.27	397	0.88	45,052	
2003	91,940	96.48	1,511	1.59	714	0.75	1,130	1.18	95,295	
2004	94,480	97.32	855	0.88	431	0.45	1,314	1.35	97,080	
2005	103,601	97.87	652	0.62	243	0.23	1,352	1.28	105,848	

**Non-Performing Loans**

Non-performing loans are defined as loans past due by greater than 90 days. These loans are generally rated substandard or below.

The following table shows, as of the dates indicated, certain details of the total non-performing loan portfolio.

	As of December 31,				
	2001	2002	2003	2004	2005
<b>(In billions of Won, except percentages)</b>					
Total non-performing loans	W 530	W 518	W 1,844	W 1,750	W 1,594
As a percentage of total loans	1.57%	1.15%	1.94%	1.80%	1.51%



**Table of Contents****Analysis of Non-Performing Loans**

The following table sets forth, for the periods indicated, the total non-performing loans by type of borrower.

As of December 31,

2001			2002			2003			2004			2005		
Total	Ratio of Non-Performing	Non-Performing	Total	Ratio of Non-Performing	Non-Performing	Total	Ratio of Non-Performing	Non-Performing	Total	Ratio of Non-Performing	Non-Performing	Total	Ratio of Non-Performing	Non-Performing
Loans	Loans	Loans	Loans	Loans	Loans	Loans	Loans	Loans	Loans	Loans	Loans	Loans	Loans	Loans
(In billions of Won, except percentages)														
W 13,459	W 342	2.54%	W 15,800	W 211	1.34%	W 35,617	W 739	2.07%	W 35,653	W 898	2.52%	W 35,728	W 898	2.52%
6,748	125	1.85	9,352	205	2.19	17,378	558	3.21	17,988	468	2.60	21,409	342	1.58
598	3	0.50	636	1	0.16	1,091	8	0.73	981	19	1.94	754	19	2.52
20,805	470	2.26	25,788	417	1.62	54,086	1,305	2.41	54,622	1,385	2.54	57,891	1,385	2.39
7,253	28	0.39	11,539	34	0.29	20,517	133	0.65	22,180	126	0.57	25,840	126	0.49
3,537	16	0.45	4,962	19	0.38	14,580	232	1.59	15,546	155	1.00	17,875	155	0.87
2,070	16	0.77	2,763	48	1.74	6,112	174	2.85	4,732	84	1.78	4,242	84	1.98
12,860	60	0.47	19,264	101	0.52	41,209	539	1.31	42,458	365	0.86	47,957	365	0.76
W 33,665	W 518	1.57%	W 45,052	W 518	1.15%	W 95,295	W 1,844	1.94%	W 97,080	W 1,750	1.80%	W 105,848	W 1,750	1.63%

**Table of Contents*****Top Twenty Non-Performing Loans***

As of December 31, 2005, our twenty largest non-performing loans accounted for 22.0% of our total non-performing loan portfolio. The following table shows, at the date indicated, certain information regarding our twenty largest non-performing loans.

<b>As of December 31, 2005</b>					
<b>Industry</b>			<b>Gross Principal Outstanding</b>	<b>Allowance for Loan Losses</b>	
<b>(In billions of Won)</b>					
1	Borrower A	Manufacturing	W	65	
2	Borrower B	Manufacturing		54	W
3	Borrower C	Manufacturing		36	25
4	Borrower D	Manufacturing		32	33
5	Borrower E	Manufacturing		27	12
6	Borrower F	Real estate, leasing and service		16	
7	Borrower G	Manufacturing		12	
8	Borrower H	Finance and insurance		12	4
9	Borrower I	Hotel and leisure		12	7
10	Borrower J	Other service		11	
11	Borrower K	Construction		10	1
12	Borrower L	Real estate, leasing and service		10	
13	Borrower M	Real estate, leasing and service		9	7
14	Borrower N	Manufacturing		8	
15	Borrower O	Manufacturing		7	7
16	Borrower P	Transportation, storage and communication		6	1
17	Borrower Q	Manufacturing		6	6
18	Borrower R	Manufacturing		6	6
19	Borrower S	Retail and wholesale		6	
20	Borrower T	Manufacturing		6	
			W	351	W
					163

***Non-Performing Loan Strategy***

One of our primary objectives is to prevent our loans from becoming non-performing. Through our corporate credit rating system, we believe that we have reduced our credit risk relating to future non-performing loans. Our credit rating system is designed to prevent our loan officers from extending new loans to borrowers with high credit risks based on the borrower's credit rating. Our early warning system is designed to bring any sudden increase in a borrower's credit risk to the attention of our loan officers, who then closely monitor such loans.

Notwithstanding the above, if a loan becomes non-performing, an officer at the branch level responsible for monitoring non-performing loans will commence due diligence of the borrower's assets, send a notice demanding payment or a notice that we will take legal action or prepare for legal action.

At the same time, we also initiate our non-performing loan management process, which begins with: identifying loans subject to a proposed sale by assessing the estimated losses from such sale based on the estimated recovery value of collateral, if any, for such non-performing loans;

identifying loans subject to charge-off based on the estimated recovery value of collateral, if any, for such non-performing loans and the estimated rate of recovery of unsecured loans; and

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on a limited basis, identifying commercial loans subject to normalization efforts based on the cash-flow situation of the borrower.

Once the details of a non-performing loan are identified, we pursue early solutions for recovery. Actual recovery efforts on non-performing loans are handled by several of our departments or units, depending on the nature of, including the borrower, such loans.

The officers or agents of the responsible departments and units use a variety of methods to resolve non-performing loans, including:

making phone calls and paying visits to the borrower requesting payment;

continuing to assess and evaluate assets of our borrowers; and

if necessary, initiating legal action such as foreclosures, attachments and litigation.

In order to promote speedy recovery on loans subject to foreclosures and litigation, our policy is to permit the branch responsible for handling these loans to transfer them to the relevant unit at headquarters or regional headquarters.

Our policy is to commence legal action within one month after default on promissory note and four months after delinquency of payment on loans. For loans to insolvent or bankrupt borrowers, we take legal action immediately.

In addition to making efforts to collect on these non-performing loans, we also undertake measures to reduce the level of our non-performing loans, which include:

selling non-performing loans to third parties including the Korea Asset Management Corporation;

entering into asset-backed securitization transactions with respect to non-performing loans;

managing consumer loans that are three months or more past due through Shinhan Credit Information under an agency agreement in the case of Shinhan Bank and through Consumer Loan Collection Division in the case of Chohung Bank; and

using third-party collection agencies including the Solomon Credit Information.

***Allocation of Allowance for Loan Losses***

The following table presents the allocation of our loan loss allowance by loan type. The ratio represents the percentage of loan loss allowance of each loan type to total loan loss allowance.

**As of December 31,**

**2001                      2002                      2003                      2004                      2005**

**(In billions of Won, except percentages)**

	2001		2002		2003		2004		2005	
Corporate										
Commercial and Industrial	W 323	44.86%	W 341	34.24%	W 1,383	38.09%	W 1,065	46.08%	W 753	49.80%
Other commercial	275	38.19	365	36.65	626	17.24	410	17.74	305	20.17
Lease financing	35	4.86	22	2.21	45	1.24	24	1.04	16	1.06
Total corporate	633	87.91	728	73.10	2,054	56.57	1,499	64.86	1,074	71.03

Consumer										
Mortgages and home equity	9	1.25	30	3.01	53	1.46	36	1.56	19	1.26
Other consumer	22	3.06	59	5.92	659	18.15	368	15.92	183	12.10
Credit cards	56	7.78	179	17.97	865	23.82	408	17.66	236	15.61
Total consumer	87	12.09	268	26.90	1,577	43.43	812	35.14	438	28.97
Total allowance for loan losses	W 720	100.00%	W 996	100.00%	W 3,631	100.00%	W 2,311	100.00%	W 1,512	100.00%

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Our total allowance for loan losses decreased by W799 billion, or 34.6%, to W1,512 billion as of December 31, 2005 from W2,311 billion as of December 31, 2004. During 2004, the allowance for loan losses decreased by W1,320 billion, or 36.4%, from W3,631 billion as of December 31, 2003 to W2,311 billion as of December 31, 2004, due primarily to an increase in charge-offs from 2003 to 2004 resulting from improving credit quality of corporate loans. During 2005, the allowance for loan losses decreased by W799 billion primarily as a result of continued improvement in the credit quality of our overall loan portfolios. The total loan balance increased by W8,768 billion in 2005, 41.7% of which, or W3,660 billion, was accounted for by the increase in mortgage and home equity loans which are considered to have a lower credit risk than other types of loans. On the other hand, our credit card portfolio which tends to have a higher credit risk decreased by W490 billion in 2005. In addition, the ratio of nonaccrual loans to total loans significantly decreased from 2.53% as of December 31, 2004 to 1.94% as of December 31, 2005. The ratio of non-performing loans to total loans also decreased to 1.51% as of December 31, 2005 from 1.80% as of December 31, 2004. Accordingly, this improvement in the credit quality of our loan portfolios resulted in a sizable decrease in the amount of loans charged off and a reversal of provision for credit losses in 2005.

The allowance for corporate loan losses decreased by W555 billion, or 27.0%, from W2,054 billion as of December 31, 2003 to W1,499 billion as of December 31, 2004. This decrease is primarily attributable to a reduction in impaired loans. The allowance for corporate loan losses decreased by W425 billion, or 28.4%, from W1,499 billion as of December 31, 2004 to W1,074 as of December 31, 2005, primarily due to the improved credit quality of our loans to large corporations and small- to medium enterprises.

In the consumer sector, our allowance for loan losses decreased by W765 billion, or 48.5%, from W1,577 billion as of December 31, 2003 to W812 billion as of December 31, 2004, primarily due to a reduction in marketing scoring system loans and credit card loans. The allowance for loan losses decreased by W374 billion, or 46.1%, from W812 billion as of December 31, 2004 to W438 as of December 31, 2005, primarily due to the reduction in Chohung Bank-originated credit card loans (including revolving loans) and favored customer loans and improved credit quality in unsecured loans to individuals.

**Table of Contents*****Analysis of the Allowance for Loan Losses***

The following table presents an analysis of our loan loss experience for each of the years indicated.

	2001	2002	2003	2004	2005
<b>(In billions of Won, except percentages)</b>					
Balance at the beginning of the period	W 828	W 720	W 996	W 3,631	W 2,311
Amounts charged against income	411	236	1,011	195	(255)
Allowance relating to loans repurchased from the Korea Asset Management Corporation	45	65	32	2	
Gross charge-offs:					
Corporate:					
Commercial and industrial	379	105	255	465	297
Other commercial	345	22	223	26	18
Lease financing	5	10	6		
Consumer:					
Mortgage and home equity	2	2	12	18	19
Other consumer	9	17	135	441	296
Credit cards	39	60	765	872	316
Total gross charge-offs	(779)	(216)	(1,396)	(1,822)	(946)
Recoveries:					
Corporate:					
Commercial and industrial	60	53	82	105	69
Other commercial	58	21	73	121	217
Lease financing	1	2		2	4
Consumer:					
Mortgage and home equity			1	1	3
Other consumer	2	1	23	22	34
Credit cards	7	17	69	56	72
Total recoveries	128	94	248	307	399
Net charge-offs	(651)	(122)	(1,148)	(1,515)	(547)
Acquisition of Chohung Bank		20	2,740		
Acquisition of Jeju Bank		77	2,740		
Acquisition of Good Morning Securities	64		2,740		
Acquisition of Shinhan Securities	23		2,740		
Acquisition of Shinhan Life Insurance					3
Balance at the end of the period	W 720	W 996	W 3,631	W 2,311	W 1,512
Ratio of net charge-offs during the period to average loans outstanding during the period	2.07%	0.30%	1.74%	1.52%	0.53%

***Loan Charge-Offs***

Our level of gross charge-offs declined from W779 billion in 2001 to W216 billion in 2002 primarily due to a small number of large exposures within our corporate portfolio that we deemed to be uncollectible, based on events occurring, in 2001. The number of corporate loans charged off was similar in both years but the amounts charged off in 2001 were, on average, significantly higher. The five largest charge-offs in the aggregate were W419 billion and W49 billion in 2001 and 2002, respectively. The charge-offs in 2001 included W271 billion in respect of Hynix Semiconductor and W18 billion in respect of Incheon Oil Refinery. The

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exposures charged off in 2001 were individually identified as impaired and therefore included within our allowance as of December 31, 2000 at an amount consistent with the level of gross charge off. Similarly, charge-offs occurring in 2002 were recorded at a consistent amount within our allowance as of December 31, 2001. The decrease in gross charge offs was partly offset by increases in credit card and other consumer charge-offs from W48 billion in 2001 to W77 billion in 2002 reflecting increased delinquencies within these portfolios. Our level of gross charge-offs increased from W1,396 billion in 2003 to W1,822 billion in 2004 primarily due to an increase in charge-offs of marketing scoring system loans, which are loans offered to certain of our customers primarily based on the number of transactions such customers make with us rather than the credit rating of such customers. The charge-offs in 2003 included W128 billion in respect of SK Networks. Our level of gross charge-offs decreased from W1,822 billion in 2004 to W946 billion in 2005 primarily due to a decrease in credit card charge-offs in 2005 compared to 2004, when charge-offs were aggressively made.

*Basic Principles*

We attempt to minimize loans to be charged off, by practicing a sound credit approval process based on credit risk analysis prior to extending loans and a systematic management of outstanding loans.

*Loans To Be Charged-Off*

Loans are charged-off if they are deemed to be uncollectible by falling under any of the following categories:  
loans for which collection is not foreseeable due to insolvency or bankruptcy, dissolution or the shutting down of the business of the debtor;

loans for which collection is not foreseeable due to the death or disappearance of debtors;

loans for which expenses of collection exceed the collectable amount;

loans on which collection is not possible through legal or any other means;

payments in arrears in respect of credit cards, which are overdue for more than six months;

payments outstanding on unsecured consumer loans, which have been overdue for more than six months;

payments in arrears in respect of leases, which have been overdue for more than twelve months; or

the portion of loans classified as estimated loss, net of any recovery from collateral, which is deemed to be uncollectible.

*Procedure for Charge-off Approval*

An application for Shinhan Bank's loans to be charged-off is submitted by a branch to the Corporate Credit Collection Department in the case of corporate loans and foreign branches, and Consumer Credit Collection Department in the case of individual loans. An application for charge off must be submitted four months prior to the date of the write-off, which is the end of every quarter. The General Manager in charge of review evaluates the application. The General Manager of Audit and Examination Department conducts review of compliance with our internal procedures for charge-offs. The General Manager in charge of review gets approval from the President of Shinhan Bank.

*Treatment of Loans Charged-Off*

Once loans are charged-off, they are derecognized from our balance sheet. Shinhan Bank still continues its collection efforts in respect of these loans through third-party collection agencies including the Korea Asset Management Corporation and Shinhan Credit Information. Chohung Bank also continues its collection efforts in respect of these loans internally using credit information produced by third parties or through third-party collection agencies including Solomon Credit Information.



**Table of Contents*****Treatment of Collateral***

When Shinhan Bank determines that a loan collateralized by real estate cannot be recovered through normal collection channels, then Shinhan Bank will petition a court to foreclose and sell the collateral through a court-supervised auction within one month after default and insolvency and within four months after delinquency. When Chohung Bank determined that a loan collateralized by real estate cannot be recovered through normal collection channels, Chohung Bank would petition a court to foreclose and sell the collateral through a court-supervised auction within one month after default and insolvency, within four months after delinquency and immediately upon default occurring at the branch level. However, this treatment does not apply to companies under restructuring, composition, workout or other court proceedings subjecting them to restrictions on such auction procedures. In our experience, the filing of this petition with the court generally encourages the debtor to repay the overdue loan. If a debtor ultimately fails to repay and the court grants its approval for foreclosure, we will sell the collateral and recover the full principal amount and accrued interest up to the sales price, net of expenses incurred from the auction. Foreclosure proceedings under laws and regulations in Korea typically take from seven months to one year from initiation to collection depending on the nature of the collateral.

***U.S. GAAP Financial Statement Presentation***

Our U.S. GAAP financial statements include as charges-offs all unsecured consumer loans, including credit cards, that are overdue for more than six months. Leases are charged-off when past due for more than twelve months.

**Investment Portfolio*****Investment Policy***

We invest in and trade Won-denominated and, to a lesser extent, foreign currency-denominated securities for our own account to:

maintain the stability and diversification of our assets;

maintain adequate sources of back-up liquidity to match our funding requirements; and

supplement income from our core lending activities.

In making securities investments, we take into account a number of factors, including macroeconomic trends, industry analysis and credit evaluation in determining whether to make investments in particular securities.

Our investments in securities are also subject to a number of guidelines, including limitations prescribed under the Financial Holding Companies Act and the Bank Act. Under these regulations, a financial holding company may not invest in securities as defined in the Securities and Exchange Act (other than those securities issued by its direct and indirect subsidiaries) in excess of the amount of its shareholders' equity less the total amount of investment in subsidiaries, subject to certain exceptions. Generally, a financial holding company is prohibited from acquiring more than 5% of the total issued and outstanding shares of another company (other than its direct and indirect subsidiaries). Furthermore, under these regulations, Shinhan Bank (and, prior to the merger, also Chohung Bank) must limit its investments in shares and securities with a maturity in excess of three years (other than monetary stabilization bonds issued by the Bank of Korea and national government bonds) to 60.0% of our total Tier I and Tier II capital. Generally, Shinhan Bank (and, prior to the merger, also Chohung Bank) is also prohibited from acquiring more than 15.0% of the shares with voting rights issued by any other corporation (other than for the purpose of establishing or acquiring a subsidiary). Further information on the regulatory environment governing our investment activities is set out in *Supervision and Regulation* *Principal Regulations Applicable to Banks* *Restrictions on Investments in Property* , *Principal Regulations Applicable to Banks* *Restrictions on Shareholdings in Other Companies* , *Principal Regulations Applicable to Financial Holding Companies* *Liquidity* and

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Principal Regulations Applicable to Financial Holding Companies    Restrictions on Shareholdings in Other Companies .

***Book Value and Market Value***

The following table sets out the book value and market value of securities in our investment portfolio as of the dates indicated.

	As of December 31, 2003		As of December 31, 2004		As of December 31, 2005	
	Book Value	Market Value	Book Value	Market Value	Book Value	Market Value
(In billions of Won)						
<b>Available-for-sale securities</b>						
Marketable equity securities	W 435	W 435	W 507	W 507	W 1,978	W 1,978
Debt securities:						
Korean treasury and governmental agencies	8,982	8,982	8,835	8,835	8,299	8,299
Financial institutions	5,998	5,998	5,675	5,675	9,255	9,255
Corporations	1,552	1,552	1,292	1,292	1,952	1,952
Foreign government	13	13	57	57	50	50
Mortgage-backed and asset-backed securities	1,119	1,119	1,742	1,742	946	946
Total Available-for-sale	18,099	18,099	18,108	18,108	22,480	22,480
<b>Held-to-maturity securities</b>						
Debt securities:						
Korean treasury and governmental agencies	2,351	2,472	1,662	1,814	1,686	1,706
Financial institutions	553	574	1,219	1,268	1,211	1,208
Corporations	365	376	218	225	66	66
Mortgage-backed and asset-backed securities	336	339				
Total Held-to-maturity	3,605	3,761	3,099	3,307	2,963	2,980
<b>Trading Securities</b>						
Marketable equity securities	279	279	312	312	465	465
Debt securities:						
Korean treasury and governmental agencies	1,152	1,152	1,995	1,995	493	493
Financial institutions	1,013	1,013	1,322	1,322	1,145	1,145
Corporations	369	369	965	965	1,307	1,307
Mortgage-backed and asset-backed securities	40	40	20	20	140	140
Other trading assets(1)	4	4	25	25	23	23

Total	Trading	2,857	2,857	4,639	4,639	3,573	3,573
<b>Total securities</b>		W 24,561	W 24,717	W 25,846	W 26,054	W 29,016	W 29,033

*Note:*

(1) Consists of commodity indexed deposits.

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The following table categorizes our securities by maturity and weighted average yield as of December 31, 2005.

	1 Year or Less		Over 1 Year Through 5 Years		Over 5 Years Through 10 Years		Over 10 Years		Securities Not Due In a Single Maturity(1)		Total	
	Weighted- Carrying Amount	Average Yield(2)	Weighted- Carrying Amount	Average Yield(2)	Weighted- Carrying Amount	Average Yield(2)	Weighted- Carrying Amount	Average Yield(2)	Weighted- Carrying Amount	Average Yield(2)	Weighted- Carrying Amount	Average Yield(2)

(In billions of Won, except percentages)

**Available-for-sale  
securities:**

Korean treasury and governmental agencies	W 1,822	4.60%	W 4,391	4.36%	W 326	4.16%	W		W 1,760	6.24%	W 8,299	4.80%
Financial institutions	5,563	4.06	3,329	4.44	227	6.46	60	6.17%	76	4.93	9,255	4.28
Corporations	552	4.93	1,277	5.29	96	3.92	27	5.94			1,952	5.13
Foreign government	18	2.70	23	5.14	4	6.38	5	4.94			50	4.35
Mortgage-backed and asset-backed securities	143	5.04	523	5.11	280	5.21					946	5.13
<b>Total Available for sale</b>	<b>8,098</b>	<b>4.26%</b>	<b>9,543</b>	<b>4.55%</b>	<b>933</b>	<b>5.01%</b>	<b>92</b>	<b>6.04%</b>	<b>1,836</b>	<b>6.19%</b>	<b>20,502</b>	<b>4.61%</b>

**Held-to-maturity  
securities:**

Korean treasury and governmental agencies	338	6.72%	1,318	5.71%	30	4.01%					1,686	5.88%
Financial institutions	373	4.85	821	5.17	17	5.36					1,211	5.08
Corporations	11	6.07	55	5.56							66	5.64
<b>Total Held-to- maturity</b>	<b>722</b>	<b>5.74%</b>	<b>2,194</b>	<b>5.51%</b>	<b>47</b>	<b>4.50%</b>					<b>2,963</b>	<b>5.55%</b>

<b>Trading securities:</b>												
Korean treasury and governmental agencies	72	4.41%	362	4.15%	8	3.90%	1	4.79%	50	5.05%	493	4.27%
Financial institutions	950	4.13	195	4.61							1,145	4.21
Corporations	417	4.35	890	5.42							1,307	4.99
Mortgage-backed and asset-backed securities	140	4.09									140	4.09
<b>Total Trading</b>	<b>1,579</b>	<b>4.16%</b>	<b>1,447</b>	<b>4.59%</b>	<b>8</b>	<b>3.80%</b>	<b>1</b>	<b>4.79%</b>	<b>50</b>	<b>5.05%</b>	<b>3,085</b>	<b>4.33%</b>
<b>Total Securities</b>	<b>W 10,399</b>		<b>W 13,184</b>		<b>W 988</b>		<b>W 93</b>		<b>W 1,886</b>		<b>W 26,550</b>	

*Note:*

- (1) The principal repayment schedule for such securities is based on installment due on different maturity dates.
- (2) The weighted-average yield for the portfolio represents the yield to maturity for each individual security, weighted using its amortized cost.

**Table of Contents****Concentrations of Risk**

As of December 31, 2005, we held the following securities of individual issuers where the aggregate book value of those securities exceeded 10.0% of our stockholders' equity at such date.

Name of issuer:	As of December 31, 2005			
	Book Value		Market Value	
	(In billions of Won)			
Korean Government	W	4,682	W	4,684
Korea Deposit Insurance Corporation		3,805		3,815
Bank of Korea		6,100		6,100
Korea Development Bank		1,137		1,137
Total	W	15,724	W	15,736

Our stockholders' equity as of December 31, 2005 was W7,811 billion.

All of the above entities (other than the Korean government) are controlled and owned by the government.

**Credit-Related Commitments and Guarantees**

In the normal course of our banking activities, we make various commitments and guarantees to meet the financing and other business needs of our customers. Commitments and guarantees are usually in the form of, among others, commitments to extend credit, commercial letters of credit, standby letter of credit and performance guarantees. The contractual amount of these financial instruments represents the maximum possible loss amount if the account party draws down the commitment or we should fulfill our obligation under the guarantee and the account party fails to perform under the contract.

The following table sets forth our credit-related commitments and guarantees as of the dates indicated.

	As of December 31,		
	2003	2004	2005
	(In billions of Won)		
Commitments to extend credit:			
Corporate	W 32,922	W 39,323	W 46,336
Credit cards(1)	17,207	23,606	16,080
Consumer	3,752	5,961	5,863
Commercial letters of credit(2)	3,075	3,364	2,960
Standby letters of credit, other financial and performance guarantees and liquidity facilities to SPEs	4,686	3,407	4,604
Total	W 61,642	W 75,661	W 75,843

**Notes:**

- (1) Relates to the unused portion of credit card limits that may be cancelled by us after notice to the borrower if we determine that the borrower's repayment ability is significantly impaired.

(2) These are generally short-term and collateralized by the underlying shipments of goods to which they relate.

We have credit-related commitments that are not reflected on the balance sheet, which primarily consist of commitments to extend credit and commercial letters of credit. Commitments to extend credit, including credit lines, represent unfunded portions of authorizations to extend credit in the form of loans. These commitments expire on fixed dates and a customer is required to comply with predetermined conditions to draw funds under the commitments.

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Commercial letters of credit are undertakings on behalf of customers authorizing third parties to draw drafts on us up to a stipulated amount under specific terms and conditions. They are generally short-term and collateralized by the underlying shipments of goods which they relate to and therefore have less risk.

We also have guarantees that are recorded on the balance sheet at their fair value at inception which is amortized over the life of the guarantees. Such guarantees generally include standby letters of credit, other financial and performance guarantees and liquidity facilities to SPEs.

Standby letters of credit are irrevocable obligations to pay third party beneficiaries when our customers fail to repay loans or debt instruments, which are generally in foreign currencies. A substantial portion of these standby letters of credit are secured by underlying assets, including trade-related documents.

Other financial and performance guarantees are irrevocable assurance that we make payments to beneficiaries in the event that our customers fail to fulfill their obligations or to perform under certain contracts. Liquidity facilities to SPEs represent irrevocable commitments to provide contingent liquidity credit lines to SPEs established by our customers in the event that a triggering event such as shortage of cash occurs. See Note 30 in Item 18. Financial Statements Notes to consolidated financial statements of Shinhan Financial Group for details.

The commitments and guarantees do not necessarily represent our exposure since they often expire unused.

**Derivatives**

As discussed under Business Overview Our Principal Activities Treasury and Securities Investment above, we engage in derivatives trading activities primarily on behalf of our customers so that they may hedge their risks and also enter into back-to-back derivatives with other financial institutions to cover exposures arising from such transactions. In addition, we enter into derivatives transactions to hedge against risk exposures arising from our own assets and liabilities, some of which are nontrading derivatives that do not qualify for hedge accounting treatment.

The following shows, as of December 31, 2005, the gross notional or contractual amounts of derivatives and foreign exchange contracts held or issued for (i) trading and (ii) nontrading that qualify for hedge accounting.

**As of December 31, 2005**

	<b>Underlying Notional Amount(1)</b>	<b>Estimated Fair Value Assets</b>	<b>Estimated Fair Value Liabilities</b>
<b>(In billions of won)</b>			
<b>Trading:</b>			
Foreign exchange contracts:			
Forward contracts	W 32,420	W 341	W 376
Futures	140		
Options purchased	4,067	19	26
Options written	2,810	12	23
Sub-total	39,437	372	425
Interest rate contracts:			
Swaps(2)	29,468	173	238
Futures	98		
Options purchased	10		
Options written			
Sub-total	29,576	173	238
Cross currency swaps	11,336	310	268



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As of December 31, 2005						
	Underlying Notional Amount(1)	Estimated Fair Value Assets	Estimated Fair Value Liabilities			
(In billions of won)						
Equity contracts:						
Futures	312					
Option purchased	935	68				
Option written	1,005					72
Sub-total	2,252	68				72
Other derivatives:						
Option purchased	103	11				
Option written	103					11
Sub-total	206	11				11
Credit derivatives	66					
<b>Total</b>	<b>W 82,873</b>	<b>W 934</b>	<b>W 1,014</b>			
Hedge accounting:						
Interest rate swaps	1,041	1				13
Sub-total	1,041	1				13
Nontrading that do not qualify for hedge accounting						
Interest rate swaps	5,587	13				100
Cross currency swaps	777	2				11
<b>Total</b>	<b>W 6,364</b>	<b>W 15</b>	<b>W 111</b>			

*Notes:*

- (1) Notional amounts in foreign currencies were converted into Won at prevailing exchange rates as of December 31, 2005.
- (2) While we engage in derivatives trading activities to hedge the interest rate risk exposure that arise from our own assets and liabilities, as these nontrading derivative contracts do not qualify for hedge accounting under U.S. GAAP, they are accounted for as trading derivatives in the financial statements. As a result, includes interest rate swaps and cross-currency swaps held for nontrading that do not qualify for hedge accounting treatment in the underlying notional amount, estimated fair value of assets and estimated fair value of liabilities of W6,364 billion, W15 billion and W111 billion, respectively.

**Funding**

We obtain funding for our lending activities from a variety of sources, both domestic and foreign. Our principal source of funding is customer deposits obtained from our banking operations. In addition, Shinhan Bank and Chohung Bank acquire funding through call money, borrowings from the Bank of Korea, other short-term borrowings and other long-term debt.

Our primary funding strategy has been to achieve low-cost funding by increasing the average balances of low-cost retail deposits. Customer deposits accounted for 68.3% of our total funding as of December 31, 2003, 66.9% of our total funding as of December 31, 2004 and 65.4% of our total funding as of December 31, 2005. As of December 31, 2003, 2004 and 2005, W4,205 billion, W4,329 billion and W5,002 billion, or 10.8%, 11.2% and 12.6%, respectively, of Chohung Bank's total deposits in Korean Won were deposits made by litigants in connection with legal proceedings in Korean courts. Court deposits carry interest rates, which are generally lower than market rates.

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In addition, we acquire funding through the issuance of bonds, primarily through our banking subsidiary. Our borrowings consist mainly of borrowings from financial institutions, the Korean government and Korean government-affiliated funds. Call money, which is available in both Won and foreign currencies, is obtained from the domestic call loan market, a short-term loan market for loans with maturities of less than one month.

**Deposits**

Although the majority of our bank deposits are short-term, it has been our experience that the majority of our depositors generally roll over their deposits at maturity, providing our banking operation with a stable source of funding.

The following table shows the average balances of our deposits and the average rates paid on our deposits for the periods indicated.

	2003		2004		2005	
	Average Balance(1)	Average Rate Paid	Average Balance(1)	Average Rate Paid	Average Balance(1)	Average Rate Paid
<b>(In billions of Won, except percentages)</b>						
<b>Interest-bearing deposits:</b>						
Interest-bearing demand deposits	W 2,653	1.39%	W 7,880	1.33%	W 6,594	1.90%
Savings deposits	15,922	1.46	21,987	1.24	26,100	0.96
Certificates of deposit	4,954	4.44	6,735	4.08	8,838	3.81
Other time deposits	27,776	4.19	41,863	3.83	39,031	3.69
Mutual installment deposits(2)	2,109	5.36	2,487	4.54	1,997	4.16
<b>Total interest-bearing deposits(3)</b>	<b>W 53,414</b>	<b>3.31%</b>	<b>W 80,952</b>	<b>2.93%</b>	<b>W 82,560</b>	<b>2.71%</b>

**Notes:**

- (1) Average balances are based on daily balances for our primary banking operation and quarterly balances for subsidiaries.
- (2) Mutual installment deposits are interest-bearing deposits offered by Shinhan Bank which enable customers to become eligible for loans while they maintain an account with us. The customer's account does not have to secure loan amounts once made but is a requirement for loan eligibility. Prior to qualifying for a loan a customer must make required periodic deposits to the mutual installment account for a contracted term of less than five years. A customer is not required to fulfill the deposit term prior to requesting a loan from Shinhan Bank, but loan amounts and terms are not as favorable in the event of a loan request prior to completing the deposit contract term.
- (3) Under U.S. GAAP, does not include cover bills sold or bonds sold under repurchase agreements, which are offered to our customers as deposit products. These are reflected as short-term borrowings and secured borrowings, respectively.

For a breakdown of retail deposit products, see [Business Overview](#) [Our Principal Activities](#) [Deposit-taking Activities](#) , except that cover bills sold are reflected on short-term borrowings and securities sold under repurchase agreements are reflected as secured borrowings.

**Table of Contents***Certificates of Deposit and Other Time Deposits*

The following table presents the balance and remaining maturities of our other time deposits, certificates of deposit and mutual installment deposits which had a fixed maturity in excess of W100 million or more as of December 31, 2005.

	<b>As of December 31, 2005</b>			
	<b>Certificates of Deposit</b>	<b>Other Time Deposits</b>	<b>Mutual Installment Deposits</b>	<b>Total</b>
	<b>(In billions of Won)</b>			
Maturing within three months	3,775	4,971	83	8,829
After three but within six months	2,247	2,526	62	4,835
After six but within 12 months	2,947	11,402	117	14,466
After 12 months	1,261	1,939	135	3,335
<b>Total</b>	<b>10,230</b>	<b>20,838</b>	<b>397</b>	<b>31,465</b>

A majority of our certificates of deposit accounts and other time deposits issued by our foreign offices is in the amount of US\$100,000 or more.

*Japanese Yen Deposits and Dispute with the Korean National Tax Service*

Beginning in 2002, commercial banks in Korea, including Shinhan Bank and Chohung Bank, offered to their customers deposit products that utilize Korean Won and Japanese Yen swaps to maximize the return for such customers. According to the terms of these deposit products, deposits made by customers in Korean Won are converted into Japanese Yen and repaid in Japanese Yen at maturity. The repayment amount is then converted back into Korean Won. While these deposit products typically carry a low interest rate, ranging from 0.05% to 0.30% per annum, the actual return to the customers was higher as a result of foreign exchange gains. These deposit products are attractive to customers, in particular high net worth customers, since the gains from foreign exchange were deemed not to be interest subject to income tax. However, in 2005, the Korean National Tax Service announced that foreign currency deposits disguised as derivative products would be subject to tax and tax withholding and issued a recommendation that the banks should refile its tax returns to include the unwithheld amounts. Eight of the commercial banks in Korea, who are subject to this adverse tax treatment, have announced their intention to challenge the foregoing decision by the Korean National Tax Service while complying with the Tax Service's information requests.

The commercial banks had marketed these deposit products to their customers on the basis that such deposit products were exempt from income tax or tax withholding. We believe that few, if any, of these customers have reported the gains from such deposit products as interest income subject to taxation in their tax returns. According to the Korean National Tax Service, these deposit customers are also responsible for including the income received from these deposits in their final individual tax returns relating to comprehensive financial taxable income. However, depending on the amount of income received from these products, the individual customers may be subject to (i) a higher tax rate on all of his or her taxable income, (ii) a fine for failing to properly report the interest income in an amount equal to 20% of the unreported amount, and (iii) a fine for failing to pay tax on such interest income in an amount equal to interest applied at a rate of 10.95% per annum to such unpaid tax amount. No assurance can be given that aggrieved customers will not bring claims against these commercial banks, including Shinhan Bank and Chohung Bank, if their tax liabilities are increased as a result of the foregoing events.

Beginning in September 2005, we have been subject to a tax audit by the Korean National Tax Service. In May 2006, based upon its tax audit of us and other relevant banks, the Korean National Tax Service reached a decision to impose additional taxes (including interest thereon) of W36 billion on Shinhan Bank. This decision did not include a judgment on deposits utilizing the Korean Won and Japanese Yen swaps as described above, but such judgment is expected soon. In anticipation of an adverse tax ruling against these deposit products utilizing Korean Won and Japanese Yen swaps, we have determined, on a voluntary basis, to

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indemnify our customers for their increased tax liability to the extent resulting from their investment in these deposit products, including any additional tax liability that our customers may have against the Korean National Tax Service for gifts tax from the benefit of this indemnity. We currently estimate that we may be subject to maximum additional tax-related liability, including the liability from the indemnity to our customers, of W85 billion as of December 31, 2005. Accordingly, we recorded a total charge to our income of W78 billion in the year ended December 31, 2005, consisting of additional tax expenses of W29 billion and provision for other losses of W49 billion. In addition, we also recorded W7 billion as deferred tax assets on our balance sheet as of December 31, 2005.

See Item 3. Key Information Risk Factors Risks Relating to Our Banking Business Our current dispute with the Korean National Tax Service relating to certain deposit products, if adversely resolved, and together with potential claims from our customers, may materially and adversely affect our financial condition and results of operations.

**Table of Contents****Short-term Borrowings**

The following table presents information regarding our short-term borrowings (borrowings with an original maturity of one year or less) for the periods indicated.

2003				2004				2005			
Highest Balances at		Weighted Average		Highest Balances at		Weighted Average		Highest Balances at		Weighted Average	
Average Balance Outstanding	Any Month-End	Average Interest Rate(2)	Year-End Interest Rate	Average Balance Outstanding	Any Month-End	Average Interest Rate(2)	Year-End Interest Rate	Average Balance Outstanding	Any Month-End	Average Interest Rate(2)	Year-End Interest Rate
W 1,122	W 2,669	2.41%	1.12- 2.50%	W 1,568	W 1,737	W 2,056	2.32%	2.00- 2.50%	W 1,668	W 1,581	W 1,737
1,803	3,742	3.55%	0.15- 3.65%	1,156	3,512	5,238	3.30%	0.75- 5.00%	994	2,930	5,612
8,475	11,300	2.04%	0.05- 10.15%	8,230	9,685	11,166	2.21%	0.04- 18.00%	9,306	10,464	11,934
W 11,400	W 17,711	2.82%		W 10,954	W 14,934	W 18,460	2.48%		W 11,968	W 14,975	W 19,300

(In billions of Won, except for percentages)

**Notes:**

- (1) Average outstanding balances have been calculated using daily balances for our primary banking operations and quarterly balances for subsidiaries.
- (2) Weighted-average interest rates during this year are calculated by dividing the total interest expenses by the average amount borrowed.
- (3) Borrowings from the Bank of Korea generally mature within one month for borrowings in Won and six months for borrowings on foreign currencies.
- (4) Other short-term borrowings included borrowings from trust accounts, bills sold, borrowings in domestic and foreign currencies and short-term debentures.

Our short-term borrowings have maturities of less than one year which are generally unsecured with the exception of borrowings from the Bank of Korea.

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### **Risk Management**

#### ***Overview***

As a financial services provider, we are exposed to various risks relating to our lending, securities investment, credit card, insurance, trading and leasing businesses, our deposit taking and borrowing activities and our operating environment. The principal risks to which we are exposed are credit risk, market risk, liquidity risk and operational risk. These risks are recognized, measured and reported in accordance with risk management guidelines established at our holding company level.

Our risk management is guided by several principles, including:

identifying and managing all inherent risks;

standardizing risk management process and methodology;

ensuring supervision and control of risk management independent of business activities;

continuously assessing risk preference;

preventing risk concentration;

operating a precise and comprehensive risk management system including statistical models; and

balancing profitability and risk management through risk-adjusted profit management.

#### ***Organization***

Risk management and oversight begins with the Group Risk Management Committee of the board of directors at the holding company level. The Group Risk Management Committee establishes the overall risk management guidelines and risk limits applicable to the group and each subsidiary, while delegating the day-to-day risk management and oversight functions to the Managing Director of Risk Management and the Risk Management Team. The Managing Director of Risk Management discusses the risk management policies and strategies of the Group and its subsidiaries at the Group Risk Management Council, comprised of the Managing Director of Risk Management, as its chairperson, and the executive officers of risk management from its subsidiaries. The Risk Management Team provides support to the Group Risk Management Committee, the Managing Director of Risk Management and the Group Risk Management Council, oversees the overall risk management for the Group and coordinates the risk management strategies among the Group's subsidiaries.

In order to maintain the Group's risk at an appropriate level, we have established a hierarchical limit system, where the Group Risk Management Committee establishes risk limits for the holding company and each subsidiary, and each subsidiary establishes and manages more detailed risk limits by type of risk and type of product for each department and division within the respective subsidiary. In accordance with the group risk management policies and strategies, each subsidiary's risk management committee establishes its own risk management policies and strategies in more detail and the respective risk management department implements those policies and strategies. The risk management department, operating independently from business operations of each subsidiary, monitors, assesses, manages and controls the overall risk of its operations and reports all major risk-related issues to the Group's Risk Management Team, which then reports to the Managing Director of Risk Management.

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The following table sets forth the levels of our risk management system.

***Group Risk Management Committee***

The Group Risk Management Committee consists of three outside directors of the holding company. The Group Risk Management Committee convenes at least once every quarter and may also convene on an *ad hoc* basis as needed. The Group Risk Management Committee makes decisions related to:

establishing basic risk management policies consistent with business strategy;

establishing risk limits appropriate for the group and each subsidiary;

establishing and amending, as necessary, risk management regulations, which regulates risk management activities of the group as well as each subsidiary, establishes risk limits and provides risk management guidelines; and

other risk management-related issues the board of directors or the Group Risk Management Committee see fit to discuss.

The results of Group Risk Management Committee meetings are reported to the board of directors of the holding company. The Group Risk Management Committee makes decisions through affirmative votes by a majority of the committee members.

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***Group Risk Management Council***

The Group Risk Management Council provides a forum for risk management executives from each subsidiary to discuss the group's risk management guidelines and strategy in order to maintain consistency in the group risk policies and strategies. The Group Risk Management Council consists of the holding company's Managing Director of Risk Management, as chairman, the executive officers in charge of risk management of each of our subsidiaries and the head of the Risk Management Team of the holding company. The Group Risk Management Council discusses:

changes in risk management policies and strategies for each subsidiary;

matters warranting discussion of risk management at the group level and cooperation among the subsidiaries;

the effect of externalities on the group's risk; and

other risk management-related matters.

The Group Risk Management Council has a sub-council, consisting of working-level risk management officers, to discuss the above-related matters in advance. The principal function of the Risk Management Team is to oversee the risk management operations at the subsidiary level.

***Credit Risk Management of Shinhan Bank***

Credit risk, which is the risk of loss from default by an obligor or counter-party, is the greatest risk we face. A substantial majority of our credit risk is derived from Shinhan Bank (including the operations of Chohung Bank after the merger) and Shinhan Card. The discussion in this section focuses on credit risk management of Shinhan Bank and takes into account the merger of Shinhan Bank and Chohung Bank which became effective on April 3, 2006.

Shinhan Bank's credit risk management is guided by the following principles:

achieve profit level corresponding to the level of risks involved;

improve asset quality and achieve optimal industrial and rating loan portfolio;

focus on the small- and medium-sized enterprises and markets;

avoid excessive loan concentration to a particular borrower or sector;

focus on borrower's ability to repay the debt; and

financially support our select customers' growth.

Major policies for Shinhan Bank's credit risk management are determined by the Credit Policy Committee, the executive decision-making body for management of credit risk. The Credit Policy Committee is led by the Deputy President & head of Risk Management Group. The Credit Policy Committee further consists of chief officers from nine business divisions. The Credit Review Committee makes decisions by 2/3 or more votes of the attending members, which must constitute at least two-thirds of the committee members to satisfy the quorum.

Shinhan Bank performs credit risk management procedures pursuant to internal guidelines and regulations and continually monitors and improves these guidelines and regulations. Its credit risk management procedures include:

credit evaluation and approval;

credit review and monitoring; and

credit risk assessment and control.

**Table of Contents***Credit Evaluation and Approval*

All loan applicants and guarantors are subject to credit review evaluation before approval of any loans. Credit evaluation of loan applicants are carried out on a separate level by Credit Officer and Senior Credit Officer and (senior) credit officer committees consisting of loan evaluation specialists from different areas. Loan evaluation is carried out by a group rather than by an individual level through objective and deliberate process. Shinhan Bank uses a credit scoring system for consumer loans and credit-risk rating system for commercial loans.

*Consumer loans*

Loan applications for consumer loans are reviewed in accordance with Shinhan Bank's credit scoring system and the objective statistics methodology regarding secured and unsecured loans maintained and operated by Shinhan Bank's Retail Banking Division. The credit scoring system is an automated credit approval systems used to evaluate loan applications and determine the appropriate pricing for the loan.

Shinhan Bank's credit scoring system takes into account factors such as a borrower's personal information, transaction history with Shinhan Bank and other financial institutions and other relevant credit information. The applicant is given a score which is used to decide whether to approve loans as well as determine loan amounts. The score determines whether the applicant is approved for credit, conditionally approved, subject to further assessment, or denied. If the applicant becomes subject to further assessment, the appropriate discretionary body, either at the branch level or at the headquarters level, makes a reassessment, which considers qualitative factors as well as quantitative factors, such as credit history, occupation and past relationship with Shinhan Bank.

For mortgage loans and loans secured by real estate, Shinhan Bank evaluates the value of the real estate offered as collateral for a loan using a database Shinhan Bank has developed, which contains information about real estate values throughout Korea. In addition, Shinhan Bank uses information from a third party provider of information about the real estate market in Korea, which gives Shinhan Bank up-to-date market value information for Korean real estate values. Staffs from the processing centers appraise the real estate. In addition, for loans of W5 billion or more, Shinhan Bank hires certified appraisers to review the appraisal value of real estate collateral that have an appraisal value exceeding W10 billion, as initially determined by the processing centers. Shinhan Bank reevaluates internally, on a summary basis, the appraisal value of collateral at least every two years. To protect against fraudulent transfers, Shinhan Bank has established an underwriting standard for adequacy of collaterals and the procedure of legal screening for whether or not there is a perfection of ownership.

For loans secured by securities, Shinhan Bank evaluates the value of the securities based upon the market value of the securities. If the value of the securities declines over the life of a loan, the borrower will be required to post additional securities as collateral. For loans secured by deposits, Shinhan Bank will grant loans in an amount up to 95% of the deposit amount if the deposit is held with Shinhan Bank or, if the deposits are held with another financial institution, up to 90% of the deposit amount. Shinhan Bank also requires borrowers in respect of secured obligations to observe specified collateral ratios.

*Corporate loans*

Shinhan Bank rates all of its corporate borrowers using a rating system. Shinhan Bank uses internally developed credit evaluation models to rate potential borrowers. Shinhan Bank fully integrated the corporate credit rating systems in October 1998. We established a task force to integrate and harmonize the credit decision-making processes of Shinhan Bank and Chohung Bank, and as a result, implemented a uniform credit risk rating system that applies similarly to both Shinhan Bank and Chohung Bank, effective February 2005.

The credit risk-rating systems take into account a variety of evaluation criteria in order to standardize credit decisions, by focusing on the quality of borrowers rather than the volume of loans. The systems include both quantitative factors based on the borrower's financial and other data, and qualitative factors based on the

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judgment of Shinhan Bank's credit officers. Financial evaluation factors Shinhan Bank considers include financial variables and ratios based on Shinhan Bank's customer's financial statements, such as return on assets and cash flow to total debt ratios. Non-financial evaluation factors include the industry in which the borrower operates, its competitive position in its industry, its operating and funding capabilities, Shinhan Bank's belief regarding its financial prospects, the quality of its management and controlling stockholders (based in part on interviews with its officers and employees), technological capabilities, labor relations, the status of its auditors and information gathered from outside sources such as rating agencies or industrial associations.

Shinhan Bank consults reports prepared by external credit rating services, such as Korea Information Service, National Information & Credit Evaluation Inc. and Korea Management Consulting & Credit Rating Corporation. Shinhan Bank uses these services to provide it with support for the accuracy of the credit review it conducts.

Shinhan Bank monitors and improves the effectiveness of the credit risk-rating systems using a database that it updates continually with actual default records.

Based on the scores calculated under the credit rating system, which takes into account the evaluation criteria described above and the probability of default, Shinhan Bank assigns the borrower one of twenty grades (AAA to D). Grades AA through B are further broken down into +, 0 or -. Grades AAA through B- are classified as normal, grade CCC precautionary, and grades CC through D non-performing. The credit risk-rating model is further differentiated by the size of the corporate borrower and the type of credit facilities.

*Loan Approval Process*

Evaluations of general loans are approved after combined evaluation and approval of the relationship manager of each branch and the committee of the applicable business unit. Depending on the size and the importance of the loan, the approval process passes through review of Credit Officer Committee or Senior Credit Officer Committee. In the case where the loan is considered significant or the amount exceeds the discretion limit of the Senior Credit Officer Committee, the credit evaluation is carried out at the highest decision-making credit approval body, the Credit Review Committee. The Credit Review Committee evaluates and approves large credits in excess of W10 billion for unsecured and W15 billion for secured lending. Meetings to approve these large credits are held twice a week. The Credit Review Committee makes decisions by 2/3 or more votes of the attending members, which must constitute at least two-thirds of the committee members to satisfy the quorum.

The chart below summarizes the credit approval process of our banking operation. The Senior Credit Officer and the Head of Business Division does not make individual decisions on loan approval, but is part of the decision-making process at the group level.

The discretion at each level of the approval process is determined by the credit level of the applicant based on credit review, whether the loan is secured by collateral and the level of credit risk established by the credit rating system.

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The discretionary levels are divided into five categories depending on the credit rating assigned and the existence and value of collateral. The loan amount determines the approval body – branch manager, branch manager and Credit Officer, Credit Officer Committee, Senior Credit Officer Committee or Credit Review Committee.

**Approval Limit of Loan Amount**

<b>Category</b>	<b>Approval Body</b>	<b>Grade B-</b>	<b>Grade AAA</b>
1	Branch Manager (Individual Loans)		
	Unsecured	₩100 million or less	₩2 billion or less
	Secured	₩500 million ₩1 billion or less	₩4 billion or less
2	Branch Manager (Corporate loans)		
	Unsecured	₩300 million or less	₩3 billion or less
	Secured	₩2 billion or less	₩6 billion or less
3	Branch Manager and Credit Officer		
	Unsecured	₩500 million or less	₩5 billion or less
	Secured	₩3 billion or less	₩10 billion or less
4	Credit Officer Committee		
	Unsecured	₩1 billion or less	₩10 billion or less
	Secured	₩5 billion or less	₩20 billion or less
5	Senior Credit Officer Committee		
	Unsecured	₩10 billion or less	₩30 billion or less
	Secured	₩15 billion or less	₩80 billion or less
6	Credit Review Committee		
	Unsecured	More than ₩10 billion	More than ₩30 billion
	Secured	More than ₩15 billion	More than ₩80 billion

*Credit Review and Monitoring*

Shinhan Bank continually reviews and monitors existing credit risks primarily with respect to borrowers. In particular, Shinhan Bank's automated early warning system conducts weekly examination for borrowers using over 60 financial and non-financial factors, and the relationship manager and the credit officer must conduct periodic loan review and report to independent loan review team which analyzes in detail the results and adjusts credit rating accordingly. Based on these reviews, Shinhan Bank adjusts a borrower's credit rating, credit limit, applied interest rates and credit policies. In addition, the group credit rating of the borrower's group, if applicable, may be adjusted following a periodic review of the main debtor groups identified by the Governor of the Financial Supervisory Service based on their outstanding credit exposures, of which 36 were identified most recently in April 2006. Shinhan Bank also continually reviews other factors, such as industry conditions in which borrowers operate and their domestic and overseas asset base and operations, to ensure that ratings are appropriate. The Credit Review Department provides credit review reports, independent of underwriting, to Chief Risk Officer and CEO on a monthly basis.

The early warning system makes automatic weekly check for borrowers with whom Shinhan Bank has more than ₩3 billion of exposure. The relationship manager and the Credit Officer monitor those borrowers, and then the Credit Review Department further reviews the results of the monitoring. In addition, Shinhan Bank carries out special review of each borrower in accordance with changing credit risk based on changing commercial environment. The results of such special review are continually reported to the Chief Risk Officer of Shinhan Bank.

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Depending on the nature of the problem detected by the early warning system, a borrower may be classified as a deteriorating credit and undergo evaluation for a possible downgrade in its customer rating, or may be initially classified as a borrower showing early warning signs or re-attain normal borrower status. For borrowers classified as showing early warning signs, the relevant relationship manager gathers information and conducts a review of the borrower to determine whether it should be classified as a deteriorating credit or whether to impose management improvement warnings or implement joint creditors management. In the case where the borrower becomes non-performing, Shinhan Bank's collection department directly manages such borrower's account in order to maximize recovery rate, and conducts auctions, court proceedings, sale of assets or corporate restructuring as needed.

*Credit Risk Assessment and Control*

To assess credit risk in a systematic manner, Shinhan Bank has developed systems designed to quantify credit risks based on selection and monitoring of various statistic, including delinquency rate, non-performing loan ratio, expected loan loss and weighted average risk rating.

Shinhan Bank controls loan concentration by monitoring and managing loans at two levels portfolio level and individual loan account level. In order to prevent concentration of loans, Shinhan Bank has established a credit limit per country, industry, affiliates, corporation and financial institution, and has encouraged extension of credit to customers with good credit and reduction of credit to customers with less than good credit. In addition, Shinhan Bank utilizes the results of credit portfolio analysis in allocating asset quality based on forward looking criteria, increasing discretion and adjusting loan to value ratio.

Shinhan Bank measures credit risk using internally accumulated data. Shinhan Bank measures expected and unexpected losses with respect to total assets monthly, which Shinhan Bank refers to when setting risk limits for, and allocate capital to, its business groups. Expected loss is calculated based on the probability of default, the loss given default, the exposure at default and the past bankruptcy rate and recovery rate, and Shinhan Bank provides allowance for loan losses under Korean GAAP accordingly. Shinhan Bank selects the higher of the two provisioning levels, as determined by the Financial Supervisory Service requirement or Shinhan Bank's internal calculation. Unexpected loss is predicted based on Value at Risk, or VaR, under the historical simulation method. Shinhan Bank plans to apply the more advanced Monte Carlo simulation method rather than the historical simulation method going forward, and plans to operate an integrated and systematic credit risk management rather than risk management based on credit limitation.

*Credit Card Approval Process of Shinhan Card*

Approval of credit card applications is processed using automated credit scoring system retooled for credit cards. Credit scoring system for credit cards is divided into two sub-systems: Application Scoring System and Behavior Scoring System. Behavior Scoring System is based largely on the credit history and Application Scoring System is based largely on personal information of the applicant. For credit card applicants with whom we have an existing relationship, credit scoring system factors in internally gathered information such as repayment ability, total assets, the length of the existing relationship and the applicant's contribution to profitability. Credit scoring system also automatically conducts credit checks on all credit card applicants. Shinhan Card gathers information about applicants transaction history with financial institutions, including banks and credit card companies, from a number of third party credit reporting agencies including National Information & Credit Evaluation Inc., other credit card companies in Korea, the Korea Federation of Banks, Korea Non-bank Financing Association and credit rating agencies. These credit checks reveal a list of the delinquent customers of all the credit card issuers in Korea.

If the credit score awarded to an applicant is above a minimum threshold, then the application is approved unless overridden by other policy factors such as delinquencies with other credit card companies. In respect of credit card applications by our long-standing customers with good credit history, Shinhan Card has discretion to waive the application of the awarded credit score unless overridden by other policy factors. All of these factors also act as the basis for setting a credit limit if Shinhan Card approves an application.

**Table of Contents*****Market Risk Management of Shinhan Bank***

Market risk is the risk of loss generated by fluctuations in market prices such as interest rates, foreign exchange rates and equity prices. The principal market risks to which we are exposed are interest rate risk and, to a lesser extent, equity price risk, foreign exchange risk and commodity risk. These risks stem from our trading and nontrading activities relating to financial instruments such as loans, deposits, securities and financial derivatives. We divide market risk into risks arising from trading activities and risks arising from nontrading activities.

Market risk to which we are exposed arises primarily from Shinhan Bank and Chohung Bank and the other subsidiaries do not incur significant market risk, except for Good Morning Shinhan Securities, our securities trading and brokerage subsidiary, which incurs market risk relating to its trading activities. For Shinhan Bank's market risk management, the Risk Management Committee establishes overall market risk management principles for both the trading and nontrading activities of Shinhan Bank. Based on these principles, the Asset & Liability Management Committee, or the ALM Committee, of Shinhan Bank assesses and controls market risks arising from trading and nontrading activities. The ALM Committee, which consists of eight executive vice presidents and the head of the Treasury Department, is the executive decision-making body for Shinhan Bank's risk management and asset and liability management operations. At least on a monthly basis, the ALM Committee reviews and approves reports, which include the position and value-at-risk, or VaR, with respect to Shinhan Bank's trading activities and the position, VaR, duration gap and market value analysis and net interest income simulation with respect to its nontrading activities. Shinhan Bank measures market risk with respect to all assets and liabilities in the bank accounts and trust accounts in accordance with the regulations promulgated by the Financial Supervisory Commission.

Good Morning Shinhan Securities manages its market risk based on its overall risk limit established by its risk management committee as well as the risk limits and detailed risk management guidelines for each product and department established by its management's committee. Good Morning Shinhan Securities assesses the adequacy of these limits at least annually.

As the merger of Shinhan Bank and Chohung Bank occurred only recently, market risk management of Chohung Bank has not yet been fully integrated with the market risk management of Shinhan Bank, although subject to overall group risk management policies. For a detailed description of Chohung Bank's market risk management, see [Market Risk Management of Chohung Bank](#).

We use Korean GAAP numbers on a nonconsolidated basis for our market risk management and, unless otherwise specified, the numbers presented for quantitative market risk disclosure were prepared in accordance with Korean GAAP on a nonconsolidated basis.

***Market Risk Exposure from Trading Activities***

Shinhan Bank's trading activities consist of:

trading activities to realize short-term trading profits in debt and stock markets and foreign exchange markets based on Shinhan Bank's short-term forecast of changes in market situation and customer demand, for its own account as well as for the account of the trust accounts of Shinhan Bank's customers; and

trading activities primarily to realize profits from arbitrage transactions in derivatives such as swap, forward, futures and option transactions, and, to a lesser extent, to sell derivative products to Shinhan Bank's customers and to cover market risk incurred from those trading activities.

As a result of these trading activities, Shinhan Bank is exposed to interest rate risk, foreign exchange risk and equity risk.

***Interest Rate Risk***

Shinhan Bank's exposure to interest rate risk arises primarily from Won-denominated debt securities, directly held or indirectly held through beneficiary certificates, and, to a lesser extent, from interest rate

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derivatives. Shinhan Bank's exposure to interest rate risk arising from foreign currency-denominated trading debt securities is minimal since its net position in those securities is not significant. As Shinhan Bank's trading accounts are marked-to-market daily, it manages the interest rate risk related to its trading accounts using VaR, a market value-based tool.

*Foreign Exchange Risk*

Foreign exchange risk arises because of Shinhan Bank's assets and liabilities, including derivatives such as foreign exchange forwards and futures and currency swaps, which are denominated in currencies other than the Won. Shinhan Bank manages foreign exchange risk on an overall position basis, including its overseas branches, by covering all of its foreign exchange spot and forward positions in both trading and nontrading accounts.

Shinhan Bank's net foreign currency open position, which is the difference between its foreign currency assets and liabilities as offset against forward foreign exchange positions, is Shinhan Bank's foreign exchange risk. The ALM Committee oversees Shinhan Bank's foreign exchange exposure for both trading and nontrading activities by establishing limits for the net foreign currency open position, stop loss limits and VaR limits. The management of Shinhan Bank's foreign exchange position is centralized at the FX & Derivatives Department. Dealers in the FX & Derivatives Department manage Shinhan Bank's overall position within the set limits through spot trading, forward contracts, currency options, futures and swaps and foreign exchange swaps. Shinhan Bank sets forth the limit for net open position by currency and the limits for currencies other than the U.S. dollars and Japanese yen are restrictive to minimize other foreign exchange trading.

The net open foreign currency positions held by the other subsidiaries are not significant. In the case of Shinhan Capital which incurs a considerable amount of foreign exchange exposure from its leasing business, it maintains its net exposure below US\$1 million by hedging its foreign exchange positions using forwards and currency swaps.

The following table shows Shinhan Bank's net foreign currency open positions at the end of 2003, 2004 and 2005. Positive amounts represent long exposures and negative amounts represent short exposures.

Currency	As of December 31,					
	2003		2004		2005	
	(In millions of US\$)					
U.S. dollars	US\$	4.6	US\$	52.3	US\$	(2.39)
Japanese yen		(8.7)		(1.6)		(18.36)
Euro		0.7		0.9		(0.12)
Others		1.0		(1.7)		1.29
<b>Total</b>		<b>(2.4)</b>		<b>49.9</b>		<b>(19.58)</b>

*Equity Risk*

Equity risk for Shinhan Bank's trading activities results from the trading of equity portfolio of Korean companies and Korea Stock Price Index futures and options. The trading equity portfolio consists of stocks listed on the Stock Market or the KOSDAQ Market of the Korea Exchange and nearest-month or second nearest-month futures contracts under strict limits on diversification as well as limits on positions. This has been an area of particular focus due to the level of volatility in the stock market. In addition, Shinhan Bank pays close attention to the loss limits. Although Shinhan Bank holds a substantially smaller amount of equity securities than debt securities in its trading accounts, the VaR of trading account equity risk is generally higher than that of trading account interest rate risk due to high volatility in the value of equity securities. As of December 31, 2003, 2004 and 2005, Shinhan Bank held W74.8 billion, W60.2 billion and W60.8 billion, respectively, of equity securities in its trading accounts (including the trust accounts).



**Table of Contents***Management of Market Risk from Trading Activities*

The following tables present an overview of market risk, measured by VaR, from trading activities of Shinhan Bank and Good Morning Shinhan Securities, respectively, for the year ended and as of December 31, 2005. For market risk management purposes, Shinhan Bank includes its trading portfolio in bank accounts and assets in trust accounts for which it guarantees principal or fixed return in accordance with the Financial Supervisory Commission regulations.

**Trading Portfolio VaR for the Year 2005(1)**

	Average		Minimum		Maximum		As of December 31	
	(In billions of Won)							
<b>Shinhan Bank:</b>								
Interest rate	W	3.06	W	1.62	W	6.19	W	2.54
Foreign exchange(2)		0.35		0.12		0.78		0.28
Equities		4.14		1.38		8.12		1.50
Less: portfolio diversification(3)		(3.24)		(1.78)		(5.14)		(1.74)
Total VaR(4)	W	4.31	W	1.33	W	9.96	W	2.55
<b>Good Morning Shinhan Securities(5):</b>								
Interest rate	W	0.3	W	0.1	W	1.1	W	0.2
Equities		1.3		0.3		5.0		1.3
Beneficiary certificates(6)		0.1		0.0		0.1		0.0
Less: portfolio diversification(3)		(0.4)		(0.0)		(1.2)		(0.5)
Total VaR	W	1.3	W	0.4	W	5.0	W	1.0

*Notes:*

- (1) One-day VaR results with a 99% confidence level.
- (2) Includes both trading and nontrading accounts as Shinhan Bank manages foreign exchange risk on a total position basis.
- (3) Calculation of portfolio diversification effects for the minimum and maximum VaRs as the minimum and maximum may occur on different days for different risk components. The average and December 31, 2005 VaRs are less than the sum of the VaRs due to offsets resulting from portfolio diversification.
- (4) Includes trading portfolio in Shinhan Bank's bank accounts and assets in trust accounts for which it guarantees principal or fixed return.
- (5) The change in market value of Good Morning Shinhan Securities' trading portfolio was W0.7 billion per day.
- (6) Beneficiary certificates that Good Morning Shinhan Securities holds temporarily in connection with its beneficiary certificate sales business. Most of market risk arising from the holding of these beneficiary certificates is interest rate risk and there is minimal amount of equity risk.

Shinhan Bank generally manages its market risk from trading activities at the entire portfolio level. To control its market risk for trading portfolio, Shinhan Bank uses position limits, VaR limits, and stop loss limits. Shinhan Bank prepared its risk control and management guidelines for derivative trading based on the regulations and guidelines promulgated by the Financial Supervisory Commission.

Shinhan Bank measures market risk from trading activities to monitor and control the risk of its operating divisions and teams that perform trading activities.

*Value-at-Risk analysis.* We use one-day VaRs to measure Shinhan Bank's market risk. Shinhan Bank calculates VaRs on a monthly basis based on data for the previous 12 months for the holding periods of one day. A one-day VaR is a statistically estimated maximum amount of loss that can occur for a day under

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normal market conditions. We use a 99% confidence level to measure the VaRs, which means the actual amount of loss may exceed the VaR, on average, once out of 100 business days.

We use one-day VaRs to measure market risk of Good Morning Shinhan Securities. Good Morning Shinhan Securities calculates VaRs on a daily basis based on data for the previous 12 months for the holding periods of one day. We use a 99% confidence level to measure the VaRs for Good Morning Shinhan Securities. Good Morning Shinhan Securities is currently using a variance-covariance methodology called delta-normal method for its overall VaR calculation and uses historical simulation and Monte Carlo simulation for stress test and calculation of VaRs for individual risks of options. Variance-covariance method assumes a normal distribution of risks which may underestimate market risk when the distribution of market risk is not normal. This method also does not provide accurate analysis for risks of non-linear products such as options.

Value-at-risk is a commonly used market risk management technique. However, VaR models have the following shortcomings:

By its nature as a statistical approach, VaR estimates possible losses over a certain period at a particular confidence level using past market movement data. Past market movement, however, is not necessarily a good indicator of future events, particularly potential future events that are extreme in nature.

This model may underestimate the probability of extreme market movements.

The time periods used for the model, generally one or ten days, are assumed to be a sufficient holding period before liquidating the relevant underlying positions. If these holding periods are not sufficient, or too long, the VaR results may understate the potential loss.

The use of a 99% confidence level, does not take account of, nor makes any statement about, any losses that might occur beyond this confidence level.

Shinhan Bank calculates VaRs at the end of every month and therefore do not reflect market changes during a month until the end of the month.

VaR does not capture all complex effects of various risk factors on the value of positions and portfolios and could underestimate potential losses.

Currently, Shinhan Bank does not perform back-testing of VaR results whereas Good Morning Shinhan Securities conducts back-testing of VaR results against actual outcomes on a daily basis.

When Shinhan Bank calculates the VaRs for trading accounts, it measures interest risk VaRs, but not equity risk VaRs, for its equity-linked securities which are insignificant in amount. As of December 31, 2005, Shinhan bank held no equity-linked securities in its trading accounts.

Shinhan Bank plans to implement a new integrated market risk management system which will manage both Shinhan Bank's Won-denominated and foreign-denominated accounts. The new system is expected to use historical simulation, Monte Carlo simulation and variance-covariance methods to measure both linear risks arising from such products as equity and debt securities and nonlinear risks arising from other products including options. Monte Carlo simulation method is similar to historical simulation, except that it uses random numbers to generate different levels of market values instead of using historical data. Variance-covariance method is a parameter-based methodology, which takes into account diversification effects among different market risk components as well as within the same risk component to calculate VaRs. We expect the new system, when implemented, would enable Shinhan Bank to generate elaborate and consistent VaR numbers and perform sensitivity analysis and back testing to check the validity of the models on a daily basis.

*Stress test.* In addition to VaR, Shinhan Bank performs stress test to measure market risk. As VaR assumes normal market situations, Shinhan Bank assesses its market risk exposure to unlikely abnormal market fluctuations through stress test. Stress test is an important way of supplement VaR since VaR does not cover potential loss if the market

moves in a manner which is outside Shinhan Bank's normal expectations.

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Stress test projects the anticipated change in value of holding positions under certain scenarios assuming that no action is taken during a stress event to change the risk profile of a portfolio.

Shinhan Bank uses relatively simple but fundamental seven scenarios for stress test taking into account four market risk components such as foreign exchange rates, stock prices and Won-denominated and foreign currency-denominated interest rates. For the worst case scenario, we assumed instantaneous and simultaneous movements in the four market risk components depreciation of Won by 115.7%, decrease in Korea Exchange Composite Index by 46%, and increases in Won-denominated and foreign currency denominated interest rates by 150.7% and 1.2%, respectively which were based on the historical worst case movements for three months during the Asian crisis from September 1997 to December 1997. In the case of this worst-case scenario, the changes in market value of Shinhan Bank's trading portfolio was a decline of W280.1 billion as of December 31, 2005. Shinhan Bank performs stress test at least semiannually and reports the results to the Risk Management Committee and the ALM Committee.

Good Morning Shinhan Securities uses five scenarios for stress test taking into account two market risk components: stock prices and Won-denominated interest rates. As of December 31, 2005, for the worst case scenario, which was in the case of instantaneous and simultaneous drops in Korea Stock Price Index 200 by 10% and a 1% point increase in the three-year government bond yield, the changes in market value of Good Morning Shinhan Securities trading portfolio was W4.0 billion for one day.

Shinhan Life Insurance uses actual events from the past for stress testing. One example of an actual-event evaluation relates to the evaluation of events over the course of one day following the stock market crash on April 17, 2000 following the news announcement of the accounts of SK Networks, and which resulted in a drop of the KOSPI index by 12.5% on the same date and was accompanied by a 50 basis-point increase in the three-year Government bond yield and a 5.9% depreciation of the Won against the U.S. dollar. Other examples include the evaluation of events over the course of 10 days following the sudden depreciation of the Won in December 1997 and the collapse of the Daewoo Group in July 1999, each of which was accompanied by a more than 10% drop of the KOSPI index, a more than 100 basis-point decrease in the Government bond yield and a more than 10% depreciation of the Won against the U.S. dollar.

Although Shinhan Bank and Shinhan Life Insurance have not set any limits on stress testing, they monitor the impact of market turmoil or any abnormality. Good Morning Shinhan Securities sets limits on stress testing for its overall operations as well as at its department level. In the case of Shinhan Bank, Good Morning Shinhan Securities and Shinhan Life Insurance, if the impact is large, their respective chief risk officer may request a portfolio restructuring or other proper action.

*Hedging and Derivative Market Risk*

The principal objective of our hedging strategy is to manage its market risk within established limits. We use derivative instruments to hedge its market risk as well as to make profits by trading derivative products within pre-approved risk limits. Our derivative trading includes interest rate and cross-currency swaps, foreign currency forwards and futures, stock index and interest rate futures, and stock index and currency options.

While we use derivatives for hedging purposes, derivative transactions themselves incur market risk as we take trading positions and trades them for the purpose of making profits. These activities consist primarily of the following: arbitrage transactions to make profits from short-term discrepancies between the spot and derivative markets or within the derivative markets;

sales of tailor-made derivative products that meet various needs of our corporate customers, principally of Shinhan Bank and Good Morning Shinhan Securities, and related transactions to reduce its exposure resulting from those sales (in the case of Good Morning Shinhan Securities, these activities commenced from February 2003 when it acquired the relevant license);

taking positions in limited cases when we expect short-swing profits based on its market forecasts; and

trading to hedge our interest rate and foreign currency risk exposure as described above.

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Market risk from derivatives is not significant since derivative trading activities of Shinhan Bank and Good Morning Shinhan Securities are primarily driven by arbitrage and customer deals with very limited open trading positions. Market risk from derivatives is also not significant for Shinhan Life Insurance as its derivative trading activities are limited to those within pre-approved risk limits and are subject to heavy regulations imposed on the insurance industry.

*Market Risk Management for Nontrading Activities**Interest Rate Risk*

Principal market risk from nontrading activities of Shinhan Bank is interest rate risk. Interest rate risk is the risk of loss resulting from interest rate fluctuations that adversely affect the financial condition and results of operations of Shinhan Bank. Shinhan Bank's interest rate risk arises primarily due to differences between the timing of rate changes for interest-earning assets and interest-bearing liabilities.

Interest rate risk affects Shinhan Bank's earnings and the economic value of Shinhan Bank's net assets:

*Earnings:* interest rate fluctuations have an effect on Shinhan Bank's net interest income by affecting its interest-sensitive operating income and expenses.

*Economic value of net assets:* interest rate fluctuations influence Shinhan Bank's net worth by affecting the present value of cash flows from the assets, liabilities and other transactions of Shinhan Bank.

Accordingly, Shinhan Bank measures and manages interest rate risk for nontrading activities by taking into account effects of interest rate changes on both its income and net asset value. Shinhan Bank measures and manages interest rate risk on a daily basis with respect to all interest-earning assets and interest-bearing liabilities in Shinhan Bank's bank accounts (including derivatives denominated in Won) and in the trust accounts, except that it measures VaRs on a monthly basis. Most of Shinhan Bank's interest-earning assets and interest-bearing liabilities are denominated in Won.

*Interest Rate Risk Management*

The principal objectives of Shinhan Bank's interest rate risk management are to generate stable net interest income and to protect Shinhan Bank's net asset value against interest rate fluctuations. To this end, the ALM Committee sets out Shinhan Bank's interest rate risk limits at least annually and the Risk Management Office monitors Shinhan Bank's compliance with these limits and reports the monitoring results to the ALM Committee on a monthly basis. Shinhan Bank uses interest rate swaps to control its interest rate exposure limits.

On a daily basis, Shinhan Bank uses various analytical methodologies to measure and manage its interest rate risk for nontrading activities, including the following:

*Interest Rate Gap Analysis:* Interest rate gap analysis measures the difference in the amounts of interest-earning assets and interest-bearing liabilities at each maturity and re-pricing date for a specific time frame.

*Duration Gap Analysis:* Duration gap analysis measures durations of Shinhan Bank's interest-earning assets and interest-bearing liabilities, which are weighted average maturities of these assets and liabilities calculated based on discounted cash flows from these assets and liabilities using yield curves.

*Market Value Analysis:* Market value analysis measures changes in the market value of Shinhan Bank's interest-earning assets and interest-bearing liabilities based on the assumption of parallel shifts in interest rates.

*Net Interest Income Simulation Analysis:* Net interest income simulation analysis uses deterministic analysis methodology to measure changes in Shinhan Bank's annual net interest income (interest income less interest expenses) under the current maturity structure, using different scenarios for interest rates (assuming parallel shifts) and funding requirements.

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*Earnings at Risk Analysis:* Earnings-at-risk analysis, or EaR analysis, measures changes in Shinhan Bank's annual pretax earnings from its interest-earning assets and interest-bearing liabilities at a 99% confidence level using Monte Carlo simulation. Currently, Shinhan Bank uses EaR analysis as a supplemental measure for interest rate risk management.

*Interest Rate Gap Analysis*

Interest rate gap analysis measures the difference in the amounts of interest-earning assets and interest-bearing liabilities at each maturity and re-pricing date by preparing interest rate gap tables in which Shinhan Bank's interest-earning assets and interest-bearing liabilities are allocated to the applicable time buckets based on the expected cash flows and re-pricing dates. On a daily basis, Shinhan Bank performs interest rate gap analysis for Won and foreign currency denominated assets and liabilities in its bank and trust accounts. Shinhan Bank's gap analysis includes Won-denominated derivatives (which are interest rate swaps for the purpose of hedging) but excludes foreign currency-denominated derivatives, whose management is centralized at the FX & Derivatives Department. Through the interest rate gap analysis that measures interest rate sensitivity gaps, cumulative gaps and gap ratios, Shinhan Bank assesses its exposure to future interest risk fluctuations.

For interest rate gap analysis, we assume and use the following maturities for different assets and liabilities:

With respect to the maturities and re-pricing dates of Shinhan Bank's assets, we assume that the maturity of Shinhan Bank's prime rate-linked loans is the same as that of its fixed-rate loans. We also assume that the debt securities in Shinhan Bank's trading accounts have maturities of three months. Shinhan Bank excludes equity securities from interest-earning assets.

With respect to the maturities and re-pricing of Shinhan Bank's liabilities, we assume that money market deposit accounts and non-core demand deposits under the Financial Supervisory Commission guidelines have a maturity of three months or less. With respect to core demand deposits under the Financial Supervisory Commission guidelines, we assume a maturity of over three years.

The following tables show Shinhan Bank's interest rate gaps as of December 31, 2005 for (1) Won-denominated nontrading bank accounts, including derivatives and (2) foreign currency-denominated nontrading bank accounts, excluding derivatives.

**Won-denominated nontrading bank accounts (including derivatives):****As of December 31, 2005**

	<b>0-3 Months</b>	<b>3-6 Months</b>	<b>6-12 Months</b>	<b>1-2 Years</b>	<b>2-3 Years</b>	<b>Over 3 Years</b>	<b>Total</b>
<b>(In billions of Won, except percentages)</b>							
<b>Interest-earning assets</b>	W 37,723	W 8,678	W 4,983	W 3,215	W 2,710	W 2,888	W 60,197
Fixed rates	7,021	2,440	4,188	2,924	2,189	1,760	20,522
Floating rates	30,671	6,179	727	101	51	68	37,797
Interest rate swaps	30	60	67	190	470	1,060	1,877
<b>Interest-bearing liabilities</b>	W 25,769	W 6,282	W 10,627	W 6,379	W 2,730	W 7,785	W 59,572
Fixed liabilities	11,498	5,876	9,511	6,368	2,700	7,785	43,737
Floating liabilities	12,521	387	1,039	10			13,958
Interest rate swaps	1,750	20	77		30		1,877
Sensitivity gap	11,953	2,396	(5,645)	(3,164)	(20)	(4,897)	625

Cumulative gap	11,953	14,350	8,705	5,541	5,521	625
% of total assets	19.9%	23.8%	14.5%	9.2%	9.2%	1.0%

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As of December 31, 2005

	<b>0-3 Months</b>	<b>3-6 Months</b>	<b>6-12 Months</b>	<b>1-3 Years</b>	<b>Over 3 Years</b>	<b>Total</b>
<b>(In millions of US\$, except percentages)</b>						
Interest-earning assets	\$ 6,970	\$ 1,279	\$ 334	\$ 28	\$ 278	\$ 8,888
Interest-bearing Liabilities	6,511	1,512	527	38	208	8,798
Sensitivity gap	458	(233)	(194)	(11)	70	90
Cumulative gap	458	225	31	20	90	
% of total assets	5.2%	2.5%	0.4%	0.2%	1.0%	

*Duration and Market Value Analysis*

Shinhan Bank performs a duration gap analysis to measure effects of interest rate risk on the market value of its assets and liabilities. Shinhan Bank measures, on a daily basis and for each operating department, account, product and currency, durations of interest-earning assets and interest-bearing liabilities. Shinhan Bank also measures, on a daily basis, changes in the market value of Shinhan Bank's interest-earning assets and interest-bearing liabilities.

The following tables show duration gaps and market values of Shinhan Bank's Won-denominated interest-earning assets and interest-bearing liabilities in its not-trading accounts as of December 31, 2005 and changes in these market values when interest rate increases by one percentage point.

	<b>Duration as of December 31, 2005(1)</b>
	<b>(In months)</b>
Interest-earning assets	8.1
Interest-bearing liabilities	13.2
Gap	(5.1)

**Market Value as of December 31, 2005(1)**

	<b>Actual</b>	<b>1% Point Increase</b>	<b>Changes</b>
	<b>(In billions of Won)</b>		
Interest-earning assets	W 60,690	W 60,515	W (175)
Interest-bearing liabilities	58,578	58,149	(429)
Gap	2,112	2,366	254

*Note:*

(1) Includes interest rate swaps entered for the purpose of hedging.

*Net Interest Income Simulation*

Shinhan Bank performs a net interest income simulation to measure effects of interest rate risk on Shinhan Bank's results of operations. Net interest income simulation measures changes in Shinhan Bank's annual net interest income (interest income less interest expenses) under the current maturity structure, using different scenarios for interest rates

and funding requirements. Shinhan Bank applies three scenarios of parallel shifts in interest rate: (1) no change, (2) a 1% point increase in interest rates and (3) a 1% point decrease in interest rates. For funding requirement changes, Shinhan Bank uses three scenarios: (1) no change in funding requirement, (2) a 10% increase in funding requirement and (3) an increase in funding requirement by the growth rate assumed in Shinhan Bank's annual financial plan.

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The following tables illustrate by way of an example the simulated changes in Shinhan Bank's annual net interest income for 2006 with respect to Won-denominated interest-earning assets and interest-bearing liabilities, using Shinhan Bank's net interest income simulation model, when it assumes (a) the maturity structure and funding requirement of Shinhan Bank as of December 31, 2005 and (b) the same interest rates as of December 31, 2005 and a 1% point increase or decrease in the interest rates.

**Simulated Net Interest Income for 2006**  
**(For Nontrading Won-denominated Bank Accounts)(1)**

	Assumed Interest Rates		Change in Net Interest Income		Change in Net Interest Income		
			Amount	% Change	Amount	% Change	
	No Change	1% Point Increase	1% Point Decrease	(1% Point Increase)	(1% Point Increase)	(1% Point Decrease)	(1% Point Decrease)
<b>(In billions of Won, except percentages)</b>							
Simulated interest income	W 3,481	W 3,872	W 3,090	W 390	11.2%	W (391)	(11.2)%
Simulated interest expense	2,104	2,379	1,826	275	13.1	(277)	(13.2)
Net interest income	1,378	1,493	1,263	115	8.4	(114)	(8.3)

*Note:*

(1) Includes interest rate swaps for the purpose of hedging.

Shinhan Bank's Won-denominated interest earning assets and interest-bearing liabilities in nontrading accounts have a maturity structure that benefits from an increase in interest rates, because the re-pricing periods of the interest-earning assets in Shinhan Bank's nontrading accounts are shorter than those of the interest-bearing liabilities in these accounts. This is primarily due to a continuous decrease in interest rate in the recent years in Korea, which resulted in a significant increase in floating rate loans, resulting in the maturities or re-pricing periods of Shinhan Bank's loans shorter. As a result, Shinhan Bank's net interest income increases when the interest rates rise.

*Interest Rate VaRs for Nontrading Assets and Liabilities*

Shinhan Bank measures VaRs for interest rate risk from nontrading activities on a monthly basis. The following table shows, as of and for the year ended December 31, 2005, the VaRs of (i) interest rate risk from Shinhan Bank's available-for-sale investment securities and (ii) interest rate mismatch risk for other assets and liabilities, which arises from mismatches in the re-pricing dates of Shinhan Bank's nontrading interest-earning assets and interest-bearing liabilities other than the available-for-sale investment securities. Under the Financial Supervisory Commission regulations, Shinhan Bank includes in calculation of these VaRs interest-earning assets and interest-bearing liabilities in its bank accounts and its trust accounts.

**VaR for the Year 2005(1)**

	Average	Minimum	Maximum	As of December 31
--	---------	---------	---------	-------------------

		<b>(In billions of Won)</b>							
Interest rate	available-for-sale securities	W	25.65	W	22.51	W	28.56	W	25.60
Interest rate mismatch	other assets and liabilities		10.68		7.61		14.35		10.21

*Note:*

(1) One-day VaR results with a 99% confidence level.

*Equity Risk*

Substantially all of our equity risk results from its equity portfolio of Korean companies. As of December 31, 2005, we (not including Chohung Bank) held an aggregate amount of W3 billion of equity shares in unlisted foreign companies.

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The equity securities in Won held in Shinhan Bank's investment portfolio consist of stocks listed on the Stock Market or the KOSDAQ Market of the Korea Exchange and certain non-listed stocks. Shinhan Bank measures VaRs for all of these equity securities but does not manage most of the related risk using VaR limits, as most of these securities are held for reasons other than normal investment purposes. As of December 31, 2005, Shinhan Bank held equity securities in an aggregate amount of W1,222.99 billion in its nontrading accounts, unlisted securities that Shinhan Bank held for private equity investment in the amount of W745.4 billion other equity securities that it held, among other reasons, for management control purposes or as a result of debt-to-equity conversion as a part of reorganization proceedings of the companies to which it had extended loans.

Shinhan Bank previously held shares of our common stock, which it received in exchange for its treasury shares Shinhan Bank held when we restructured into a holding company in September 2001. Under the Financial Holding Companies Act, Shinhan Bank was required to dispose of these shares within three years from the date of purchase. On March 3, 2004, Shinhan Bank sold these shares for W21,000 per share, amounting to W627 billion, pursuant to a block trading on the Korea Exchange before trading hours.

As of December 31, 2005, Shinhan Bank also held Won-denominated convertible and exchangeable bonds in an aggregate amount of W39.7 billion (all of which contained conversion or exchange rights) and foreign currency convertible and exchangeable bonds in an aggregate amount of US\$0 million in its nontrading accounts. Shinhan Bank does not measure equity risk with respect to convertible and exchangeable bonds and the interest rate risk of these bonds are measured together with the other debt securities. As such, Shinhan Bank measures interest rate risk VaRs but not equity risk VaRs for these equity-linked securities.

The following table shows the VaRs of Shinhan Bank's equity risk from nontrading activities for the year and as of December 31, 2005.

	<b>VaR for the Year 2005(1)</b>			
	<b>Average</b>	<b>Minimum</b>	<b>Maximum</b>	<b>As of December 31</b>
	<b>(In billions of Won)</b>			
Equities	W 25.65	W 17.82	W 35.66	W27.15

*Note:*

(1) One-day VaR results with a 99% confidence level.

*Liquidity Risk Management*

Liquidity risk is the risk of insolvency, default or loss due to disparity between inflow and outflow of funds, including having to obtain funds at a high price or to dispose of securities at an unfavorable price due to lack of available funds or losing attractive investment opportunities.

Shinhan Bank applies the following basic principles for liquidity risk management:

maintain an appropriate level of liquidity risk through liquidity risk management based on liquidity gap or debt-to-equity ratio at each maturity date;

assess and monitor net cash flows by currency and by maturity and continuously evaluate available sources of funds and possibility of disposal of any liquid assets;

diversify sources and uses of funds by product and by maturity to prevent excessive concentration in certain periods or products; and

prepare contingency plans to cope with liquidity crisis.

Each subsidiary manages liquidity risk in accordance with the risk limits and guidelines established internally as well as those directed by the relevant regulatory authorities. Pursuant to principal regulations applicable to financial holding companies and banks as promulgated by the Financial Supervisory Commis-

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sion, We, at the holding company, are required to keep specific Won and foreign currency liquidity ratios. These ratios require us to keep the ratio of liquid assets to liquid liabilities above certain minimum levels.

Shinhan Bank manages its liquidity risk within the limits set on Won and foreign currency accounts in accordance with the regulations of the Financial Supervisory Commission. The Financial Supervisory Commission requires Korean banks to maintain a Won liquidity ratio of at least 100.0% and a foreign currency liquidity ratio of at least 85%. The Financial Supervisory Commission defines the liquidity ratio as liquid assets (including marketable securities) due within three months divided by liabilities due within three months.

The Treasury Department is in charge of liquidity risk management with respect to Shinhan Bank's Won and foreign currency funds. The Treasury Department submits Shinhan Bank's monthly funding and asset management plans to the ALM Committee for its approval, based on the analysis of various factors, including macroeconomic indices, interest rate and foreign exchange movements and maturity structures of Shinhan Bank's assets and liabilities. The Risk Management Office measures Shinhan Bank's liquidity ratio and liquidity gap ratio on a daily basis and reports whether they are in compliance with the limits to the ALM Committee on a monthly basis.

The following tables show Shinhan Bank's liquidity status and limits for Won and foreign currency accounts (including derivatives) as of December 31, 2005 in accordance with the regulations of the Financial Supervisory Commission.

**As of December 31, 2005**

<b>Won-denominated Accounts</b>	<b>0-3 Months</b>	<b>3-6 Months</b>	<b>6-12 Months</b>	<b>1-3 Years</b>	<b>Over 3 Years</b>	<b>Substandard or Below</b>	<b>Total</b>
<b>(In billions of Won except percentage)</b>							
Assets:	W 22,476	W 9,426	W 14,589	W 10,278	W 16,174	W 555	W 73,497
Liabilities:	20,063	6,910	13,344	11,900	15,227	0	67,443
For three months or less:							
Liquidity gap	2,413						
Liquidity ratio	112.0%						
Limit:	105%						

**As of December 31, 2005**

<b>Foreign Currencies Denominated Accounts:</b>	<b>7 Days or Less</b>	<b>7 Days- 1 Months</b>	<b>3 Months</b>	<b>3-6 Months</b>	<b>6-12 Months</b>	<b>Over 1 Years</b>	<b>Substandard or Below</b>	<b>Total</b>
<b>(In millions of US\$ except percentage)</b>								
Assets:	\$ 2,199	\$ 1,362	\$ 1,763	\$ 1,107	\$ 1,199	\$ 1,712	\$ 46	\$ 9,389
Liabilities	1,295	1,433	1,317	1,675	919	2,406	0	9,046
For three months or less:								
Assets			5,324					
Liabilities			4,045					
Liquidity ratio			131.6%					
Limit			85%					

Shinhan Bank maintains diverse sources of liquidity to facilitate flexibility in meeting its funding requirements. Shinhan Bank funds its operations principally by accepting deposits from retail and corporate depositors, accessing the call loan market (a short-term market for loans with maturities of less than one month), issuing debentures and borrowing from the Bank of Korea. Shinhan Bank uses the funds primarily to extend loans or purchase securities. Generally, deposits are of shorter average maturity than loans or investments.

Our subsidiaries other than Shinhan Bank and Chohung Bank fund their operations primarily through call money, bank loans, commercial paper, corporate debentures and asset-backed securities. Our holding company acts as a funding vehicle for long-term financing of our subsidiaries whose credit ratings are lower than the holding company, including Shinhan Card and Shinhan Capital, to lower the overall funding costs within regulatory limitations. Under the Monopoly Regulation and Fair Trade Act of Korea, however, a financial holding company is prohibited from borrowing funds in excess of 100% of its total stockholders

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equity. In addition, pursuant to our liquidity risk management policies designed to ensure compliance with required capital adequacy and liquidity ratios, we have set limits to the amount of liquidity support by our holding company to our subsidiaries to 70% of our total stockholders' equity and the amount of liquidity support to a single subsidiary to 35% of our total stockholders' equity.

In addition to liquidity risk management under the normal market situations, we have contingent plans to effectively cope with possible liquidity crisis. Liquidity crisis arises when we would not be able to effectively manage the situations with our normal liquidity management measures due to, among other reasons, inability to access our normal sources of funds or epidemic withdrawals of deposits as a result of various external or internal factors, including a collapse in the financial markets or abrupt deterioration of our credit. We have contingency plans corresponding to different stages of liquidity crisis, cautionary stage, near-crisis stage and crisis stage, based on the following liquidity indices:

indices that reflect the market movements such as interest rates and stock prices;

indices that reflect financial market psychology such as the size of money market funds; and

indices that reflect our internal financial condition.

***Market Risk Management of Chohung Bank***

The principal market risks to which Chohung Bank was exposed are interest rate risk and, to a lesser extent, foreign exchange risk and equity price risk. These risks stem from Chohung Bank's trading and nontrading activities relating to financial instruments such as loans, deposits, securities and financial derivatives. Chohung Bank divides market risk into risks arising from trading activities and risks arising from nontrading activities.

Chohung Bank's Risk Management Committee establishes and oversees implementation of the overall risk management policies for both trading and nontrading activities of Chohung Bank.

Chohung Bank uses Korean GAAP numbers on a nonconsolidated basis for its market risk management and, unless specified otherwise, the numbers presented for quantitative market risk disclosure were prepared in accordance with Korean GAAP on a nonconsolidated basis.

***Market Risk Exposure from Trading Activities***

Chohung Bank's trading activities consist of:

Trading activities to realize short-term trading profits in debt and equity markets and foreign exchange markets based on its short-term forecasts of changes in market conditions and customer demand, for its proprietary account as well as for the trust accounts of its customers; and

Trading activities primarily to realize profits from arbitrage transactions in derivatives such as swap, forward, futures and option transactions, and, to a lesser extent, to sell derivative products to its customers and to hedge market risk incurred from those trading activities.

As a result of these trading activities, Chohung Bank is exposed to interest rate risk, foreign exchange risk and equity risk.

***Interest Rate Risk***

Chohung Bank's exposure to interest rate risk arises primarily from Won-denominated debt securities, directly held or indirectly held through beneficiary certificates, and, to a lesser extent, from interest rate derivatives and foreign currency-denominated trading debt securities. As its trading accounts are marked-to-market daily, Chohung Bank manages the interest rate risk related to its trading accounts using value at risk or VaR, a market value-based tool.

**Table of Contents***Foreign Exchange Risk*

Foreign exchange risk arises because its assets and liabilities, including derivatives such as foreign exchange forwards, futures, options and currency swaps, are denominated in currencies other than the Won. Chohung Bank's exposure to foreign exchange risk arises primarily from bank's foreign exchange spot and forward positions in both trading and nontrading accounts.

Chohung Bank measures foreign exchange risk with its net foreign currency open position, which is the difference between its foreign currency assets and liabilities as offset against forward foreign exchange positions. Chohung Bank's ALM Committee establishes limits for the net foreign currency open position, stop loss limits and VaR limits.

The management of Chohung Bank's foreign exchange position is centralized at the Treasury Department. Dealers in the Treasury Department manage Chohung Bank's overall position within the set limits through spot trading, forward contracts, currency options, futures and swaps and foreign exchange swaps. Chohung Bank sets VaR limit for each dealer to control foreign exchange risk.

The following table shows Chohung Bank's net foreign currency open positions at the end of 2003, 2004 and 2005. Positive amounts represent long exposures and negative amounts represent short exposures.

Currency	As of December 31,					
	2003		2004		2005	
	(In millions of US\$)					
U.S. dollars	US\$	8.4	US\$	41.7	US\$	18.0
Japanese Yen		0.3		0.2		(6.1)
Euro		0.3		6.7		(5.0)
Others		9.0		10.5		9.8
<b>Total</b>	US\$	18.0	US\$	59.1	US\$	16.7

*Equity Risk*

Equity risk for Chohung Bank's trading activities results from the trading of equity portfolio of Korean companies and Korea Stock Price Index futures and options. Although Chohung Bank holds a substantially smaller amount of equity securities than debt securities in its trading accounts, the equity risk VaR of trading accounts is relatively higher than that of trading account interest rate risk due to high volatility in the prices of equity securities. As of December 31, 2005, Chohung Bank held W4.2 billion of trading equity securities in trust accounts for which it guaranteed principal and fixed return. Chohung Bank's own trading accounts had no equity securities as of December 2005.

*Market Risk Management for Trading Activities*

The following tables present an overview of market risk, measured by VaR, from trading activities of Chohung Bank for the year ended and as of December 31, 2005. For market risk management purposes, Chohung Bank includes its trading portfolio in bank accounts and trading assets in trust accounts for which it guarantees principal or fixed return in accordance with the Financial Supervisory Commission regulations.

**Trading Portfolio Ten-day VaR for the Year 2005(1)**

	Average	Minimum	Maximum	As of December 31
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(In billions of Won)

**Chohung Bank:**

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Interest rate	W	16.2	W	3.2	W	50.6	W	21.6
Foreign exchange(2)		1.8		0.7		4.2		1.1
Equities		3.2		0.2		28.7		4.1
Total VaR(3)	W	17.5	W	5.5	W	50.8	W	22.4

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- (1) Ten-day VaR results at a 99% confidence level.
- (2) Includes both trading and non-trading accounts as Chohung Bank manages foreign exchange risk on a total position basis.
- (3) Due to portfolio diversification effects, the total VaR figures are different from the simple additions of interest rate, foreign exchange and equity risks.

Chohung Bank generally manages market risk from trading activities at the entire trading portfolio level. To control its market risk for trading portfolio, Chohung Bank uses VaR limits, and stop loss limits. Chohung Bank has prepared risk control and management guidelines for derivative trading based on the regulations and guidelines promulgated by the Financial Supervisory Commission.

Chohung Bank measures market risk from trading activities to monitor and control the risk of operating divisions and teams that perform trading activities.

*Value-at-Risk Analysis.* Chohung Bank uses ten-day VaRs to measure market risk. Chohung Bank calculates VaRs on a daily basis using data for the previous 12 months or 250 business days based on a holding period of one day. Chohung Bank then calculates ten-day VaRs using these one-day VaRs. A VaR is a statistically estimated maximum amount of loss that can occur for the specified period under normal market conditions. Chohung Bank uses a 99% confidence level to measure the VaRs, which means the actual amount of loss may exceed the VaR, on average, once out of 100 business days. Chohung Bank is currently using:

a variance-covariance methodology called delta-normal method for its overall VaR calculations;

a Monte Carlo simulation for its back testing and stress testing to measure nonlinear risk products such as options; and

a historical simulation for its back testing.

The Variance-covariance method is a parameter-based methodology, which takes into account diversification effects among different market risk components as well as within the same risk component to calculate VaRs. The Variance-covariance method assumes a normal distribution of risks which may underestimate market risk when the distribution of market risk is not normal. This method also does not provide accurate analysis for risks of non-linear products such as options. The Monte Carlo simulation method is similar to historical simulation, except that it uses random numbers to generate different levels of market values instead of using historical data.

Value-at-risk is a commonly used market risk management technique. However, VaR models have the following shortcomings:

By its nature as a statistical approach, VaR estimates possible losses over a certain period at a particular confidence level using past market movement data. Past market movement, however, is not necessarily a good indicator of future events, particularly potential future events that are extreme in nature.

This model may underestimate the probability of extreme market movements.

The time periods used for the model, generally one or ten days are assumed to be a sufficient holding period before liquidating the relevant underlying positions. If these holding periods are not sufficient, or too long, the VaR results may understate the potential loss.

The use of a 99% confidence level, does not take account of, nor makes any statement about, any losses that might occur beyond this confidence level.

VaR does not capture all complex effects of various risk factors on the value of positions and portfolios and could underestimate potential losses.

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*Back Testing.* Chohung Bank currently performs back testing of VaR results on a daily basis, using both (1) actual losses and (2) estimated losses when the actual movements of interest rates, foreign exchange rates and equity values were applied while assuming that its portfolio position remains same. In 2004, there were two days when Chohung Bank's estimated loss exceeded the VaR limits set by the Financial Supervisory Service.

Since February 2001, Chohung Bank has implemented an integrated market risk management system which manages its Won-denominated and foreign-denominated bank accounts and trust accounts which are marked to market and guaranteed by Chohung Bank. This system uses the historical simulation, the Monte Carlo simulation and the variance-covariance method to measure both linear risks arising from such products as equity and debt securities and nonlinear risks arising from other products including options. This system enables Chohung Bank to generate elaborate and consistent VaR numbers and perform sensitivity analysis and back testing to check the validity of the models on a daily basis.

*Stress Testing.* In addition to VaR, Chohung Bank performs stress test to measure market risk. As VaR assumes normal market situations, Chohung Bank assesses its market risk exposure to unlikely abnormal market fluctuations through stress test. Stress test is an important way of supplement VaR since VaR does not cover potential loss if the market moves in a manner which is outside Chohung Bank's normal expectations. Stress test projects the anticipated change in value of holding positions under certain scenarios assuming that no action is taken during a stress event to change the risk profile of a portfolio.

For stress testing, Chohung Bank assumes unexpected changes in the following four market risk components: foreign exchange rates, stock prices and Won-denominated and foreign currency-denominated interest rates. For the worst case scenario, Chohung Bank assumed instantaneous and simultaneous movements in these four market risk components within the following ranges: (1) depreciation and appreciation of Won against the U.S. dollars by 20% in the direction adverse to Chohung Bank, (2) decline in Korea Exchange Composite Index by 30%, (3) increase in Won-denominated interest rates by 200 basis points, and (4) increase in foreign currency-denominated interest rates by 200 basis points. In the worst case scenario assuming appreciation of Won against the U.S. dollars by 20%, a decline in Korea Exchange Composite Index by 30%, and increases in Won-denominated and foreign currency-denominated interest rates by 200 basis points and 200 basis points, respectively, the changes in market value of Chohung Bank's trading portfolio was W2,621 billion as of December 31, 2005.

Chohung Bank performs stress testing at least monthly and reports the results to the ALM Committee. Based on these stress testing results, Chohung Bank takes measures to manage the risk exposure, including warnings and contingency plans. In addition, Chohung Bank's Risk Management Division continuously monitors movements of the market risk components and takes actions to prevent crisis situation when there is an abrupt market movement.

*Hedging and Derivative Market Risk*

The principal objective of Chohung Bank's hedging strategy is to manage market risk within established limits. Chohung Bank uses derivative instruments to hedge its market risk as well as to generate profits by trading derivative products within pre-approved risk limits. Chohung Bank's derivative trading includes interest rate and cross-currency swaps, foreign currency forwards and futures, stock index and interest rate futures, and stock index and currency options.

While Chohung Bank uses derivatives for hedging purposes, derivative transactions themselves incur market risk as Chohung Bank take trading positions and trade them for the purpose of making profits. These activities consist primarily of the following:

- arbitrage transactions to make profits from short-term discrepancies between the spot and derivative markets or within the derivative markets;

- sales of tailor-made derivatives products to meet various needs of Chohung Bank's corporate customers and the related transactions to reduce its exposure resulting from those sales;

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taking positions in limited cases when Chohung Bank expects short-swing profits based on its market forecasts; and

trading to hedge Chohung Bank's interest rate and foreign currency risk exposure as described above.

Market risk from derivatives is not significant since Chohung Bank's derivative positions are primarily driven by arbitrage and customer transactions which result in very limited open trading positions.

*Market Risk Management for Non-trading Activities**Interest Rate Risk*

The principal market risk from nontrading activities of Chohung Bank is interest rate risk. Interest rate risk is the risk of loss resulting from interest rate fluctuations that adversely affect the financial condition and results of operations of Chohung Bank. Chohung Bank's interest rate risk arises primarily due to differences between the timing of rate changes for interest-earning assets, such as loans and investment securities, and interest-bearing liabilities, such as deposits and borrowings.

Interest rate risk affects Chohung Bank's earnings and the economic value of Chohung Bank's net assets:

*Earnings:* interest rate fluctuations have an effect on Chohung Bank's net interest income by affecting its interest-sensitive operating income and expenses.

*Economic value of net assets:* interest rate fluctuations influence Chohung Bank's net worth by affecting the present value of cash flows from the assets, liabilities and other transactions of Chohung Bank.

Accordingly, Chohung Bank measures and manages interest rate risk for nontrading activities by taking into account effects of interest rate changes on both its income and net asset value. Chohung Bank measures and manages interest rate risk on a monthly basis with respect to all interest-earning assets and interest-bearing liabilities in Chohung Bank's bank accounts (including derivatives denominated in Won) and in the trust accounts. Most of Chohung Bank's interest-earning assets and interest-bearing liabilities are denominated in Won.

*Interest Rate Risk Management*

Chohung Bank's interest rate risk arises primarily due to differences between the timing of rate changes for interest-earning assets, such as loans and investment securities, and interest-bearing liabilities, such as deposits and borrowings. The principal objectives of interest-rate management are to generate stable net interest income and to protect Chohung Bank's net asset value against interest-rate fluctuations. To this end, the ALM Committee sets the interest-rate risk limits at least annually, and the Risk Management Division monitors compliance with these limits and reports the monitoring results to the ALM Committee on a monthly basis. Chohung Bank primarily uses interest rate swaps to control its interest-rate exposure limits.

On a monthly basis, Chohung Bank uses various analytical methodologies to measure and manage its interest rate risk for nontrading activities. The principal methodology that Chohung Bank uses for its non-trading interest rate risk is an earnings at risk analysis, or EaR analysis.

Other supplemental analytical methodologies that Chohung Bank uses include the following:

*Interest Rate Gap Analysis:* Interest rate gap analysis measures the difference in the amounts of interest-earning assets and interest-bearing liabilities at each maturity and re-pricing date for a specific time frame.

*Duration Gap Analysis:* Duration gap analysis measures durations of Chohung Bank's interest-earning assets and interest-bearing liabilities, which are weighted average maturities of these assets and liabilities calculated based on discounted cash flows from these assets and liabilities using yield curves.

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*Market Value Analysis:* Market value analysis measures changes in the market value of Chohung Bank's interest-earning assets and interest-bearing liabilities based on the assumption of parallel shifts in interest rates.

*Net Interest Income Simulation Analysis:* Net interest income simulation analysis uses statistical analysis methodology to measure changes in Chohung Bank's annual net interest income (interest income less interest expenses) under the current maturity structure, using different scenarios for interest rates (assuming parallel shifts) and funding requirements.

*Earnings-at-Risk Analysis*

Chohung Bank measures EaRs for interest rate risk from nontrading activities on a monthly basis. Chohung Bank uses EaR as the principal analytical tool to measure and manage its interest rate risk for non-trading activities.

Chohung Bank calculates EaRs with respect to Won-denominated and foreign-currency denominated nontrading assets and liabilities in its bank accounts. On a monthly basis, Chohung Bank calculates 500 sets of annual interest income and expense scenarios based on 500 different sets of yield curves generated by a Monte Carlo simulation. Based on these annual interest and expense scenarios, it then calculates the average and the minimum of the interest income, interest expense and net interest income at a 99% confidence level. EaRs are the differences between these average and minimum values.

The following table presents the minimum and average values of interest income, interest expense and net interest income, and the EaRs corresponding to them for 2005.

**Simulation Results for 2005**

	<b>Minimum(1)</b>	<b>Average</b>	<b>EaR(1)</b>
	<b>(In billions of Won)</b>		
Interest income (from interest-earning assets)	W 3,324.2	W 3,504.0	W 179.8
Interest expense (from interest-bearing liabilities)	1,764.2	1,852.6	88.3
Net interest income	1,560.0	1,651.5	91.5

*Note:*

(1) At a 99% confidence level.

*Interest Rate Gap Analysis*

Interest rate gap analysis measures the difference in the amounts of interest-earning assets and interest-bearing liabilities at each maturity and re-pricing date by preparing interest rate gap tables in which Chohung Bank's interest-earning assets and interest-bearing liabilities are allocated to the applicable time buckets based on the expected cash flows and re-pricing dates. On a monthly basis, Chohung Bank performs interest rate gap analysis for Won and foreign currency denominated assets and liabilities in Chohung Bank's bank and trust accounts. Chohung Bank's gap analysis includes Won-denominated derivatives (which are interest rate swaps) but excludes foreign currency-denominated derivatives, whose management is centralized at the Treasury Department. Through the interest rate gap analysis that measures interest rate sensitivity gaps, cumulative gaps and gap ratios, Chohung Bank assesses its exposure to future interest risk fluctuations.

For interest rate gap analysis, Chohung Bank assumes and uses the following maturities for different assets and liabilities:

With respect to the maturities and re-pricing dates of Chohung Bank's assets, Chohung Bank assumes that maturity of Chohung Bank's prime rate-linked loans are the same as its fixed-rate loans. For debt securities in its trading accounts, Chohung Bank assumes a maturity of three months. Chohung Bank excludes equity securities from interest-earning assets and also excluded assets classified as substandard or below from its interest rate gap analysis.



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With respect to the maturities and re-pricing of Chohung Bank's liabilities, Chohung Bank assumes that money market deposit accounts and non-core demand deposits have a maturity of three months or less. With respect to core demand deposits under the Financial Supervisory Commission guidelines, Chohung Bank assumes a maturity of three years.

The following tables show Chohung Bank's interest rate gaps as of December 31, 2005 for (1) Won-denominated nontrading bank accounts, including derivatives and (2) foreign currency-denominated non-trading bank accounts, excluding derivatives.

**Won-denominated non-trading bank accounts (including derivatives):**

As of December 31, 2005

	0-3 Months	3-6 Months	6-12 Months	1-3 Years	Over 3 Years	Total
(In billions of Won, except percentages)						
<b>Interest-earning assets</b> (Including interest rate swaps)	W 31,633	W 4,399	W 6,779	W 3,844	W 2,918	W 49,573
<b>Interest-bearing liabilities</b> (Including interest rate swaps)	20,035	6,095	8,410	10,683	5,582	50,805
Sensitivity gap	11,598	(1,696)	(1,631)	(6,839)	(2,664)	(1,232)
Cumulative gap	11,598	9,902	8,271	1,432	(1,232)	
% of total assets	23.4%	20.0%	16.7%	2.9%	(2.5)%	

**Foreign currency-denominated non-trading bank accounts (excluding derivatives):**

As of December 31, 2005

	0-3 Months	3-6 Months	6-12 Months	1-3 Years	Over 3 Years	Total
(In millions of US\$, except percentages)						
Interest-earning assets	\$ 4,151	\$ 536	\$ 135	\$ 30	\$ (183)	\$ 4,669
Interest-bearing liabilities	4,031	572	133	101	666	5,503
Sensitivity gap	120	(36)	2	(71)	(841)	(834)
Cumulative gap	120	84	86	15	(834)	
% of total assets	2.6%	1.8%	1.8%	0.3%	(17.9)%	

*Duration and Market Value Analysis*

Chohung Bank performs a duration gap analysis to measure effects of interest rate risk on the market value of its assets and liabilities. Chohung Bank measures, on a monthly basis and for each operating department, account, product and currency, durations of interest-earning assets and interest-bearing liabilities. Chohung Bank also measures, on a monthly basis, changes in the market value of Chohung Bank's interest-earning assets and interest-bearing liabilities.

The following tables show duration gaps and market values of Chohung Bank's Won-denominated interest-earning assets and interest-bearing liabilities in its nontrading accounts as of December 31, 2005 and changes in these market values when interest rate increases by 100 basis point.

	<b>Duration as of December 31, 2005(1)</b>
	<b>(In months)</b>
Interest-earning assets	4.8
Interest-bearing liabilities	9.7
Gap	(4.1)

**Table of Contents****Market Value as of December 31, 2005(1)**

	<b>Actual</b>	<b>1% Point Increase</b>	<b>Changes</b>
	<b>(In billions of Won)</b>		
Interest-earning assets	W 48,018.5	W 47,786.6	W (231.9)
Interest-bearing liabilities	39,890.7	39,505.8	(384.9)
Gap	8,127.8	8,280.8	153.0

*Note:*

(1) Includes interest rate swaps.

*Net Interest Income Simulation*

Chohung Bank performs a net interest income simulation to measure effects of interest rate risk on Chohung Bank's results of operations. Net interest income simulation measures changes in Chohung Bank's annual net interest income (interest income less interest expenses) under the current maturity structure, using different scenarios for interest rates and funding requirements. Chohung Bank applies three scenarios of parallel shifts in interest rate: (1) no change, (2) a 1% point increase in interest rates and (3) a 1% point decrease in interest rates. For funding requirement changes, Chohung Bank uses simulated funding requirements based on its funding plans.

The following table illustrates by way of an example the simulated changes in Chohung Bank's annual net interest income for 2006 with respect to Won-denominated interest-earning assets and interest-bearing liabilities, using its net interest income simulation model, when Chohung Bank assumes (a) the maturity structure and funding requirement of Chohung Bank as of December 31, 2005 and (b) the same interest rates as of December 31, 2005 and a 1% point increase or decrease in the interest rates.

**Simulated Net Interest Income for 2006  
(for Nontrading Won-denominated Bank Accounts)(1)**

	<b>Assumed Interest Rates</b>		<b>Change in Net Interest Income</b>		<b>Change in Net Interest Income</b>		
	<b>No Change</b>	<b>1% Point Increase</b>	<b>1% Point Decrease</b>	<b>Amount</b>	<b>% Change</b>	<b>Amount</b>	<b>% Change</b>
				<b>(1% Point Increase)</b>	<b>(1% Point Increase)</b>	<b>(1% Point Decrease)</b>	<b>(1% Point Decrease)</b>
Simulated interest income	W 3,321.8	W 3,629.2	W 3,013.1	W 307.4	9.25%	W (308.7)	9.29%
Simulated interest expense	1,763.5	1,997.8	1,546.7	234.3	13.29	(216.8)	12.29
Net interest income	1,558.3	1,631.4	1,466.4	73.1	4.69	(91.9)	5.90

**(In billions of Won, except percentages)**

Simulated interest income	W 3,321.8	W 3,629.2	W 3,013.1	W 307.4	9.25%	W (308.7)	9.29%
Simulated interest expense	1,763.5	1,997.8	1,546.7	234.3	13.29	(216.8)	12.29
Net interest income	1,558.3	1,631.4	1,466.4	73.1	4.69	(91.9)	5.90

*Note:*

(1) Includes interest rate swaps.

Chohung Bank's Won-denominated interest earning assets and interest-bearing liabilities in nontrading accounts have a maturity profile that benefits from an increase in interest rates, because the re-pricing periods of the interest-earning assets in Chohung Bank's nontrading accounts are shorter than those of the interest-bearing liabilities in these accounts. This is primarily due to a continuous decrease in interest rate in the recent years in Korea, which has resulted in a significant increase in floating rate loans, making the maturities or re-pricing periods of Chohung Bank's loans shorter, while fixed-rate longer-term deposits have increased. As a result, Chohung Bank's net interest income increases when the interest rates rise.

**Table of Contents***Interest Rate VaRs for Non-trading Assets and Liabilities*

Chohung Bank measures VaRs for interest rate risk from nontrading activities on a monthly basis, except for available-for-sale securities for which it measures interest rate risk on a daily basis. The following table shows, as of and for the year ended December 31, 2005, the ten-day VaRs of interest rate risk from Chohung Bank's available-for-sale investment securities. Under the Financial Supervisory Commission regulations, Chohung Bank includes in the calculation of these VaRs interest-earning assets and interest-bearing liabilities in its bank accounts and its trust accounts.

**Ten-day VaR for the Year 2005(1)**

	<b>Average</b>	<b>Minimum</b>	<b>Maximum</b>	<b>As of December 31</b>
	<b>(In billions of Won)</b>			
Interest rate available-for-sale securities	W 35.1	W 22.4	W 52.9	W 38.6

*Note:*

(1) Ten-day VaR results at a 99% confidence level.

*Equity Risk*

All of Chohung Bank's equity risk results from listed and unlisted equity securities issued by Korean companies. Chohung Bank measures VaRs the listed equity securities but does not manage most of the related risk using VaR limits, as most of these securities are held for reasons other than normal investment purposes. For unlisted equity securities, Chohung Bank does not measure VaRs. These unlisted securities were equities of its consolidated subsidiary and affiliates and those held as a result of debt-to-equity conversion as a part of reorganization proceedings of companies to which it had extended loans. As of December 31, 2004, Chohung Bank held equity securities in an aggregate amount of W1,550 billion in its nontrading accounts, including W373 billion of unlisted securities. As of December 31, 2005, it held equity securities in an aggregate amount of W2,616 billion in its nontrading accounts, including W372 billion of unlisted securities.

The following tables show the VaRs of Chohung Bank's equity risk from nontrading activities as of and for the year ended December 31, 2005.

**Trading Portfolio Ten-day VaR for the Year 2005(1)**

	<b>Average</b>	<b>Minimum</b>	<b>Maximum</b>	<b>As of December 31</b>
	<b>(In billions of Won)</b>			
Equities	W 374.8	W 257.9	W 558.1	W 557.0

(1) Ten-day VaR results at a 99% confidence level.

*Liquidity Risk Management*

Liquidity risk is the risk of insolvency, default or loss due to disparity between inflow and outflow of funds, including having to obtain funds at a high price or to dispose of securities at an unfavorable price due to lack of available funds or losing attractive investment opportunities.

Chohung Bank has the following basic principles for liquidity risk management:

maintain an appropriate level of liquidity risk through liquidity risk management based on liquidity gap or debt-to-equity ratio at each maturity date;

assess and monitor net cash flows by currency and by maturity and continuously evaluate available sources of funds and the possibility of disposal of any liquid assets;

diversify sources and uses of funds by product and by maturity to prevent excessive concentration in certain periods or products; and

prepare contingency plans to cope with a potential liquidity crisis.

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Each subsidiary manages liquidity risk in accordance with the risk limits and guidelines established internally as well as those directed by the relevant regulatory authorities. Pursuant to principal regulations applicable to financial holding companies and banks as promulgated by the Financial Supervisory Commission, Chohung Bank is required to keep specific Won and foreign currency liquidity ratios. These ratios require us to keep the ratio of liquid assets to liquid liabilities above certain minimum levels.

Chohung Bank manages its liquidity risk within the limits set on Won and foreign currency accounts in accordance with the regulations of the Financial Supervisory Commission. The Financial Supervisory Commission requires Korean banks to maintain a Won liquidity ratio of at least 100.0% and a foreign currency liquidity ratio of at least 85%. The Financial Supervisory Commission defines the liquidity ratio as liquid assets (including marketable securities) due within three months divided by liabilities due within three months.

The Treasury Department is in charge of liquidity risk management with respect to Chohung Bank's Won and foreign currency funds. The Treasury Department submits Chohung Bank's monthly funding and asset management plans to the ALM Committee for approval, based on the analysis of various factors, including macroeconomic indices, interest rate and foreign exchange movements and the maturity profile of Chohung Bank's assets and liabilities. The ALM Committee measures Chohung Bank's liquidity ratio and liquidity gap ratio on a monthly basis and reports whether they are in compliance with the limits to the ALM Committee on a monthly basis.

The following tables show Chohung Bank's liquidity status and limits for Won and foreign currency accounts as of December 31, 2005 in accordance with the regulations of the Financial Supervisory Commission.

**As of December 31, 2005**

<b>Won-denominated Accounts</b>	<b>0-3 Months</b>	<b>3-6 Months</b>	<b>6-12 Months</b>	<b>1-3 Years</b>	<b>Over 3 Years</b>	<b>Substandard or Below</b>	<b>Total</b>
<b>(In billions of Won except percentage)</b>							
Assets:	W 31,619.8	W 10,254.3	W 15,075.8	W 6,556.9	W 13,886.4	W 493.6	W 77,886.7
Liabilities:	26,801.3	6,295.7	12,878.2	8,992.7	23,625.3		78,593.2
For three months or less:							
Liquidity gap	4,818.5						
Liquidity ratio	117.98%						
Limit:	105.00%						

**As of December 31, 2005**

<b>Foreign Currencies Denominated Accounts:</b>	<b>7 Days or Less</b>	<b>7 Days- 1 Months</b>	<b>3 Months</b>	<b>3-6 Months</b>	<b>6-12 Months</b>	<b>Over 1 Years</b>	<b>Total</b>
<b>(In millions of US\$ except percentage)</b>							
Assets:	\$ 2,333.9	\$ 3,964.0	\$ 5,277.3	\$ 3,092.6	\$ 3,941.6	\$ 3,739.9	\$ 22,349.3
Liabilities	2,113.4	4,165.8	4,993.5	2,763.7	4,403.0	2,798.8	21,238.2
For three months or less:							
Assets			11,575.2				
Liabilities			11,272.7				

Liquidity ratio	102.68%
Limit	85.00%

Chohung Bank maintains diverse sources of liquidity to facilitate flexibility in meeting its funding requirements. Chohung Bank funds its operations principally through deposits from retail and corporate customers, accessing the call loan market (a short-term market for loans with maturities of less than one month), issuing debentures and borrowings from the Bank of Korea. Chohung Bank uses the funds primarily to extend loans or purchase securities. Generally, deposits are of shorter average maturity than loans or investments.

In addition to liquidity risk management under the normal market conditions, Chohung Bank has contingency plans to cope with a potential liquidity crisis. A liquidity crisis arises when Chohung Bank would

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not be able to effectively manage the situations with Chohung Bank's normal liquidity management measures due to, among other reasons, inability to access its normal sources of funds or epidemic withdrawals of deposits as a result of various external or internal factors, including a collapse in the financial markets or abrupt deterioration of its credit. Chohung Bank has contingency plans corresponding to different stages of liquidity crisis, cautionary stage, near-crisis stage and crisis stage, based on the following liquidity indices:

indices that reflect the market movements such as interest rates and stock prices;

indices that reflect financial market psychology such as the size of money market funds; and

indices that reflect Chohung Bank's internal financial condition.

*Operational Risk Management*

Operational risk is difficult to quantify and subject to different definitions. The Basle Committee defines operational risk as the risk of loss resulting from inadequate or failed internal processes, people and systems or from other external events. Similarly, we define operational risk as the risks related to our overall management other than credit risk, market risk, interest rate risk and liquidity risk. These include risks arising from system failure, human error or non-adherence to policy and procedures, from fraud or inadequate internal controls and procedures, from a mistake in strategic decision or from environmental changes, resulting in financial and non-financial loss, including reputational loss. We monitor and assess operational risks related to our business operations, including administrative risk, information technology risk, managerial risk, legal risk and reputation risk, with a view to minimizing such losses.

The Group Internal Audit Activity, reporting directly to our Audit Committee, is directly responsible for overseeing our operational risk management with a focus on legal, regulatory, operational and reputational risks. Our Audit Committee oversees and monitors our operational compliance with legal and regulatory requirements. At the holding company level, we define each subsidiary's operational process and establish an internal review system applicable to each subsidiary. Each subsidiary's operational risk is internally monitored and managed at the subsidiary level and the Group Internal Audit Activity continuously monitors the integrity of our subsidiaries' operational risk management system. Our Board of Directors, the Group Risk Management Committee and our Audit Committee establish our basic policies for operational risk management at the group level.

To monitor and manage operational risks, each of our principal banking subsidiaries, Shinhan Bank and Chohung Bank maintained, and after the merger, Shinhan Bank maintains, a system of comprehensive policies and has in place a control framework designed to provide a stable and well-managed operational environment throughout the organization. Currently, the primary responsibility for ensuring compliance with our banking operational risk procedures remains with each of the business units and operational teams. In addition, the Audit Department, the Audit Support Office, the Risk Management Department and the Compliance Office of Shinhan Bank also play important roles in reviewing and maintaining the integrity of Shinhan Bank's internal control environment.

The operational risk management system of Shinhan Bank was developed based on a two-year planning preceding the merger of the two banks and is currently managed by the operational risk team under the Risk Management Department. The current system principally consists of risk control self-assessment, risk quantification by way of key risk indicators, loss data collection, risk simulations and monitoring of at-risk operating capital. As of June 15, 2006, Shinhan Bank has conducted two risk control self-assessments on approximately 160 of its departments and branch offices, from which it has been able to derive systematized data on all of its branch offices. In addition, Shinhan Bank has accumulated risk-related data since 2003 based on approximately 40 key risk indicators, improved the procedures for monitoring operational losses and is developing risk simulation models. Shinhan Bank operates several educational and awareness programs with a view to familiarizing all of its employees to this new system. In addition, Shinhan Bank has a designated operational risk manager at each of its departments and branch offices, serving the role of a coordinator

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between the operational risk team at the headquarters and the employees in the field and seeking to provide centralized feedback to further improve the operational risk management system.

The audit committee of Shinhan Bank, which consists of three board members, including two outside directors, is an independent inspection authority that supervises Shinhan Bank's internal controls and compliance with established ethical and legal principles. The audit committee performs internal audits of, among other matters, Shinhan Bank's overall management and accounting, and supervises the Audit Department of Shinhan Bank that assists the audit committee. The audit committee also reviews and evaluates Shinhan Bank's accounting policies and their changes, financial and accounting matters and fairness of financial reporting.

The Audit Committee, the Audit Department and the Audit Support Office supervise and perform the following audits:

general audits, including full-scale audits performed annually for the overall operations, sectional audits of selected operations performed when necessary, and periodic and irregular spot audits;

special audits, performed when the Audit Committee or standing auditor deems it necessary or pursuant to requests by the chief executive officer or supervisory authorities such as the Financial Supervisory Service;

day-to-day audits, performed by the standing auditor for material transactions or operations that are subject to approval by the heads of Shinhan Bank's operational departments or senior executives;

real-time monitoring audits, performed by the computerized audit system to identify any irregular transactions and take any necessary actions; and

self-audits as a self-check by each operational department to ensure its compliance with our business regulations and policies, which include daily audits, monthly audits and special audits.

In addition to these audits and compliance activities, the Audit Support Office continuously monitors, manages and reports important operational risk related matters, including risk limit monitoring results, trading status and sources and uses of funds. The Audit Support Office also reviews in advance new business or service plans proposed by our principal banking subsidiary's operational departments to minimize operational risk.

General audits, special audits, day-to-day audits and real-time monitoring audits are performed by our examiners and self-audits are performed by the self-auditors of the relevant operational departments.

In addition to internal audits and inspections, the Financial Supervisory Service conducts general annual audits of operations at Shinhan Financial Group and also performs general annual audits of our operations. The Financial Supervisory Service also performs special audits as the need arises on particular aspects of our operations such as risk management, credit monitoring and liquidity. In the ordinary course of these audits, the Financial Supervisory Service routinely issue warning notices where it determines that a regulated financial institution or such institution's employees have failed to comply with the applicable laws or rules, regulations and guidelines of the Financial Supervisory Service. We have in the past received, and expect in the future to receive, such notices and we have taken and will continue to take appropriate actions in response to such notices.

In April 2005, the Financial Supervisory Service found that Chohung Bank's employees had embezzled approximately W40 billion of Chohung Bank's funds over a period of five months. Chohung Bank recovered approximately W4 billion of the embezzled fund. As a remedial measure, the Financial Supervisory Service issued a warning to Chohung Bank as well as its president and the statutory auditor for supervisory negligence and ordered Chohung Bank to sign a memorandum of understanding to improve its internal controls and took several remedial measures, including increasing staffing at our back office, strengthening periodic monitoring and improving internal control procedures related to fund transfer documentation.

In addition, during a periodic audit in November 2005, the Financial Supervisory Service discovered that one of Chohung Bank's employees, in collaboration with an employee of Kookmin Bank, issued counterfeit



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certificates of deposits in the course of embezzling over a period of seven months an aggregate of approximately W445 billion of customer funds deposited at the two banks, of which amount W20 billion was deposited with Chohung Bank. The Financial Supervisory Service suspended the operation of the branches of the two banks directly involved with the incident for three months and issued warnings against the presidents and statutory auditors of Chohung Bank and Kookmin Bank (including a disciplinary warning against the president of Chohung Bank) for negligent supervision. In response to this incident, Chohung Bank took several remedial measures to strengthen compliance procedures and improve the execution of the existing internal control systems.

Except as described, none of the actions we have taken so far has had a material adverse effect.

We consider legal risk as a part of operational risk. The uncertainty of the enforceability of obligations of our customers and counterparties, including foreclosure on collateral, creates legal risk. Changes in laws and regulations could also adversely affect us. Legal risk is higher in new areas of business where the law is often untested in the courts although legal risk can also increase in our traditional business to the extent that the legal and regulatory landscape in Korea is changing and many new laws and regulations governing the banking industry remain untested. We seek to minimize legal risk by using stringent legal documentation, employing procedures designed to ensure that transactions are properly authorized and consulting legal advisers. The Compliance Office operates our principal banking subsidiary's compliance inspection system. This system is designed to ensure that all of Shinhan Bank's employees comply with the law. The compliance inspection system's main function is to monitor the degree of improvement in compliance with the law, maintain internal controls (including ensuring that each department has established proper internal policies and that it complies with those policies) and educate employees about observance of the law.

***Proposed Upgrades and Integration of Risk Management***

Since prior to their merger, Shinhan Bank and Chohung Bank have launched a joint task force, a Basel II project team, to address issues relating to the adoption of a new firm-wide system for operational risk management to apply a standardized approach that meets the recommendations by the BIS New Basle Accord for Measurement and Management of Operational Risk. The Operational Risk Management Team consists of 12 members. This Basel II project team sought to develop systems, processes and organizations that would meet the relevant qualitative and quantitative requirements by applying the A-IRB method to credit risks and an advanced evaluation approach to operational risks and, beginning in May 2004, have enlisted the support of a global consulting firm to benchmark the best practices of the more advanced global banks. We believe that the Basel II project helps us not only to meet the capital adequacy requirements in the future but also to secure a source of information that will be critical in making important decisions, such as managing risks within reasonable bounds and formulating an asset portfolio strategy, by enabling us to better our understanding of the risks embedded in substantially all aspects of our banking operations. The Financial Supervisory Commission is currently reviewing Basel II-related regulations. Following the completion of such review and adoption of new regulations by the Financial Supervisory Commission, which is currently expected to happen by the end of 2006, and subject to obtaining the necessary regulatory approval, we plan to complete the implementation of the Basel II-related systems and commence its operations.

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**SUPERVISION AND REGULATION**

**Principal Regulations Applicable To Financial Holding Companies**

***General***

The Korean financial holding companies and their subsidiaries are regulated by the Financial Holding Companies Act (Law No. 6692, April 27, 2002). In addition, Korean financial holding companies and their subsidiaries are subject to the regulations and supervision of the Financial Supervisory Commission and the Financial Supervisory Service.

The Financial Supervisory Commission, established on April 1, 1998, exerts direct control over financial holding companies pursuant to the Financial Holding Companies Act, including approval for the establishment of financial holding companies, issuing regulations on capital adequacy of financial holding companies and their subsidiaries, and drafting regulations relating to the supervision of financial holding companies.

The Financial Supervisory Service was established on January 2, 1999, as a unified body of the former Banking Supervisory Authority (the successor to the Office of Bank Supervision, the Securities Supervisory Board, the Insurance Supervisory Board and the Credit Management Fund). The Financial Supervisory Service is subject to the instructions and directives of the Financial Supervisory Commission and carries out supervision and examination of financial holding companies and their subsidiaries. In particular, the Financial Supervisory Service sets requirements regarding financial holding companies' liquidity and for capital adequacy and establishes reporting requirements within the authority delegated under the Financial Supervisory Commission regulations, pursuant to which financial holding companies are required to submit quarterly reports on business performance, financial status and other matters prescribed in the Presidential Decree of the Financial Holding Companies Act.

Under the Financial Holding Companies Act, the establishment of a financial holding company must be approved by the Financial Supervisory Commission. A financial holding company is required to be mainly engaged in controlling its subsidiaries by holding the shares or equities of the subsidiaries in the amount of not less than 50% of aggregate amount of such financial holding company's assets based on the latest balance sheet. A financial holding company is prohibited from engaging in any profit-making businesses other than controlling the management of its subsidiaries and certain ancillary businesses as prescribed in the Presidential Decree of the Financial Holding Companies Act which include the following businesses:

financially supporting its subsidiaries and the subsidiaries of its subsidiaries (the direct and indirect subsidiaries);

raising capital necessary for the investment in subsidiaries or providing financial support to its direct and indirect subsidiaries;

supporting the business of its direct and indirect subsidiaries for the joint development and marketing of new product and the joint utilization of facilities or IT systems; and

any other businesses exempted from authorization, permission or approval under the applicable laws and regulations.

The Financial Holding Companies Act requires every financial holding company (other than any financial holding company that is controlled by any other financial holding company) or its subsidiaries to obtain the prior approval from the Financial Supervisory Commission before acquiring control of another company or to file with the Financial Supervisory Commission a report within thirty (30) days after acquiring such control. Permission to liquidate or to merge with any other company must be obtained in advance from the Financial Supervisory Commission. A financial holding company must report to the Financial Supervisory Commission regarding certain events including:

when there is a change of its officers;

when there is a change of its largest shareholder;

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when there is a change of major shareholders of a bank holding company;

when there is a cause for dissolution; and

when it or its subsidiary ceases to control any of its respective direct and indirect subsidiaries by disposing of the shares of such direct and indirect subsidiaries.

In January 2005, the Ministry of Finance and Economy announced that it would proceed with the amendment of the Financial Holding Companies Act to allow a foreign financial holding company to establish a domestic financial holding company, which is not allowed under the current Financial Holding Companies Act.

***Capital Adequacy***

The Financial Holding Companies Act does not provide for a minimum paid-in capital of financial holding companies. All financial holding companies, however, are required to maintain a specified level of solvency. In addition, in its allocation of the net profit earned in a fiscal term, a financial holding company is required to set aside in its legal reserve an amount equal to at least 10% of the net income after tax each time it pays dividends on its net profits earned until its legal reserve reaches at least the aggregate amount of its paid-in capital.

All financial holding companies must meet the minimum Requisite Capital Ratio of 100%, as regulated by the Financial Supervisory Commission.

Requisite Capital Ratio means the ratio of (1) Net Total Equity Capital, as defined below, to (2) Requisite Capital, as defined below.

1. Net Total Equity Capital means:

(a) the sum of:

- (i) in the case of a financial institution subsidiary (except for a financial holding company's indirect subsidiary which is consolidated into a direct subsidiary of a financial holding company), that is subject to minimum capital requirements under the Financial Supervisory Commission regulations, the actual equity capital maintained by such financial institution (e.g., in the case of commercial banks and merchant banks, total Tier I and Tier II capital actually maintained by a bank or a merchant bank); and
- (ii) in the case of a financial holding company or a financial institution subsidiary (except for a financial holding company's indirect subsidiary which is consolidated into a direct subsidiary of a financial holding company), that is not subject to minimum capital requirements under the Financial Supervisory Commission regulations, the total stockholders' equity as recorded on its balance sheet less (x) intangible assets and (y) deferred tax assets, if any.

(b) less the sum of:

- (i) the book value of investments between a financial holding company and its direct and indirect subsidiaries, if any; and
- (ii) the book value of investments among direct and indirect subsidiaries, if any.

2. Requisite Capital means the sum of:

- (a) in the case of a financial institution subsidiary (except for a financial holding company's indirect subsidiary which is consolidated into a direct subsidiary of a financial holding company), that is subject to minimum capital requirements under the Financial Supervisory Commission regulations, the minimum equity capital amount necessary to meet such requirements (e.g., in the case of commercial banks and merchant banks, the amount of Total Tier I and Tier II capital necessary to meet the 8% minimum capital adequacy ratio requirement);

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- (b) in the case of a financial institution subsidiary (except for a financial holding company's indirect subsidiary which is consolidated into a direct subsidiary of a financial holding company), that is not subject to minimum capital requirements under the Financial Supervisory Commission regulations, 8% of its total assets on its balance sheet (including off-balance sheet assets, if any); and
- (c) in the case of a financial holding company, 8% of its total assets on its balance sheet (including off-balance sheet assets, if any, but excluding the book value of investments in and financial supports to its direct and indirect subsidiaries, if any).

***Liquidity***

All financial holding companies are required to match the maturities of their assets to those of liabilities in accordance with the Financial Holding Companies Act in order to ensure liquidity. Financial holding companies are required to submit quarterly reports regarding their liquidity to the Financial Supervisory Service and must:

maintain a Won liquidity ratio (defined as Won assets due within three months, including marketable securities, divided by Won liabilities due within three months) of not less than 100%;

maintain a foreign currency liquidity ratio (defined as foreign currency liquid assets due within three months divided by foreign currency liabilities due within three months) of not less than 80%;

maintain a ratio of foreign currency liquid assets due within seven days less foreign currency liabilities due within seven days divided by total foreign currency assets of not less than 0%; and

maintain a ratio of foreign currency liquid assets due within a month less foreign currency liabilities due within a month divided by total foreign currency assets of not less than negative 10%.

A financial holding company may not invest in securities as defined in the Securities and Exchange Act (other than those securities issued by its direct and indirect subsidiaries) in excess of the amount of its shareholders' equity less the total amount of investment in subsidiaries, subject to certain exceptions such as capital reductions, a change in securities' price, a merger of a financial holding company or an acquisition of all of the business by a financial holding company, a foreclosure of collateral or strict foreclosure of securities. A financial holding company whose investment exceeds the amount of its shareholders' equity less the total amount of investment in subsidiaries as a result of these exceptions are required to take actions to comply with the foregoing limit within one year from the date it exceeded such limit.

***Financial Exposure to Any Single Customer and Major Shareholder***

Subject to certain exceptions, the total sum of credit (as defined in the Financial Holding Companies Act, the Bank Act, the Merchant Bank Act and the Securities and Exchange Act, respectively) of a financial holding company and its direct and indirect subsidiaries which are banks, merchant banks or securities companies ( Financial Holding Company Total Credit ) extended to a single group of companies that belong to the same conglomerate as defined in the Monopoly Regulations and Fair Trade Act will not be permitted to exceed 25% of the Net Total Equity Capital.

Net Total Equity Capital for the purpose of the calculation of financial exposure to any single customer and Major Shareholder (as defined below) is defined under the Presidential Decree of the Financial Holding Companies Act as

- (a) the sum of:
  - (i) in case of a financial holding company, the net asset which is total assets less total liabilities on balance sheet as of the end of the most recent quarter;
  - (ii) in case of a bank, the capital amount as defined in Article 2(1), item 5 of the Bank Act;

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- (iii) in case of a merchant bank, the capital amount as defined in Article 2, item 3 of the Merchant Bank Act; and
- (iv) in case of a securities company, the total asset amount less the total liability amount in the balance sheet as of the end of the most recent fiscal year and adjusted as determined by the Financial Supervisory Commission, such as the amount of increase or decrease in paid-in capital after the end of the most recent fiscal year;
- (b) less the sum of:
  - (i) the amount of shares of direct and indirect subsidiaries held by the financial holding company;
  - (ii) the amount of shares which are cross-held by each direct and indirect subsidiary that is a bank, merchant bank or securities company; and
  - (iii) the amount of shares of a financial holding company held by such direct and indirect subsidiaries which are banks, merchant banks or securities companies.

The Financial Holding Company Total Credit to a single individual or legal entity will not be permitted to exceed 20% of the Net Total Equity Capital. In addition, the Financial Holding Company Total Credit to a shareholder holding (together with the persons who have special relationship with such shareholder (as defined under the Presidential Decree of the Financial Holding Companies Act)) in aggregate more than 10% of the total issued and outstanding shares of the financial holding company will not be permitted to exceed the smaller of (x) 25% of the Net Total Equity Capital and (y) the amount of the equity capital of the financial holding company multiplied by the shareholding ratio of such shareholder (together with the persons who have special relationship with such shareholder).

Furthermore, the total sum of credits (as defined under the Financial Holding Companies Act, the Bank Act, the Merchant Bank Act and the Securities and Exchange Act, respectively) of a financial holding company controlling banks and its direct and indirect subsidiaries that are banks, merchant banks or securities companies as applicable ( Bank Holding Company Total Credit ) extended to a Major Shareholder (together with the persons who have special relationship with such Major Shareholder) (as defined below) will not be permitted to exceed the smaller of (x) 25% of the Net Total Equity Capital and (y) the amount of the equity capital of the financial holding company multiplied by the shareholding ratio of such Major Shareholder, except in certain cases.

Major Shareholder is defined under the Financial Holding Companies Act as follows:

- (a) a shareholder holding (together with persons who have a special relationship with such shareholder as defined in the Presidential Decree of the Financial Holding Companies Act) in excess of 10% (or in the case of a financial holding company controlling regional banks only, 15%) in the aggregate of the financial holding company's total issued and outstanding voting shares; or
- (b) a shareholder holding (together with persons who have a special relationship with such shareholder as defined in the Presidential Decree of the Financial Holding Companies Act) more than 4% in the aggregate of the total issued and outstanding voting shares of the financial holding company controlling national banks (other than a financial holding company controlling regional banks only), excluding shares related to the shareholding restrictions on non-financial business group companies as described below, where such shareholder is the largest shareholder or has actual control over the major business affairs of the financial holding company through, for example, appointment and dismissal of the officers pursuant to the Presidential Decree of the Financial Holding Companies Act.

In addition, the total sum of the Bank Holding Company Total Credit extended to all of a financial holding company's Major Shareholder must not exceed 25% of the Net Total Equity Capital. Furthermore, the financial holding company and its direct and indirect subsidiaries that intend to extend the Bank Holding Company Total Credit to the financial holding company's Major Shareholder not less than the lesser of (i) the

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amount equivalent to 0.1% of the Net Total Equity Capital or (ii) W5 billion, with respect to a single transaction, must obtain prior unanimous board resolutions and then immediately after the completion of the transaction, must file a report with the Financial Supervisory Commission and publicly disclose the filing of such report (e.g., via the Internet).

***Restrictions on Transactions Among Direct and Indirect Subsidiaries and Financial Holding Company***

Generally, a direct or indirect subsidiary of a financial holding company may not extend credit to the financial holding company which directly or indirectly controls such subsidiary. In addition, a direct and indirect subsidiary of a financial holding company may not extend credit to any other single direct or indirect subsidiary of the financial holding company in excess of 10% of its shareholders' equity and to any other direct and indirect subsidiaries of the financial holding company in excess of 20% of its shareholders' equity in the aggregate. The direct or indirect subsidiaries of a financial holding company must obtain an appropriate level of collateral for the credits extended to the other direct and indirect subsidiaries unless otherwise approved by the Financial Supervisory Commission. The appropriate level of collateral for each type of credit is as follows:

- (i) For deposits and installment savings, obligations of the Korean government or The Bank of Korea, obligations guaranteed by the Korean government or The Bank of Korea, obligations secured by securities issued or guaranteed by the Korean government or The Bank of Korea: 100% of the amount of the credit extended;
- (ii) (a) For obligations of local governments under the Local Autonomy Act, local public enterprises under the Local Public Enterprises Act, and investment institutions and other quasi-investment institutions under the Basic Act on the Management of Government-Invested Institution (hereinafter, the public institutions and others); (b) obligations guaranteed by the public institutions and others, and (c) obligations secured by the securities issued or guaranteed by public institutions and others: 110% of the amount of the credit extended; and
- (iii) For any property other than those set forth in the above (i) and (ii): 130% of the amount of the credit extended.

Subject to certain exceptions, a direct or indirect subsidiary of a financial holding company is prohibited from owning the shares of any other direct or indirect subsidiaries (other than those directly controlled by the direct and indirect subsidiaries in question) in common control by the financial holding company. In April 2005, the Ministry of Finance and Economy announced that it will allow a direct or indirect subsidiary of a financial holding company to invest as a limited partner in a private equity fund that is a direct or indirect subsidiary of the same financial holding company, and the Presidential Decree of the Financial Holding Companies Act was amended in May 2005 accordingly. Before the amendment, under the Financial Holding Companies Act, a direct or indirect subsidiary of a financial holding company was prohibited from acquiring the shares of another subsidiary of the same financial holding company. A direct or indirect subsidiary of a financial holding company is also generally prohibited from owning the shares of the financial holding company controlling the direct or indirect subsidiary in question. The transfer of certain assets subject to or below the precautionary criteria between the financial holding company and its direct or indirect subsidiary or between the direct and indirect subsidiaries of a financial holding company is prohibited except for (i) the transfer to an asset-backed securitization company (an SPV), or the entrustment with a trust company, under the Asset-Backed Securitization Act, (ii) the transfer to a mortgage-backed securitization company under the Mortgage-Backed Securitization Company Act or (iii) the transfer or in-kind contribution to a corporate restructuring vehicle under the Corporate Restructuring Investment Company Act.

***Disclosure of Management Performance***

For the purpose of protecting the depositors and investors in the subsidiaries of the financial holding companies, the Financial Supervisory Commission requires financial holding companies to disclose certain material matters including (i) financial condition and profit and loss of the financial holding company and its direct and indirect subsidiaries, (ii) how capital was raised by the financial holding company and its direct and indirect subsidiaries and how such capital was used, (iii) any sanctions levied on the financial holding



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company and its direct and indirect subsidiaries under the Financial Holding Companies Act or any corrective measures or sanctions under the Law on Improvement of Structure of Financial Industry or (iv) occurrence of any non-performing assets or financial incident which may have a material adverse effect.

***Restrictions on Shareholdings in Other Companies***

Subject to certain exceptions, a financial holding company may not own more than 5% of the total issued and outstanding shares of another company (other than its direct and indirect subsidiaries). If the financial holding company owns shares of another company (other than its direct and indirect subsidiaries) which is not a finance-related company, the financial holding company is required to exercise its voting rights in the same manner and same proportion as the other shareholders of the company exercise their voting rights in favor of or against any resolutions under consideration at the shareholders' meeting of the company.

Generally, a financial holding company is not allowed to own its subsidiary's outstanding shares in excess of its net assets (total assets *minus* total liabilities), except, among other reasons, (i) where the financial holding company invests in its subsidiary up to 130% of its net assets (total assets *minus* total liabilities) for the purpose of the improvement of the financial condition of a subsidiary which is classified as an unsound financial institution under the Law on the Improvement of Structure of Financial Industry or as an unsound or potentially unsound financial institution under the Depositor Protection Act, (ii) where the financial holding company invests in a company controlled by the indirect subsidiaries up to 130% of its net assets (total assets *minus* total liabilities) in order to make the company as a subsidiary of the financial holding company, (iii) where the financial holding company has already been holding the outstanding shares of its subsidiary not more than 130% of its net assets (total assets *minus* total liabilities) at the time when it becomes a financial holding company, (iv) where in order to make its subsidiary as a 100% owned subsidiary or a special purpose vehicle under the Asset Backed Securitization Act as its subsidiary, the financial holding company invests in such company up to 130% of its net assets, (v) where as the amount of investments in the subsidiaries increases, the financial holding company's net assets increase so that the ratio of the total amount of investments in subsidiaries divided by the financial holding company's net assets do not increase, or (vi) where the total investment amount in its subsidiaries exceeds its net assets due to (a) a reduction of the financial holding company's net assets, (b) a spin-off, merger or transfer of its whole business of a financial holding company, (c) a spin-off, merger or transfer of their whole business of its direct or indirect subsidiaries, or (d) a foreclosure of collateral or strict foreclosure. The financial holding company, however, must dispose of the ownership of excess shares within two years in case of (i) through (v) and within six months in case of (vi), unless such time period is otherwise extended by the Financial Supervisory Commission.

***Restrictions on Shareholdings by Direct and Indirect Subsidiaries***

Generally, a direct subsidiary of a financial holding company is prohibited from controlling any other company; *provided* that a direct subsidiary of a financial holding company may control (as an indirect subsidiary of the financial holding company): (i) subsidiaries in foreign jurisdiction which are engaged in the same business as the direct subsidiary, (ii) certain financial institutions which are engaged in the business that the direct subsidiary may conduct without any licenses or permits, (iii) certain financial institutions whose business is related to the business of the direct subsidiary as prescribed under the Presidential Decree of the Financial Holding Companies Act (e.g., the companies which a bank subsidiary may control are limited to credit information companies, credit card companies, trust business companies, securities investment management companies, investment advisory companies, futures business companies, and asset management companies), (iv) certain financial institutions whose business is related to financial business as prescribed by the regulations of the Ministry of Finance and Economy, (v) certain companies which are not financial institutions but whose business is related to the financial business of the financial holding company as prescribed by the Presidential Decree of the Financial Holding Companies Act (e.g. finance-related research company, finance-related IT company, etc.) and (vi) private equity funds established in accordance with the Act on Business of Operating Indirect Investment and Asset. Acquisition by the direct subsidiaries of such indirect subsidiaries requires prior permission from the Financial Supervisory Commission or report to be

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submitted to the Financial Supervisory Commission, depending on the types of the indirect subsidiaries and the amount of total assets of the indirect subsidiaries.

The indirect subsidiary of a financial holding company is prohibited from controlling any other company, provided, however, that in the case where a company held control over another company at the time such company initially became an indirect subsidiary of a financial holding company, such indirect subsidiary shall be required to dispose of its interest in such other company within two (2) years after becoming an indirect subsidiary of a financial holding company.

In April 2005, the Ministry of Finance and Economy announced that it will allow a subsidiary of a financial holding company to invest in a special purpose company as its largest shareholder for purposes of making investments under the Act on Private Investment in Social Infrastructure without being deemed as controlling such special purpose company. Accordingly, the Presidential Decree of the Financial Holding Companies Act was amended in May 2005 and such special purpose company is not considered as a subsidiary of the financial holding company under the Financial Holding Companies Act.

In addition, a private equity fund established in accordance with the Act on Business of Operating Indirect Investment and Asset is not considered to be a subsidiary of a financial holding company even if the financial holding company is the largest investor in the private equity fund unless the financial holding company is the asset management company for the private equity fund.

***Restrictions on Transactions between a Financial Holding Company and its Major Shareholder***

A financial holding company which controls banks and its direct and indirect subsidiaries is prohibited from acquiring (including acquisition by a trust account of its subsidiary bank) shares issued by such financial holding company's Major Shareholder in excess of 1% of the Net Total Equity Capital as used in the calculation of financial exposure to Major Shareholder. In addition, the financial holding company and its direct and indirect subsidiaries which intend to acquire shares issued by such Major Shareholder not less than the lesser of (i) the amount equivalent to 0.1% of the Equity Capital or (ii) W5 billion, with respect to a single transaction, must obtain prior unanimous board resolutions and then, immediately after the acquisition, must file a report with the Financial Supervisory Commission and publicly disclose the filing of such report (e.g., via the Internet).

***Restriction on Financial Holding Company Ownership***

Under the Financial Holding Companies Act, subject to certain exceptions, a financial institution may not control any financial holding company. In addition, any single shareholder and persons who stand in a special relations with such shareholder (as defined under the Presidential Decree to the Financial Holding Companies Act) may acquire beneficial ownership of up to 10% of the total issued and outstanding shares with voting rights of a financial holding company controlling national banks and 15% of the total issued and outstanding shares with voting rights of a financial holding company controlling regional banks only. The Government and the Korea Deposit Insurance Corporation are not subject to such ceiling. Also, in January 2005, the Ministry of Finance and Economy announced that it would proceed with the amendment of the Financial Holding Companies Act to allow a private equity fund to control financial holding companies, which is currently prohibited.

However, non-financial business group companies (as defined below) may not acquire beneficial ownership of shares of a financial holding company which controls national banks in excess of 4% of such financial holding company's outstanding voting shares, provided that such non-financial business group companies may acquire beneficial ownership of up to 10% of such financial holding company's outstanding voting shares with the approval of the Financial Supervisory Commission under the condition that such non-financial business group companies will not exercise voting rights in respect of such shares in excess of the 4% limit. In addition, any person (whether a Korean national or a foreigner), with the exception of non-financial business group companies described above, may also acquire in excess of 10% of total voting shares issued and outstanding of a financial holding company which controls national bank, provided that an approval from the Financial Supervisory Commission is obtained in instances where the total holding exceeds 10% (or 15% in

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the case of a financial holding company controlling regional banks only), 25% or 33% of the total voting shares issued and outstanding of such financial holding company which controls national banks. Also, in the event a person (whether a Korean national or a foreigner, but excluding persons prescribed under the Presidential Decree to the Financial Holding Companies Act) (i) acquires in excess of 4% of the total voting shares issued and outstanding of any financial holding company (other than a financial holding company controlling regional banks only), (ii) becomes the largest shareholder of such financial holding company in which such person acquired in excess of 4% of the total voting shares issued and outstanding, or (iii) has its shareholding in such financial holding company, in which it had acquired in excess of 4% of the total voting shares issued and outstanding shares, changed by not less than 1% of the total voting share issued and outstanding of such financial holding company, a report as prescribed by the Presidential Decree to the Financial Holding Companies Act shall be filed with the Financial Supervisory Commission.

Non-financial business group companies are defined under the Financial Holding Companies Act as the companies, which include:

- (i) any same shareholder group with aggregate net assets of all non-financial business companies belonging to such group of not less than 25% of the aggregate net assets of all members of such group;
- (ii) any same shareholder group with aggregate assets of all non-financial business companies belonging to such group of not less than W2

trillion; or

- (iii) any mutual fund in which a same shareholder group identified in (1) or (2) above owns more than 4% of the total shares issued and outstanding of such mutual fund.

**Principal Regulations Applicable to Banks****General**

The banking system in Korea is governed by the Bank Act of 1950, as amended (the Bank Act ) and the Bank of Korea Act of 1950, as amended (the Bank of Korea Act ). In addition, Korean banks are subject to the regulations and supervision of the Bank of Korea, the Bank of Korea's Monetary Policy Committee, the Financial Supervisory Commission and its executive body, the Financial Supervisory Service.

The Bank of Korea, established in June 1950 under the Bank of Korea Act, performs the customary functions of a central bank. It seeks to contribute to the sound development of the national economy by price stabilization through establishing and implementing efficient monetary and credit policies. The Bank of Korea acts under instructions of the Monetary Policy Committee, the supreme policy-making body of the Bank of Korea.

Under the Bank of Korea Act, the Monetary Policy Committee's primary responsibilities are to formulate monetary and credit policies and to determine the operations, management and administration of the Bank of Korea. The Financial Supervisory Commission, established on April 1, 1998, exerts direct control over commercial banks pursuant to the Bank Act, including establishing guidelines on capital adequacy of commercial banks, and prepares regulations relating to supervision of banks. Furthermore, pursuant to the Amendment to the Government Organization Act and the Bank Act on May 24, 1999, the Financial Supervisory Commission, instead of the Ministry of Finance and Economy, now regulates market entry into the banking business.

The Financial Supervisory Service is subject to the instructions and directives of the Financial Supervisory Commission and carries out supervision and examination of commercial banks. In particular, the Financial Supervisory Service sets requirements both for prudent control of liquidity and for capital adequacy and establishes reporting requirements within the authority delegated to it under the Financial Supervisory Commission regulations, pursuant to which banks are required to submit annual reports on financial performance and shareholdings, regular reports on management strategy and non-performing loans, including write-offs, and management of problem companies and plans for the settlement of bad loans.

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Under the Bank Act, permission to commence a commercial banking business or a long-term financing business must be obtained from the Financial Supervisory Commission. Commercial banking business is defined as the lending of funds acquired predominantly from the acceptance of deposits for a period not exceeding one year or subject to the limitation established by the Financial Supervisory Commission, for a period between one year and three years. Long-term financing business is defined as the lending, for periods in excess of one year, of funds acquired predominantly from paid-in capital, reserves or other retained earnings, the acceptance of deposits with maturities of at least one year, or the issuance of bonds or other securities. A bank wishing to enter any business other than commercial banking and long-term financing businesses, such as the trust business, must obtain permission from the Financial Supervisory Commission. Permission to merge with any other banking institution, to liquidate, to close a banking business or to transfer all or a part of a business must also be obtained from the Financial Supervisory Commission.

If the Korean government deems a bank's financial condition to be unsound or if a bank fails to meet the applicable capital adequacy ratio set forth under Korean law, the government may order:

capital increases or reductions;

stock cancellations or consolidations;

transfers of a part or all of business;

sale of assets;

closures of branch offices;

mergers or becoming a subsidiary under the Financial Holding Companies Act of a financial holding company;

acquisition of a bank by a third party;

suspensions of a part or all of business operation; or

assignments of contractual rights and obligations relating to financial transactions.

***Capital Adequacy***

The Bank Act requires a minimum paid-in capital of W100 billion in the case of national banks, such as Shinhan Bank and Chohung Bank, and W25 billion in the case of regional banks such as our Jeju Bank.

In addition to minimum capital requirements, all banks including foreign bank branches in Korea are required to maintain a prescribed solvency position. Until March 31, 1999, a bank's outstanding liabilities arising from guarantees and other contingent liabilities (except those specifically excluded under the Bank Act) were not permitted to exceed 20 times its equity capital amount. However, beginning on April 1, 1999, such limitation on guarantees and contingent liabilities was eliminated and, for regulatory purposes, guarantees provided by banks are counted as an extension of credit and will be regulated accordingly. See Financial Exposure to Any Individual Customer and Major Shareholders below. Also, in its allocation of the net profit earned in a fiscal term, a bank is required to credit at least 10% of such profit to a legal reserve each time it pays dividends on net profits earned until such time when the reserve equals the amount of its total paid-in capital.

Under the Bank Act, the capital of a bank is divided into two categories pursuant to Bank for International Settlements ( BIS ) standards, which were originally envisaged by the Basel Committee. Tier I capital (core capital) consists of stockholders' equity, capital surplus, retained earnings, equity representing new types of equity securities deemed to be functionally equivalent to capital which are designated by the Financial Supervisory Commission and undistributed stock dividends. Tier II capital (supplementary capital) consists of revaluation reserves, gain on valuation of investment in securities, allowance for bad debts set aside for loans classified as normal or precautionary ,

perpetual subordinated debt, cumulative preferred shares, redeemable preferred shares (with a right to redeem after the fifth anniversary of the date of issuance) and certain other subordinated debt.

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All banks must meet standards regarding minimum ratios of Tier I and Tier II capital (less any capital deductions) to risk-weighted assets, determined in accordance with the Financial Supervisory Commission requirements that have been formulated based on BIS Standards. These standards were adopted by the Monetary Board and the Office of Bank Supervision (the predecessor of the Financial Supervisory Service) and became effective in 1993. Under these regulations, all domestic banks and foreign bank branches were required to satisfy at least 8% as of the end of 1995, and thereafter, in accordance with the standards regarding minimum ratios of Tier I and Tier II capital (less any capital deductions) to risk-weighted assets.

The Financial Supervisory Commission amended the Regulation on the Supervision of the Banking Business in November 2002 to include a more conservative risk-weighting system on certain newly extended mortgage and home equity loans. As a result, for mortgage and home equity loans extended after November 13, 2002, Korean banks are required to calculate a risk-weight of 60% on certain mortgage and home equity loans if either of the following two conditions are satisfied, and a risk-weight of 70% if both of the following two conditions are satisfied: (1) if the mortgage and home equity loans are overdue for at least 30 consecutive days as of the date of calculating the bank's BIS capital adequacy ratio, or the total number of overdue days for the past one year from the date of calculating the bank's BIS capital adequacy ratio is at least 30 days; and (2) the borrower's debt ratio (i.e., total borrowed amount, including the borrowed amount provided by other financial institutions, of the borrower against the borrower's annual income) exceeds 250%. For all other home mortgages, a 50% risk-weight is applicable.

Under Korean GAAP, pursuant to the loan loss allowance guidelines established by the Financial Supervisory Commission, banks are generally required to maintain allowances for outstanding loans and other credits (including confirmed guarantees and acceptances and trust account loans) in an aggregate amount covering not less than 0.5% of normal credits (excluding confirmed guarantees and acceptances), 2% of precautionary credits (excluding confirmed guarantees and acceptances), 20% of substandard credits, 50% of doubtful credits and 100% of estimated loss credits.

In April 2002, the Financial Supervisory Service issued guidelines pursuant to which the minimum ratio of allowances for outstanding loans by banks to individuals and households was increased to 0.75% of normal credits, 5% of precautionary credits and 55% of doubtful credits, and the minimum ratio of allowances for their outstanding credit card receivables and credit card loans was increased to 1% of normal credits, 7% of precautionary credits and 60% of doubtful credits. In addition, in October 2002, the Financial Supervisory Service issued new guidelines pursuant to which the minimum ratio of allowance for their outstanding loans to individuals and households was increased to 8% of credits classified as precautionary and the minimum ratio of allowance for their outstanding credit card receivables and credit card loans was increased to 12% of credits classified as precautionary. These guidelines were reflected in the Regulation on Supervision of Banking Business prescribed by the Financial Service Commission in November 2002.

The BIS adopted changes to its capital adequacy standards to take into account market risk from equity securities, foreign exchange and derivative instruments held by banks. These changes have become applicable to most Korean banks commencing in 2002. Before 2002, all assets received risk weighting according to the risk weights applicable to the type of assets. For example, assets relating to government received a risk weight of 0%, assets relating to securities companies and banks received a 20% risk weight and assets relating to other companies received a risk weight of 100%. Starting from 2002, risk weights for assets that are subject to market risks, such as publicly-traded securities, foreign exchange and interest rate, are calculated in accordance with a formula based on market risk.

Basel II, the new convention entered into by the Basel committee in June 2004 for the purpose of improving risk management and increasing capital adequacy of banks is expected to be effective as of the end of 2007 in Korea. Pursuant to Basel II, operational risk, such as inadequate procedure, loss risk by employees, internal system, occurrence of unexpected event, as well as credit risk and market risk, should be taken into account in calculating the risk-weighted assets. However, as the current capital adequacy ratio of 8% for banks would be maintained, it would become more onerous for banks to satisfy the minimum capital requirements.

**Table of Contents*****Liquidity***

All banks are required to match the maturities of their assets and liabilities in accordance with the Bank Act in order to ensure adequate liquidity. Banks may not invest in excess of an amount exceeding 60% of their Tier I and Tier II capital (less any capital deductions) in stocks and other securities with a period remaining to maturity of over three years. However, this restriction does not apply to government bonds or to Monetary Stabilization Bonds issued by the Bank of Korea.

In 1999, the Financial Supervisory Commission adopted a new requirement to ascertain a bank's liquidity. Starting from January 1, 1999, the Financial Supervisory Commission requires each Korean bank to maintain a Won liquidity ratio (defined as Won assets due within three months, including marketable securities, divided by Won liabilities due within three months) of not less than 100% and to make quarterly reports to the Financial Supervisory Service. The Financial Supervisory Commission also requires each Korean bank to (1) maintain a foreign-currency liquidity ratio due within three months (defined as foreign-currency liquid assets due within three months divided by foreign-currency liabilities due within three months) of not less than 85%, (2) maintain a ratio of foreign-currency liquid assets due within seven days (defined as foreign-currency liquid assets due within seven days less foreign-currency liabilities due within seven days, divided by total foreign-currency assets) of not less than 0% and (3) maintain a ratio of foreign-currency liquid assets due within a month (defined as foreign-currency liquid assets due within a month less foreign currency liabilities due within a month, divided by total foreign-currency assets) of not less than negative 10%. The Financial Supervisory Commission also requires each Korean bank to submit monthly reports with respect to maintenance of these ratios.

The Monetary Policy Committee is authorized to fix and alter minimum reserve requirements that banks must maintain against their deposit liabilities. The current minimum reserve ratio is 5.0% of average balances for Won currency demand deposits outstanding, 1.0% of average balances for Won currency employee asset establishment savings deposits, employee long-term savings deposits, employee house purchase savings deposits, long-term house purchase savings deposits, household long-term savings deposits and employee preferential savings deposits outstanding and 2.0% of average balances for Won currency time and savings deposits, mutual installments, housing installments and certificates of deposit outstanding. For foreign currency deposit liabilities, a 2.0% minimum reserve ratio is applied to savings deposits outstanding and a 5% minimum reserve ratio is applied to demand deposits, while a 1.0% minimum reserve ratio is applied for offshore accounts, immigrant accounts and resident accounts opened by foreign exchange banks.

***Financial Exposure to Any Single Customer and Major Shareholders***

Under the Bank Act, the sum of material credit exposures by a bank, that is, the total sum of its credits to single individuals, legal entities or business groups that exceed 10% of the sum of Tier I and Tier II capital (less any capital deductions), must not exceed five times the sum of Tier I and Tier II capital (less any capital deductions), subject to certain exceptions. Beginning on January 1, 2000, subject to certain exceptions, no bank is permitted to extend credit (including loans, guarantees, purchases of securities (only in the nature of a credit) and such other transactions which directly or indirectly create credit risk) in excess of 20% of the sum of Tier I and Tier II capital (less any capital deductions) to a single individual or legal entity, and no bank may grant credit in excess of 25% of the sum of Tier I and Tier II capital (less any capital deductions) to a single group of companies that belong to the same conglomerate as defined in the Monopoly Regulations and Fair Trade Act.

Pursuant to an amendment to the Bank Act, which became effective on July 28, 2002, the restrictions on extending credits to a major shareholder have been amended. The definition of a major shareholder is as follows:

a shareholder holding (together with persons who have a special relationship with such shareholder as defined in the Presidential Decree of the Bank Act) in excess of 10% (or in the case of regional banks, 15%) in the aggregate of the bank's total issued and outstanding voting shares; or

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a shareholder holding (together with persons who have a special relationship with such shareholder as defined in the Presidential Decree of the Bank Act) more than 4% in the aggregate of the bank's (excluding regional banks) total issued and outstanding voting shares (excluding shares relating to the shareholding restrictions on non-financial group companies, which include:

any same shareholder group with the aggregate net assets of all non-financial companies belonging to such group of not less than 25% of the aggregate net assets of all members of such group;

any same shareholder group with aggregate assets of all non-financial companies belonging to such group of not less than W2 trillion; or

any mutual fund in which a same shareholder group identified in (1) or (2) above, owns more than 4% of the total shares issued and outstanding),

where such shareholder is the largest shareholder or is able to actually control the major business affairs of the bank, for example, through appointment and dismissal of the chief executive officer or of the majority of the executives.

According to such amendment, banks are prohibited from extending credits in the amount greater than the lesser of (1) 25% of the sum of such bank's Tier I and Tier II capital (less any capital deductions) or (2) the relevant major shareholder's shareholding ratio multiplied by the sum of the bank's Tier I and Tier II capital (less any capital deductions) to a major shareholder (together with persons who have special relationship with such major shareholder as defined in the Presidential Decree of the Bank Act). Also, no bank is allowed to grant credit to its major shareholders in the aggregate in excess of 25% of its Tier I and Tier II capital (less any capital deductions).

Recently, there has been a rapid increase in the use of credit support agreements between banks and special purpose companies that have been established for asset-backed securitization. When managing the credit risk of banks, among the methods for providing credit support by banks, a loan agreement, a purchase agreement for asset-backed commercial papers, purchase of subordinate beneficiary certificates, and assumption of liability by providing warranty against default under asset-backed securitization are deemed as creating financial exposure to banks.

***Interest Rates***

Korean banks remain dependent on the acceptance of deposits as their primary source of funds. There are no legal controls on interest rates on loans in Korea. Historically, interest rates on deposits and lending rates were regulated by the Monetary Board of the Bank of Korea. Under the government's Financial Reform Plan issued in May 1993, controls on deposit interest rates in Korea have been gradually reduced. In February 2004, the Korean government removed restrictions on all interest rates, except for the prohibition on interest payments on current account deposits. Deregulation of interest rates on deposits has increased competition for deposits based on interest rates offered and therefore may increase our banking operation's interest expense.

***Lending to Small- and Medium-Sized Enterprises***

In order to obtain funding from the Bank of Korea at concessionary rates for their small- and medium-sized enterprise loans, banks are required to extend to small- and medium-sized enterprises a certain minimum percentage of any monthly increase in their Won currency lending. Currently, this minimum percentage is 45% in the case of national banks and 60% in the case of regional banks. If a bank does not comply with the foregoing, all or a portion of the Bank of Korea funds provided to such bank in support of loans to small- and medium-sized enterprises may have to be prepaid to the Bank of Korea or the credit limit from the Bank of Korea for such bank may be decreased.

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***Disclosure of Management Performance***

For the purpose of enforcing mandatory disclosure of management performance so that the general public, especially depositors and stockholders, will be in a better position to monitor banks, the Financial Supervisory Commission requires commercial banks to disclose certain matters as follows:

loans bearing no profit made to a single business group in an amount exceeding 10% of the sum of the bank's Tier I and Tier II capital (less any capital deductions) as of the end of the previous month (where the loan exposure to such borrower is calculated as the sum of substandard credits, doubtful credits and estimated loss credits) except where the loan exposure to a single business group is not more than W4 billion;

occurrence of any financial event involving embezzlement, malfeasance or misappropriation of funds the amount of which exceeds 1% of the sum of the bank's Tier I and Tier II capital (less any capital deductions), unless the bank has lost or expects to lose not more than W1 billion as a result thereof, or the Governor of the Financial Supervisory Service has made a public announcement regarding such an occurrence;

any loss due to court judgments or similar decisions in civil proceedings in an amount exceeding 1% of the sum of the bank's Tier I and Tier II capital (less any capital deductions) as of the end of the previous month except where the loss is not more than W1 billion;

any event which can cause a material change in the financial status, such as a capital increase or reduction, issuance of convertible bonds, bonds with warrants, exchangeable bonds, or depositary receipts, cancellation of shares with profit, and split or consolidation of shares;

any event which can cause a material change in a bank's management, such as knowledge of imposition of a fine (such as negligence fine, surcharges or collection charges) in an amount exceeding 1% (or 0.5% in the case of a large company whose total assets as of the end of the most recent fiscal year is W2 trillion or more (hereinafter the Large Company)) or more of the bank's Tier I and Tier II capital, proposal or confirmation of a litigation that can have a material effect on the management of the bank such as litigation regarding appointment or dismissal of an officer, or a change in bank's largest shareholder, representative director, major shareholder, affiliate company, or a business objective;

any event which can cause a material change in the bank's property, such as a natural disaster which causes damages in an amount exceeding 5% (or 2.5% in the case of a Large Company) or more of its total assets as of the end of the most recent fiscal year, or giving or receiving of a gift in excess of 1% (or 0.5% in the case of a Large Company) or more of the bank's Tier I and Tier II capital;

any event which can cause a material change in the bank's credit or liability, such as dissolution of, or default of a bill or a check of, an unlisted company in which the bank invested 3% (or 1.5% in the case of a Large Company) or more of the bank's Tier I and Tier II capital, or commencement or termination of any court receivership of the bank or notification from the court thereof;

any event which can cause a material change in the bank's investment, such as acquisition or sale of fixed assets in an amount exceeding 5% (or 2.5% in the case of a Large Company) of its total assets, investment in other companies in an amount exceeding 5% (or 2.5% in the case of a Large Company) or more of the bank's Tier I and Tier II capital, becoming an oligopoly shareholder (meaning anyone owning 51% or more of the total issued and outstanding shares of a company, including the shares owned by specially related persons, as defined under the Framework Act on National Taxes) of a mutual savings bank or a change in such shareholder status;

any event which can cause a material change in the bank's profit or loss, such as an increase or decrease in profit or loss of 30% (or 15% in the case of a Large Company) or more when compared to the previous fiscal year, or

profit or loss from derivative transaction representing 5% (or 2.5% in the case of a Large Company) or more of the bank's Tier I and Tier II capital; and

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any other events which can have material effects on the bank's operation, such as payment of cash dividend, changes in accounting policy, or distribution of stock option.

***Restrictions on Lending***

According to the Bank Act, commercial banks are prohibited from making any of the following categories of loans:

loans made for the purpose of speculation in commodities or securities;

loans made directly or indirectly on the pledge of a bank's own shares, or on the pledge of shares in excess of 20% of the issued and outstanding shares of any other corporation (subject to certain exceptions with respect to financing for infrastructure projects);

loans made directly or indirectly to enable a natural or legal person to buy the bank's own shares;

loans made directly or indirectly to finance political campaigns and other related activities;

loans made to any of the bank's officers or employees other than de minimis loans of up to (1) ₩20 million in the case of a general loan, (2) ₩50 million in the case of a general loan plus a housing loan, or (3) ₩60 million in the aggregate for general loans, housing loans and loans to pay damages arising from wrongful acts of employees in financial transactions;

credit (including loans) provided on the pledge of shares of a subsidiary corporation of the bank or to enable a natural or legal person to buy shares of a subsidiary corporation of the bank; and

loans made to any officers or employees of a subsidiary corporation of the bank other than de minimis loans of up to ₩20 million in the case of a general loan or ₩50 million in the aggregate in the case of general and housing loans.

***Restrictions on Investments in Property***

A bank may possess real estate property only to the extent necessary for the conduct of its business; provided that the aggregate value of such real estate property must not exceed 60% of the sum of its Tier I and Tier II capital (less any capital deductions). Any property acquired by a bank (1) through the exercise of its rights as a secured party or (2) the acquisition of which is prohibited by the Bank Act must be disposed of within one year, subject to certain exceptions.

***Restrictions on Shareholdings in Other Companies***

Under the Bank Act, a bank may not own more than 15% of shares outstanding with voting rights of another company, except where, among other reasons:

the company issuing such shares is engaged in category of financial businesses set forth by the Financial Supervisory Commission (including private equity funds); or

the acquisition of shares by the bank is necessary for the corporate restructuring of the issuer and is approved by the Financial Supervisory Commission.

In the above cases, a bank must satisfy either of the following requirements:

the total investment in companies in which the bank owns more than 15% of the outstanding shares with voting rights does not exceed 15% of the sum of Tier I and Tier II capital (less any capital deductions); or

the acquisition satisfies the requirements determined by the Financial Supervisory Commission.

According to an amendment to the Bank Act, which became effective on July 28, 2002, a bank using its bank accounts and its trust accounts is not permitted to acquire the shares issued by the Major Shareholder of such bank in excess of an amount equal to 1% of the sum of Tier I and Tier II capital (less any capital deductions).



**Table of Contents*****Restrictions on Bank Ownership***

Under an amendment to the Bank Act, which became effective on July 28, 2002, subject to certain exceptions, a single shareholder and persons who stand in a special relationship with such shareholder (as described in the Presidential Decree to the Bank Act) may acquire beneficial ownership of up to 10% of a national bank's total issued and outstanding shares with voting rights and up to 15% of a regional bank's total issued and outstanding shares with voting rights. The government, the Korea Deposit Insurance Corporation and financial holding companies qualifying under the Financial Holding Companies Act are not subject to such ceilings. However, non-financial business group companies (i.e., (1) any same shareholder group with an aggregate net assets of all non-financial companies belonging to such group of not less than 25% of the aggregate net assets of all corporations that are members of such group, (2) any group with aggregate assets of all non-financial companies belonging to such group of not less than W2 trillion or (3) any mutual fund in which a same shareholder group, as described in items (1) and (2) above, owns more than 4% of the total shares issued and outstanding) may not acquire beneficial ownership of shares of a national bank in excess of 4% of such bank's outstanding voting shares, provided that such non-financial business group companies may acquire beneficial ownership of:

up to 10% of a national bank's outstanding voting shares with the approval of the Financial Supervisory Commission under the condition that such non-financial group companies will not exercise voting rights in respect of such shares in excess of the 4% limit; and

in the event that a foreigner, as defined in the Foreign Investment Promotion Act, owns in excess of 4% of a national bank's outstanding voting shares, up to 10% of such bank's outstanding voting shares without the approval of the Financial Supervisory Commission, and in excess of 10%, 25% or 33% of such bank's outstanding voting shares, with the approval of the Financial Supervisory Commission, up to the number of shares owned by such foreigner.

In addition, any person (whether a Korean national or a foreigner), with the exception of non-financial business group companies described above, may also acquire in excess of 10% of a national bank's total voting shares issued and outstanding, provided that an approval from the Financial Supervisory Commission is obtained in instances where the total holding exceeds 10% (or 15% in the case of regional banks), 25% or 33% of the bank's total voting shares issued and outstanding.

***Deposit Insurance System***

The Depositor Protection Act provides, through a deposit insurance system, insurance for certain deposits of banks in Korea. Under the Depositor Protection Act, all banks governed by the Bank Act, including Shinhan Bank, Chohung Bank and Jeju Bank, are required to pay to the Korea Deposit Insurance Corporation an insurance premium on a quarterly basis at such rate as determined by the Presidential Decree to the Depositor Protection Act, which shall not exceed 0.5% of the bank's insurable deposits in any given year. The current insurance premium is 0.025% of insurable deposits for each quarter. If the Korea Deposit Insurance Corporation pays the insured amount, it will acquire the claims of the depositors within the payment amount. Under current rules, the Korea Deposit Insurance Corporation insures only up to a total of W50 million for deposits and interest, regardless of when the deposits were made and the size of the deposits. However, the maximum limit of W50 million is not applicable to interest-free settlement accounts (for example, a checking account), for any insurable event occurring during the period from January 1, 2001 to December 31, 2003.

***Restrictions on Foreign Exchange Position***

Under the Korean Foreign Exchange Transaction Regulations, a bank's net overpurchased and oversold positions are each limited to 20% of the stockholders' equity as of the end of the prior month.

***Trust Business***

A bank that intends to enter into the trust business must obtain the approval of the Financial Supervisory Commission. Trust activities of banks are governed by the Trust Act and Trust Business Act. Banks engaged

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in the banking business and trust business are subject to certain legal and accounting procedures requirements, including the following:

under the Bank Act, assets accepted in trust by a bank in Korea must be segregated from its other assets in the accounts of such bank; accordingly, banks engaged in the banking and trust businesses must maintain two separate accounts, the banking accounts and the trust accounts, and two separate sets of records which provide details of their banking and trust businesses, respectively; and

assets comprising the trust accounts are not available to depositors or other general creditors of such bank in the event the trustee is liquidated or is wound up.

With respect to each unspecified money trust account for which a bank guarantees the principal amount and a minimum yield thereon, the bank must make a special reserve of 25% or more of fees and commissions from such trust account until the total reserve for such trust account equals 5% of the trust amount in such trust account. However, effective January 1, 1999, Korean banks have been prohibited from offering new guaranteed fixed rate trust account products whose principal and interest are guaranteed by the bank.

In addition, a trustee bank must deposit with a court an amount equal to 0.02% of its paid-in capital each year until the aggregate amount of such court deposits reaches 2.5% or more of its paid-in capital. In the event that a trustee bank breaches its duty of care as a trustee and causes loss to its customers, the court deposits will be available as compensation for such loss.

On January 17, 2005, in accordance with the amendment to the Trust Business Act, a comprehensive trust system was introduced to allow banks engaged in trust businesses to accept in trust two or more properties such as money, securities, or real estate with one trust deed. In addition, intellectual property rights can also be held as trust asset.

The Act on Business of Operating Indirect Investment and Asset, which applies to unspecified money trust account products under the Trust Business Act, securities investment trusts under the Securities Investment Trust Business Act, securities investment companies under the Securities Investment Company Act and variable insurance products under the Insurance Business Act, took effect on January 5, 2004. In accordance with the Act on Business of Operating Indirect Investment and Asset, we ceased offering unspecified money trust account products from our banking subsidiaries and instead began to offer products developed by our investment trust management business that fulfills the requirements as an asset management company.

In the event that a bank qualifies and operates as an asset management company, a trustee, a custodian or a general office administrator under the Act on Business of Operating Indirect Investment and Asset, it is required to establish relevant operation and management systems to prevent potential conflicts of interest among the banking business, the asset management business, the trustee or custodian business and general office administration. These measures include:

prohibitions against officers, directors and employees of one particular business operation from serving as an officer, director and employee in another business operation, except where an officer or a director (1) serving in two or more business operations with no significant conflict of interest in accordance with the Presidential Decree on the Act on Business of Operating Indirect Investment and Asset or (2) serving in a trustee business or a custodian business and simultaneously serving in a general office administrator business in accordance with the Act on Business of Operating Indirect Investment and Asset;

prohibitions against the joint use or sharing of computer equipment or office equipment; and

prohibitions against the sharing of information by and among officers, directors and employees engaged in the different business operations.

In addition, a bank is also required to establish an Indirect Investment Asset Management Committee consisting of three directors, two of whom must be outside directors of such bank.

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A bank which qualifies and operates as an asset management company may engage in the sale of beneficiary certificates of investment trusts which are managed by such bank. However, such bank is prohibited from engaging in the following activities:

acting as trustee of an investment trust managed by such bank;

purchasing with such bank's own funds beneficiary certificates of an investment trust managed by such bank;

using in its sales activities information relating to the trust property of an investment trust managed by such bank;

selling through a financial institution established under the Bank Act beneficiary certificates of an investment trust managed by such bank;

establishing a short-term financial indirect investment vehicle; and

establishing a mutual fund.

***Laws and Regulations Governing Other Business Activities***

To enter the foreign exchange business, a bank must register with the Minister of the Ministry of Finance and Economy. The foreign exchange business is governed by the Foreign Exchange Transaction Law. To enter the securities business, a bank must obtain the permission of the Financial Supervisory Commission. The securities business is governed by regulations under the Securities and Exchange Act. Pursuant to the above-mentioned laws, we are permitted to engage in the foreign exchange business, securities brokerage business and securities (including, governmental/public bonds) underwriting business.

**Principal Regulations Applicable to Credit Card Companies**

***General***

Any person, including a bank, wishing to engage in the credit card business must obtain a license from the Financial Supervisory Commission. In addition, in order to enter the credit card business, a bank must obtain a license from the Financial Supervisory Commission (hereinafter, a bank which obtains such license is defined as "licensed bank engaged in the credit card business"). The credit card business is regulated and governed by the Specialized Credit Financial Business Act. As a result of recent amendments to the Specialized Credit Financial Business Act and regulations thereunder, a company in the same conglomerate group (as defined in the Monopoly Regulation and Fair Trade Act) may engage in the credit card business even though another company in the same conglomerate group is already engaged in such business, which was previously not permitted.

The Specialized Credit Financial Business Act establishes guidelines on capital adequacy and provides for other regulations relating to the supervision of credit card companies. The Specialized Credit Financial Business Act delegates regulatory authority over credit card companies to the Financial Supervisory Commission and its executive body, the Financial Supervisory Service.

A licensed bank engaging in the credit card business is regulated by the Financial Supervisory Commission and the Financial Supervisory Service.

The Financial Supervisory Commission exerts direct control over credit card companies and licensed banks engaged in the credit card business by establishing guidelines or regulations on management of such companies. Moreover if the Financial Supervisory Commission deems the financial condition of a credit card company or a licensed bank engaged in the credit card business to be unsound or such companies fail to satisfy the guidelines or regulations, the Financial Supervisory Commission may take certain measures to improve the financial condition of such companies.

**Table of Contents*****Restrictions on Scope of Business***

Under the Specialized Credit Financial Business Act, a credit card company may conduct only the following types of business: (i) credit card business as licensed pursuant to the Specialized Credit Financial Business Act; (ii) the businesses ancillary to the credit card business, (*i.e.*, providing cash advance loans to existing credit card members, issuing and settling of debit cards and issuing, selling and settling of pre-paid cards); (iii) provision of unsecured or secured loans; (iv) provision of discount on notes; (v) purchase, management and collection of account receivables originated by companies in the course of providing goods and services; (vi) provision of payment guarantee; (vii) asset management business under the Asset Backed Securitization Act; (viii) credit investigation; and (ix) other incidental businesses related to the foregoing. As a result of the amendment to the Specialized Credit Financial Business Act on January 27, 2005, a credit card company's scope of business presently includes businesses that utilize existing manpower, assets or facilities in a credit card company, as designated by the Financial Supervisory Commission. Under the current regulation established by the Financial Supervisory Commission, a credit card company may engage in various types of business including, but not limited to, e-commerce, operation of insurance agency, delegation of card issuance and supply of payment settlement system.

Pursuant to the Presidential Decree of the Specialized Credit Financial Business Act, as of the end of each quarter, a credit card company's average balance of claim amounts during such quarter from engaging in the businesses set forth above in (iii) and (iv), excluding claim amounts arising from the provision of loans to companies, extension of new loans in connection with rescheduling of outstanding loans, the provision of mortgage loans and the provision of cash advances or any other loans to credit card members, may not exceed the average balance of claim amounts during such quarter from engaging in the businesses set forth above in (i) and (v); provided, however, that with respect to any excess amount existing as of April 21, 2004, credit card companies have until December 31, 2008 to eliminate such excess amount.

***Capital Adequacy***

The Specialized Credit Financial Business Act provides for a minimum paid-in capital amount of: (i) W20 billion in the case of a specialized credit financial business company which wishes to engage in no more than two kinds of core businesses (*i.e.* credit card, installment finance, leasing and new technology business) and (ii) W40 billion in the case of an specialized credit financial business company, which wishes to engage in three or more kinds of core businesses.

Under the Specialized Credit Financial Business Act and regulations thereof, a credit card company must maintain a capital adequacy ratio, defined as the ratio of adjusted equity capital to adjusted total asset, of 8% or more and a delinquent claim ratio, defined as the ratio of delinquent claims to total claims as set forth under the regulations relating to the Specialized Credit Financial Business Act, of less than 10% for claims outstanding for one month or longer.

Under the Specialized Credit Financial Business Act and regulations thereof, the minimum ratio of allowances for losses on loans, leased assets (except assets subject to an operating lease) and suspense receivables as of the date of accounting settlement (including semiannual preliminary accounts settlement) would be 0.5% of normal assets, 1% of precautionary assets and 20% of substandard assets, 75% of doubtful assets and 100% of estimated loss assets, and the minimum ratio of allowances for losses on credit card receivables and cash advances would be 1% of normal assets, 0.5% of the amount calculated by deducting sum of cash advances which were actually drawn by card members, from the maximum limit of sum of cash advances times 0.75 (excluding the maximum limit of sum of cash advances for card members who have not drawn cash advances for the latest 6 months), 12% of precautionary assets and 20% of substandard assets, 60% of doubtful assets and 100% of estimated loss assets.

***Liquidity***

Under the Specialized Credit Financial Business Act and regulations thereof, a credit card company must maintain a Won liquidity ratio (Won-denominated current assets/ Won-denominated current liabilities) of 100% or more. In addition, once a credit card company is registered as a foreign exchange business institution

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with the Minister of the Ministry of Finance and Economy, such credit card company is required to (1) maintain a foreign-currency liquidity ratio within three months (defined as foreign-currency liquid assets due within three months divided by foreign-currency liabilities due within three months) of not less than 80%, (2) maintain a ratio of foreign-currency liquid assets due within seven days (defined as foreign-currency liquid assets due within seven days less foreign-currency liabilities due within seven days, divided by total foreign-currency assets) of not less than 0% and (3) maintain a ratio of foreign-currency liquid assets due within a month (defined as foreign-currency liquid assets due within a month less foreign-currency liabilities due within a month, divided by total foreign-currency assets) of not less than negative 10%. The Financial Supervisory Commission requires a credit card company to submit quarterly reports with respect to maintenance of these ratios.

***Restrictions on Funding***

Under the Specialized Credit Financial Business Act, a credit card company may raise funds using only the following methods: (i) borrowing from financial institutions, (ii) issuing corporate debentures or notes, (iii) selling securities held by the credit card company, (iv) transferring claims held by the credit card company, (v) transferring claims held by the credit card company in connection with its businesses, or (vi) issuing securities backed by the claims held by the credit card company relating to its businesses.

Further, the credit card company may borrow funds offshore or issue foreign currency denominated securities once it is registered as a foreign exchange business institution with the Minister of the Ministry of Finance and Economy.

With respect to the issuance of debentures and notes, the credit card company may issue debentures up to an amount equal to ten times the company's total equity capital. In addition, a credit card company may issue, on a temporary basis, debentures exceeding the maximum limit for the purpose of redeeming the outstanding debentures, but must repay such outstanding debentures within one month after the date of issuance of new debentures.

***Restrictions on Loans to Affiliate Companies***

Under the Specialized Credit Financial Business Act and regulations thereof, a credit card company may not provide loans exceeding 100% of its equity capital, in the aggregate, to its specially related persons (as defined under the relevant laws) including, but not limited to, its affiliates.

***Restrictions on Assistance to Other Companies***

Under the Specialized Credit Financial Business Act, a credit card company shall not engage in any of the following acts in conjunction with other financial institutions or companies; (i) holding voting shares under cross shareholding or providing credit for the purpose of avoiding the restrictions on loans to affiliate companies; (ii) acquiring shares under cross shareholding for the purpose of avoiding the limitation on purchase of its treasury shares under the Korean Commercial Code or the Securities and Exchange Act; or (iii) other acts which are likely to have a material adverse effect on the interests of transaction parties as stipulated by the Presidential Decree to the Specialized Credit Financial Business Act, which are not yet provided.

A credit card company shall not extend credit for enabling another person to purchase the shares of such credit card company or to arrange financing for the purpose of avoiding the restrictions on loans to affiliate companies.

***Restrictions on Investment in Real Estate***

Under the Specialized Credit Financial Business Act and the regulations thereof, a credit card company is allowed to possess real estate only to the extent that such business conduct is designated by such laws and regulations, with certain exceptions such as for the purposes of factoring or leasing or as a result of enforcing its security rights, provided that the Financial Supervisory Commission may limit the maximum amount a

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credit card company may invest in real estate investments for business purposes up to a percentage equal to or in excess of 100% of its equity capital.

***Restrictions on Shareholding in Other Companies***

Under the Specialized Credit Financial Business Act and the Law on Improvement of Structure of Financial Industry, a credit card company and its affiliate financial institutions (together a group) are required to obtain prior approval of the Financial Supervisory Commission if such credit card company, together with its affiliate financial institutions, (i) owns 20% or more of outstanding voting shares of a target company or (ii) owns 5% or more of outstanding voting shares of a target company, and shall be deemed to have control of the target company, including being the largest shareholder of such target company or otherwise.

The indirect subsidiary of the financial holding company is prohibited from controlling any other company.

***Disclosure and Reports***

Pursuant to the Specialized Credit Financial Business Act and the regulations thereof, the ordinary disclosure requirement for a credit card company is to disclose any material matters relating to management performance, profit and loss, corporate governance, manpower or risk management within three months from the end of each fiscal year and within two months from the end of the first half of the fiscal year. Also, a credit card company is required to disclose on an on-going basis certain matters such as the occurrence of non-performing loans, a financial accident or the occurrence of losses exceeding certain amounts. Prior to December 29 2005, a credit card company or a licensed bank engaging in the credit card business was required to submit its business reports and reports on actual results of management to the Financial Supervisory Commission within one month from the end of each quarter. However, after the amendment to the regulations issued by the Financial Supervisory Commission on December 29, 2005, a credit card company or a licensed bank engaging in the credit card business must submit such report as required by the Governor of Financial Supervisory Service, with certain important matters being reported as frequently as each month. In addition, all companies engaged in the specialized credit financial business under the Specialized Credit Financial Business Act, including, without limitation, credit card companies, must file a report with the Financial Supervisory Service regarding the result of settlement of accounts within one month after the end of its fiscal year. Also, these companies are required to conduct a provisional settlement of accounts for each quarter and file a report with the Financial Supervisory Service within one month after the end of such quarter.

***Risk of Loss due to Lost, Stolen, Forged or Altered Credit Cards***

Under the Specialized Credit Financial Business Act, upon notice from the holder of a credit card or debit card of its loss or theft, the credit card company or a licensed bank engaging in the credit card business, as the case may be, is liable for any loss arising from the unauthorized use of credit cards or debit cards thereafter as well as any loss from unauthorized transactions made within 60 days prior to such notice. However, a credit card company or a licensed bank engaged in the credit card business, as the case may be, may transfer to the cardholder all or part of the risks of loss associated with unauthorized transactions made within 60 days prior to such notice, in accordance with the standard terms and conditions agreed between the credit card company or a licensed bank engaged in the credit card business, as the case may be, and the cardholder, provided that the loss or theft must be due to the cardholder's willful misconduct or negligence. Disclosure of a cardholder's password under duress or threat to the cardholder's or his/her family's life or health will not be deemed as the cardholder's willful misconduct or negligence.

Moreover, a credit card company or a licensed bank engaging in the credit card business, as the case may be, is also responsible for any losses resulting from the use of forged or altered credit cards, debit cards and pre-paid cards. However, a credit card company or a licensed bank engaging in the credit card business, as the case may be, may transfer all or part of this risk of loss to holders of credit cards in the event of willful misconduct or gross negligence by holders of such cards if the terms and conditions of the written agreement

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entered between the credit card company or a licensed bank engaging in the credit card business, as the case may be, and holders of such cards specifically provide for such transfer. For these purposes, disclosure of a customer's password that is made intentionally or through gross negligence, or the transfer of or giving as collateral of the credit card or debit card, is considered willful misconduct or gross negligence.

In addition, the Specialized Credit Financial Business Act prohibits a credit card company from transferring to merchants the risk of loss arising from lost, stolen, forged or altered credit cards, debit cards or pre-paid cards; provided, however, that a credit card company may enter into an agreement with a merchant under which the merchant agrees to be responsible for such loss if caused by the merchant's gross negligence or willful misconduct.

Each credit card company or a licensed bank engaged in the credit card business must institute appropriate measures such as establishing reserves, purchasing insurance or joining a cooperative association in order to fulfill its obligations when the risk of loss arises from unauthorized use due to lost, stolen, forged or altered credit cards, debit cards or pre-paid cards.

Pursuant to the Specialized Credit Financial Business Act, the Financial Supervisory Commission may either impose the limit or take other necessary measures against the credit card company or a licensed bank engaged in the credit card business including, without limitation, with respect to the following:

maximum limits for cash advances on credit cards;

use restrictions on debit cards with respect to per day or per transaction usage; or

aggregate issuance limits and maximum limits on the amount per card on pre-paid cards.

***Lending Ratio in Ancillary Business***

Pursuant to the Presidential Decree to the Specialized Credit Financial Business Act, as amended in December 2003, a credit card company or a licensed bank engaging in the credit card business, as the case may be, must maintain an aggregate quarterly average outstanding lending balance to credit card holders (including cash advances and credit card loans, but excluding restructured loans and revolving cash advances) no greater than its aggregate quarterly average outstanding credit card balance arising from the purchase of goods and services (excluding receivables arising from the purchase of goods and services by specially-related persons using exclusive use card for business purposes (as defined in the Tax Incentives Limitation Act)) plus its aggregate quarterly amount of payments made by members using their debit cards; provided that, with respect to any excess amount existing as of December 31, 2003, the credit card companies have a grace period until December 31, 2007 to eliminate such excess amount.

***Issuance of New Cards and Solicitation of New Card Holders***

The Presidential Decree to the Specialized Credit Financial Business Act establishes the conditions under which a credit card company or a licensed bank engaging in the credit card business may issue new cards and solicit new members. Specifically, new credit cards may be issued only to the following persons: (i) persons who are at the age of 18 years or more at the time of applying for issuance of a credit card; (ii) persons whose capability to pay bills as they come due, as determined according to standards established by the credit card company or a licensed bank engaging in the credit card business, is verified; (iii) in the case of minors, persons who submit a guardian's consent along with documents evidencing income, such as an employment certificate or a tax certificate; and (iv) person whose identity has been verified.

In addition, a credit card company or a licensed bank engaging in the credit card business, as the case may be, may not engage in the following methods of soliciting credit card members: (i) providing economic benefits or conditioning such benefits in excess of 10% of the annual credit card fee (in the case of no-annual fee credit cards, the average annual fees will be W10,000) in connection with issuance of credit cards; (ii) street solicitation of card members on roads and private roads as prescribed under the Road Act and Private Road Act, public place and along corridors used by the general public; and (iii) solicitation through

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visits, except those visits made upon prior consent and visits to a business area; and (iv) solicitation through pyramid sales methods.

Recent changes in the law have resulted in the application of more stringent standards in the issuance of credit cards and solicitation of credit card applicants, such as requiring a credit card company or a licensed bank engaged in the credit card business to check whether the credit card applicant has any delinquent debt owing to any other credit card company or other financial institutions which the applicant is unable to repay, and also requiring, in principle, with respect to solicitations made through the Internet, the certified electronic signature of the applicant. Moreover, persons who intend to engage in solicitation of credit card applicants must register with the Financial Supervisory Commission, unless the solicitation is made by officers or employees of a credit card company or a company in business alliance with such credit card company.

### ***Compliance Rules on Collection of Receivable Claims***

Pursuant to the Specialized Credit Financial Business Act and its regulations, a credit card company or a licensed bank engaging in the credit card business may not:

exerting violence or threat of violence;

informing a Related Party (a guarantor of the debtor, blood relative or fiancée of the debtor, a person living in the same household as the debtor or a person working in the same workplace as the debtor) of the debtor's liability without just cause;

providing false information relating to the debtor's obligation to the debtor or his/her Related Party;

threatening to sue or suing the debtor for fraud despite lack of affirmative evidence to establish that the debtor has submitted forged or false documentation with respect to his/her capacity to make payment;

visiting or telephoning the debtor during late hours between 9:00 p.m. – 8:00 a.m.; and

utilizing other uncustomary methods to collect the receivables thereby invading the privacy or the peacefulness in the workplace of the debtor or his/her Related Party.

## **Principal Regulations Applicable to Securities Companies**

### ***General***

The securities business is regulated and governed by the Securities and Exchange Act. Securities companies are under the regulation and supervision of the Financial Supervisory Commission, the Financial Supervisory Service and the Securities and Futures Commission.

Under the Securities and Exchange Act, permission to commence a brokerage business, a trading business or an underwriting business must be obtained from the Financial Supervisory Commission. A securities company may also engage in certain businesses ancillary to the primary business without obtaining any separate license and certain other additional businesses by obtaining separate licenses from the Financial Supervisory Commission. Permission to merge with any other entity or to transfer all or substantially all of a business must also be obtained from the Financial Supervisory Commission.

If the Korean government deems a securities company's financial condition to be unsound or if a securities company fails to meet the applicable Net Operating Equity Ratio (as defined below), the government may order any of the following:

capital increase or reduction;

a stock cancellation or consolidation;

a transfer of business;

closing of branch offices;

acquisition of such company by a third party;

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- a merger with any other entity;
- becoming a subsidiary (under the Financial Holding Companies Act) of a financial holding company;
- a suspension or assignment of a part or all of business operation;
- an assignment of contractual rights and obligations relating to financial transactions; or
- suspension of officer's performance and appointment of a receiver.

***Scope of Business***

The 2005 amendment to the Securities and Exchange Act and the Presidential Decree and regulations thereunder resulted in enlarging the scope of business of securities companies by allowing them to engage in the following businesses:

brokerage, trading, or underwriting business of equity of undisclosed association (as defined under the Korean Commercial Code) or limited partnership and certain derivative securities linked with prices, interest rates, indices and indicators relating to securities (under the Securities and Exchange Act and the Presidential Decree), foreign securities of similar character, currencies, commodities (under the Futures and Exchange Act), or linked with credit risks;

trust business under the Trust Business Act or over-the-counter derivative trading linked to credit risks, price of securities, interest rate or indices based on the foregoing, or currency rate, price of goods or indices based on the foregoing, if the company obtains necessary license from the Financial Supervisory Commission. A securities company intending to engage in the business of over-the-counter derivative trading will be subject to the limit of 30% of its equity capital as the total amount of risks from over-the-counter derivative trading, and further subject to the limit of 5% of equity capital for the amount of risks from a credit-linked derivative transaction with a person or a company (including specially-related person of such person or company), with the 300% of minimum equity capital regulation rate and with the W100 billion of minimum equity capital requirement (provided that the W100 billion requirement will be applicable only until May 29, 2007) in order to conduct over-the-counter derivative trading Pursuant to the amendment of the Trust Business Act effective as of July 29, 2005, a securities company is exempted from regulations under the Trust Business Act regarding the use of the word "trust" in the corporate name, the qualifications of officers, restrictions on the management of the trustee's own fund, and internal control standards; and

ancillary businesses such as (1) real estate brokerage or consulting business on real estates owned by clients who are being provided with services relating to brokerage on mergers and acquisitions or business management and financing consulting, (2) selling books, reports or electronic documents containing securities-related information and (3) arranging loans to customers of securities companies based on business alliances established with such securities companies.

***Regulations on Financial Soundness – Capital Adequacy***

The Securities and Exchange Act and the Presidential Decree thereunder provide for a minimum paid-in capital of W50 billion in the case of a securities company engaged in the brokerage, trading and underwriting businesses.

The financial soundness of a securities company is to be assessed under the Securities and Exchange Act and the regulations of the Financial Supervisory Commission in accordance with the net operating equity ratio of the company, which is to be calculated as follows and to be expressed as a percentage.

Net operating equity ratio = Net operating equity/ Total risk × 100

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The terms Net Operating Equity and Total Risk for the purpose of the above-stated formula are defined and elaborated in the regulations of the Financial Supervisory Commission. Generally, the net operating equity and the Total risk is to be calculated according to the following formula:

Net operating equity = Net assets (total assets - total liabilities) - the total of items that may be deducted + the total of items that may be added

Total risk = market risk + counterparty risk + basic risk + credit concentration risk - risk offsetting factor

The regulations of the Financial Supervisory Commission requires, among other things, securities companies to maintain the net operating equity ratio at a level equal to or higher than 150%, at the end of the each quarter of the fiscal year.

In addition, all Korean companies, including securities companies, are required to set aside, as a legal reserve, 10% of the cash portion of the annual dividend or interim dividend in each fiscal year until the reserve reaches 50% of its stated capital.

Under the Securities and Exchange Act and regulations thereunder, the minimum ratio of allowances for losses on loans and suspense receivables specified under such regulations is 0.5% of normal assets, 2% of precautionary assets, 20% of substandard assets, 75% of doubtful assets and 100% of estimated loss assets.

The regulations of the Financial Supervisory Commission as amended in 2004 imposed stricter standards on the capital adequacy ratio by allowing term subordinated debt with a maturity of five years or more, to be recognized as an additional item to be added to the net operating equity and by also allowing only up to an amount equal to 50% of the net assets as an item to be added. By comparison, the amendment of the regulations of the Financial Supervisory Commission on June 29, 2005, in certain cases, allows treating a subordinated debt with a maturity of two years or more as an item to be added to the net operating equity under the Act on the Structural Improvement of the Financial Industry.

***Other Provisions on Financial Soundness***

The Securities and Exchange Act, the Presidential Decree of the Securities and Exchange Act and the regulations of the Financial Supervisory Commission also include certain provisions which are designed to regulate certain types of activities relating to the management of the assets of a securities company with certain exceptions. Such provisions include:

restrictions on the holdings by a securities company of securities issued by another company which is the largest shareholder or the major shareholder (each as defined under the Securities and Exchange Act) of such securities company;

restrictions on providing money or credit to the largest shareholder (including specially-related persons of such shareholder), major shareholders, officers and specially-related persons of the securities company; and

special provisions concerning the payment guarantee by a securities company. For instance, a securities company is not allowed to provide payment guarantees for third parties other than its overseas subsidiaries.

A securities company may invest in shares, bonds (whether listed or unlisted) and stock price index futures and options or other derivative transactions. However, a securities company may not enter into cross-border financial futures, swaps, options or other derivative transactions without obtaining prior approval from the Bank of Korea, except in the case when such securities company, which has been registered as a foreign exchange business institution with the Minister of the Ministry of Finance and Economy, is confirmed by the Financial Supervisory Commission to satisfy certain conditions set forth in the Foreign Exchange Transaction Regulations and the counterparty (other than an individual) is an institutional investor, a company listed on the Stock Market Division or the KOSDAQ Market Division of the Korea Exchange or not a resident of Korea. Furthermore, a securities company that it registered as a foreign exchange business institution and

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licensed to engage in over-the-counter derivative transactions may enter into Won currency derivative transactions (except for credit-linked derivative transactions) without obtaining prior approval from the Bank of Korea. As a result of the 2005 amendment to the Securities and Exchange Act and the Presidential Decree and regulations thereunder, a securities company licensed to engage in over-the-counter derivative trading may enter into credit-linked derivative transactions. However, a securities company must obtain prior approval from the Bank of Korea when entering into a cross-border credit-linked derivative transaction even if the securities company is registered as a foreign exchange business institution.

In November 2005, the Ministry of Finance and Economy announced its plan to amend some provisions of the Securities and Exchange Act. The purpose of this amendment is to prevent capital of the industrial business from dominating the financial markets. For this purpose, certain regulations is expected to be adopted, including, among others, (a) defining the largest shareholder and major shareholders as large shareholders, and defining major shareholders as the shareholders that have shares (including the shares owned by their specially-related persons) that are more than 10% of all the outstanding shares, (b) requiring a securities company to obtain approval from its board of directors for extension of credit to its large shareholders and to report to the Financial Supervisory Committee following such extension and (c) prohibiting large shareholders from exerting improper influence on the securities company.

***Business Conduct Rules***

Effective May 2001, the Financial Supervisory Commission adopted the business conduct rules applicable to securities companies. The business conduct rules impose greater responsibilities on securities companies, strictly banning unfair practices such as front running or scalping and ensuring suitability of investment solicitation by securities companies.

***Disclosure and Reports***

Pursuant to the Securities and Exchange Act, a securities company has a continuing obligation to disclose certain material matters including (i) financial condition and profit and loss of the securities company, (ii) any sanctions levied on the securities company under the Securities and Exchange Act or any corrective measures or sanctions under the Law on Improvement of Structure of Financial Industry or (iii) occurrence of any matters which may have a material adverse effect on the operation or management of the securities company.

A securities company is also required to submit reports on actual results of operation to the Financial Supervisory Commission within 45 days from the end of each quarter. In addition, a securities company is required to submit financial documents, including financial statements and audit reports to the Financial Supervisory Commission, within three months from the end of the fiscal year.

A securities company engaging in over-the-counter derivative trading is required to submit a detailed report of such trading during each month on every 10<sup>th</sup> day of the following month.

***Customer Protection***

Under Korean law, the relationship between a customer and a securities company in connection with a securities sell or buy order is deemed to be consignment and the securities acquired by a consignment agent (i.e., the securities company) through such sell or buy order are regarded as belonging to the customer in so far as the customer and the consignment agent's creditors are concerned. Therefore, in the event of a bankruptcy or reorganization procedure involving a securities company, the customer of the securities company is entitled to the proceeds of the securities sold by the securities company.

As the cash deposited with a securities company is regarded as belonging to the securities company, which is liable to return the same at the request of its customer, the customer cannot take back deposited cash from the securities company if a bankruptcy or reorganization procedure is instituted against the securities company and, therefore, can suffer from loss or damage as a result. However, the Depositor Protection Act provides that Korea Deposit Insurance Corporation will, upon the request of the investors, pay each investors

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up to W50 million per financial institution in case of the securities company's bankruptcy, liquidation, cancellation of securities business license or other insolvency events. Securities companies are required to pay the premiums related to this insurance. Pursuant to the Securities and Exchange Act, securities companies are required to deposit the cash received from its customers with the Korea Securities Finance Corporation, a special entity established pursuant to the Securities and Exchange Act. Set-off or attachment of cash deposits by securities companies with the Korea Securities Finance Corporation is prohibited. In addition, in the event of bankruptcy or dissolution of the securities company, the cash so deposited shall be withdrawn and paid to the customer prior to payment to other creditors of the securities company.

### **Principal Regulations Applicable to Insurance Companies**

#### ***General***

Insurance companies are regulated and governed by the Insurance Business Act of 1962, as amended (the Insurance Business Act). In addition, Korean insurance companies are under the regulation and supervision of the Financial Supervisory Commission and its governing entity, the Financial Supervisory Service.

Under the Insurance Business Act, permission to commence an insurance business must be obtained from the Financial Supervisory Commission based on the type of insurance businesses, which are classified as life insurance business, non-life insurance business and third insurance business. Life insurance business means an insurance business which deals with life insurance policies or pension insurance policies (including retirement insurance policies). Non-life insurance business means an insurance business which deals with fire insurance policies, marine insurance policies, car insurance policies, guaranty insurance policies, reinsurance policies, liability insurance policies or other insurance policies prescribed under the Presidential Decree of the Insurance Business Act. Third party insurance business means an insurance business which deals with injury insurance policies, sickness insurance policies or nursing care insurance policies. According to the Insurance Business Act, insurance companies are not allowed to engage in both a life insurance business and a non-life insurance business, with certain exceptions.

If the Korean government deems an insurance company's financial condition to be unsound or if an insurance company fails to properly manage the business as set forth under relevant Korean law, the government may order:

capital increase or reduction;

stock cancellation or consolidation;

transfer of a part or all of business;

sale of assets;

closing of branch offices;

merger with any other entity;

becoming a subsidiary (under the Financial Holding Companies Act) of a financial holding company;

acquisition of an insurance company by a third party;

suspension or assignment of a part or all of business operation;

assignment of contractual rights and obligations relating to financial transactions; or

suspension of officer's performance and appointment of a receiver.

#### ***Capital Adequacy***

The Insurance Business Act provides for a minimum paid-in capital of W300 billion for an insurance company, provided that the insurance company which intends to engage in only certain types of insurance policies may have a lower paid-in capital pursuant to the Presidential Decree of the Insurance Business Act.

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In addition to the minimum capital requirement, an insurance company is required to maintain a Solvency Ratio of 100% or more. Solvency Ratio is the ratio of Solvency Margin to Standard Amount of Solvency Margin. Solvency Margin is the aggregate amount of paid-in capital, reserve for dividends to policyholders, allowance for bad debt and subordinated debt amount, less unused expenses for new contracts, goodwill and others similar thereto as determined by the Financial Supervisory Commission. Standard Amount of Solvency margin is defined under the regulation of the Financial Supervisory Commission and is calculated as follows:

1. (Net premium type policy reserve - Non-amortized acquisition cost) × (Corresponding ratio of risk factor for policy reserve) (4%); and
2. (Net insurance benefits) × (Corresponding ratio of insurance risk factor).

Under the Insurance Business Act, the Presidential Decree and other regulations thereunder, for each accounting period, insurance companies are required to appropriate policy reserve that is earmarked for future payments of insurance money, refund and dividends to policyholders (hereinafter collectively referred to as Insurance Money ) for each insurance contract. However, if an insurance company has reinsured a portion of its insurance contracts with a creditworthy reinsurance company in order to lower its overall risk, the insurance company is not required to appropriate policy reserve for the reinsured contracts but instead the reinsurance company is required to appropriate such policy reserve for the reinsured contracts. Further, insurance companies are required to submit written calculation methods for insurance premiums and policy reserves by insurance types when applying for the insurance business license. If an insurance company develops a new insurance product or amends the policy reserve calculation method, it is required to report such matters to the Financial Supervisory Commission and obtain approval thereof.

The policy reserve amount consists of the following; (i) premium reserves and prepaid insurance premiums which are calculated under the methods determined by the written calculation methods for insurance premiums and policy reserves by insurance types or by lapses of insurance period, with regard to the contracts for which the causes for payment of the Insurance Money have yet to occur as of the end of each accounting period, (ii) amounts for which a lawsuit is pending on the Insurance Money or amounts for which a payment has been fixed with regard to the contracts for which the causes for payment of Insurance Money have occurred as of the end of each accounting period, and amounts which have not been paid yet due to an unsettled amount for paying the Insurance Money, even if the causes for payment of the Insurance Money have already occurred; and (iii) amounts reserved by an insurance company for allocation to policyholders.

Pursuant to the regulations established by the Financial Supervisory Commission, insurance companies are required to maintain allowances for outstanding loans, accounts receivables and other credits (including accrued income, payment on account, and bills receivables or dishonored) in an aggregate amount covering not less than 0.5% of normal credits (excluding confirmed guarantees and acceptances), 2% of precautionary credits, 20% of substandard credits, 50% of doubtful credits and 100% of estimated loss credits, provided that the minimum ratio of allowances for certain type of outstanding loans by insurance companies to individuals and households (including, consumer loans, housing loans, and other forms of consumer loans extended to individuals not registered for business), is increased to 0.75% of normal credits and 5% of precautionary credits.

**Liquidity**

According to the Insurance Business Act and regulations thereunder, if an insurance company is registered as a foreign exchange business institution with the Ministry of Finance and Economy, such insurance company is required to (1) maintain a ratio of foreign-currency liquid assets due within three months (defined as foreign-currency liquid assets due within three months divided by foreign-currency liabilities due within three months) of not less than 80%, (2) maintain a ratio of foreign-currency liquid assets due within seven days (defined as foreign-currency liquid assets due within seven days less foreign-currency liabilities due within seven days, divided by total foreign-currency assets) of not less than 0% and (3) maintain a ratio of foreign-currency liquid assets due within a month (defined as foreign-currency liquid assets due within a month less foreign-currency liabilities due within a month, divided by total foreign-currency assets)



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of not less than negative 10%, if the ratio of foreign-currency liabilities to the Total Assets (defined as the assets on the balance sheet less unused expenses for new contracts, goodwill and assets in special accounts) is 1% or more.

***Variable Insurance***

Prior to the enactment of the Act on Business of Operating Indirect Investment and Asset on January 4, 2004, insurance companies were engaged in the variable insurance business by establishing special accounts pursuant to the Insurance Business Act. Although the assets held in each special account was separated from other assets held in other special account and other assets of the company and was required to have separate accounting, prior to the enactment of the Act on Business of Operating Indirect Investment and Asset, it was difficult to protect against the bankruptcy risk of an insurance company.

After the enactment of the Act on Business of Operating Indirect Investment and Asset, variable insurance is regulated pursuant to the Insurance Business Act and the Act on Business of Operating Indirect Investment and Asset. After the enactment of the Act on Business of Operating Indirect Investment and Asset, in order for an insurance company to sell variable insurance to a policyholder and operate such variable insurance, the insurance company must obtain an approval as an asset management company and register as a selling company with the Financial Supervisory Commission. In this case, according to the Act on Business of Operating Indirect Investment and Asset, an insurance company will be regulated as an investment trust and assets acquired in connection with variable insurance must be held by a trust company that is registered with the Financial Supervisory Commission pursuant to the Act on Business of Operating Indirect Investment and Asset. However, for those special accounts that were established prior to the enactment of the Act on Business of Operating Indirect Investment and Asset, the Insurance Business Act will apply, provided however, upon six months after its enactment, further enrollment into such special accounts is prohibited, with certain exceptions.

According to the Act on Business of Operating Indirect Investment and Asset, insurance companies may operate variable insurance through (i) mandating all of the management and the management instruction business to another asset management company, (ii) operating by way of discretionary investment all of the assets constituting the investment advisory assets out of the investment trust assets, or (iii) operating all of the investment trust assets into other indirect investment securities, thereby allowing all of the particular variable insurance assets to be outsourced. However, according to the Act on Business of Operating Indirect Investment and Asset and the Presidential Decree thereunder, indirect investment vehicles may purchase only up to 20% of the indirect investment securities issued by another single indirect investment vehicle, which is inconsistent with the above regulation. The Ministry of Finance and Economy recently announced that if variable insurance assets are invested in other funds, the proposed amendment would allow such investment up to 100%.

Insurance companies may not transfer assets held in a special account into a general account or a different special account, provided that, for efficient operation of a special account, insurance companies may transfer the initial investment funds held in a general account into a special account. The assets which may be transferred from a general account to a special account must be the lower of 1% of the total asset value in the account or W10 billion. If the value of the assets held in a special account is more than 200% of the initial investment fund at the end of any quarter, the initial investment fund must be transferred back to the general account within three months from the end of such quarter, the value of the assets to be transferred is estimated by the value of the assets in the special account at the time of such transfer.

***Solicitation of Insurance Policy & Bancassurance Agents***

Under the Insurance Business Act, the following persons are permitted to solicit subscription of insurance: (i) financial planners registered with the Financial Supervisory Service, (ii) insurance agents registered with the Financial Supervisory Service, (iii) insurance brokers registered with the Financial Supervisory Service, (iv) officers and employees of insurance companies and (v) officers and employees of the insurance agents and brokers described above who are notified to solicit insurance subscription pursuant to

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the Insurance Business Act. In order for these persons to solicit subscription of insurance contracts that are required to be managed under a special account (including, without limitation, variable insurance contracts), they must pass the examination or complete additional training sessions administered or offered by the Financial Supervisory Commission.

The amendment to the Insurance Business Act which became effective on August 30, 2003 permits banks, securities companies, credit card companies and other financial institutions to register as insurance agents or insurance brokers and engage in the insurance business (the Bancassurance Agents). At the time of the amendments of the Insurance Business Act and the related regulations, the range of insurance products to be sold by the Bancassurance Agents was expected to expand in three stages, the first of which occurred at the time of the amendments, the second of which was to occur in April 2005 and the third of which was to occur in April 2007 when all types of life and non-life insurance products were to be sold by the Bancassurance Agents. However, when the amendment to the Enforcement Decree of the Insurance Business Act, which took effect as of April 2005, delayed and limited the scope of such deregulations, it became unclear whether or when the Bancassurance Agents would be allowed to solicit business insurance subscription.

No Bancassurance Agents with the total assets in excess of W2 trillion as of the end of the most recent operating year is permitted to solicit subscription for insurance products of any single life insurance company or non-life insurance company in excess of 25% of the total amount of the subscriptions for all life insurance products or all non-life insurance products, as the case may be, solicited by such Bancassurance Agents during any operating year. In addition, the aggregate amount of subscriptions solicited by any Bancassurance Agents for insurance products of any life insurance company or non-life insurance company and those of any other companies that have special relationships with such insurance company as prescribed under the Enforcement Decree of the Insurance Business Act is not allowed to exceed 33% of the total amount of the subscriptions for all life insurance products or all non-life insurance products, as the case may be, solicited by such Bancassurance Agents during any operating year. The Bancassurance Agents is only allowed to solicit subscription for insurance products at its office with no more than two persons per office who are officers or employees registered with the Financial Supervisory Service through face-to-face meetings with potential policyholders at designated places or is allowed to solicit subscription from the general public by introducing its products on its websites. The Bancassurance Agents is not allowed to cause officers or employees of insurance companies, financial planners, or insurance brokers or agents dispatched to such Bancassurance Agents to solicit subscription for insurance products, nor is it allowed to exert undue influence on the operation of insurance companies.

***Financial Exposure to Any Single Borrower and Major Shareholders***

Under the Insurance Business Act, an insurance company is not allowed to extend credit or any equivalent thereof to a single individual or legal entity, similarly situated borrowers (as defined below), its subsidiary or major shareholder, in each case in excess of the following amount:

with respect to the sum of credit to a single individual or legal entity, 3% of its Total Asset (as defined above);

with respect to the total amount of investment in the debentures or shares issued by a single legal entity, 7% of its Total Asset;

with respect to the sum of (i) credit to a single individual or legal entity and any other persons who share the credit risk of such individual or legal entity (the similarly situated borrowers) and (ii) the amount of investment in the debentures or shares issued by such similarly situated borrowers, 12% of its Total Asset;

with respect to the sum of the large credit which is credit to a single individual or legal entity, similarly situated borrowers or major shareholders that exceeds 1% of its Total Asset, 20% of its Total Asset;

with respect to the sum of credit to a single subsidiary, 10% of the Equity Capital (defined as the sum of paid-in capital, capital surplus, earned surplus and others equivalent thereto (excluding any recapitalization) that are

obtained by subtracting the aggregate amount of items such as goodwill and

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others equivalent thereto prescribed by the Presidential Decree from the aggregate amount of the items prescribed by the Presidential Decree) of such insurance company;

with respect to the sum of credit to major shareholders or subsidiaries designated by the Presidential Decree, the lesser of (i) 40% of its Equity Capital and (ii) 2% of its Total Asset; and

with respect to the total amount of investment in the debentures or shares issued by major shareholders or subsidiaries designated by the Presidential Decree, the lesser of (i) 60% of its Equity Capital and (ii) 3% of its Total Asset.

According to the Insurance Business Act and the Presidential Decree thereunder, an insurance company which intends to extend credit to its major shareholder in an amount equal to or in excess of the lesser of 1% of its Equity Capital and W1 billion or to buy debentures or shares issued by such person for the purchase price equal to or in excess of such amount must obtain the unanimous approval of its board of directors. Furthermore, an insurance company is not allowed to, directly or indirectly, extend any credit for the purpose of assisting any major shareholder in equity investment in other companies, or transfer of any asset to the major shareholder without consideration, or sell or exchange any assets or extend any credit to the major shareholder on terms that are materially adverse to such company.

***Restrictions on Investment of Assets***

According to the Insurance Business Act, insurance companies are prohibited from making any of the following investment of assets:

subject to certain exceptions, owning precious metals, antiques and paintings and writings;

owning any real estate (excluding any real estate owned as a result of enforcing their own security interest) other than real estate for the conduct of its business as designated by the Presidential Decree. In any case, the total amount of real estate owned by an insurance company must not exceed 25% of its Total Asset;

loans made for the purpose of speculation in commodities or securities;

loans made directly or indirectly to enable a natural or legal person to buy their own shares;

loans made directly or indirectly to finance political campaigns and other similar activities; and

loans made to any of the insurance company's officers or employees other than loans based on insurance policy or de minimis loans of up to (1) W20 million in the case of a general loan, (2) W50 million in the case of a general loan plus a housing loan, or (3) W60 million in the aggregate for general loans, housing loans and loans to pay damages arising from wrongful acts of employees in financial transactions.

In addition, insurance companies are not allowed to exceed the following limits in making the following investments:

with respect to holding unlisted stock, 10% of its Total Asset;

with respect to holding foreign currency under the Foreign Exchange Transaction Act or owning offshore real estate, 30% of its Total Asset; and

with respect to the sum of margins for a futures exchange designated by the Presidential Decree or a foreign futures exchange, 5% of its Total Asset.

Life insurance companies are required to extend loans of not less than 35% of the annual increase in the corporate loans (with the exclusion of those to the banks and securities companies) to the small and medium-sized enterprises.

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***Restrictions on Shareholdings in Other Companies***

*Under the Insurance Business Act, an insurance company may not own more than 15% of the issued and outstanding voting shares of another company, except when the insurance company obtains approval of the Financial Supervisory Service with respect to having subsidiaries that are engaged in any of the following business:*

the finance-related business of the financial institutions as designated under the Act on Structural Improvement of Financial Industry;

The credit information business designated by the Use and Protection of Credit Information Act (excluding the credit evaluation business designated thereunder);

The business of administering insurance contracts including the maintenance, rescission, amendment and reinstatement and the like; and

Other businesses that do not undermine the soundness of the insurance business as prescribed under the Presidential Decree.

***Disclosure of Management Performance***

Pursuant to the Insurance Business Act and regulations thereunder, an insurance company is required to make a periodic disclosure of any material matters relating to management performance, profit and loss, corporate governance, workforce, risk management or others within three months following the end of each fiscal year and within two months following the end of the first half of the fiscal year.

Furthermore, an insurance company must disclose, on an ongoing basis, the public and the Financial Supervisory Service of the occurrence of any events designated by the regulations of the Financial Supervisory Commission and the guidelines of the Korea Life Insurance Commission or the Korea Non-Life Insurance Commission that may have a material adverse effect on the management of such insurance company immediately after such occurrence.

***Deposit Insurance System***

The Depositor Protection Act provides for, through a deposit insurance system, insurance for certain premiums and other amounts payable to policyholders by insurance companies (other than those relating to variable insurance contracts). Under the Depositor Protection Act, all insurance companies subject to the Insurance Business Act, including Shinhan Life Insurance, are required to pay to the Korea Deposit Insurance Corporation an insurance premium for such insurance on a quarterly basis at such rate as determined by the Presidential Decree of the Depositor Protection Act, which shall not exceed 0.5% of the amount designated by the Presidential Decrees of the Depositor Protection Act, taking into account the policy reserves of insurance companies in any given year (the Premium Amount ). The current insurance premium payable by Shinhan Life Insurance is 0.003% of the Premium Amount for each quarter. If the Korea Deposit Insurance Corporation pays the insured amount to any policyholders, it will acquire the claims of the policyholders in an amount not to exceed the amount of such payment. Under the current rules, the Korea Deposit Insurance Corporation insures only up to a total of W50 million for premiums, surrender value to a policyholder or any other amount payable to such policyholder by the insurance company, regardless of when the premiums were paid and the size of the amount payable to such policyholder.

**Table of Contents****PROPERTIES**

Our registered office and corporate headquarters are located at 120, 2-Ga, Taepyung-Ro, Jung-Gu, Seoul 100-102, Korea. Information regarding certain of our properties in Korea is presented in the following table.

Type of Facility	Location	Area (Square Meters)	
		Building	Site (If Different)
Registered office and corporate headquarters	120, 2-Ga, Taepyung-Ro, Jung-Gu, Seoul 100-102, Korea	59,743	4,416
Good Morning Shinhan Securities	23-2, Yoido-Dong, Youngdungpo-Gu, Seoul, Korea 150-312	70,170	4,765
Shinhan Centennial Building	117, Samgak-Dong, Jung-Gu, Seoul, Korea	19,697	1,389
Shinhan Bank Gwanggyo Branch	14, 1-Ga, Namdaemun-Ro, Jung-Gu, Seoul, Korea	20,379	6,724
Shinhan Myongdong Branch	53-1, 1-Ga, Myong-Dong, Jung-Gu, Seoul, Korea	8,936	1,014
Shinhan Youngdungpo Branch	57, 4-Ga, Youngdungpo-Dong, Youngdungpo-Gu, Seoul, Korea	6,171	1,983
Shinhan IT center	781, Janghang-Dong, Ilsan-Gu, Goyang-Si, Kyunggi Province, Korea	24,496	5,856
	731, Yoksam-Dong, Kangnam-Gu, Seoul, Korea	23,374	7,964
Shinhan Cheongju IT back-up center	1704-Ga, Yongam-Dong, Sangdang-Gu, Cheongju-Si, Chungcheongbuk-Do	5,756	6,398

Our subsidiaries own or lease various land and buildings for their branches and sales offices.

As of December 31, 2005, Shinhan Bank had a countrywide network of 402 branches. Approximately 19.9% of these facilities was housed in buildings owned by us, while the remaining branches are leased properties. As of December 31, 2005, Chohung Bank had a countrywide network of 537 branches. Approximately 35.4% of these facilities were housed in buildings owned by us, while the remaining branches are leased properties. As of December 31, 2005, Jeju Bank had 31 branches of which we own 18 of the buildings in which the facilities are located, representing 58.1% of its total branches. Lease terms are generally from two to three years, and seldom exceed five years.

As of December 31, 2005, Shinhan Life had 117 branches all of which we leased for a term of generally one to two years. As of December 31, 2005, Good Morning Shinhan Securities had 77 branches of which we own 15 of the buildings in which the facilities are located, representing 19.5% of its total branches. Lease terms are generally from two to three years, and seldom exceed five years. As of December 31, 2005, Shinhan Card had 19 sales offices all of which are leased. Lease terms are generally from two to three years, and seldom exceed five years.

Shinhan Bank houses its central mainframe computer system at its information technology center in Ilsan, one of the suburban districts outside of Seoul. Chohung Bank's central mainframe computer system is located at its information technology center in Kangnam-Gu, Seoul and the back-up center is located separately in Cheongju, Korea.

The net book value of all the properties owned by us at December 31, 2005 was W1,499 billion. We do not own any material properties outside of Korea.



**Table of Contents****ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

*You should read the following discussion and analysis of our financial condition and results of operations together with our consolidated financial statements included in this document. The following discussion is based on our consolidated financial statements, which have been prepared in accordance with U.S. GAAP.*

**Overview*****The Korean Economy***

Economic conditions in Korea, elsewhere in Asia, in the United States and elsewhere in the world materially affect our business. Financial turmoil in Asia in the late 1990 s adversely affected the Korean economy and in turn Korean financial institutions. In 1997 and 1998, Korea experienced a severe financial and economic downturn characterized by, among other things, significant corporate failures, instability in the financial sector, credit and liquidity concerns and volatility in the domestic financial and currency markets. In response, the International Monetary Fund provided a financial aid package to Korea and in late 1997, the government initiated a comprehensive program to address some of the structural weaknesses in the Korean economy. As part of that program, there have been certain significant changes in regulations specifically affecting financial institutions, including changes in loan classification and loss provisioning guidelines, Korean GAAP, securities valuation methods and liquidity requirements.

As a result of the downturn, in 1998 there was a general increase in interest rates in Korea and we experienced a decrease in the demand for loans and other products. Chohung Bank experienced significant losses in its large corporate loan portfolio that led to government intervention and a support package. As a result, Korea Deposit Insurance Corporation acquired 80.04% of the outstanding shares of Chohung Bank. After the government intervention, Chohung Bank continued to be adversely affected by its exposure to the large corporate sector. With the economy on the rebound from 1999, Chohung Bank diversified its business into the retail, credit card and small-and medium-sized enterprises markets. Since financial crisis of the late 1990 s, the general level of interest rates have continued to decrease and demand for financial products have increased.

Deterioration in the Korean economy can also occur as a result of deterioration in the global economic conditions. The worldwide economy has been in a slump since the beginning of 2001, as the United States and other G8 countries have experienced recessionary conditions which have been exacerbated by the terrorist attacks in the United States on September 11, 2001, the looming prospect of war in Iraq throughout much of 2002, on-going tensions between the United States and North Korea and the impact of SARS, on global exports and GDP growth rates. Recently, we have witnessed mixed signals of recovery and continuing difficulties in the global economy. While the global economy has shown signs of recovery, the recent increase in oil price and other raw materials as well as concerns raised by the rapid economic growth and expansion in China have negatively affected this trend.

In addition, the economic conditions of Korea s major trading partners, such as China and the United States, and volatility in exchange rates and commodity prices (including oil prices) continue to affect the Korean economy. In particular, the recent and significant appreciation of the Korean Won against the U.S. dollar and other major foreign currencies have resulted in adverse effects on the price competitiveness of Korean companies in export markets.

***Government Regulation and Policy***

Over the past twelve years successive Korean government administrations have taken steps to reform the Korean economy in line with prevailing international standards. The reforms have focused on restructuring the large corporate sector and reducing *chaebol* influence; modernizing the banking sector to eliminate policy lending and most interest rate regulations, to improve credit risk evaluation and provisioning, and to increase transparency; creating a more liquid and efficient domestic capital market; and fostering changes in the law to support these developments. This ongoing proactive government role has had, and will continue to have, a profound effect on the Korean banking sector. Over the past several years national banks have undergone

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consolidation and banks lending primarily to large corporate borrowers have shifted their focus to the retail and small- and medium-sized enterprise sectors. This shift has led to very intense competition in sectors which have historically been our principal markets. The result so far has been a major increase in retail sector lending levels, including credit cards and home mortgages, with attendant pressures on margins and credit quality for the sector as a whole.

Government initiatives to further regulate this sector have also affected the market. In the consumer loan sector, the Korean government enacted a number of changes to laws governing retail lending volumes, including the lowering of maximum loan-to-value ratio of mortgage and home equity loans to 60%, and in certain cases to 40%. In recent years, the Korean government has issued several policy-driven regulations to suppress the increasing real estate prices in certain zones of the Seoul Metropolitan area that are in high demand, including the further reduction of maximum loan-to-value ratio applicable to mortgage and home equity loans for real estate in those regulated zones. In addition, we expect that the current focus on small- and medium-sized enterprise lending will lead to competitive pressures and possibly regulatory initiatives in this segment as well. Our ability to anticipate and respond to government initiatives and their competitive implications will have a significant effect on our future performance.

***Market Developments***

The Korean government's deregulation of the financial sector and policy to increase consumer spending through credit cards, and excessive competition among credit card companies resulted in the deterioration of credit companies assets and large number of individual credit delinquencies. These events have led to financial difficulties of LG Card which was Korea's largest credit card company in terms of assets. Currently, the principal creditor banks of LG Card commenced corporate restructuring procedures against LG Card based on a debt-to-equity swap plan.

Since 2001, home purchases through mortgage and home equity loans increased significantly due to soaring real estate prices. As a result, consumer debt has constantly increased since 2002. The recent increase in real estate prices can be attributable to increase in investment demand in real estate and a highly liquid market condition. However, consumer spending has not increased due to slowdown in the overall economy and decrease in consumer income, which was further aggravated by the effects from restructuring the credit card industry.

In 2003, the credit risk of large corporations increased significantly as a result of accounting irregularities discovered at SK Networks. In 2004, credit risk of large corporations improved as a result of reduced leverage through corporate restructuring and increase in cash flow from exports of corporate customers. However, decrease in consumer spending continued to adversely affect corporate expenditures as well as revenues earned by small- and medium-sized enterprises focusing on the domestic market, which in some cases led to heightened risk of insolvency for small- and medium-sized enterprises. Although small- and medium-size enterprises have gradually been adjusting to changes in market conditions, the financial difficulties of these small- and medium-size enterprises have continued through the first half of 2005.

**Table of Contents****Interest Rates**

Over the past ten years, we have operated in environments characterized by high interest rates, periods of significant interest-rate volatility and low interest rates. The following table shows certain benchmark Won-denominated borrowing interest rates as of the dates indicated.

	<b>Corporate Bond Rates(1)</b>	<b>Treasury Bond Rates(2)</b>	<b>Certificate of Deposit Rates(3)</b>
June 30, 1998	16.00	N/A	16.30
December 31, 1998	8.00	6.95	7.70
June 30, 1999	7.96	7.20	6.35
December 31, 1999	9.95	9.03	7.34
June 30, 2000	9.37	8.31	7.18
December 31, 2000	8.13	6.70	6.87
June 30, 2001	7.10	5.93	5.57
December 31, 2001	7.04	5.91	4.86
June 30, 2002	6.59	5.66	4.91
December 31, 2002	5.68	5.11	4.90
June 30, 2003	5.45	4.16	4.30
December 31, 2003	5.58	4.82	4.36
June 30, 2004	4.84	4.24	3.93
December 31, 2004	3.72	3.28	3.43
June 30, 2005	4.41	4.02	3.54
December 31, 2005	5.52	5.08	4.09
March 31, 2006	5.25	4.93	4.27

Source: The Bank of Korea

N/A = not available.

Notes:

(1) Measured by the yield on three-year AA- rated corporate bonds.

(2) Measured by the yield on three-year treasury bonds.

(3) Measured by the yield on certificates of deposit (with maturity of 91 days).

Interest rate movements on the asset and liability side have often been divergent, both in terms of the size of the movement as well as the timing thereof, and the movements together with this divergence have had a significant impact on our margins, particularly with respect to financial products that are sensitive to such fluctuations. We continually manage our respective balance sheet to minimize volatility exposure, but the impact has been, and may continue to be, significant in analyzing period-to-period margin comparisons and the trends that they may indicate for our business.

**Financial Holding Company Restructuring**

On September 1, 2001, we restructured our corporate existence as a financial holding company by exchanging the shares of our common stock for the respective shares of common stock held by the shareholders of Shinhan Bank, Shinhan Capital, Shinhan Securities and Shinhan Investment Trust Management Company. Upon successful restructuring into a financial holding company, Shinhan Bank, Shinhan Capital, Shinhan Securities and Shinhan Investment Trust Management Company have all become our wholly-owned subsidiaries. This restructuring has been

accounted for using the purchase method of accounting, with Shinhan Bank being the accounting acquirer. Our consolidated financial statements prior to September 1, 2001 reflect the historical financial results of operations and financial position of Shinhan Bank.

**Table of Contents*****Financial Impact of Acquisitions******Acquisition of Chohung Bank***

On August 19, 2003, we acquired 80.04% of the outstanding common shares of Chohung Bank. The acquisition of Chohung Bank was accounted for under the purchase method of accounting and has been reflected in our consolidated financial statements as of the acquisition date. The fair value of net assets acquired, including other tangible assets, amounted to W2,012 billion. In connection with this acquisition, we recorded core deposit intangible assets aggregating W957 billion and credit card relationship intangible assets aggregating W184 billion. In addition, goodwill of W341 billion was recognized. As of December 31, 2003, Chohung Bank had total assets of W57,110 billion, representing 41.9% of our total consolidated assets, and total liabilities of W55,842 billion, representing 42.4% of our total consolidated liabilities. Accordingly, our total assets and liabilities as of December 31, 2003 represent a substantial increase from those as of December 31, 2002. Also included in our results of operations for the year ended December 31, 2003 are Chohung Bank's results of operations from September 1, 2003 to December 31, 2003, resulting in a significant increase from our results of operations of prior periods.

The following table sets forth the selected income statement data of Chohung Bank for the period from September 1, 2003 to December 31, 2003 and selected balance sheet data of Chohung Bank as of December 31, 2003.

	<b>From September 1 to December 31,</b>	
	<b>2003</b>	<b>2003</b>
	<b>(In billions of Won and millions of US\$, except per common share data)</b>	
Interest and dividend income	W 1,286	\$ 1,079
Interest expense	574	482
Net interest income	712	597
Provision for loan losses	427	358
Provision for guarantees and acceptances	(19)	(16)
Non interest income	163	137
Non interest expense	558	468
Income tax expense	19	16
Minority interest	1	1
Net loss	W (111)	\$ (93)

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	<b>As of December 31,</b>	
	<b>2003</b>	<b>2003</b>
	<b>(In billions of Won and millions of US\$)</b>	
<b>Assets</b>		
Cash and cash equivalents	W 1,276	\$ 1,070
Restricted cash	502	421
Interest-bearing deposits	159	133
Call loans and securities purchased under resale agreements	392	329
Trading assets:		
Trading securities	1,191	999
Derivatives instruments	156	131
Securities:		
Available-for-sale securities	7,274	6,102
Held-to-maturity securities		
Loans (net of allowance for loan losses of W2,498 billion in 2003)	41,233	34,592
Customers liability on acceptances	1,107	928
Premises and equipment, net	1,164	977
Goodwill and intangible assets	35	29
Security deposits	483	405
Other assets	2,138	1,796
<b>Total assets</b>	<b>W 57,110</b>	<b>\$ 47,912</b>
<b>Liabilities and Stockholders Equity</b>		
<i>Liabilities:</i>		
<i>Deposits:</i>		
Interest-bearing	W 38,917	\$ 32,649
Noninterest-bearing	322	270
Trading liabilities	128	107
Acceptances outstanding	1,107	928
Short-term borrowings	4,804	4,030
Secured borrowings	1,432	1,201
Long-term debt	6,504	5,456
Accrued expenses and other liabilities	2,628	2,206
<b>Total liabilities</b>	<b>55,842</b>	<b>46,847</b>
Minority interest	15	12
<i>Stockholders equity:</i>		
Common stock	3,596	3,016
Additional paid-in capital	1,722	1,445
Accumulated deficit	(4,300)	(3,607)
Accumulated other comprehensive income, net of taxes	235	199
<b>Total stockholders equity</b>	<b>1,253</b>	<b>1,053</b>

Total liabilities, minority interest and stockholders' equity	W	57,110	\$	47,912
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In December 2003, we injected an additional W200 billion into Chohung Bank to strengthen its capital base in light of increased delinquencies, provisions and net losses at Chohung Bank. In June 2004, we acquired

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the remaining 18.85% of the outstanding shares of Chohung Bank's common stock through a cash tender offer followed by a small-scale share swap pursuant to the applicable laws of Korea. Effective as of April 3, 2006, Shinhan Bank and Chohung Bank merged together, with Chohung Bank being the surviving legal entity. Immediately after the merger, Chohung Bank changed its name to Shinhan Bank. See Item 4. Information on the Company The Merger of Shinhan Bank and Chohung Bank.

*Acquisition of Good Morning Securities*

During 2002, through a series of transactions, we acquired 31.7% of common stock (or 30.7% of voting equity securities) of Good Morning Securities. Subsequently, we merged Shinhan Securities into Good Morning Securities and renamed it Good Morning Shinhan Securities. As of December 31, 2002, following the foregoing transactions, we effectively owned 60.5% of Good Morning Shinhan Securities. The total fair value of net assets acquired amounted to W237 billion. In connection with this acquisition, we recorded goodwill of W282 billion, of which W244 billion relates to the brokerage unit and W38 billion relates to the capital markets unit, a component of our business. In addition, W80 billion of the intangible assets, primarily the brokerage relationship intangible assets, were acquired.

Later in 2002, however, we recorded W137 billion of impairment loss on goodwill due to a severe downturn in market conditions affecting Good Morning Shinhan Securities in the last six months of 2002. We believe that this market downturn was due primarily to:

the uncertainties of the global economy following the terrorist attack in Bali, Indonesia and as the Iraqi war began to unfold;

the uncertainties of the Korean economy due to the presidential election in late 2002 and increased tensions on the Korean peninsula with North Korea reported to have resumed its nuclear program; and

significant deterioration of the financial market and a 40% decline in the share price of Good Morning Shinhan Securities since the acquisition.

These adverse market developments have resulted in a significant decline in the market trading volume of the Good Morning Shinhan Securities' brokerage unit, negatively impacting brokerage commission income, which is the main source of revenue for the brokerage unit. In addition, anticipated growth in the futures and options market and the sale of beneficial certificate products did not occur. This was further aggravated by a decline in the market share of Good Morning Shinhan Securities since the acquisition, which contradicted our original projection at the time of acquisition. The downturn in market conditions also had a negative impact on profits generated from proprietary trading at the capital market unit of Good Morning Shinhan Securities, resulting in a significant decline in the value of the capital market unit.

In December 2004, we acquired a 100% ownership in Good Morning Shinhan Securities through a small-scale share exchange pursuant to applicable Korean laws. Good Morning Shinhan Securities was delisted from the Stock Market Division of the Korea Exchange on January 5, 2005.

*Acquisition of Jeju Bank*

In April 2002, we acquired 51% of the total outstanding common stock of Jeju Bank from Korea Depository Insurance Corporation and subsequently increased our ownership to 62% on July 5, 2002. The total purchase price was approximately W43 billion in cash. The acquisition of Jeju Bank was accounted for under the purchase method of accounting and has been reflected in our consolidated financial statements as of the acquisition date. The fair value of net assets acquired amounted to W69 billion. In connection with this acquisition, we recorded core deposit intangible assets of W17 billion. In addition, a negative goodwill of W26 billion was recognized. The negative goodwill was allocated to identifiable intangible assets and premises and equipment on a pro rata basis.

**Table of Contents***Spin-off of Shinhan Card*

On June 4, 2002, Shinhan Bank spun off its credit card business into Shinhan Card Co., Ltd., a monoline credit card subsidiary. As a result of the spin-off, Shinhan Card was required to obtain its own funding, primarily through the issuance of short-term corporate debt securities with maturities of less than one year and commercial papers with maturities of three months. The amount of short-term borrowings of Shinhan Card was W276 billion as of December 31, 2005. While we, at the holding company level, may provide long-term funding to Shinhan Card, we are subject to certain regulatory limitations. See *Liquidity and Capital Resources*.

With the deterioration in asset quality of Korean credit card companies and investors' reluctance to invest in corporate debt securities of credit card companies, many credit card companies, including Shinhan Card, have begun to experience financial and liquidity difficulties. In respect of Shinhan Card, this change of events has led to increased funding requirements at the holding company level to provide liquidity support to Shinhan Card, subject to regulatory and internal limitations described above. Our long-term debt, as a result, increased in the first half of 2003. In addition, to the extent that Shinhan Card needs funding in excess of what the holding company is able to provide, Shinhan Card will be compelled to seek its own funding in an environment unfavorable to it, resulting in increased funding costs and/or liquidity difficulties for Shinhan Card and us.

*Acquisition of Shinhan Life Insurance*

In December 2005, in a series of related transactions, we acquired 100% of Shinhan Life Insurance, an insurance company, through a small scale share exchange mechanism provided under applicable Korean law, pursuant to which we issued 17,528,000 new shares of our common stock to the shareholders of Shinhan Life Insurance in exchange for all outstanding common stock of Shinhan Life Insurance held by them for an aggregate purchase price of W612 billion, or W15,300 per share. As part of this share exchange, Shinhan Bank exchanged 5,524,772 shares of common stock of Shinhan Life Insurance previously held by it into 2,420,955 shares of our common stock and Good Morning Shinhan Securities exchanged 464,800 shares of common stock of Shinhan Life Insurance previously held by it into 203,675 shares of our common stock. Similarly, as part of this transaction, Shinhan Life Insurance also exchanged 9,000 shares of its common stock, which Shinhan Life Insurance acquired as a result of the exercise of appraisal rights by dissenting shareholders of Shinhan Life Insurance, into 3,943 shares of our common stock. All of such shares of our common stock received by Shinhan Life Insurance were sold in the market on December 29, 2005.

*Liquidation of e-Shinhan*

Pursuant to a shareholders' resolution on August 26, 2005, we liquidated e-Shinhan in order to improve the efficiency by focusing our resources on our growing banking division.

***Certain Income Tax Expenses and Provision for Other Losses***

Beginning in 2002, commercial banks in Korea, including Shinhan Bank and Chohung Bank, offered to their customers deposit products that utilize Korean Won and Japanese Yen swaps to maximize the return for such customers. According to the terms of these deposit products, deposits made by customers in Korean Won are converted into Japanese Yen and repaid in Japanese Yen at maturity. The repayment amount is then converted back into Korean Won. While these deposit products typically carry a low interest rate, ranging from 0.05% to 0.3% per annum, the actual return to the customers was higher as a result of foreign exchange gains. These deposit products are attractive to customers, in particular high net worth customers, since the gains from foreign exchange were deemed not to be interest subject to income tax. However, in 2005, the Korean National Tax Service announced that foreign currency deposits disguised as derivative products would be subject to tax and tax withholding and issued a recommendation that the banks should refile its tax returns to include the unwithheld amounts. Eight of the commercial banks in Korea, who are subject to this adverse tax treatment, have announced their intention to challenge the foregoing decision by the Korean National Tax Service while complying with the Tax Service's information requests. Following the announcement, Shinhan Bank ceased to offer these deposit products.

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The commercial banks had marketed these deposit products to their customers on the basis that such deposit products were exempt from income tax or tax withholding. We believe that few, if any, of these customers have reported the gains from such deposit products as interest income subject to taxation in their tax returns. According to the Korean National Tax Service, these deposit customers are also responsible for including the income received from these deposits in their final individual tax returns relating to comprehensive financial taxable income. However, depending on the amount of income received from these products, the individual customers may be subject to (i) a higher tax rate on all of his or her taxable income, (ii) a fine for failing to properly report the interest income in an amount equal to 20% of the unreported amount, and (iii) a fine for failing to pay tax on such interest income in an amount equal to interest applied at a rate of 10.95% per annum to such unpaid tax amount. No assurance can be given that aggrieved customers will not bring claims against these commercial banks, including Shinhan Bank and Chohung Bank, if their tax liabilities are increased as a result of the foregoing events.

Beginning in September 2005, we have been subject to a tax audit by the Korean National Tax Service. In May 2006, based upon its tax audit of us and other relevant banks, the Korean National Tax Service reached a decision to impose additional taxes (including interest thereon) of W36 billion on Shinhan Bank. This decision did not include a judgment on deposits utilizing the Korean Won and Japanese Yen swaps as described above, but such judgment is expected soon. In anticipation of an adverse tax ruling against these deposit products utilizing Korean Won and Japanese Yen swaps, we have determined, on a voluntary basis, to indemnify our customers for their increased tax liability to the extent resulting from their investment in these deposit products, including any additional tax liability that our customers may have against the Korean National Tax Service for gifts tax from the benefit of this indemnity. We currently estimate that we may be subject to maximum additional tax-related liability, including the liability from the indemnity to our customers, of W85 billion as of December 31, 2005. Accordingly, we recorded a total charge to our income of W78 billion in the year ended December 31, 2005, consisting of additional tax expenses of W29 billion and provision for other losses of W49 billion. In addition, we also recorded W7 billion as deferred tax assets on our balance sheet as of December 31, 2005.

**Critical Accounting Policies**

Our consolidated financial statements are prepared in accordance with US GAAP, including prevailing practices within the financial services industry. The preparation of consolidated financial statements requires management to make judgments, involving significant estimates and assumptions, in the application of certain accounting policies about the effects of matters that are inherently uncertain. These estimates and assumptions, which may materially affect the reported amounts of certain assets, liabilities, revenues and expenses, are based on information available to us as of the date of the financial statements, and changes in this information over time could materially impact amounts reported in the financial statements as a result of the use of different estimates and assumptions. Certain accounting policies, by their nature, have a greater reliance on the use of estimates and assumptions, and could produce results materially different from those originally reported.

Based on the sensitivity of financial statement amounts to the methods, estimates and assumptions underlying reported amounts, we have identified the following significant accounting policies that involve critical accounting estimates. These policies require subjective or complex judgments, and as such could be subject to revision as new information becomes available. Our significant accounting policies are described in more detail in Note 1 in Item 18. Financial Statements Notes to the consolidated financial statements of Shinhan Financial Group .

***Allowance for Credit Losses***

The allowance for credit losses includes allowance for loan losses and allowance for off-balance sheet credit instruments. The allowance for credit losses represents the amount available for estimated probable credit losses existing in our lending portfolio. The methodology used to provide the appropriate level of reserve is inherently subjective and involves many complex estimates and assumptions. We perform periodic

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systematic reviews of our credit portfolios to identify inherent losses and assess the overall probability of collection. Each loan portfolio is evaluated based on its respective characteristics.

We evaluate large impaired corporate loans individually as part of our normal corporate review practice due to the unique characteristics of such borrowers. As described in more detail in the footnotes to our consolidated financial statements, we consider a loan to be impaired when, after consideration of risk characteristics and current information and events, we believe it is probable that we will be unable to collect all amounts owed under the contractual terms of the agreement, including principal and interest, according to the contractual terms of the loan.

We generally consider the following corporate loans to be impaired:

loans classified as substandard or below according to the asset classification guidelines of the Financial Supervisory Commission;

loans that are 90 days or more past due; and

loans which are troubled debt restructuring as defined under U.S. GAAP.

Once we have identified a loan as impaired, we value that loan either based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. Each of these variables involves judgment and the use of estimates. For instance, discounted cash flows are based on estimates of the amount and timing of expected future cash flows. Forecasts of expected future cash flows are based on various data including restructuring plans, due diligence reports, as well as industry forecasts among other quantitative tools. The fair value of collateral is determined by using third party valuation reports. Additional consideration is given to recent auction results and court valuations. If the resulting value is less than the carrying amount of the loan, we establish a specific allowance for the difference.

We generally evaluate consumer loans and certain smaller balance corporate loans, including leases, mortgage and home equity loans, and credit card balances, as individual pools for credit loss allowance purposes due to their homogeneous nature based on historical loss experience. Such allowances have been established using a risk rating migration model when considering consumer loans and a delinquency roll-rate model when considering credit cards.

The allowance for off-balance sheet credit instruments represents the amounts available for estimated probable credit loss existing in our unfunded credit facilities such as commitments to extend credit, guarantees, acceptances, standby and commercial letters of credit and other financial instruments. As stated above, we perform periodic systematic reviews of our credit portfolio including off-balance sheet credit instruments to identify inherent losses and assess the overall probability of collection.

When we evaluate large impaired corporate loans individually for specific allowance, the related guarantees and acceptances made to the same borrowers are also evaluated for inherent loss. We generally evaluate the remaining guarantees and acceptances, which are generally smaller balances, on a pool basis. Allowance for the remaining guarantees and acceptances is generally established using estimated payout ratios and loss severity which are based on historical loss experience and various factors such as macroeconomic factors.

The adequacy of the allowance for credit losses requires a great deal of judgment and the use of estimates as discussed above. As such, we have also considered changes in underwriting, credit monitoring, the Korean and global economic environment, industry concentrations, and delinquencies among other factors when concluding on the level of the allowance for credit losses.

***Fair Value of Financial Instruments***

Our securities and trading assets and liabilities include debt and marketable equity securities, equity securities that do not have readily determinable fair values and derivatives. Fair value of financial instruments is the current amount that would be exchanged between willing parties, other than in a forced sale or

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liquidation. The fair values of our securities and trading assets and liabilities are estimated based on quoted market prices or internally developed pricing models.

Fair value is best determined based on quoted market prices, if available. If quoted market prices are not available, fair value is estimated using the present value of expected future cash flows calculated by using market interest rates comparable with the credit rating and maturity of the security. An alternative to estimate fair value is to use internally developed pricing models based on external market variables including interest rate yield curves, option volatilities and foreign exchange rates. The estimation of fair value involves the assessment of various financial variables, prices of comparable financial instruments, credit ratings of counterparties, liquidity of the financial instruments and transaction costs. Our management applies judgments in assessing the variables used in the fair valuation process and also if certain external market variables are less readily available. Changes in model assumptions, market conditions and unexpected circumstances can affect the fair values of the securities and trading assets and liabilities.

Debt securities and equity securities with readily determinable fair values classified as available-for-sale are carried at fair value with corresponding changes recognized in other comprehensive income within stockholders equity net of taxes. Debt securities classified as held-to-maturity securities are recorded at amortized cost. Equity securities that do not have readily determinable fair values are carried at cost. Declines in values of available-for-sale securities, held-to-maturity debt securities and equity securities that do not have readily determinable fair values that are deemed to be other-than-temporary are reflected in earnings as realized losses. We perform regular assessment of various quantitative and qualitative factors to determine whether impairment is other-than-temporary. Such factors include the duration and extent of the decline in the fair values of securities, the current operating and future expected performance, market values of comparable companies, and changes in industry and market prospects. These factors can be adversely affected by changing economic conditions that are global or regional in nature or are issuer or industry specific. For certain securities without readily determinable fair values or with sales restrictions exceeding one year, we may periodically utilize external valuations performed by qualified independent valuation consulting firms.

Trading assets and liabilities are carried at fair value with the corresponding changes recognized in earnings. The majority of our trading assets and liabilities that are actively traded are valued based on quoted market prices except for derivatives. Since few derivatives are actively traded, the majority of our derivatives are valued using internally developed models based on external market variables that can be independently validated by third party sources. However, certain derivatives are valued based on external market variables that are less readily available and are subject to management judgment. For certain derivatives not valued by our internally developed models, we periodically utilize external valuations performed by qualified independent valuation consulting firms.

In August 2003, we issued Redeemable Preferred Stock and Redeemable Convertible Preferred Stock as part of the consideration paid to the Korea Deposit Insurance Corporation in connection with our acquisition of Chohung Bank. Our redeemable stock and Redeemable Convertible Preferred Stock are evaluated and recognized initially at fair value based on the present value of its future cash dividend payments and repayment provisions. Changes in the expected future cash dividend payments, repayment provisions or model assumptions and variables used can affect the fair values of the preferred stock. Note 22 to our consolidated financial statements in Item 18. Financial Statements Notes to consolidated financial statements of Shinhan Financial Group provides additional information related to our Redeemable Preferred Stock.

***Goodwill and Other Intangible Assets***

Effective January 1, 2002, we adopted Statement of Financial Accounting Standards, or SFAS, No. 142, *Goodwill and Other Intangible Assets*, ( SFAS No. 142 ) as required by the accounting principles generally accepted in the United States.

SFAS No. 142 classified intangible assets into three categories: (1) intangible assets with definite lives subject to amortization; (2) intangible assets with indefinite lives not subject to amortization; and (3) goodwill. For intangible assets with definite lives, tests for impairment must be performed if conditions exist that

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indicate the carrying amount may not be recoverable. For intangible assets with indefinite lives and goodwill, tests for impairment must be performed at least annually.

We recognized a significant amount of goodwill in connection with our acquisition of Good Morning Securities. In addition, we acquired core deposit, brokerage customer relationship and Korea Securities Finance Corporation deposit in connection with our acquisitions of Good Morning Securities and Jeju Bank in 2002. We also recognized a significant amount of goodwill in connection with our acquisition of Chohung Bank. In addition, we acquired core deposit, credit card and core deposit intangible assets in connection with our acquisitions of Chohung Bank in 2003. For discussions on the nature and accounting for goodwill and intangible assets see Notes 1, 3 and 10 in Item 18. Financial Statements Notes to the consolidated financial statements of Shinhan Financial Group .

Our core deposit, credit card relationship and brokerage customer relationship intangibles determined to have definite lives are amortized over their useful lives. If conditions exist that indicate the carrying amount may not be recoverable, we review these intangible assets with definite lives for impairment to ensure they are appropriately valued. Such conditions may include adverse changes in business or political climate, actions by regulators and customer account run-off rates.

We do not amortize goodwill or indefinite-lived intangibles consisting of court deposits and borrowings from Korea Securities Finance Corporation. Instead, we perform tests for impairment of goodwill annually or more frequently if events or circumstances indicate it might be impaired. Such tests include comparing the fair value of a reporting unit with its carrying amount, including goodwill. If the fair value is less than the carrying value, a second test is required to measure the amount of goodwill impairment. The second step of the goodwill impairment test compares the implied fair value of reporting unit goodwill with the carrying value of that goodwill. If the carrying value of reporting unit goodwill exceeds the implied fair value of that goodwill, we recognize an impairment loss in an amount equal to that excess. Test for indefinite-lived intangible assets, including borrowings from Korea Securities Finance Corporation and court deposits at Chohung Bank, is also carried out on an annual basis on an asset-by-asset basis, or more frequently if events or circumstances indicate they might be impaired. Impairment assessments are performed using a variety of valuation methodologies, including discounted cash flow estimates. Management estimates the future cash flows expected to be derived from the use and, if applicable, the terminal value of the assets. The key variables that management must estimate include, among other factors, market trading volume, market share, fee income, growth rate and profitability margin. Although the assumptions used are consistent with our internal planning, significant management judgment is involved in estimating these variables, which include inherent uncertainties. A discount rate is applied to the cash flow estimates considering our cost of capital rate and specific country and industry risk factors. The cash flows of Chohung Bank's reporting units were discounted using discount rates ranging from 6.76% to 16.89%.

The sharp decline in the Korean financial industry during the second half of 2002 prompted a re-assessment of all key assumptions underlying our goodwill valuation judgments. As result of our review, we determined that goodwill impairment charges of W115 billion and W22 billion were required on the goodwill recorded in the brokerage and capital market units of Good Morning Shinhan Securities. The amount of these charges were equal to the difference between the carrying amount of goodwill and its implied fair value, which is based on the fair value of the net assets in respect of reporting units.

The assumptions and conditions for goodwill and intangible assets reflect management's best assumptions and estimates. However, these items involve inherent uncertainties, as described above, that may or may not be controllable by management. Economic and political conditions, such as movements in interest rates, delinquencies in Korea and tension with North Korea, represent uncertainties that are not controllable by management. As a result, if other assumptions and conditions had been used in the current period, the carrying amount of goodwill and other intangible assets could have been materially different. Furthermore, if management uses different assumptions, including the discount rates used to determine the implied fair value of reporting units, or if different conditions occur in future periods, future operating results could be materially impacted.

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Notes 3, 10 and 20 to our consolidated financial statements in Item 18. Financial Statements Notes to consolidated financial statements of Shinhan Financial Group provide additional information related to goodwill and intangible assets.

**Consolidation**

Under the provisions of Financial Accounting Standards Board ( FASB ) Interpretation No. 46 and 46R, *Consolidation of Variable Interest Entities* ( FIN 46 and FIN 46R ), a variable interest entity ( VIE ) is consolidated by the company holding the variable interest that will absorb a majority of the VIE s expected losses, or receive a majority of the expected residual returns, or both. All other entities are evaluated for consolidation under Statement of Financial Accounting Standards, or SFAS, No. 94, *Consolidation of All Majority-owned Subsidiaries* ( SFAS 94 ). The company that consolidates a VIE is referred to as the primary beneficiary. A variety of complex estimation processes involving both qualitative and quantitative factors are used to determine whether an entity is a variable interest entity, to analyze and calculate expected losses and expected residual returns, which involves estimating the future cash flows of the VIE and analyzing the variability in those cash flows, and allocating the losses and returns among the parties holding variable interests. Also, there is a significant amount of judgment required in interpreting the provisions of FIN 46 and FIN 46R and applying them to specific transactions.

In our case, FIN 46 and FIN 46R apply to certain asset securitization transactions involving our corporate loans, credit card receivables, mortgage and student loans, financing activities conducted for corporate clients, including conduits that we administer and/or provide liquidity facilities, as well as for our own funding needs, and investing activities conducted for our own account, such as beneficial certificates in investment trusts and for our customers, such as guaranteed trusts.

Note 36 in Item 18. Financial Statements Notes to the consolidated financial statements of Shinhan Financial Group provides additional information related to VIEs.

In connection with certain asset securitization transactions, we do not sell assets to an entity referred to as a qualifying special-purpose entity (QSPE) as defined pursuant to the FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities, a replacement of FASB Statement 125*.

**Contingent Liabilities**

We are subject to contingent liabilities, including judicial, tax, regulatory and arbitration proceedings, recourse obligations related to loans sold to Korea Asset Management Corporation, contingent payments to the Korea Deposit Insurance Corporation related to our acquisition of Chohung Bank, commitments provided to our customers and other claims arising from the conduct of our business activities. We establish allowances against these contingencies in our financial statements based on our assessment of the probability of occurrence and our estimate of the obligation. We involve internal and external advisors, such as attorneys, consultants and other professionals, in assessing probability and in estimating any amounts involved. Throughout the life of a contingency, we or our advisors may learn of additional information that can affect our assessments about probability or about the estimates of amounts involved. Changes in these assessments can lead to changes in allowances recorded on our financial statements. In addition, the actual costs of resolving these claims may be substantially higher or lower than the amounts provided in our financial statements for those claims.

Note 31 in Item 18. Financial Statements Notes to the consolidated financial statements of Shinhan Financial Group provides additional information related to the commitments and contingencies, and Note 3 to our consolidated financial statements describe our contingent considerations to the Korea Deposit Insurance Corporation in connection with our acquisition of Chohung Bank.

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***Valuation allowance for Deferred Tax Assets***

We recognize deferred tax assets and liabilities for the future tax consequences attributes to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, net operating loss carryforwards and tax credits. A valuation allowances is maintained for deferred tax assets that we estimate are more likely than not to be unrealizable based on available evidence at the time the estimate is made. Determining the valuation allowance requires significant management judgments and assumptions. In determining the valuation allowance, we use historical and forecasted future operating results, based upon approved business plans, including a review of the eligible carryforward periods, tax planning opportunities and other relevant considerations.

We believe that the accounting estimate related to the valuation allowance is a critical accounting estimate because the underlying assumptions can change from period to period. For example, tax law changes or variance in future projected operating performance could result in a change in the valuation allowance. If we were not able to realize all or part of our net deferred tax assets in the future, an adjustment to our deferred tax assets valuation allowance would be charged to income tax expense in the period such determination was made.

In 2005, based on the anticipated split-merger of the credit card operations of Chohung Bank and Shinhan Card, we decided that it is more likely than not that we will not be able to utilize in the future certain net deferred tax assets of credit card operations of Chohung Bank and thus recorded valuation allowance of W47 billion on such net deferred tax assets.

Note 25 in Item 18. Financial Statements Notes to the consolidated financial statements of Shinhan Financial Group provides additional information related to deferred tax assets and valuation allowance.

**Table of Contents****Average Balance Sheet and Volume and Rate Analysis*****Average Balance Sheet and Related Interest***

The following table shows our average balances and interest rates, as well as the net interest spread, net interest margin and asset liability ratio, for the years ended December 31, 2003, 2004 and 2005.

	Year Ended December 31,								
	2003			2004			2005		
	Average Balance(1)	Interest Income/ Expense	Yield/ Rate	Average Balance(1)	Interest Income/ Expense	Yield/ Rate	Average Balance(1)	Interest Income/ Expense	Yield/ Rate
(In billions of Won, except percentages)									
<b>Assets:</b>									
Interest-bearing deposits	W 1,618	W 66	4.08%	W 1,322	W 44	3.33%	W 1,778	W 64	3.60%
Call loans and securities purchased under resale agreements	1,609	48	2.98	3,012	93	3.09	2,499	85	3.40
Trading assets	1,824	102	5.59	3,666	168	4.58	3,394	111	3.27
Securities(2)	17,053	928	5.44	20,924	1,265	6.05	19,348	932	4.82
<b>Loans:(3)</b>									
Commercial and industrial	25,294	1,279	5.06	35,753	1,876	5.25	36,079	2,075	5.75
Other commercial	13,434	851	6.33	21,632	1,311	6.06	20,130	1,145	5.69
Lease financing	786	70	8.91	1,039	62	5.97	749	47	5.80
Total corporate	39,514	2,200	5.57	58,424	3,249	5.56	56,958	3,267	5.74
Mortgage and home equity	12,076	697	5.77	21,408	1,138	5.32	24,630	1,290	5.24
Credit cards	3,568	495	13.87	5,575	609	10.92	4,574	589	12.88
Other consumer	10,747	795	7.40	14,481	1,146	7.91	15,552	1,150	7.39
Total consumer	26,391	1,987	7.53	41,464	2,893	6.98	44,756	3,029	6.77
Total loans	65,905	4,187	6.35	99,888	6,142	6.15	101,714	6,296	6.19

Other  
interest-earning  
assets

<b>Total interest-earning assets</b>	W 88,009	W 5,331	6.06%	W 128,812	W 7,712	5.99%	W 128,733	W 7,488	5.82%
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Non-interest-earning  
assets:

Cash and cash equivalents	2,165			3,467			3,855		
Other assets	5,990			12,507			16,779		
<b>Total assets</b>	W 96,164	W 5,331		W 144,786	W 7,712		W 149,367	W 7,488	

**Table of Contents****Year Ended December 31,**

	2003			2004			2005		
	Average Balance(1)	Interest Income/ Expense	Yield/ Rate	Average Balance(1)	Interest Income/ Expense	Yield/ Rate	Average Balance(1)	Interest Income/ Expense	Yield/ Rate

(In billions of Won, except percentages)

**Liabilities:**Interest-bearing  
deposits:

Interest-bearing demand deposits	W 2,653	W 37	1.39%	W 7,880	W 105	1.33%	W 6,594	W 125	1.90%
Savings deposits	15,922	232	1.46	21,987	272	1.24	26,100	250	0.96
Certificates of deposit	4,955	220	4.44	6,735	275	4.08	8,838	338	3.81
Other time deposits	27,780	1,164	4.19	41,863	1,605	3.83	39,031	1,439	3.69
Mutual installment deposits	2,110	113	5.36	2,487	113	4.54	1,997	83	4.16

Total  
interest-bearing  
deposits

	53,420	1,766	3.31	80,952	2,370	2.93	82,560	2,235	2.71
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Short-term  
borrowings

	11,400	322	2.82	14,934	370	2.48	14,975	357	2.38
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Secured  
borrowings

	5,331	207	3.88	7,102	299	4.21	6,584	240	3.65
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## Long-term debt

	13,736	703	5.12	20,136	1,099	5.46	22,209	1,182	5.32
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Other  
interest-bearing  
liabilities**Total interest  
bearing  
liabilities**

	W 83,887	W 2,998	3.57%	W 123,124	W 4,138	3.36%	W 126,328	W 4,014	3.18%
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Non-interest-bearing  
liabilities:Non-interest-bearing  
deposits

	1,002			2,287			2,393		
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Trading  
liabilities

	290			668			1,177		
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	1,416			1,539			1,944		
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Acceptance outstanding					
Accrued expenses and other liabilities	5,765		11,455		11,031
Minority interest	428		324		73
Redeemable convertible preferred stock	263		723		585
Stockholders equity	3,113		4,666		5,836
<b>Total liabilities and stockholders equity</b>	<b>W 96,164</b>	<b>W 2,998</b>	<b>W 144,786</b>	<b>W 4,138</b>	<b>W 149,367</b>
Net interest spread(4)		2.48%		2.63%	2.64%
Net interest margin(5)		2.65%		2.78%	2.70%
Average asset liability ratio(6)		104.91%		104.62%	101.90%

*Notes:*

- (1) Average balances are based on (a) daily balances for Shinhan Bank, Chohung Bank and Jeju Bank and (b) quarterly balances for other subsidiaries.
- (2) The average balance and yield on securities are based on amortized cost. The yield on the available-for-sale portfolio is based on average historical cost balances, therefore, the yield information does not give effect to changes in fair value that are reflected as a component of stockholders equity.
- (3) Non-accruing loans are included in the respective average loan balances. Income on such non-accruing loans is no longer recognized from the date the loan is placed on nonaccrual status. We reclassify loans as accruing when interest (including default interest) and principal payments are current.
- (4) The difference between the average rate of interest earned on interest-earning assets and the average rate of interest paid on interest-bearing liabilities.
- (5) The ratio of net interest income to average interest-earning assets.
- (6) The ratio of average interest-earning assets to average interest-bearing liabilities.

**Table of Contents****Analysis of Changes in Net Interest Income Volume and Rate Analysis**

The following tables provide an analysis of changes in interest income, interest expense and net interest income between changes in volume and changes in rates for (i) 2004 compared to 2003 and (ii) 2005 compared to 2004. Volume and rate variances have been calculated on the movement in average balances and the change in the interest rates on average interest-earning assets and average interest-bearing liabilities in proportion to absolute volume and rate change. The variance caused by the change in both volume and rate has been allocated in proportion to the absolute volume and rate change.

	<b>From 2003 to 2004</b>		
	<b>Interest Increase (Decrease)</b>		
	<b>Due to Change in</b>		
	<b>Volume</b>	<b>Rate</b>	<b>Change</b>
	<b>(In billions of Won)</b>		
<b>Increase (decrease) in interest income</b>			
Interest-bearing deposits	W (11)	W (11)	W (22)
Call loans and securities purchased under resale agreements	43	2	45
Trading assets	87	(21)	66
Securities	226	111	337
Loans:			
Commercial and industrial	547	50	597
Other commercial	498	(38)	460
Lease financing	19	(27)	(8)
Total corporate	1,064	(15)	1,049
Mortgage and home equity	500	(59)	441
Credit cards	235	(121)	114
Other consumer	292	59	351
Total consumer	1,027	(121)	906
Total loans	2,091	(136)	1,955
Other interest-earning assets			
Total interest income	2,436	(55)	2,381
<b>Increase (decrease) in interest expense</b>			
Interest bearing deposits:			
Demand deposits	70	(2)	68
Savings deposits	79	(39)	40
Certificates of deposit	74	(19)	55
Other time deposits	547	(106)	441
Mutual installment deposits	19	(19)	
Total interest-bearing deposits	789	(185)	604

Short-term borrowings	91	(43)	48
Secured borrowings	73	19	92
Long-term debt	347	49	396
Other interest-bearing liabilities			
Total interest expense	1,300	(160)	1,140
<b>Net increase (decrease) in net interest income</b>	<b>1,136</b>	<b>105</b>	<b>1,241</b>

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	<b>From 2004 to 2005</b>					
	<b>Interest Increase (Decrease)</b>					
	<b>Due to Change in</b>					
	<b>Volume</b>		<b>Rate</b>		<b>Change</b>	
	<b>(In billions of Won)</b>					
<b>Increase (decrease) in interest income</b>						
Interest-bearing deposits	W	16	W	4	W	20
Call loans and securities purchased under resale agreements		(17)		9		(8)
Trading assets		(12)		(45)		(57)
Securities		(90)		(243)		(333)
Loans:						
Commercial and industrial		17		182		199
Other commercial		(88)		(78)		(166)
Lease financing		(18)		3		(15)
Total corporate		(89)		107		18
Mortgage and home equity		169		(17)		152
Credit cards		(119)		99		(20)
Other consumer		82		(78)		4
Total consumer		132		4		136
Total loans		43		111		154
Other interest-earning assets						
Total interest income		(60)		(164)		(224)
<b>Increase (decrease) in interest expense</b>						
Interest bearing deposits:						
Demand deposits		(19)		39		20
Savings deposits		46		(68)		(22)
Certificates of deposit		81		(18)		63
Other time deposits		(106)		(60)		(166)
Mutual installment deposits		(21)		(9)		(30)
Total interest-bearing deposits		(19)		(116)		(135)
Short-term borrowings		1		(14)		(13)
Secured borrowings		(21)		(38)		(59)
Long-term debt		111		(28)		83
Other interest-bearing liabilities						
Total interest expense		72		(196)		(124)

<b>Net increase (decrease) in net interest income</b>	(132)	32	(100)
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**Table of Contents****Operating Results****2005 Compared to 2004***Net Interest Income*

The following table shows, for the periods indicated, the principal components of our net interest income.

	<b>Year Ended December 31,</b>		
	<b>2004</b>	<b>2005</b>	<b>% Change</b>
<b>(In billions of Won, except percentages)</b>			
<b>Interest and dividend income:</b>			
Interest and fees on loans	W 6,142	W 6,296	2.5%
Interest and dividends on securities	1,265	932	(26.3)
Trading assets	168	111	(33.9)
Other interest income	137	149	8.8
<b>Total interest and dividend income</b>	<b>W 7,712</b>	<b>W 7,488</b>	<b>(2.9)</b>
<b>Interest expense:</b>			
Interest on deposits	W 2,370	W 2,234	(5.7)%
Interest on short-term borrowings	341	340	(0.6)
Interest on secured borrowings	299	240	(19.7)
Interest on long-term debt	1,099	1,182	7.6
Other interest expense	29	18	(37.9)
<b>Total interest expense</b>	<b>4,138</b>	<b>4,014</b>	<b>(3.0)</b>
<b>Net interest income</b>	<b>W 3,574</b>	<b>W 3,474</b>	<b>(2.8)%</b>
<b>Net interest margin(1)</b>	<b>2.78%</b>	<b>2.70%</b>	

*Note:*

(1) The ratio of net interest income to average interest-earning assets. See Average Balance Sheet and Volume and Rate Analysis Average Balance Sheet and Related Interest.

*Interest and dividend income.* The 2.9% decrease in interest and dividend income is due primarily to a 26.3% decrease in interest and dividends on securities, which was partially offset by a 2.5% increase in interest and fees on loans. The average balance of our interest earning assets decreased 0.1% from W128,812 billion in 2004 to W128,733 billion in 2005, principally as a result of the decrease in our average balance of securities.

The 26.3% decrease in interest and dividends on securities was due primarily to a decline by 123 basis points in average yield on securities from 6.05% in 2004 to 4.82% in 2005 and a 7.5% decrease in average balance of securities from W20,924 billion in 2004 to W19,348 billion in 2005. The decline in average yield on securities results primarily from the continuing general decline in average market interest rates during the periods under review and the reduction in interest income in the redemption at maturity of high-interest bearing notes. Approximately 87% of our securities portfolio consists of debt securities issued or guaranteed by the Korean government or government-controlled entities and debt securities issued by financial institutions and other Korean banks as of December 31, 2005.

The 2.5% increase in interest and fees on loans was due primarily to the following:  
a 10.6% increase in interest and fees on commercial and industrial loans from W1,876 billion in 2004 to W2,075 billion in 2005, which was due primarily to an increase by 50 basis points in the average yield on such loans from 5.25% in 2004 to 5.75% in 2005 and a 0.9% increase in average balance of such loans from W35,753 billion in 2004 to W36,079 billion in 2005; and

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a 13.4% increase in interest and fees on mortgage and home equity loans from W1,138 billion in 2004 to W1,290 billion in 2005, which was due primarily to a 15.1% increase in average balance of mortgage and home equity loans from W21,408 billion in 2004 to W24,630 billion in 2005, which was partially offset by a decline of 8 basis points in the average yield on such loans from 5.32% in 2004 to 5.24% in 2005, which more than offset:

a 12.7% decrease in interest and fees on other commercial loans from W1,311 billion in 2004 to W1,145 billion in 2005, which was due primarily to a 6.9% decrease in average balance of other commercial loans from W21,632 billion in 2004 to W20,130 billion in 2005 and a decrease by 37 basis points in the average yield on such loans from 6.06% in 2004 to 5.69% in 2005.

Our loans in 2005 recorded a 1.8% increase in average volume from W99,888 in 2004 to W101,714 in 2005 primarily as a result of increased average balance of consumer loans (except credit cards) as follows:

mortgage and home equity loans increased by 15.1% from W21,408 billion in 2004 to W24,630 billion in 2005, which was partially offset by a decrease in the average yield on such loans by eight basis points from 5.32% in 2004 to 5.24% in 2005; and

other consumer loans increased by 7.4% from W14,481 billion in 2004 to W15,552 billion in 2005, the effect of which was partially offset by a decline of 52 basis points in the average yield on such loans from 7.91% in 2004 to 7.39% in 2005.

As noted, our average yield on loans increased by four basis points from 6.15% in 2004 to 6.19% in 2005, primarily reflecting the improvement in asset quality of our loans, which was partially offset by continuing general decline in average market interest rates during the periods under review and increased competition in the Korean lending market.

Our credit cards experienced a 18.0% decrease in average volume from W5,575 billion in 2004 to W4,574 billion in 2005 due primarily to continued charge-offs of delinquent accounts. The average yield on credit cards increased by 196 basis points from 10.92% in 2004 to 12.88% in 2005 due primarily to the improvement in asset quality of our credit card balances.

*Interest Expense.* Interest expense decreased 3.0% from W4,138 billion in 2004 to W4,014 billion in 2005, due primarily to a 5.7% decrease in interest on deposits and a 19.7% decrease in interest on secured borrowings, which more than offset a 7.6% increase in interest on long-term debt.

The 5.7% decrease in interest expense on deposits from W2,370 billion in 2004 to W2,234 billion in 2005 was primarily the result of a decline of 22 basis points in the cost of interest bearing deposits from 2.93% in 2004 to 2.71% in 2005, which was partially offset by a 2.0% increase in average volume of interest bearing deposits from W80,952 billion in 2004 to W82,560 billion in 2005.

The principal reason for the decline in interest rates payable on our interest-bearing deposits was the general decline in market interest rates. The average interest rate paid on our time deposits other than certificates of deposit, which accounted for 47.3% of our average interest-bearing deposits in 2005, decreased from 3.83% in 2004 to 3.69% in 2005. The average interest rate paid on our savings deposits, which accounted for 31.6% of our average interest-bearing deposits in 2005, decreased from 1.24% in 2004 to 0.96% in 2005. The average interest rate paid on our interest-bearing demand deposits, on the other hand, increased from 1.33% in 2004 to 1.90% in 2005 due primarily to an increase in the interest rate applicable to court deposits.

The increase in average volume of interest bearing deposits is due primarily to a 18.7% increase in average volume of savings deposits from W21,987 billion in 2004 to W26,100 billion in 2005 and a 31.2% increase in average volume of certificate of deposits from W6,735 billion in 2004 to W8,838 billion in 2005, which more than offset a 6.8% decrease in average volume of other time deposits from W41,863 billion in 2004 to W39,031 billion in 2005 and a decrease in the average volume of other deposit products. Our growth in deposit products in 2005 was focused on savings deposits and certificates of deposit because of the growing customer preference for short-term deposit products such as money market deposit accounts due to the decline in

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interest rate payable to interest-bearing deposits. Other time deposits decreased due primarily to an increasing customer aversion to time deposits following the general decline in interest rates payable on interest-bearing deposits.

The 19.7% decrease in interest on secured borrowings was due primarily to a decline in the average interest rate paid by 56 basis points from 4.21% in 2004 to 3.65% in 2005, resulting from the decline in interest rates payable on secured borrowings following the general decline in average market interest rates.

The 7.6% increase in interest expense on long-term debt was due to a 10.4% increase in average volume of long-term debt from W20,136 billion in 2004 to W22,209 billion in 2005 resulting from the issuance of corporate debentures and long-term debt in response to the smaller growth in the volume of deposits compared to the growth in the volume of loans, partially offset by a decline of 14 basis points in average interest rates paid on our long-term debt from 5.46% in 2004 to 5.32% in 2005, which reflects the general decline in average market interest during the period.

*Net interest margin.* Net interest margin represents the ratio of net interest income to average interest earning assets. As net interest income decreased 2.8% from W3,574 billion in 2004 to W3,474 billion in 2005 and the average volume of our interest earning assets decreased 0.1% from W128,812 billion in 2004 to W128,733 billion in 2005, our overall net interest margin decreased eight basis points from 2.78% in 2004 to 2.70% in 2005.

*Provision for credit losses*

Our provision for loan losses was W195 billion in 2004 as compared to a reversal of provision for loan losses of W255 billion in 2005, primarily reflecting a decrease in total allowance for loan losses. The decrease in our total allowance for loan losses reflects continuous improvement in the credit quality of our overall loan portfolios following continued improvements in Korean economy in 2005 as compared to 2004.

The total loan balance increased by W8,768 billion in 2005, and mortgage and home equity loans which are considered to have a lower credit risk than other types of loans accounted for W3,660 billion, or 41.7% of the increase in our total loan balance. On the other hand, our credit card portfolio which is with a higher credit risk decreased by W490 billion in 2005. Our ratio of non-performing loans over total loans slightly decreased to 1.51% as of December 31, 2005 from 1.80% as of December 31, 2004. In addition, our nonaccrual loans, which represent one day and over delinquent loans, decreased to W2,052 billion, or 1.94% of total loans, as of December 31, 2005 from W2,454 billion, or 2.53% of total loans, as of December 31, 2004.

The foregoing contributed to a significant decrease in our provision for loan losses in 2005, which may be further explained by reference to the following:

*changes in the asset quality of individually identified impaired corporate loans* Changes in the asset quality of individually identified impaired corporate loans are attributed to a decrease in the outstanding balance which may result from collection through the disposal of collateral or relaxing requirements for troubled debt restructurings. Such changes have a direct impact on provisioning for loan losses through individual analysis of those loans. See

Item 4. Information on the Company Description of Assets and Liabilities Loans individually identified for review and considered impaired . Specific allowances are established by discounting the estimated cash flows expected to receive using the loan s effective interest rate or by reference to the fair value of the collateral; and

*the improvement in asset quality classifications of loans which are not specially identified as impaired* For loans which are not specially identified as impaired, the general allowance for loan losses is determined based on loss factors taking into consideration past performance of the portfolio, previous loan loss history and charge-off information which are developed through a migration model. See Item 4. Information on the Company Description of Assets and Liabilities Loans not specifically identified as impaired . Due primarily to enhanced condition of the Korean economy, our asset quality classifications of non-impaired loans improved and the loss rates decreased in 2005 as compared to 2004. As a result, provision for loan losses against non-impaired loans decreased from 2004 to 2005.

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The extent of the reversal of provision for credit losses in 2005 were partially offset by an increase in provision for credit losses in respect of unused portions of lines of credits that we extended to our customers, which are not immediately cancelable at our option. In 2004, our provision for credit losses on such unused portions of credit lines was W23 billion. In 2005, following certain guidelines announced by the bank regulatory authorities in Korea, the scope of unused portions of lines of credit that are deemed immediately cancelable at our option has been reduced significantly. Accordingly, the amount of unused portions of lines of credit subject to credit loss provisioning increased compared to 2004. As a result, we raised provisions for losses on such unused portions of lines of credit in the amount of W111 billion in 2005.

The following table sets forth for the periods indicated the components of provision for credit losses by product type.

	<b>As of December 31,</b>		
	<b>2004</b>	<b>2005</b>	<b>% Change</b>
	<b>(In billions of Won, except percentages)</b>		
<b>Total provision for loan losses(A):</b>			
Corporate	W (293)	W (402)	37.2%
Mortgages and home equity	(1)	(1)	
Other consumer	130	76	(41.5)
Credit cards	359	72	(79.9)
	195	(255)	N/M
<b>Total provision for off-balance sheet credit instruments(B):</b>			
Guarantees and acceptances	W (83)	W (39)	(53.0)%
Unused portions of credit line	23	111	382.6
	(60)	72	N/M
<b>Total provision for credit losses (A+B)</b>	<b>W 135</b>	<b>W (183)</b>	<b>N/M</b>

*N/ M = not meaningful.*

Reversal of provision for loan losses against corporate loans increased by 37.2% from W293 billion in 2004 to W402 billion in 2005 due primarily to the improved quality of loans. Our loan loss allowance against corporate loans decreased 28.4% from W1,499 billion as of December 31, 2004 to W1,074 billion as of December 31, 2005 due primarily to due to the improved quality of loans following decreased levels of delinquencies within the portfolio and improved credit quality of impaired loans. Non- performing corporate loans decreased from W1,385 billion as of December 31, 2004 to W1,263 billion as of December 31, 2005, representing 2.4% and 2.2% of the total corporate loan portfolio, respectively. Total net charge offs decreased by 90.5% from W263 billion in 2004 to W25 billion in 2005.

Reversal of provision for loan losses against mortgage and home equity loans remained stable at W1 billion in 2004 and 2005 due primarily to the substantial offset between the effects of the increased volume of loans and the effects of improved quality of loans. Our loan loss allowance against mortgage and home equity loans decreased 47.2% from W36 billion as of December 31, 2004 to W19 billion as of December 31, 2005 while our mortgage and home equity loans increased 16.5% from W22,180 billion as of December 31, 2004 to W25,840 billion as of

December 31, 2005 reflecting the increased demand for such loans. The ratio of non-performing loans to total loans within this portfolio declined from 0.6% in 2004 to 0.4% in 2005.

Our provision for loan losses against other consumer loans decreased 41.5% from W130 billion in 2004 to W76 billion in 2005 primarily reflecting a decrease in the amount of write-offs. Net charge-offs within the other consumer loan portfolio has decreased from W419 billion in 2004 to W261 billion in 2005. Other consumer loans have increased 14.9% from W15,546 billion as of December 31, 2004 to W17,875 billion as of December 31, 2005. However, the allowance for loan losses has decreased 50.3% from W368 billion as of December 31, 2004 to W183 billion as of December 31, 2005, reflecting continued aggressive charge-offs of

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delinquent accounts, decreased levels of delinquencies within the portfolio, and improved credit quality of impaired loans. The ratio of non-performing loans to total loans within this portfolio remained stable at 1.0% as of December 31, 2004 and December 31, 2005.

Our provision for loan losses against credit cards decreased 79.9% from W359 billion in 2004 to W72 billion in 2005 reflecting decreased delinquencies during 2005 and a decrease in the size of the portfolio. Net charge-offs within the credit card portfolio has decreased from W816 billion in 2004 to W244 billion in 2005. Our credit card balances resulted in a 10.4% decrease from W4,732 billion as of December 31, 2004 to W4,242 billion as of December 31, 2005. Our allowance for losses against credit cards has decreased 42.2% from W408 billion as of December 31, 2004 to W236 billion as of December 31, 2005, primarily due to an improvement in overall quality of our credit card assets following continued charge-offs of delinquent accounts. The ratio of non-performing loans to total loans within our credit card portfolio decreased from 1.8% as of December 31, 2004 to 1.1% as of December 31, 2005.

Total provision for off-balance sheet credit instruments increased from 2004 to 2005 due to the reduction in the reversal of guarantees and acceptances and an increase in provision for the unused portions of credit lines. The reduction in the reversal of guarantees and acceptances was primarily due to the improved credit quality of the underlying portfolio. The increase in provision for unused portions of credit lines was primarily due to an increase in the amount of credit lines that were not immediately cancelable at our option. Based on prior industry practice, we considered a substantial portion of our outstanding credit lines with customers as being immediately cancelable at our option during the periods before 2005. During 2005, the Korean bank regulatory authorities strengthened the provisioning for credit losses in respect of unused portions of credit lines under Korean GAAP. In response to, among other things, this bank regulatory guidance, we adopted a more conservative approach in 2005 and applied a narrower definition when identifying which of our outstanding credit lines with customers should be deemed immediately cancelable at our option. Accordingly, the amount of unused portions of lines of credit which became subject to credit loss provisioning increased in 2005, resulting in higher provisions as compared to 2004.

*Noninterest Income*

The following table sets forth for the periods indicated the components of our noninterest income.

	<b>As of December 31,</b>		
	<b>2004</b>	<b>2005</b>	<b>% Change</b>
	<b>(In billions of Won, except percentages)</b>		
<b>Commissions and fees from non-trust management:</b>			
Brokerage fees and commissions(1)	W 232	W 345	48.7%
Other fees and commissions(2)	947	1,160	22.5
Net trust management fees(3)	84	100	19.0
Net trading profits	143	101	(29.3)
Net gains (losses) on securities	(77)	96	N/M
Gain on other investment	53	284	435.8
Net gain on foreign exchange	353	94	(73.4)
Insurance income		189	N/M
Other	357	333	(6.7)
<b>Total noninterest income</b>	<b>W 2,092</b>	<b>W 2,702</b>	<b>29.1%</b>

*Notes:*

- (1) Consists of commissions, fees and markup on securities brokerage activities.
- (2) Includes commissions received on remittance, commissions received on imports and export letters of credit and commissions received from foreign exchange transactions.

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(3) Consists principally of fees from management of trust accounts in our banking operations.

The 29.1% increase in noninterest income was attributable to a 435.8% increase in gain on other investment, our recording of insurance income in 2005 that we did not record in 2004 following the consolidation of Shinhan Life Insurance into our results of operations, our recording of net gain on securities in 2005 as compared to net loss in 2004, a 22.5% increase in other fees and commissions, including commissions received on remittance, and 48.7% increase in brokerage fees and commissions, which more than offset a 73.4% decrease in net gain on foreign exchange. In 2005, we recorded gain on other investment of W284 billion primarily as a result of our sales of equity securities of LG Card and Hynix Semiconductor that we previously received in connection with the debt restructuring of these companies. These sales were made into the market following the expiration of the lock-up period. The W189 billion of insurance income that we recorded in 2005 results from insurance premiums received by Shinhan Life Insurance during the last month of 2005 which was consolidated into our results of operations. We recorded net gain on securities in 2005 compared to net loss on securities in 2004, primarily due to gains from the sale of the equity securities of Ssangyong Motors held by Chohung Bank in 2005 and the absence of significant losses from the write-down of investment securities in 2005 as compared to 2004. The 48.7% increase in brokerage fees and commissions from 2004 to 2005 was due primarily to the increased volume of securities transactions involving the beneficiary certificates sold by investment trust companies. The 22.5% increase in other fees and commissions from 2004 to 2005 was primarily due to the increase in investment banking activities, including, among others, real estate financing, asset-backed securities and project financing. The 73.4% decrease in net gain on foreign exchange reflects the reduced transaction gains as a result of the appreciation of the Korean Won against foreign currencies and the decrease in foreign exchange transaction volume after Shinhan Bank ceased to offer deposit products utilizing the Korean Won and Japanese Yen swaps as described in [Overview](#) [Certain Income Tax Expenses and Provision for Other Losses](#).

*Noninterest Expenses*

The following table shows, for the periods indicated, the components of our noninterest expense.

	<b>Year Ended December 31,</b>		
	<b>2004</b>	<b>2005</b>	<b>% Change</b>
	<b>(In billions of Won, except percentages)</b>		
Employee compensation and other benefits	W 1,217	W 1,480	21.6%
Depreciation and amortization	429	377	(12.1)
General and administrative expenses	543	516	(5.0)
Credit card fees	147	134	(8.8)
Provision for other losses	16	113	N/M
Other fees and commission expenses	364	417	14.6
Taxes (except income taxes)	92	110	19.6
Insurance operating expense		200	N/M
Other	344	315	(8.4)
<b>Total noninterest expenses</b>	<b>W 3,152</b>	<b>W 3,662</b>	<b>16.2%</b>

The 16.2% increase in noninterest expenses was due primarily to our recording insurance operating expenses of W200 billion in 2005 including payment of insurance premiums and provision for insurance payment reserves following the consolidation of operations of Shinhan Life Insurance into our results of operations, a 21.6% increase in employee compensation and severance benefits, which primarily resulted from increase in our salaries and bonuses for our labor force in connection with the harmonization of compensation between Shinhan Bank and Chohung Bank, and

a significant increase in provision for other losses which reflects the additional W49 billion of provisions we raised in anticipation of the losses from our dispute with the Korean National Tax Service in respect of certain deposit products utilizing Korean Won and Japanese Yen swaps as described in [Overview](#) [Certain Income Tax Expenses and Provision for Other Losses](#).

**Table of Contents***Income Tax Expense*

Income tax expense increased from W764 billion in 2004 to W942 billion in 2005 as a result of our increased income and the additional tax expense incurred as a result of the events described in Certain Income Tax Expenses and Provision for Other Losses above. The statutory tax rate was 29.7% in 2004 and 27.5% in 2005.

Our effective rate of income tax increased to 35.0% in 2005 from 32.1% in 2004 due primarily to an increase in expenses not deductible for tax purposes and an increase of valuation allowance on net deferred tax assets that we determined to be unlikely to be available following the split-merger of Chohung Bank's credit card operations into Shinhan Card as described in Critical Accounting Policies Income Taxes .

*Net Income Before Extraordinary Item*

As a result of the foregoing, our net income before extraordinary items increased by 18.9% from W1,462 billion in 2004 to W1,739 billion in 2005.

**2004 Compared to 2003***Net Interest Income*

The following table shows, for the periods indicated, the principal components of our net interest income.

	<b>Year Ended December 31,</b>		
	<b>2003</b>	<b>2004</b>	<b>% Change</b>
	<b>(In billions of Won, except percentages)</b>		
<b>Interest and dividend income:</b>			
Interest and fees on loans	W 4,187	W 6,142	46.7%
Interest and dividends on securities	928	1,265	36.3
Trading assets	102	168	64.7
Other interest expense	114	137	20.2
<b>Total interest and dividend income</b>	<b>W 5,331</b>	<b>W 7,712</b>	<b>44.7</b>
<b>Interest expense:</b>			
Interest on deposits	W 1,766	W 2,370	34.2%
Interest on short-term borrowings	315	341	8.3
Interest on secured borrowings	207	299	44.4
Interest on long-term debt	703	1,099	56.3
Other interest expense	7	29	314.3
<b>Total interest expense</b>	<b>2,998</b>	<b>4,138</b>	<b>38.0</b>
<b>Net interest income</b>	<b>W 2,333</b>	<b>W 3,574</b>	<b>53.2%</b>
<b>Net interest margin(1)</b>	<b>2.65%</b>	<b>2.78%</b>	

*Note:*

(1) The ratio of net interest income to average interest earning assets. See Average Balance Sheet and Volume and Rate Analysis Average Balance Sheet and Related Interest.

*Interest and dividend income.* The 44.7% increase in interest and dividend income is due primarily to the 46.7% increase in interest and fees on loans. The average balance of our interest earning assets increased 46.4% from W88,009 billion in 2003 to W128,812 billion in 2004, principally as a result of the full-year consolidation of Chohung

Bank, while only the four-months result was included in 2003.

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The 46.7% increase in interest and fees on loans was primarily a result of:

a 41.3% increase in commercial and industrial loans from W25,294 billion in 2003 to W35,753 billion in 2004, and an increase by 19 basis points in the average yield on such loans from 5.06% in 2003 to 5.25% in 2004;

a 61.0% increase in other commercial loans from W13,434 billion in 2003 to W21,632 billion in 2004, partially offset by a decline of 27 basis points in the average yield on such loans from 6.33% in 2003 to 6.06% in 2004;

a 77.3% increase in mortgage and home equity loans from W12,076 billion in 2003 to W21,408 billion in 2004, partially offset by a decline of 45 basis points in the average yield on such loans from 5.77% in 2003 to 5.32% in 2004; and

a 34.7% increase in other consumer loans from W10,747 billion in 2003 to W14,481 billion in 2004, and an increase by 51 basis points in the average yield on such loans from 7.40% in 2003 to 7.91% in 2004.

The average volume of our loans increased as a result of full-year consolidation of Chohung Bank, while only the four-months result was included in 2003. Our average yield on loans decreased by 20 basis points from 6.35% to 6.15% primarily as a result of the continuing general decline in average market interest rates during the periods under review. Our average volume growth in consumer loans and the average volume growth in corporate loans are due primarily to the full-year consolidation of Chohung Bank, while only the four-months result was included in 2003.

Interest and dividends on investment securities increased 36.3% from W928 billion in 2003 to W1,265 billion in 2004. Approximately 78.03% of our securities portfolio consists of debt securities issued or guaranteed by the Korean government or government-controlled entities and debt securities issued by financial institutions and other Korean banks as of December 31, 2004. The increase in interest and dividends on investment securities in 2004 was due primarily to the full-year consolidation of Chohung Bank, while only the four-months result was included in 2003.

*Interest Expense.* Interest expense increased 38.0% from W2,998 billion in 2003 to W4,138 billion in 2004, due primarily to a 34.2% increase in interest on deposits and a 56.3% increase in interest on long-term debt.

The 34.2% increase in interest expense on deposits from W1,766 billion in 2003 to W2,370 billion in 2004 was primarily the result of a 51.5% increase in average volume of interest bearing deposits from W53,420 billion in 2003 to W80,952 billion in 2004, partially offset by a decline of 38 basis points in the cost of interest bearing deposits from 3.31% in 2003 to 2.93% in 2004. The principal reason for the increase in average volume of interest bearing deposits is the full-year consolidation of Chohung Bank, while only the four-months result was included in 2003. The principal reason for the decline in interest rates payable on these liabilities is the general decline in market interest rates. The average interest rate paid on our time deposits other than certificates of deposit, which accounted for 51.7% of our average interest-bearing deposits in 2004, decreased from 4.19% in 2003 to 3.83% in 2004 due primarily to a general decline in average market interest rates in 2004. The average interest rate paid on our savings deposits, which accounted for 27.2% of our average interest-bearing deposits in 2004, decreased from 1.46% in 2003 to 1.24% in 2004.

The 46.8% increase in average balance of our interest bearing liabilities was due primarily to a 52.1% increase in average interest-bearing deposits. The 51.5% increase in average interest-bearing deposit volume from W53,420 billion in 2003 to W80,952 billion in 2004 was due to a 50.7% increase in average volume of other time deposits from W27,780 billion in 2003 to W41,863 billion in 2004 and a 38.1% increase in average volume of savings deposits from W15,922 billion in 2003 to W21,987 billion in 2004, resulting from the full-year consolidation of Chohung Bank, while only the four-months result was included in 2003.

The 56.3% increase in interest expense on long-term debt was due to a 46.6% increase in average long-term debt from W13,736 billion in 2003 to W20,136 billion in 2004 resulting from the full-year consolidation of Chohung Bank, while only four month result was included in 2003, and an increase by 34 basis points in average interest rates paid on our long-term debt from 5.12% in 2003 to 5.46% in 2004, which reflects an

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increase in the issuance of subordinated debt which in general carries a higher interest rate and the recognition of a full-year interest on our Redeemable Preferred Stock issued to Korea Deposit Insurance Corporation.

The 44.4% increase in interest on secured borrowings was primarily a result of a 33.2% increase in average secured borrowings from W5,331 billion in 2003 to W7,102 billion in 2004, resulting from the full-year consolidation of Chohung Bank, while only the four-months result was included in 2003.

*Net interest margin.* Net interest margin represents the ratio of net interest income to average interest earning assets. As net interest income increased 53.2% from W2,333 billion in 2003 to W3,574 billion in 2004 and the average volume of our interest earning assets increased 46.4% from W88,009 billion in 2003 to W128,812 billion in 2004, our overall net interest margin increased 13 basis points from 2.65% in 2003 to 2.78% in 2004.

*Provision for credit losses*

Our provision for loan losses decreased 80.7% from W1,011 billion in 2003 to W195 billion in 2004, primarily as a result of the improvement in the asset quality classifications of our portfolio loans retained following enhanced conditions of the Korean economy in 2004 as compared to 2003.

Our ratio of non-performing loans over total loans slightly decreased to 1.80% as of December 31, 2004 from 1.94% as of December 31, 2003. Our nonaccrual loans, which represent one day and over delinquent loans, also decreased to W2,454 billion, or 2.52% of total loans, as of December 31, 2004 from W3,132 billion, or 3.28% of total loans, as of December 31, 2003. The foregoing contributed to a significant decrease in our provision for loan losses in 2004, which may be further explained by reference to the following:

*changes in the asset quality of individually identified impaired corporate loans* Changes in the asset quality of individually identified impaired corporate loans are attributed to a decrease in the outstanding balance which may result from collection through the disposal of collateral or relaxing requirements for troubled debt restructurings. Such changes have a direct impact on provisioning for loan losses through individual analysis of those loans. See

Item 4. Information on the Company Description of Assets and Liabilities Loans individually identified for review and considered impaired . Specific allowances are established by discounting the estimated cash flows expected to receive using the loan's effective interest rate or by reference to the fair value of the collateral;

*the improvement in asset quality classifications of loans which are not specially identified as impaired* For loans which are not specially identified as impaired, the general allowance for loan losses is determined based on loss factors taking into consideration past performance of the portfolio, previous loan loss history and charge-off information which are developed through a migration model. See Item 4. Information on the Company Description of Assets and Liabilities Loans not specifically identified as impaired . Due primarily to enhanced condition of the Korean economy, our asset quality classifications of non-impaired loans improved and the loss rates decreased in 2004 as compared to 2003. As a result, provision for loan losses against non-impaired loans decreased from 2003 to 2004; and

*the effect of adjustments in loss factors* We adjusted loss factors developed through a migration model with other qualitative and quantitative factors that affect the collectibility or the portfolio as of the evaluation date including prevailing economic and business conditions. See Item 4. Information on the Company Description of Assets and Liabilities Loans collectively evaluated for impairment . In 2003, we identified a sharp increase in delinquency ratios of loans to small- and medium-sized enterprises which continued to increase until early 2004. To reflect this trend of performance, we applied shorter period migration rates and recognized additional provision for loan losses in the amount of W76 billion in 2003. In 2004, however, as such analysis showed no adverse trend in the performance of this loan portfolio, the additional allowance for loan losses provided in 2003 was reversed in 2004 and resulted in the decrease in provision for loan losses of W151 billion.

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The following table sets forth for the periods indicated the components of provision for credit losses by product type.

	<b>As of December 31,</b>		
	<b>2003</b>	<b>2004</b>	<b>% Change</b>
	<b>(In billions of Won, except percentages)</b>		
<b>Total provision for loan losses(A):</b>			
Corporate	W 428	W (293)	N/M
Mortgages and home equity	1	(1)	N/M
Other consumer	63	130	106.3%
Credit cards	519	359	(30.8)
	1,011	195	(80.7)
<b>Total provision for off-balance sheet credit instruments(B):</b>			
Guarantees and acceptances	W (46)	W (83)	80.4%
Unused portions of credit line		23	N/M
	(46)	(60)	(30.4)
<b>Total provision for credit losses(A+B)</b>	<b>W 965</b>	<b>W 135</b>	<b>(86.0)%</b>

We recorded reversal of provision for loan losses against corporate loans of W293 billion in 2004 as compared to recording provision for loan losses of W428 billion in 2003 due primarily to a reduction in impaired loans to large corporations including SK Networks, LG Card and Incheon Oil Refinery which were not classified as non-performing. Our loan loss allowance against corporate loans decreased 27.1% from W2,054 billion as of December 31, 2003 to W1,499 billion as of December 31, 2004 due primarily to a decrease in impaired loans. Non-performing corporate loans rose from W1,305 billion as of December 31, 2003 to W1,385 billion as of December 31, 2004, representing 2.4% and 2.5% of the total corporate loan portfolio, respectively. Total net charge offs declined 20.1% from W329 billion in 2003 to W263 billion in 2004.

We recorded a reversal of provision for loan losses against mortgage and home equity loans of W1 billion in 2004 as compared to recording provision for credit losses of W1 billion in 2003 due primarily to the improved quality of loans. Our loan loss allowance against mortgage and home equity loans decreased 32.1% from W53 billion as of December 31, 2003 to W36 billion as of December 31, 2004 while our mortgage and home equity loans increased 8.1% from W20,517 billion as of December 31, 2003 to W22,180 billion as of December 31, 2004 reflecting increased lending corresponding to increased demand. The ratio of non-performing loans to total loans within this portfolio declined from 0.65% in 2003 to 0.57% in 2004.

Our provision for loan losses against other consumer loans increased 106.4% from W63 billion in 2003 to W130 billion in 2004 primarily reflecting an increase in the amount of write-offs. Other consumer loans have increased 6.6% from W14,580 billion as of December 31, 2003 to W15,546 billion as of December 31, 2004. However, the allowance for loan losses has decreased 44.0% from W659 billion as of December 31, 2003 to W368 billion as of December 31, 2004 reflecting the charge-offs of marketing scoring system loans extended by Chohung Bank and decreased levels of delinquencies within the portfolio. The ratio of non-performing loans to total loans within this portfolio declined from 1.6% as of December 31, 2003 to 1.0% as of December 31, 2004 due to an improvement in asset quality of this portfolio.

Our provision for loan losses against credit cards decreased 30.83% from W519 billion in 2003 to W359 billion in 2004 reflecting decreased delinquencies during 2004 and a decrease in the size of the portfolio. The level of net charge-offs within the credit card portfolio have increased from W696 billion in 2003 to W816 billion in 2004. Our credit card balances resulted in a 22.6% decrease from W6,112 billion as of December 31, 2003 to W4,732 billion as of December 31, 2004. Our allowance has decreased 52.8% from W865 billion to W408 billion due to the decrease in volume and an improvement in asset quality. The ratio of

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non-performing loans to total loans within this portfolio decreased from 2.8% as of December 31, 2003 to 1.8% as of December 31, 2004.

The 30.4% decrease in reversal of provision for off-balance credit instruments from 2003 to 2004 was primarily due to the increase in the reversal of guarantees from 2003 and 2004 and the inclusion of provision for unused portions of credit lines in 2004 in respect of unused portions of lines of credit extended to customers that are not immediately cancelable at our option.

*Noninterest Income*

The following table sets forth for the periods indicated the components of our noninterest income.

	As of December 31,		
	2003	2004	% Change
(In billions of Won, except percentages)			
<b>Commissions and fees from non-trust management:</b>			
Brokerage fees and commissions(1)	W 260	W 232	(10.8)%
Other fees and commissions(2)	580	947	63.3
Net trust management fees(3)	59	84	42.4
Net trading profits	72	143	98.6
Net gains (losses) on securities	(128)	(77)	(39.8)
Gain on other investment	28	53	89.3
Net gain on foreign exchange	91	353	287.9
Insurance income			
Other	156	357	128.8
<b>Total noninterest income</b>	<b>W 1,118</b>	<b>W 2,092</b>	<b>87.1%</b>

*Notes:*

- (1) Consists of commissions, fees and markup on securities brokerage activities.
- (2) Includes commissions received on remittance, commissions received on imports and export letters of credit and commissions received from foreign exchange transactions.
- (3) Consists principally of fees from management of trust accounts in our banking operations.

The 87.1% increase in noninterest income was due primarily to a 63.3% increase in other fees and commissions, including commissions received on remittance, letters of credit and foreign exchange transactions, a 287.9% increase in net gain in foreign exchange and a 128.8% increase in other noninterest income, all of which was primarily attributable to the full-year consolidation of Chohung Bank in 2004 while only the four-months results were included in 2003. The 287.9% increase in net gain on foreign exchange was also due to increased foreign exchange transactions corresponding to the increase in Shinhan Bank's deposit products utilizing the Korean Won and Japanese Yen swaps.

**Table of Contents***Noninterest Expenses*

The following table shows, for the periods indicated, the components of our noninterest expense.

	Year Ended December 31,		
	2003	2004	% Change
	(In billions of Won, except percentages)		
Employee compensation and other benefits	W 705	W 1,217	72.6%
Depreciation and amortization	247	429	73.7
General and administrative expenses	392	543	38.5
Credit card fees	90	147	63.3
Provision for other losses		16	N/M
Other fees and commission expenses	250	364	45.6
Taxes (except income taxes)	62	92	48.4
Insurance operating expense			
Other	191	344	80.1
 Total noninterest expenses	 W 1,937	 W 3,152	 62.7%

*N/M= not meaningful*

The 62.7% increase in noninterest expenses was due primarily to full year consolidation of Chohung Bank in 2004 while only four month results were included in 2003 and, to a lesser extent, a 38.5% increase in general and administrative expenses primarily attributable to increased expenses relating to integration of Shinhan Bank and Chohung Bank and a 72.6% increase in employee compensation and other benefits due primarily to an increase in our labor force following our acquisition of Chohung Bank. The 80.1% increase in other noninterest expenses was due primarily to expenses arising from Shinhan Bank's abolishing its cumulative severance payment system.

*Income Tax Expense*

Income tax expense increased from W248 billion in 2003 to W764 billion in 2004 as a result of our increased income. The statutory tax rate was 29.7% in both 2003 and 2004.

Our effective rate of income tax decreased to 32.1% in 2004 from 45.1% in 2003 due primarily to a significant increase in the effective tax rate in 2003 resulting from the anticipated reduction of statutory tax rate from current 29.7% to 27.5% beginning January 2005.

*Net Income Before Extraordinary Item*

As a result of the foregoing and the effect of changes in accounting principles, our net income before extraordinary items increased by 431.6% from W275 billion in 2003 to W1,462 billion in 2004.

**Business Outlook**

As a result of reduced domestic consumption, increase in credit card and other consumer loan delinquencies, lower levels of investments by corporations, increased unemployment, together with the on-going tensions between the United States and North Korea, we expect the Korean economy to continue to experience difficulties, with prospects of recovery remaining uncertain. These weak economic conditions in Korea, coupled with intense competition in the banking sector, will have an adverse impact on us in the near future.

In corporate banking, lending to small- and medium-sized enterprises has long been our core focus of business. Our small- and medium-sized enterprises lending portfolio has grown steadily from a balance of W38,055 billion in 2003 to W38,713 billion in 2004 and to W39,943 billion in 2005. During this period, most



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of the national banks have shifted their focus to, or increased their emphasis on, this type of lending, as opportunities in the large corporate and retail sectors diminish. While we expect the competition in this sector to intensify and result in lower margins from lending to this customer sector, we believe our established customer base, quality brand image and experienced lending staff will provide an opportunity to maintain steady growth in this environment. This increase in lending has brought with it increasing delinquencies in this portion of our portfolio, in particular in loans to the real estate, leasing and service industry and the hotel and leisure industry (principally consisting of hotels, motels and restaurants) in 2004, resulting in higher charge-offs and provisions in 2004 and 2005. We believe that the rate of delinquencies in these industry sectors have begun to slow down in 2005 and expect such trend to continue.

In retail banking, over the past several years, we have experienced a significant growth in home mortgage-based secured consumer lending, both for home purchases as well as for general purpose borrowing through home equity loans. Our mortgage and home equity lending portfolio increased from an average balance of W12,076 billion during 2003 to W21,408 billion during 2004 and to W24,630 billion in 2005. The volume of such lending by us is significantly dependent on competitive conditions, real estate prices, interest rate levels and government policies affecting these markets, and the trends indicated by prior periods will be altered accordingly. In 2006, given the relative low home ownership ratio in Korea, the increasing demand for ownership of larger homes and the growing trend within the newly financially independent young population to seek their own housing, we expect the demand for home mortgage-based secured lending to be fairly strong and the banks to increase their lending. In addition, since the home mortgage-based loans were introduced only in 2004, we believe that the market for such loans has a strong growth potential. We believe that consumer demand for the 15-year or longer term loans is likely to continue to grow given the tax benefits applicable to their interest payments. However, this trend may be counter-balanced by recent regulatory developments in Korea. For example, in the consumer loan sector, the Korean government enacted a number of changes to laws governing retail lending volumes, including the lowering of maximum loan-to-value ratio of mortgage and home equity loans to 60%, and in certain cases to 40%. In recent years, the Korean government has issued several policy-driven regulations to suppress the increasing real estate prices in certain zones of the Seoul Metropolitan area that are in high demand, including the further reduction of maximum loan-to-value ratio applicable to mortgage and home equity loans for real estate in those regulated zones. We have also experienced a significant increase in other consumer loans (principally general unsecured loans) as we seek to diversify our consumer lending portfolio. Our other consumer loans increased from an average balance of W10,747 billion during 2003 to W14,481 billion during 2004 and to W15,552 billion in 2005.

In the credit card business, we have witnessed our customers become more active borrowers until the first half of 2003 as the credit card markets expanded rapidly. Beginning in 2003, however, the growth in credit card usage and balances have been moderated as a result of heightened concerns about increasing delinquencies, credit defaults and asset quality deterioration. Our growth in this sector, represented by Shinhan Card, was not so dramatic as that experienced by other Korean banks and credit card companies, some of whom were shifting from large corporate lending to the credit card sector and others of whom chose to expand more aggressively. Our credit card portfolio growth trend reflects this difference, and this in turn was reflected in a lower level of credit defaults and delinquencies. Three credit card companies, including Shinhan Card, with sound asset quality recorded profit in 2004. The credit card asset size stabilized during 2005 and we also expect a continued improvement in the profitability of the credit card companies in 2006 primarily as a result of a decrease in the provision for credit losses due to improved asset quality and, to a lesser extent, an increase in lending. Our acquisition of Chohung Bank, on the other hand, has led to a significant increase in our credit card assets, including considerable amounts of credit card assets with higher level of delinquencies and credit defaults compared to our credit card assets of Shinhan Card. However, in 2005, our provision for possible losses relating to the credit card assets of Chohung Bank decreased significantly compared to prior years. Simultaneous with the merger of Shinhan Bank and Chohung Bank, the credit card division of Chohung Bank was merged into Shinhan Card in April 2006. We believe that the credit card industry has improved its overall asset quality resulting in lower provisioning for loan losses. Our future outlook for our credit card business, however, will largely depend on whether we will be able to acquire LG Card and, if so, the form of the acquisition as well as the overall asset quality of the credit card assets of LG Card. See Item 3. Key Information of the Company Risk Factors Developments adversely affecting the business



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and liquidity of credit card companies in Korea, including LG Card, may result in losses in respect of our exposure to such companies .

In securities brokerage services, we expect an increase in brokerage fees and commissions due primarily to improving stock market performance based on increased investment in equity funds by individual investors, growing interest in asset management products and anticipated improvement in corporate earnings, as well as an anticipated increase in volume through the use of our banking network to promote our securities brokerage services and products.

We believe that, over the long term, the establishment of the Shinhan Financial Group as a diversified financial services platform and the addition of subsidiaries, such as Chohung Bank and Shinhan Life Insurance, to that platform will provide significant opportunities to enhance our prospects as and when economic conditions improve.

**Results by Principal Business Segment Under Korean GAAP**

During 2005, we were organized into twelve major business segments as follows:

Shinhan Bank, further consisting of the following:

retail banking;

corporate banking;

treasury and securities investment; and

other banking services;

Chohung Bank, further consisting of the following:

retail banking;

corporate banking;

treasury and international business;

credit card; and

other banking services;

securities brokerage services of Good Morning Shinhan Securities;

credit card services of Shinhan Card; and

others.

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The following discussion of our results of operations by principal business segment is provided on a Korean GAAP basis since this is the basis of accounting that we currently use to manage our business. Our chief operating decision maker regularly makes decisions about resources to be allocated to these activities and assesses performance of the activities using this information, and consequently this forms the basis of our segment reporting included in Note 34 to our consolidated financial statements in Item 18. Financial Statements Notes to consolidated financial statements of Shinhan Financial Group .

	Segment Results(1)			Total Revenues(2)		
	Year Ended December 31,					
	2003	2004	2005	2003	2004	2005
(In billions of Won, except percentages)						
Shinhan Bank:						
Retail banking	W 560	W 655	W 778	W 1,221	W 1,401	W 1,350
Corporate banking	212	550	701	749	1,006	976
Treasury and securities investment	62	82	(67)	904	1,292	1,745
Other banking services	(148)	(87)	(346)	339	469	245
Chohung Bank:(3)						
Retail banking	30	132	307	513	1,395	1,385
Corporate banking	(58)	185	95	133	333	407
Treasury and international business	(53)	(5)	(26)	208	2,611	3,379
Credit card	(89)	(320)	150	237	590	699
Other banking services	(50)	275	169	(3)	498	573
Good Morning Shinhan Securities	69	44	121	656	697	880
Shinhan Card	(90)	6	59	322	348	358
Other subsidiaries	36	10	39	305	355	620
Total(4)	W 481	W 1,527	W 1,980	W 5,584	W 10,995	W 12,617

*Notes:*

- (1) Represents income per segment before income taxes.
- (2) Represents net interest income plus noninterest income.
- (3) As we acquired Chohung Bank in August 2003, the segment results for Chohung Bank only reflect the results of operations from the date of our acquisition to December 31, 2003 and is not available on a meaningful comparative basis.
- (4) Before elimination or adjustments.

**Table of Contents*****Shinhan Bank's Retail Banking***

Shinhan Bank's retail banking segment products include mortgage and home equity loans and other consumer loans, deposits and other savings products.

	Year Ended December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
(In billions of Won)					
<b>Income statement data</b>					
Net interest income	W 782	W 844	W 959	7.9%	13.6%
Noninterest income	439	557	391	26.9	(29.8)
Total revenues	1,221	1,401	1,350	14.7	(3.6)
Provision for credit losses(1)	(64)	(30)	(11)	(53.1)	(63.3)
Noninterest expense including depreciation and amortization	(597)	(716)	(561)	19.9	(21.6)
Segment results(2)	W 560	W 655	W 778	17.0%	18.8%

*Notes:*

(1) Includes provision for guarantees and acceptances. We recorded no such provision in 2003, 2004 and 2005.

(2) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result increased by 18.8% from W655 billion in 2004 to W778 billion in 2005.

The 13.6% increase in net interest income from retail banking activities was due primarily to an increase in average lending volume to individuals and households, particularly, mortgage and home equity loans, which more than offset the effects of an increase in average deposits, particularly, certificates of deposits, and the decrease in net interest margin.

The increase in average lending volume to individuals, mortgage and home equity loans in particular, is due primarily to the continuing trend and preference by commercial banks, including ourselves, to lend to consumers on a secured basis. The increase in average deposits, certificate of deposits in particular, is due primarily to customer demand for short-term deposit products in Korean Won which was partially offset by the decrease in time deposit products that utilize Korean Won and Japanese Yen swaps after such deposits were found to be subject to taxation. We are currently experiencing a dispute with the Korean National Tax Service in respect of these time deposit products as described in [Overview](#) [Certain Income Tax Expenses and Provision for Other Losses](#).

Noninterest income decreased by 29.8% due primarily to a decrease in transaction volume of derivatives resulting from the decrease in time deposit products that utilize Korean Won and Japanese Yen swaps as described above, which was partially offset by an increase in agency fees and commissions income from increased level of cross-selling bancassurance, investment trust funds and asset management products, which we attribute to our customers' response to the generally low interest rate environment.

Provision for credit losses on consumer loans decreased by 63.3% due primarily to improved asset quality despite the increase in Shinhan Bank's average lending volume.

Noninterest expense including depreciation and amortization decreased by 21.6% from W716 billion in 2004 to W561 billion in 2005, due primarily to a decrease in costs attributable to time deposit products that utilize Korean Won and Japanese Yen swaps, which we ceased to offer during 2005 following the adverse tax rulings, which more

than offset an increase in salaries, wages, employee welfare and benefits paid to Shinhan Bank's employees.

**Table of Contents***Comparison of 2004 to 2003*

Our overall segment result increased by 17.0% from W560 billion in 2003 to W655 billion in 2004.

The 7.9% increase in net interest income from retail banking activities was due primarily to an increase in average lending volume to individuals and households, particularly, mortgage and home equity loans, partially offset by an increase in average deposits, particularly, time deposits.

The increase in average lending volume to individuals, mortgage and home equity loans in particular, is due primarily to the trend and preference by commercial banks, including ourselves, to lend to consumers on a secured basis. The increase in average deposits, time deposits in particular, is due primarily to customer demand for stable time deposit products in Korean Won and the increase in time deposit products that utilize Korean Won and Japanese Yen swaps, the return on which deposit were initially deemed to be tax-free. We are currently experiencing a dispute with the Korean National Tax Service in respect of these time deposit products as described in *Overview* *Certain Income Tax Expenses and Provision for Other Losses*.

Noninterest income increased by 26.9% due primarily to an increase in gross gains from derivatives transactions and an increase in gains from foreign currency transactions, each as a result of increase in transaction volume, partially offset by a decrease in agency fees and commissions income from cross-selling products of our other subsidiaries through Shinhan Bank's retail banking branch network. Agency fees decreased due primarily to a decrease in agency fees from credit card operations, which was substantially offset by increases in agency fees from cross-selling bancassurance products and beneficiary certificates.

Provision for credit losses on consumer loans decreased by 53.1% due primarily to improved asset quality despite the increase in Shinhan Bank's average lending volume.

Noninterest expense including depreciation and amortization increased by 19.9% from W597 billion in 2003 to W716 billion in 2004, due primarily to an increase in gross losses from derivatives transactions, resulting from higher transaction volume and increased employee welfare and benefits paid to Shinhan Bank's employees, which more than offset a decrease in fees for perfecting security interests and related legal and administrative expenses.

***Shinhan Bank's Corporate Banking***

Shinhan Bank's large corporate banking segment handles its transactions with all of its corporate customers, including small- and medium-sized enterprises, *chaebols* and public enterprises. Activities within the segment include loans, overdrafts and other credit facilities, gathering deposits and investment banking activities.

	Year Ended December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
(In billions of Won)					
<b>Income statement data</b>					
Net interest income	W 434	W 530	W 579	22.1%	9.2%
Noninterest income	315	476	397	51.1	(16.6)
Total revenues	749	1,006	976	34.3	(3.0)
Provision for credit losses(1)	(273)	(66)	(12)	(75.8)	(81.8)
Noninterest expense including depreciation and amortization	(264)	(390)	(263)	47.7	(32.6)
Segment results(2)	W 212	W 550	W 701	159.4%	27.5%

*Notes:*

(1) Includes provision for guarantees and acceptances. We recorded no such provision in 2003, 2004 and 2005.

(2) Net income per segment before income taxes.

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*Comparison of 2005 to 2004*

Our overall segment result increased by 27.5% from W550 billion in 2004 to W701 billion in 2005, due primarily to a W127 billion decrease in noninterest expense including depreciation and amortization and a W54 billion decrease in provision for credit losses during the period under review.

Net interest income increased by 9.2% due primarily to an increase in average volume of lending to small- and medium-sized enterprises, which results primarily from the continued growth in the small- and medium-sized lending market, together with Shinhan Bank's continued efforts to focus its marketing on this customer sector to achieve growth, which more than offset the effects of increased funding cost resulting from an increase in average balance of certificates of deposits.

Noninterest income decreased by 16.6% due primarily to a decrease in gross gains from derivatives transactions resulting from a volume increase in derivatives transactions, which more than offset an increase in fees and commissions from Shinhan Bank's investment banking activities, including asset-backed securitization, and gains on investment securities, including gains from sale of investment securities, dividends and valuation gains using the equity method of accounting.

Provision for credit losses on corporate loans decreased by 81.8% due primarily to improved asset quality despite the increase in Shinhan Bank's average lending volume.

Noninterest expense including depreciation and amortization decreased by 32.6% due primarily to a decrease in gross losses from derivatives transactions, resulting from a volume increase in derivatives transactions.

*Comparison of 2004 to 2003*

Our overall segment result increased by 159.4% from W212 billion in 2003 to W550 billion in 2004, due primarily to a W257 billion increase in total revenues and a W207 billion decrease in provision for credit losses during the period under review.

Net interest income increased by 22.1% due primarily to the increase in average volume of lending to small- and medium-sized enterprises, which results primarily from the continued growth in the small- and medium-sized lending market, together with Shinhan Bank's continued efforts to focus its marketing on this customer sector to achieve growth.

Noninterest income increased by 51.1% due primarily to an increase in gross gains from derivatives transactions and, to a lesser extent, an increase in fees and commissions from Shinhan Bank's investment banking activities, including asset-backed securitization.

The lower level of provision for credit losses in 2004 is due primarily to resolutions of credit problems experienced by certain large corporate borrowers, including SK Networks and LG Card.

Noninterest expense including depreciation and amortization increased by 47.7% due primarily to an increase in gross losses from derivatives transactions, resulting from a volume increase in derivatives transactions.

**Table of Contents*****Shinhan Bank's Treasury and Securities Investment***

Shinhan Bank's treasury and securities investment segment primarily handles the trading of and investment in debt securities and, to a lesser extent, in equity securities for its own accounts, handling its treasury activities such as correspondence banking, and entering into derivatives transactions.

	Year Ended December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
(In billions of Won)					
<b>Income statement data</b>					
Net interest income (expense)	W 65	W 4	W (272)	(93.8)%	N/M
Noninterest income	839	1,288	2,017	53.5	56.6%
Total revenues	904	1,292	1,745	42.9	35.1
Provision for credit losses	11	(8)		N/M	N/M
Noninterest expense including depreciation and amortization	(853)	(1,202)	(1,812)	40.9	50.7
Segment results(1)	W 62	W 82	W (67)	32.3%	N/M

*N/M = not meaningful*

*Note:*

(1) Net income per segment before income taxes.

***Comparison of 2005 to 2004***

Our overall segment result recorded a loss of W67 billion in 2005 as compared to a gain of W82 billion in 2004.

We recorded net interest expense of W272 billion in 2005 as compared to net interest income of W4 billion in 2004, due primarily to a decrease in interest and dividend income from securities resulting from the low average market interest rates and a decrease in interest income from foreign currency-denominated loans following the appreciation of the Korean Won against foreign currencies.

Noninterest income increased by 56.6% from W1,288 billion in 2004 to W2,017 billion in 2005 due primarily to an increase in gains from increased volume of derivatives transactions, principally foreign exchange hedging and advisory services, as well as an increase in gains from foreign currency transactions resulting from the appreciation of the Korean Won against foreign currencies.

In 2005, Shinhan Bank did not record any provision for credit losses in this segment as compared to provisions for loan losses of W8 billion in 2004 since no event occurred during 2005 that required Shinhan Bank to adjust provision for credit losses in this segment.

Noninterest expense including depreciation and amortization increased by 50.7% due primarily to an increase in derivative liabilities resulting from an increase in volume of back-to-back transactions to cover risk exposures that arose in connection with Shinhan Bank's transactions with customers and an increase in losses from foreign currency transactions with customers.

***Comparison of 2004 to 2003***

Our overall segment result increased by 32.3% from W62 billion in 2003 to W82 billion in 2004.

Net interest income decreased by 93.8% due primarily to a decrease in the volume of investment portfolio.

Noninterest income increased by 53.5% from W839 billion in 2003 to W1,288 billion in 2004 due primarily to an increase in gains from increased volume of Shinhan Bank's derivatives transactions with customers as well as an increase in gains from foreign currency transactions with customers.



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In 2004, Shinhan Bank recorded provision for credit losses in this segment of W8 billion in 2004 as compared to a reversal of provisions for loan losses of W11 billion in 2003. The provision for credit losses in 2004 resulted from Shinhan Bank's converting its credit exposure to LG Card to equity in connection with the rescue plan for LG Card. The reversal of provision for credit losses in 2003 was necessary to make adjustments in the contra-account to reflect increased provisioning in Shinhan Bank's overseas branches.

Noninterest expense including depreciation and amortization increased by 40.9% due primarily to an increase in derivative liabilities resulting from an increase in volume of back-to-back transactions to cover risk exposures that arose in connection with Shinhan Bank's transactions with customers, an increase in losses from foreign currency transactions with customers and, to a lesser extent, valuation losses from Shinhan Bank's equity investment in Shinhan Finance Limited, which was partially offset by decreases in impairment losses from securities and losses from dispositions of securities.

***Shinhan Bank's Other Banking Services***

The revenue-generating activities in this segment consist primarily of Shinhan Bank's trust account management services and any gains and losses from our overseas branches. This segment also reflects the expenses and provision for credit losses of Shinhan Bank that are not, as a matter of management policy, allocated to either retail banking or corporate banking.

For management reporting purposes, each of the retail banking and corporate banking segments computes and reflects provision for credit losses that are discounted based on average balances of loans to show a meaningful comparison of performance within and *vis-à-vis* other activities. This has the effect of understating the provision for credit losses that are reflected in our segment reporting as compared to the bankwide provision for credit losses reflected in Shinhan Bank's financial statements. The excess provision for credit losses arising from the difference in computations are not allocated to retail banking or corporate banking but are reflected in this segment. As a result, segment results will generally be in the negative. In 2003, 2004 and 2005, those excess provision for credit losses that were not allocated to either retail banking or corporate banking amounted to W86 billion, W124 billion and W166 billion, respectively. In addition, in 2005, Shinhan Bank raised W99 billion of other provisions as a result of our new policy to establish allowance for losses on unused portions of lines of credits extended to its customers in accordance with guidelines announced by the Financial Supervisory Service.

In addition, Shinhan Bank frequently issues subordinated debt securities, which carry interests that are higher than market interest rates. As subordinated debt securities has the overall effect of improving Shinhan Bank's capital adequacy and benefits Shinhan Bank in its entirety, the management believes it is inappropriate to allocate the higher costs associated with issuing subordinated debt to a particular business segment. Accordingly, we allocate and reflect the difference between the higher costs associated with subordinated debt and market interest rates in this segment as interest expenses.

	Year Ended December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
(In billions of Won)					
<b>Income statement data</b>					
Net interest income	W 212	W 182	W 151	(14.2)%	(17.0)%
Noninterest income	127	287	94	126.0	(67.2)
Total revenues	339	469	245	38.3	(47.8)
Provision for credit losses(1)	(109)	(98)	(150)	(10.1)	53.1
Noninterest expense including depreciation and amortization	(378)	(458)	(441)	21.2	(3.7)

Segment results(2)	W (148)	W (87)	W (346)	(41.2)%	297.7%
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**Table of Contents***Notes:*

(1) Includes provision for guarantees and acceptances of W(0.3) billion, W(1.0) billion and W21.0 billion in 2003, 2004 and 2005, respectively.

(2) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result increased from a loss of W87 billion in 2004 to a loss of W346 billion in 2005, showing a 297.7% increase, primarily as a result of a 67.2% decrease in noninterest income combined with a 53.1% increase in provision for credit losses.

Net interest income decreased by 17.0% due primarily to a decrease in recoveries of interest on non-performing loans by Shinhan Bank's division in charge of collection on such non-performing loans, which in turn resulted from a decrease in volume of non-performing loans following improvement in overall asset quality of Shinhan Bank's loan portfolio, and, to a lesser extent, a decrease in net interest income from Shinhan Bank's overseas subsidiaries, reflecting the appreciation of the Korean Won against foreign currencies.

Noninterest income decreased by 67.2% due primarily to the sale by Shinhan Bank of common shares of the holding company in March 2004, resulting in a gain of W228 billion in the prior period, and the effect of eliminating certain double-counting between segments of investment banking and derivatives transactions.

Provision for credit losses increased by 53.1% due to additional provisioning on mortgage and home equity loans required by the Financial Supervisory Service and the increased provisioning on unused portions of credit lines to customers during 2005, all of which provisions were allocated to this business segments, despite improved asset quality of Shinhan Bank's overall loan portfolio.

Noninterest expense including depreciation and amortization decreased by 3.7% due primarily to the incurrence of W95 billion of expenses relating to the change in Shinhan Bank's employee retirement in 2004, which was substantially offset by the increases in salaries and wages to Shinhan Bank's employees and donations and contributions in 2005.

*Comparison of 2004 to 2003*

Our overall segment result improved from a loss of W148 billion in 2003 to a loss of W87 billion in 2004, showing a 41.2% decrease, primarily as a result of a 126.0% increase in noninterest income combined with a 10.1% decrease in provision for credit losses.

Net interest income decreased by 14.2% due primarily to a decrease in market interest which we use to record interest from inter-segment lendings and borrowings and, to a lesser extent, a decrease in net interest income from Shinhan Bank's overseas subsidiaries, reflecting the appreciation of the Korean Won against foreign currencies.

Noninterest income increased by 126.0% due primarily to the sale by Shinhan Bank of common shares of the holding company in March 2004, resulting in a gain of W228 billion, partially offset by the effect of eliminating certain double-counting between segments of investment banking and derivatives transactions.

Provision for credit losses decreased by 10.1% due to a lower amount of allocation of provisions to Shinhan Bank's other business segments based on average balance calculation and decreased provisioning at Shinhan Bank's overseas branches in 2004 resulting from improved asset quality of exposures to SK Networks.

Noninterest expense including depreciation and amortization increased by 21.2% due primarily to the incurrence of W95 billion of expenses relating to the change in Shinhan Bank's employee retirement plan.

**Table of Contents*****Chohung Bank's Retail Banking***

Chohung Bank's retail banking segment products include mortgage and home equity loans and other consumer loans, deposits and other savings products.

		From		Year Ended		% Change	
		September 1 to December 31, 2003	2004	December 31, 2005	2003/2004	2004/2005	
(In billions of Won)							
<b>Income statement data</b>							
Net interest income	W	418	W 1,107	W 1,081	164.8%	(2.3)%	
Noninterest income		95	288	304	203.2	5.6	
Total revenues		513	1,395	1,385	171.9	(0.7)	
Provision for credit losses		(150)	(466)	(246)	210.7	(47.2)	
Noninterest expense including depreciation and amortization		(333)	(797)	(832)	139.3	4.4	
Segment results(1)	W	30	W 132	W 307	340.0%	132.6%	

*Note:*

(1) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result increased by 132.6% from W132 billion in 2004 to W307 billion in 2005.

The 2.3% decrease in net interest income from retail banking activities was due primarily to the effects of an increase in average deposits and the decrease in net interest margin which more than offset an increase in average lending volume.

The increase in average deposits is due primarily to customer demand for short-term deposit products in Korean Won. We attribute the decrease in net interest margin to the low market interest environment. The increase in average lending volume to individuals, mortgage and home equity loans in particular, is due primarily to the continuing trend and preference by commercial banks, including ourselves, to lend to consumers on a secured basis.

Noninterest income increased by 5.6% due primarily to an increase in agency fees and commissions income from increased level of cross-selling bancassurance, investment trust funds and asset management products, which we attribute to our customers' response to the generally low interest rate environment.

Provision for credit losses on consumer loans decreased by 47.2% due primarily to improved asset quality despite the increase in Chohung Bank's average lending volume.

Noninterest expense including depreciation and amortization increased by 4.4% from W797 billion in 2004 to W832 billion in 2005, due primarily to an increase in salaries, wages, employee welfare and benefits paid to Chohung Bank's employees and payments of consulting fees in connection branch network reconfiguration in anticipation of Chohung Bank's merger with Shinhan Bank in 2006.

*Comparison of 2004 to 2003*

Since we acquired Chohung Bank in August 2003, the segment results relating to Chohung Bank's business for the year ended December 31, 2003 only exist from September 1, 2003 to December 31, 2003 while Chohung Bank's segment results for the year ended December 31, 2004 reflects the segment results and other income statement information for this segment for the full year ended December 31, 2004. As a result, the comparison of the two periods is not available on a comparable basis and thus is not meaningful.



**Table of Contents*****Chohung Bank's Corporate Banking***

Chohung Bank's large corporate banking segment handles its transactions with all of its corporate customers, including small- and medium-sized enterprises, chaebols and public enterprises. Activities within the segment include loans, overdrafts and other credit facilities, gathering deposits and investment banking activities.

		From		Year Ended		% Change	
		September 1 to December 31, 2003	December 31, 2004	2005	2003/2004	2004/2005	
<b>(In billions of Won)</b>							
<b>Income statement data</b>							
Net interest income	W	62	W 258	W 294	316.1%	14.0%	
Noninterest income		71	75	113	5.6	50.7	
Total revenues		133	333	407	150.4	22.2	
Provision for credit losses(1)		(145)	12	(111)	N/M	N/M	
Noninterest expense including depreciation and amortization		(46)	(160)	(201)	247.8	25.6	
Segment results(2)	W	(58)	W 185	W 95	419.0%	(48.6)%	

*Notes:*

(1) Includes provision for guarantees and acceptances of W(35) billion in 2003, W(22) billion in 2004 and W(49) billion in 2005.

(2) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result decreased by 48.6% from W185 billion in 2004 to W95 billion in 2005, due primarily to a W111 billion decrease in provision for credit losses recorded in 2005 as compared to a reversal of W12 billion in 2004 and a W41 billion increase in noninterest expense including depreciation and amortization, which more than offset a W74 billion increase in total revenues.

Net interest income increased by 14.0% due primarily to an increase in average volume of lending to small- and medium-sized enterprises, which results primarily from the continued growth in the small- and medium-sized lending market, together with Chohung Bank's continued efforts to focus its marketing on this customer sector to achieve growth.

Noninterest income increased by 50.7% due primarily to an increase in fees and commissions from export and import-related trade financing that Chohung Bank focused on during 2005 and increased fees and commissions from transactions, such as foreign exchange transactions and discounting of commercial paper.

We recorded W111 billion in provisions for credit losses in 2005 as compared to W12 billion reversal of provisions for credit losses in 2004, due primarily to the new regulation introduced by the Financial Supervisory Service which required our banking subsidiaries to establish allowance for losses on unconfirmed guarantees & acceptances and commitments.

Noninterest expense including depreciation and amortization increased by 25.6% due primarily to an increase in salaries, wages, employee welfare and benefits paid to Chohung Bank's employees.

*Comparison of 2004 to 2003*

Since we acquired Chohung Bank in August 2003, the segment results relating to Chohung Bank's business for the year ended December 31, 2003 only exist from September 1, 2003 to December 31, 2003 while Chohung Bank's segment results for the year ended December 31, 2004 reflects the segment results and

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other income statement information for this segment for the full year ended December 31, 2004. As a result, the comparison of the two periods is not available on a comparable basis and thus is not meaningful.

**Chohung Bank's Treasury and International Business**

Chohung Bank's treasury and international business segment primarily handles the trading of and investment in debt securities and, to a lesser extent, in equity securities for its own accounts, handling its treasury activities such as correspondence banking, and entering into derivatives transactions and any gains and losses from our overseas branches and subsidiaries.

	From		Year Ended		% Change	
	September 1 to	December 31,	December 31,	December 31,	2003/2004	2004/2005
	2003	2004	2004	2005		
(In billions of Won)						
Net interest income (expense)	W (26)	W (1)	W 45		(96.2)%	N/M
Noninterest income	234	2,612	3,334		N/M	27.6%
Total revenues	208	2,611	3,379		N/M	29.5
Provision for credit losses		13	40		N/M	207.7
Noninterest expense including depreciation and amortization	(261)	(2,629)	(3,445)		N/M	31.0
Segment results(1)	W (53)	W (5)	W (26)		(90.6)%	N/M

*N/M = not meaningful*

*Note:*

(1) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result deteriorated significantly from a loss of W5 billion in 2004 to a loss of W26 billion in 2005.

We recorded net interest income of W45 billion in 2004 as compared to net interest expense of W1 billion in 2005, due primarily to an increase in interest income from foreign currency-denominated loans as the average interest rates on such loans increased by 52 basis points from 2.96% to 3.48%, together with a decrease in interest expenses on Won-denominated borrowings resulting from a decrease in the average balance of such borrowings.

Noninterest income increased by 27.6% from W2,612 billion in 2004 to W3,334 billion in 2005, due primarily to gains from sale of available-for-sale securities, gains on foreign exchange transactions and net gains on derivative trading resulting from an increased volume of derivatives transactions, principally foreign exchange hedging and advisory services, as well as an increase in gains from foreign currency transactions resulting from the appreciation of the Korean Won against foreign currencies.

We recorded reversal of provision for credit losses in the amount of W40 billion in 2005, a 207.7% increase from a reversal of provision for credit losses in the amount of W13 billion in 2004 due primarily to the improvement in our asset quality, in particular the quality of our foreign currency-denominated loans.

Noninterest expense including depreciation and amortization increased by 31.0% due primarily to losses recorded on sales of trading securities in 2005.

*Comparison of 2004 to 2003*

Since we acquired Chohung Bank in August 2003, the segment results relating to Chohung Bank's business for the year ended December 31, 2003 only exist from September 1, 2003 to December 31, 2003 while Chohung Bank's segment results for the year ended December 31, 2004 reflects the segment results and

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other income statement information for this segment for the full year ended December 31, 2004. As a result, the comparison of the two periods is not available on a comparable basis and thus is not meaningful.

***Chohung Bank's Credit Card***

Chohung Bank's segment handles credit card activities primarily managed by BC Card, Chohung Bank's credit card business.

	From		Year Ended		% Change	
	September 1 to December 31, 2003		December 31, 2004	2005	2003/2004	2004/2005
(In billions of Won)						
<b>Income statement data</b>						
Net interest income	W	237	W 588	W 599	148.1%	1.9%
Noninterest income			2	100	N/M	N/M
Total revenues		237	590	699	148.9	18.5
Provision for credit losses		(199)	(673)	(392)	238.2	(41.7)
Noninterest expense including depreciation and amortization		(127)	(237)	(157)	86.6	(33.8)
Segment results(1)	W	(89)	W (320)	W 150	259.6%	N/M

*Note:*

(1) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result improved from a loss of W320 billion in 2004 to a gain of W150 billion in 2005.

Net interest income increased by 1.9% due primarily to a decreased level of delinquencies on Chohung Bank's credit card assets.

Noninterest income increased from W2 billion in 2004 to W100 billion in 2005 due primarily to gains from sale of written-off credit card receivables in 2005 amounting to W93 billion.

Provision for credit losses decreased by 41.8% as a result of continued improvement in the asset quality of Chohung Bank's credit card assets.

Noninterest expense including depreciation and amortization decreased by 33.8% due primarily to a decrease in losses from sale of credit card loans corresponding to a decrease in volume of sale of such loans in 2005 as compared to 2004.

*Comparison of 2004 to 2003*

Since we acquired Chohung Bank in August 2003, the segment results relating to Chohung Bank's business for the year ended December 31, 2003 only exist from September 1, 2003 to December 31, 2003 while Chohung Bank's segment results for the year ended December 31, 2004 reflects the segment results and other income statement information for this segment for the full year ended December 31, 2004. As a result, the comparison of the two periods is not available on a comparable basis and thus is not meaningful.

***Chohung Bank's Other Banking Services***

The revenue-generating activities in this segment consist primarily of Chohung Bank's merchant banking business and trust account management services. Chohung Bank's merchant banking segment products include short-term financing for both deposit and lending sides, including cash management accounts,



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factoring financing and bill discounting, leasing, investment banking activities, mergers and acquisitions advice, and project financing services. This segment also reflects the expenses incurred by Chohung Bank's support and management functions performed at the headquarters level, including Chohung Bank's risk management and information technology systems.

	From		Year Ended		% Change	
	September 1 to December 31, 2003	December 31, 2004	2004	2005	2003/2004	2004/2005
<b>(In billions of Won)</b>						
<b>Income statement data</b>						
Net interest income (expense)	W	(10)	W 138	W 53	N/M	(61.6)%
Noninterest income		7	360	521	N/M	44.8
Total revenues		(3)	498	574	N/M	15.1
Provision for credit losses			83	73	N/M	(12.0)
Noninterest expense including depreciation and amortization		(47)	(306)	(478)	N/M	56.2
Segment results(1)	W	(50)	W 275	W 169	N/M	(38.9)%

*Note:*

(1) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result decreased by 38.9% from a gain of W275 billion in 2004 to a gain of W169 billion in 2005.

The 61.6% decrease in net interest income was due primarily to decreases in average interest rates and average volume of loans to large corporate customers reflected in Chohung Bank's merchant banking accounts.

The 44.8% increase in noninterest income was due primarily to an increase in upfront fees for arranging loans as a result of the increased number of loan transactions of such loans and increased fees and commissions from trust-related products.

Noninterest expense including depreciation and amortization increased by 56.2%, due primarily to an increase in general and administrative expenses principally related to severance benefits for a special program for voluntary retirements.

*Comparison of 2004 to 2003*

Since we acquired Chohung Bank in August 2003, the segment results relating to Chohung Bank's business for the year ended December 31, 2003 only exist from September 1, 2003 to December 31, 2003 while Chohung Bank's segment results for the year ended December 31, 2004 reflects the segment results and other income statement information for this segment for the full year ended December 31, 2004. As a result, the comparison of the two periods is not available on a comparable basis and thus is not meaningful.

**Table of Contents****Securities Brokerage Services**

Securities brokerage services segment primarily reflects securities brokerage and dealing services on behalf of customers, which is conducted by Good Morning Shinhan Securities, our principal securities brokerage subsidiary.

	Year Ended December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
(In billions of Won)					
<b>Income statement data</b>					
Net interest income	W 34	W 54	W 63	58.8%	16.7%
Noninterest income	622	643	817	3.4	27.1
Total revenues	656	697	880	6.3	26.3
Provision for credit losses		5	4	N/M	(20.0)
Noninterest expense including depreciation and amortization	(587)	(658)	(763)	12.1	16.0
Segment results(1)	W 69	W 44	W 121	(36.2)%	175.0%

*Note:*

(1) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result increased by 175.0% from a gain of W44 billion in 2004 to a gain of W121 billion in 2005.

The 16.7% increase in net interest income was due primarily to a significant increase in the balance of interest-accruing accounts receivables arising from trading of securities.

The 27.1% increase in noninterest income was due primarily to an increase in brokerage fees resulting from an increased sales of equity-linked securities and short-term marketable securities and brokerage of marketable securities underlying investment trust company products.

Noninterest expense including depreciation and amortization increased 16.1%, due primarily to an increase in losses on derivatives transactions.

*Comparison of 2004 to 2003*

Our overall segment result decreased by 36.2% from a gain of W69 billion in 2003 to a gain of W44 billion in 2004.

The 58.8% increase in net interest income was due primarily to interest income from equity-linked securities that Good Morning Shinhan Securities acquired to hedge its position against the equity-linked securities sold to its customers.

The 3.4% increase in noninterest income was due primarily to an increase in brokerage fees resulting from increased sales of equity-linked securities and short-term marketable securities.

Noninterest expense including depreciation and amortization increased 12.1%, due primarily to an increase in losses from sales of short-term marketable securities.

**Table of Contents*****Credit Card Services of Shinhan Card***

Credit Card Services segment handles credit card activities primarily managed by Shinhan Card, our wholly-owned subsidiary.

	Year Ended December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
(In billions of Won)					
<b>Income statement data</b>					
Net interest income	W 322	W 348	W 356	8.1%	2.3%
Noninterest income			2	N/M	N/M
Total revenues	322	348	358	8.1	2.9
Provision for credit losses	(236)	(176)	(86)	(25.4)	(51.1)
Noninterest expense including depreciation and amortization	(176)	(166)	(213)	(5.7)	28.3
Segment results(1)	W (90)	W 6	W 59	N/M	N/M

*N/M = not meaningful*

*Note:*

(1) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result increased significantly from W6 billion in 2004 to W59 billion in 2005.

The 2.3% increase in net interest income was due primarily to an increase in fees received on credit card transactions, including fees from participating merchants, which more than offset the decrease in interest income from credit card loans or cash advances.

Provision for credit losses decreased by 51.1%, in 2005 as a result of continued improvement in the asset quality of Shinhan Card's credit card assets.

Noninterest expense including depreciation and amortization increased by 28.3% due primarily to an increase in fees paid on credit card transactions and an increase in general and administrative expenses.

*Comparison of 2004 to 2003*

Our overall segment result improved from a loss of W90 billion in 2003 to a gain of W6 billion in 2004.

The 8.1% increase in net interest income was due primarily to a reduction in funding costs corresponding to a decrease in average market interest rates and a decrease in interest expense as a result of reduced borrowings corresponding to reduced credit card assets.

Provision for credit losses decreased by 25.4% in 2004 as a result of improvement in the asset quality of Shinhan Card's credit card assets.

Noninterest expense including depreciation and amortization decreased by 5.7% due primarily to impairment losses recorded from asset securitization transactions in 2003 and a reduction in fees for handling credit cards that Shinhan Card pays to our other distribution channels, primarily Shinhan Bank.

**Table of Contents****Other**

Other segment primarily reflects all other activities of our subsidiaries, including the results of operations of Jeju Bank, Shinhan Capital, SH&C Life Insurance, Shinhan Credit Information and Shinhan Macquarie Financial Advisory and back-office functions maintained at the holding company as well as the addition of Shinhan Life Insurance in 2005.

	Year Ended December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
(In billions of Won)					
<b>Income statement data</b>					
Net interest income	W 198	W 155	W 174	(21.7)%	12.3%
Noninterest income	107	200	446	86.9	123.0
Total revenues	305	355	620	16.4	74.6
Provision for credit losses	9	(33)	(22)	N/M	(33.3)
Noninterest expense including depreciation and amortization	(278)	(312)	(559)	12.2	79.2
Segment results(1)	W 36	W 10	W 39	(72.2)%	290.0%

*N/M = not meaningful.*

*Note:*

(1) Net income per segment before income taxes.

*Comparison of 2005 to 2004*

Our overall segment result increased by 290.0% from W10 billion in 2004 to W39 billion in 2005, due primarily to the consolidation of Shinhan Life Insurance in our results of operations following our acquisition of 100% equity ownership in Shinhan Life Insurance.

Net interest income increased by 12.3% from W155 billion in 2004 to W174 billion in 2005, due primarily to a W16 billion increase in interest income from factoring of receivables at Shinhan Capital and a W14 billion increase in interest income of Shinhan Life, which more than offset a decrease in interest income resulting from a reduced level of lending by our holding company to our non-bank subsidiaries such as Shinhan Card and Shinhan Capital.

Noninterest income increased by 123.0% from W200 billion in 2004 to W446 billion in 2005 due primarily to the effects of including Shinhan Life Insurance into consolidation during 2005, which resulted in the insurance premiums received from customers by Shinhan Life Insurance being recorded as noninterest income in 2005.

Provision for credit losses decreased by 33.3% from W33 billion in 2004 to W22 billion in 2005 due primarily to improvements in asset quality experienced at Jeju Bank and Shinhan Capital.

Noninterest expense including depreciation and amortization increased by 79.2% from W312 billion in 2004 to W559 billion in 2005 due primarily to the effects of including Shinhan Life Insurance into consolidation during 2005, which resulted in the insurance proceeds paid out to customers by Shinhan Life Insurance and the reserves established in connection with Shinhan Life's insurance policies being recorded as noninterest expense in 2005.

*Comparison of 2004 to 2003*

Our overall segment result decreased from W36 billion in 2003 to W10 billion in 2004, due primarily to a decrease in net interest income and an increase in noninterest expense of the holding company.

Net interest income decreased from W198 billion in 2003 to W155 billion in 2004, due primarily to an increase in interest expense as a result of increased average balance of securities issued by our holding company to finance

non-bank subsidiaries such as Shinhan Card and Shinhan Capital and a decrease in interest income from income Jeju Bank as a result of reduced credit card assets.

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Noninterest income increased significantly due primarily to an increase in gross gains from foreign currency translation recorded at Shinhan Capital and the effects of including two additional subsidiaries, which were Shinhan Macquarie Financial Advisory and Shinhan Credit Information, into consolidation during 2004.

We recorded provision for credit losses of W33 billion in 2004 due primarily to an increase in provision for credit losses with respect to finance leases of Shinhan Capital.

Noninterest expense including depreciation and amortization increased 9.4% due primarily to an increase in gross losses from foreign currency translation recorded at Shinhan Capital and the effects of including two additional subsidiaries, which were Shinhan Macquarie Financial Advisory and Shinhan Credit Information, into consolidation during 2004.

**Financial Condition****Assets**

The following table sets forth, as of the dates indicated, the principal components of our assets.

	As of December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
<b>(In billions of Won, except percentages)</b>					
Cash and cash equivalents	W 1,897	W 2,444	W 2,434	28.8%	(0.4)%
Restricted cash	3,662	3,301	3,644	(9.9)	10.4
Interest-bearing deposits	409	220	627	(46.2)	185.0
Call loans and securities purchased under resale agreements	1,898	1,591	1,499	(16.2)	(5.8)
<b>Trading assets:</b>					
Trading securities	2,857	4,639	3,573	62.4	(23.0)
Derivative assets	520	1,678	934	222.7	(44.3)
<b>Securities:</b>					
Available-for-sale securities	18,099	18,108	22,480	0.1	24.1
Held-to-maturity securities	3,605	3,099	2,963	(14.0)	(4.4)
<b>Loans:</b>					
Corporate	54,086	54,622	57,891	1.0	6.0
Consumer	41,209	42,458	47,957	3.0	12.9
Total loans, gross	95,295	97,080	105,848	1.9	9.0
Deferred origination costs	127	99	110	(22.0)	11.1
Less allowance for loan losses	3,631	2,311	1,511	(36.4)	(34.6)
Total loans, net	91,791	94,868	104,447	3.4	10.1
Customers liability on acceptances	2,365	2,012	1,879	(14.9)	(6.6)
Premises and equipment, net	2,003	1,848	1,876	(7.7)	1.5
Goodwill and intangible assets	1,676	1,660	2,957	(1.0)	78.1
Security deposits	966	968	1,078	0.2	11.4
Other assets	4,601	7,072	4,724	53.7	(33.2)
Total assets	W 136,349	W 143,508	W 155,115	5.3%	8.1%

*2005 Compared to 2004*

Our assets increased by 8.1% from W143,508 billion as of December 31, 2004 to W155,115 billion as of December 31, 2005 principally due to increases in loans and available-for-sale securities. Our loans increased 10.1%, on a net basis, from W94,868 billion as of December 31, 2004 to W104,447 billion as of December 31, 2005. This increase was due largely to an increase in mortgage and home equity loans and other consumer loans. Mortgage and home equity loans increased by 16.5% from W22,180 billion as of December 31, 2004 to W25,840 billion as of December 31, 2005, mainly due to increased demand for such loans. Other consumer

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loans increased 15.0% from W15,546 billion as of December 31, 2004 to W17,875 billion as of December 31, 2005, mainly due to the inclusion of consumer loans in connection with our acquisition of Shinhan Life Insurance in 2005 and an increase in unsecured loans related to housing construction.

*2004 Compared to 2003*

Our assets increased 5.3% from W136,349 billion as of December 31, 2003 to W143,508 billion as of December 31, 2004 principally due to increased lending, trading activities and derivatives transactions. Our loans increased 3.4% from W91,791 billion as of December 31, 2003 to W94,868 billion as of December 31, 2004. This increase was due largely to increases in mortgage and home equity loans and other consumer loans. Mortgage and home equity lending increased by 8.1% from W20,517 billion as of December 31, 2003 to W22,180 billion as of December 31, 2004, mainly due to increased demand for such loans. Other consumer lending increased 6.6% from W14,580 billion as of December 31, 2003 to W15,546 billion as of December 31, 2004, mainly due to a change in classification of certain loans to construction companies from mortgage and home equity loans as of December 31, 2003 to other unsecured loans as of December 31, 2004 as described in Item 4. Information on the Company Business Overview Our Principal Activities Retail Banking Services Consumer Lending Activities .

For further information on our assets, see Item 4. Information on the Company Description of Assets and Liabilities .

*Liabilities and Stockholders Equity*

The following table sets forth, as of the dates indicated, the principal components of our liabilities. -

	As of December 31,			% Change	
	2003	2004	2005	2003/2004	2004/2005
(In billions of Won, except percentages)					
<b>Deposits:</b>					
Interest bearing	W 82,161	W 79,934	W 83,278	(2.7)%	4.2%
Noninterest bearing	1,328	2,746	3,143	106.8	14.5
Trading liabilities	513	1,758	1,048	242.7	(40.4)
Acceptances outstanding	2,365	2,012	1,879	(14.9)	(6.7)
Short-term borrowings	11,204	10,954	11,968	(2.2)	9.3
Secured borrowings	6,316	6,308	7,502	(0.1)	18.9
Long-term debt	21,218	23,617	26,172	11.3	10.8
Future policy benefit			4,778		N/M
Accrued expenses and other liabilities	6,555	9,713	7,089	48.2	(27.0)
<b>Total liabilities</b>	<b>131,660</b>	<b>137,042</b>	<b>146,857</b>	<b>4.1</b>	<b>7.2</b>
Minority interest	583	66	80	(88.7)	21.2
Redeemable convertible preferred stock	711	736	368	3.5	(50.0)
Stockholders equity	3,395	5,664	7,810	66.8	37.9
<b>Total liabilities, minority interest and stockholders equity</b>	<b>W 136,349</b>	<b>W 143,508</b>	<b>W 155,115</b>	<b>5.3%</b>	<b>8.1%</b>

N/M = not meaningful.



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*2005 Compared to 2004*

Our total liabilities increased by 7.2% from W137,042 billion as of December 31, 2004 to W146,857 billion as of December 31, 2005. This increase reflects an increase in interest-bearing deposits and long-term debt.

Our interest-bearing deposits increased by 4.2% from W79,934 billion as of December 31, 2004 to W83,278 billion as of December 31, 2005 due primarily to an increased volume of certificates of deposit and court deposit.

Our long-term debt increased by 10.8% from W23,617 billion as of December 31, 2004 to W26,172 billion as of December 31, 2005 due primarily to increased funding through issuance of financial debentures.

Our stockholders' equity increased 37.9% from W5,664 billion as of December 31, 2004 to W7,810 billion as of December 31, 2005.

*2004 Compared to 2003*

Our total liabilities increased 4.1% from W131,660 billion as of December 31, 2003 to W137,042 billion as of December 31, 2004. This increase reflects an increase in trading liabilities and long-term debt.

Our trading liabilities increased 242.7% from W513 billion as of December 31, 2003 to W1,758 billion as of December 31, 2004 due primarily to increased volume of derivatives transactions.

Our long-term debt increased by W2,399 billion from W21,218 billion as of December 31, 2003 to W23,617 billion as of December 31, 2004 due primarily to increased funding through issuance of financial debentures.

Our stockholders' equity increased 66.8% from W3,395 billion as of December 31, 2003 to W5,664 billion as of December 31, 2004.

**Liquidity and Capital Resources**

We are exposed to liquidity risk arising from the funding of our lending, trading and investment activities and in the management of trading positions. The goal of liquidity management is for us to be able, even under adverse conditions, to meet all of our liability repayments on time and fund all investment opportunities. For an explanation of how we manage our liquidity risk, see Item 4. Information on the Company Description of Assets and Liabilities Risk Management Market Risk Management of Shinhan Bank Liquidity Risk Management and Risk Management of Chohung Bank Liquidity Risk Management .

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The following table sets forth our capital resources as of December 31, 2005.

	<b>As of December 31, 2005</b>	
	<b>(In billions of Won)</b>	
Deposits	W	86,421
Long-term debt(1)		26,172
Call money		994
Borrowings from the Bank of Korea		1,668
Other short-term borrowings		9,306
Asset securitizations		7,502
Redeemable convertible preferred stock		368
Stockholders' equity		7,810
<b>Total</b>	<b>W</b>	<b>140,241</b>

*Note:*

(1) Long-term debt includes Redeemable Preferred Stock.

Due to our history as a traditional commercial bank, our primary source of funding has historically been and continues to be customer deposits. Deposits amounted to W82,680 billion and W86,421 billion as of December 31, 2004 and 2005, respectively, which represented approximately 63.6% and 61.6%, respectively, of our total funding as of such dates.

As we offer competitive interest rates on our deposits, we do not anticipate any material losses in deposit customers to other banks and financial institutions. As of December 31, 2005, approximately 90.7% of our total deposits had current maturities of one year or less or were payable on demand. However, in the past, a substantial portion of such customer deposits has been rolled over upon maturity or otherwise maintained with us, and such short-term deposits have been a stable source of funding over time. For example, of our total deposits outstanding as of December 31, 2005 with remaining maturities of four months or less, 57.01% in the case of Chohung Bank and 54.46% in the case of Shinhan Bank were rolled over or otherwise maintained with us, respectively.

We may use secondary and other funding sources to complement, or, if necessary, replace funding through customer deposits. As Shinhan Bank (and, prior to the merger, Chohung Bank) maintains the highest debt rating in the fixed-income market in Korea, we believe that Shinhan Bank will be able to obtain replacement funding through the issuance of long-term debt securities. Shinhan Bank's (and, prior to the merger, Chohung Bank's) interest rates on long-term debt securities are in general 20 to 30 basis points higher than the interest rates offered on their deposits. However, since long-term debt are not subject to premiums paid for deposit insurance and the Bank of Korea reserves, we estimate that our funding costs on long-term debt securities are on a par with our funding costs on deposits.

We depend on long-term debt as a significant source of funding, principally in the form of corporate debt securities. Since 1999, we have actively issued and continue to issue long-term debt securities with maturities of over one year in the Korean fixed-income market. Shinhan Bank has maintained the highest credit rating in the domestic fixed-income market since 1999 and our holding company has also maintained the highest credit rating since its inception in 2001. In 2004, Chohung Bank's domestic credit rating was upgraded to and maintained at the highest credit rating in the domestic fixed-income market following its inclusion into Shinhan Financial Group. In addition, both Shinhan Bank and Chohung Bank may also issue long-term debt



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securities denominated in foreign currency in the overseas market. As of March 31, 2006, the credit ratings by S&P and Moody's assigned to Shinhan Bank and Chohung Bank were as follows:

	<b>As of March 31, 2006</b>	
	<b>S&amp;P</b>	<b>Moody's</b>
Shinhan Bank	A-	Baa1
Chohung Bank	A-	Baa1

The cost and availability of unsecured financing are influenced by credit ratings. We expect our domestic credit ratings to remain at the highest level and, accordingly, do not anticipate any material increase in funding cost. Shinhan Bank's overseas credit ratings have continued to improve since the financial crisis of late 1997 until 2002. During 2003, S&P lowered the debt ratings of Shinhan Bank one notch to BBB following the announcement of our acquisition of Chohung Bank. Chohung Bank's credit rating, on the other hand, was upgraded to match that of Shinhan Bank to BBB from BBB- in April 2004. In September 2005, S&P upgraded the credit ratings of Shinhan Bank and Chohung Bank to A-. Our holding company did not receive ratings by either of these credit rating agencies since it has not obtained funding from overseas sources to date.

As of December 31, 2003, 2004 and 2005, our long-term debt amounted to W21,218 billion, W23,617 billion and W26,172 billion, respectively.

Secondary funding sources include call money, borrowings from The Bank of Korea and other short-term borrowings which amounted to W11,204 billion, W10,954 billion and W11,968 billion as of December 31, 2003, 2004 and 2005, each representing 8.9%, 8.4% and 8.5%, respectively, of our total funding as of such dates.

Additional funding flexibility is provided by our ability to access the repurchase and asset securitization markets. These alternatives are evaluated on an ongoing basis to achieve the appropriate balance of secured and unsecured funding. The ability to securitize loans, and the associated gains on those securitizations, are principally dependent on the credit quality and yields on the assets securitized and are generally not dependent on the ratings of the issuing entity. Transactions between us and our securitization structures are reflected in our consolidated financial statements. See Note 14 to our consolidated financial statements in Item 18. Financial Statements Notes to consolidated financial statements of Shinhan Financial Group.

In limited situations, we may also issue Redeemable Preferred Stock and Redeemable Convertible Preferred Stock (convertible into our common shares). As consideration for our acquisition of Chohung Bank, on August 18, 2003, we issued to the Korea Deposit Insurance Corporation (i) 46,583,961 shares of our Redeemable Preferred Stock, with an aggregate redemption price of W842,517,518,646 and (ii) 44,720,603 shares of our Redeemable Convertible Preferred Stock, with an aggregate redemption price of W808,816,825,858, which were convertible into shares of our common stock. Of these shares of our Redeemable Convertible Preferred Stock, in November 2005, Korea Deposit Insurance Corporation converted 22,360,302 shares into shares of our common stock, representing 6.22% of our total issued shares (or 5.86% of our total issued common stock on a fully diluted basis). In April 2006, Korea Deposit Insurance Corporation sold to BNP Paribas S.A. and other institutional investors all of our common shares held by it. As of the date hereof, Korea Deposit Insurance Corporation does not hold any share of our common stock but still holds 22,360,301 shares of Redeemable Convertible Preferred Stock, representing 6.22% of the total issued shares (or 5.86% of the total issued shares on a fully diluted basis) of our common stock. Korea Deposit Insurance Corporation is entitled to convert such shares into our common stock beginning in August 2006.

In addition, in order to partly fund our acquisition of Chohung Bank, in August 2003, we raised W900 billion in cash through the issuance of 6,000,000 shares of Redeemable Preferred Stock, all of which were sold in the domestic fixed-income market through Strider Securitization Specialty Co., Ltd., a special purpose vehicle. We are required to redeem these preferred shares issued to the special purpose vehicle in three installments in 2006, 2008 and 2010. See

Item 4. Information on the Company The Merger of Shinhan Bank and Chohung Bank Liquidity and Capital



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tion Articles of Incorporation Description of Capital Stock Description of Redeemable Preferred Stock .

Our policy is to encourage our subsidiaries to secure their own funding and liquidity source. With respect to Shinhan Capital and Shinhan Card, we have, in certain cases, provided funding through our holding company to take advantage of lower cost of funding within regulatory limitations. Under the Monopoly Regulation and Fair Trade Act of Korea, however, a financial holding company is prohibited from borrowing funds in excess of 100% of its total stockholders' equity. In addition, pursuant to our liquidity risk management policies designed to ensure compliance with required capital adequacy and liquidity ratios, we have set limits to the amount of liquidity support by our holding company to our subsidiaries to 70% of our total stockholders' equity and the amount of liquidity support to a single subsidiary to 35% of our total stockholders' equity.

In light of the financial market instability in Korea resulting from the liquidity problems faced by credit card companies during the first quarter of 2003, in April 2003 the Korean government announced temporary measures designed to provide liquidity support to credit card companies. These measures included, among other things:

a request by the government for credit card companies to effect capital increase in the aggregate amount of W4.6 trillion, as part of their self-rescue efforts;

banks and other financial institutions agreeing with each other to extend the maturity of all debt securities of credit card companies that they hold;

asset management companies agreeing with each other to extend the maturity of 50% of the aggregate amount of the debt securities of credit card companies that they hold which are scheduled to mature by June 2003; and

with respect to the remaining 50% of such credit card company debt securities, banks and other financial institutions agreeing with each other to contribute an aggregate amount of W5.6 trillion to purchase such debt securities from asset management companies.

We funded this obligation through the issuance of debt securities. In addition, Shinhan Bank agreed to extend the maturities of the W436 billion of credit card company debt securities that it held in April 2003 or that have become due in June 2003 (including W426 billion of such debt securities Shinhan Bank transferred from its trust accounts to its bank accounts). Of the W5.6 trillion aggregate contribution made by Korean financial institutions to purchase credit card company debt securities held by asset management companies, the portion allocated for Shinhan Bank to purchase was approximately W263 billion, all of which were repaid as of July 31, 2003. Chohung Bank also agreed to extend the maturities of the W177 billion of loans to and debt securities issued by credit card companies that Chohung Bank held in April 2003 or that have become due in June 2003. Of the W5.6 trillion aggregate contribution made by Korean financial institutions to purchase credit card company debt securities held by asset management companies, the portion allocated for Chohung Bank to purchase was approximately W183 billion, all of which was repaid as of July 31, 2003.

We generally may not acquire our own shares except in certain limited circumstances including, without limitation, a reduction in capital. However, pursuant to the Securities and Exchange Act and regulations under the Financial Holding Companies Act, we may purchase our own shares on the Stock Market Division of the Korea Exchange or through a tender offer, or retrieve our own shares from a trust company upon termination of a trust agreement subject to the restrictions that (1) the aggregate purchase price of such shares may not exceed the total amount available for distribution of dividends at the end of the preceding fiscal year less the amounts of dividends and reserves for such fiscal year, subtracted by the sum of (a) the purchase price of treasury stock acquired if any treasury stock has been purchased after the end of the preceding fiscal year pursuant to the Commercial Act or the Securities and Exchange Act, (b) the amount subject to a trust contract, and (c) the amount of dividends approved at the ordinary general shareholders' meeting after the end of the preceding fiscal year and the amount of retained earnings reserve required under the Commercial Act; plus if any treasury stock has been disposed of after the end of the preceding fiscal year, the acquisition cost of such treasury stock, and (2) the purchase of such shares shall meet the requisite ratio under the Financial Holding Companies Act and regulations thereunder. We may purchase our own shares for



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the purpose of cancellation with profits through the Stock Market Division of the Korea Exchange, or through a tender offer acquire interests in our own shares through agreements with trust companies, subject to the same restrictions on the purchase price as described in this paragraph.

In July and August 2001, pursuant to these procedures, Shinhan Bank repurchased 32,432,800 shares of common stock of Shinhan Bank and sold 5,935,721 such shares to BNP Paribas in connection with our alliance with BNP Paribas as described under Item 7. Major Shareholders and Related Party Transactions. Related Party Transactions. We do not use equity derivatives contracts to hedge the risk relating to these repurchases. In addition, pursuant to the Securities and Exchange Act of Korea, in certain limited circumstances, dissenting holders of shares have the right to require us to purchase their shares.

In connection with our restructuring into a holding company, in August 2001, Shinhan Bank repurchased 3,376,216 shares of its common stock from the dissenting shareholders of Shinhan Bank. These shares were subsequently exchanged for shares of the holding company and Shinhan Bank disposed of such shares in March 2004. No share repurchases were made in 2002.

In June 2004, we acquired 108,438,628 shares of common stock of Chohung Bank that we previously did not own through a cash tender offer and a small-scale share swap pursuant to Korean laws. In connection with the share swap transaction, we issued 14,682,590 new shares of our common stock to the existing shareholders of Chohung Bank in exchange for the shares of Chohung Bank's common stock, of which 8,985,567 shares of our common stock were issued to Chohung Bank in exchange for its treasury shares. Chohung Bank acquired these treasury shares from its shareholders who dissented to the share swap at Chohung Bank's shareholders' meeting pursuant to the exercise by those dissenting shareholders the right to request Chohung Bank to purchase their shares in accordance with Korean law. Under the Financial Holding Companies Act of Korea, the voting rights relating to the 8,985,567 shares of our common stock currently held by Chohung Bank in treasury are restricted.

In December 2004, we issued 10,235,121 shares of our common stock issued in exchange for the minority equity interest, consisting of both common and preferred shares, of Good Morning Shinhan Securities through a cash tender offer and a small-scale share swap pursuant to Korean laws, of which 1,444 shares of our common stock was issued to Good Morning Shinhan Securities in exchange for its treasury shares. Good Morning Shinhan Securities acquired these treasury shares from its shareholders who dissented to the share swap at Good Morning Shinhan Securities' shareholders' meeting pursuant to the exercise by those dissenting shareholders the right to request Good Morning Shinhan Securities to purchase their shares in accordance with Korean law. Good Morning Shinhan Securities sold in the market the 1,444 shares of our common stock that it held in March 2005.

In December 2005, in a series of related transactions, we acquired 100% of Shinhan Life Insurance, an insurance company, through a small scale share exchange mechanism provided under applicable Korean law, pursuant to which we issued 17,528,000 new shares of our common stock to the shareholders of Shinhan Life Insurance in exchange for all outstanding common stock of Shinhan Life Insurance held by them for an aggregate purchase price of W612 billion, or W15,300 per share. See Overview. Financial Impact of Acquisitions. Acquisition of Shinhan Life Insurance.

As of December 31, 2005, we had 11,610,197 treasury shares of our common stock, which were held by Chohung Bank, Shinhan Bank and Good Morning Shinhan Securities. Of such treasury shares, 1,708,050 shares were granted to the employees of the newly merged Shinhan Bank in April 2006 and 916,580 shares were sold in the market in June 2006. As of the date hereof, 8,985,567 treasury shares of our common stock are held by Shinhan Bank which must be disposed of by June 2007 in accordance with the Financial Holding Company Act of Korea. Under the Financial Holding Company Act of Korea, the voting rights on our treasury shares are subject to certain restrictions and the treasury shares must be sold within six months of acquisition with certain exceptions.

**Table of Contents****Contractual Obligations, Commitments and Guarantees**

In the ordinary course of our business, we have certain contractual cash obligations and commitments which extend for several years. As we are able to obtain liquidity and funding through various sources as described in

Liquidity and Capital Resources above, we do not believe that these contractual cash obligations and commitments will have a material effect on our liquidity or capital resources.

**Contractual cash obligations**

The following table sets forth our contractual cash obligations as of December 31, 2005.

**December 31, 2005**  
**Payments Due by Period**

	<b>Up to 1 Year</b>	<b>Between 1 and 3 Years</b>	<b>Between 3 and 5 Years</b>	<b>Beyond 5 Years</b>	<b>Total</b>
<b>(In billions of Won)</b>					
Long-term debt(1)	W 5,663	W 13,442	W 2,600	W 4,561	W 26,266
Lease obligations	8				8
Secured borrowings	4,182	2,528	792		7,502
Provisions for accrued severance indemnities(2)	13	6	8	50	77
Deposits(3)	41,091	6,089	1,606	352	49,138
<b>Total</b>	<b>W 50,957</b>	<b>W 22,065</b>	<b>W 5,006</b>	<b>W 4,963</b>	<b>W 82,991</b>

*Notes:*

- (1) Long-term debt includes senior debt, subordinated debt and Redeemable Preferred Stock.
- (2) In accordance with our policy and the Korean Labor Standard Law, employees with one year or more of service are entitled, upon termination of employment, to receive a lump sum severance payment based upon the length of their service and the average of the last three months wages. We make provisions for accrued severance indemnities based upon the assumption that all employees terminate their employment with us at the same time.
- (3) Deposits include certificate of deposits, other time deposits and mutual installment deposits.

**Table of Contents****Commitments and Guarantees**

The following table sets forth our commitments and guarantees as of December 31, 2005. These commitments, apart from certain guarantees and acceptances, are not included within our consolidated balance sheet. Guarantees issued after December 31, 2002 are recorded at their fair value at inception, which is amortized over the life of guarantees.

	<b>As of December 31, 2005</b>			
	<b>Commitment Expiration by Period</b>			
	<b>Up to 1 Year</b>	<b>Between 1 and 5 Years</b>	<b>Beyond 5 Years</b>	<b>Total</b>
<b>(In billions of Won)</b>				
<b>Commitments to extend credit:</b>				
Corporate	W 43,313	W 2,357	W 666	W 46,336
Credit card lines(1)	8,430	7,507	143	16,080
Consumer(2)	5,644	218	1	5,863
Commercial letters of credit(3)	2,759	190	11	2,960
Financial Standby letters of credit	227	29		256
Other Financial guarantees	697	168	2	867
Performance letters of credit and guarantees	743	111	141	995
Liquidity facilities to SPEs	522	1,765	199	2,486
Acceptances	1,879			1,879
Loans sold with recourse			14	14
Guarantee on trust accounts	315	312	2,462	3,089
<b>Total</b>	<b>W 64,529</b>	<b>W 12,657</b>	<b>W 3,639</b>	<b>W 80,825</b>

*Notes:*

(1) Relates to the unused portion of credit card limits that may be cancelled by us after notice to the borrower if we determine that the borrower's repayment ability is significantly impaired.

(2) Excludes credit cards.

(3) These are generally short-term and collateralized by the underlying shipments of goods to which they relate.

Commitments to extend credit represent unfunded portions of authorizations to extend credit in the form of loans. The commitments expire on fixed dates and a customer is required to comply with predetermined conditions to draw funds under the commitments.

Commercial letters of credit are undertakings on behalf of customers authorizing third parties to draw drafts on us up to a stipulated amount under specific terms and conditions. Commitments to extend credit, including credit lines, are in general subject to provisions that allow us to withdraw such commitments in the event there are material adverse changes affecting an obligor.

Financial standby letters of credit are irrevocable obligations to pay third party beneficiaries when our customers fail to repay loans or debt instruments, which are generally in foreign currencies. A substantial portion of these standby letters of credit are secured by underlying assets, including trade-related documents.

Other financial guarantees are used in various transactions to enhance the credit standing of our customers. They represent irrevocable assurance, subject to satisfaction of certain conditions, that we will make payment in the event

that our customers fail to fulfill their obligations to third parties. Such financial obligations include a return of security deposits and the payment of service fees.

Performance letters of credit and guarantees are issued to guarantee customers' tender bids on construction or similar projects or to guarantee completion of such projects in accordance with contractual

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terms. They are also issued to support a customer's obligation to supply products, commodities, maintenance or other services to third parties.

Liquidity facilities to SPEs represent irrevocable commitments to provide contingent credit lines including commercial paper purchase agreements to SPEs for which we serve as the administrator.

Loans sold with recourse represent certain non-performing loans we sold to Korea Asset Management Corporation prior to 1999. The sales agreements contain a recourse obligation under which Korea Asset Management Corporation can obligate us to repurchase the related loans. The recourse obligation has no expiration date.

Guarantees on trust funds represent guarantee of principal issued to trust fund investors.

Acceptances are a guarantee by us to pay a bill of exchange drawn on a customer. We expect most acceptances to be presented, but reimbursement by the customer is normally immediate.

Details of our credit commitments and obligations under guarantees are provided in Note 31 in Item 18. Financial Statements Notes to the consolidated financial statements of Shinhan Financial Group .

**Off-Balance Sheet Arrangements**

We have several types of off-balance sheet arrangements, including guarantees for loans, debentures, trade financing arrangements, guarantees for other financings, credit lines, letters of credit and credit commitments. In the normal course of our banking activities, we make various commitments and guarantees to meet the financing needs of our customers. Commitments and guarantees are usually in the form of, among others, commitments to extend credit, commercial letters of credit, standby letter of credit and performance guarantees. The contractual amount of these financial instruments represents the maximum possible loss amount if the account party draws down the commitment or we should fulfill our obligation under the guarantee and the account party fails to perform under the contract. See

Item 4. Information on the Company Description of Assets and Liabilities Credit-Related Commitments and Guarantees .

Details of our off-balance sheet arrangements are provided in Note 31 in Item 18. Financial Statements Notes to the consolidated financial statements of Shinhan Financial Group .

**Selected Financial Information under Korean GAAP**

The selected consolidated financial and other data shown below have been derived from our consolidated financial statements, prepared in accordance with Korean GAAP.

Under Korean GAAP, consolidated financial statements include the accounts of fully or majority owned subsidiaries and substantially controlled affiliates that have assets in the amount equal to or more than 7 billion as of the end of the previous fiscal year. Substantial control is deemed to exist when the investor is the largest shareholder and owns more than 30% of the investee's voting shares. Korean GAAP does not require the consolidation of subsidiaries, or substantially controlled affiliates, where activities are dissimilar from ours.

Under Korean GAAP effective since 1994, financial statements of our trust accounts, on which we guarantee a fixed rate of return and/or the repayment of principal, are consolidated, whereby assets and liabilities of third parties held by such trusts are reflected as assets and liabilities, and revenues and expenses generated from such third party assets are reflected in the statement of operations. Activities between trust accounts and us are eliminated.

Beginning January 1, 1999, the financial statements are prepared in accordance with financial accounting standards generally accepted for banking institutions issued by the Korean Securities and Futures Commission.

Capital adequacy ratios have been calculated from the financial statements prepared in accordance with Korean GAAP and using the guidelines issued by the Financial Supervisory Commission.

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We have included narrative disclosure in the footnotes to more clearly identify where significant accounting policy changes have taken place, which line items would be affected and how the balances would be affected. The areas where such significant changes have occurred are as follows:

Trading and investment securities;

Deferred taxation;

Guarantees and acceptances (including allowances for losses); and