2010

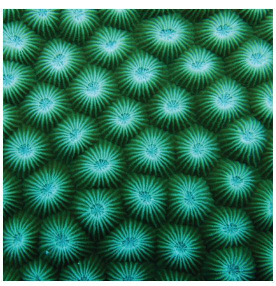
BSP Annual Report

Bank of South Pacific Limited

Community

Life

Wealth



Happiness

The vision

- To be the leading bank in the South Pacific

BSP School Kriket Programme, winner International Cricket Council Award for Best Cricket Development Programme globally in 2010.

2010
BSP Annual Report

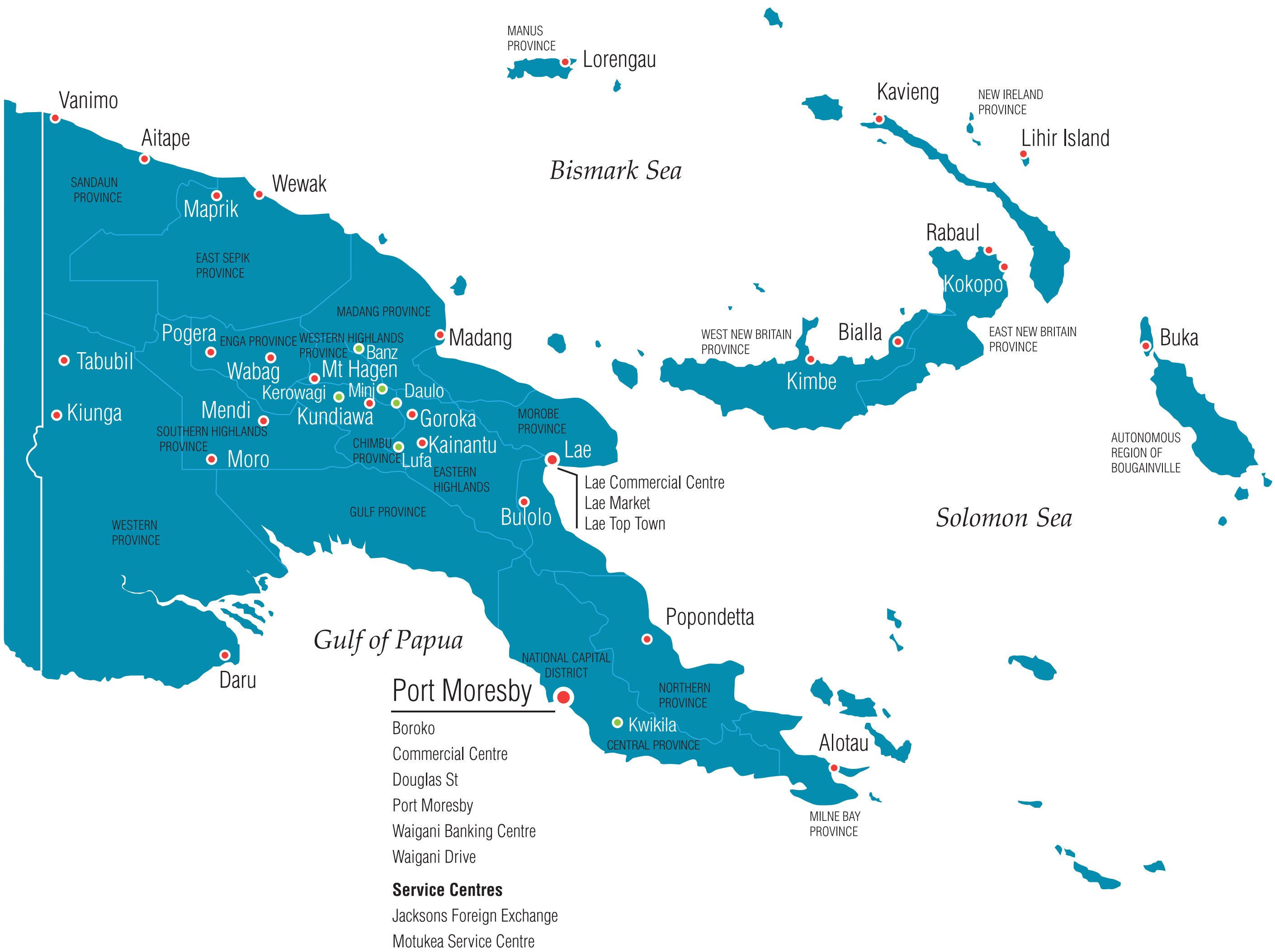


key features

The key features of BSP's strategy:

- A focus on sales and services
- Operational excellence
- High performing teams
- Profitable growth

BSP bank locations



BSP - Fiji

BSP - Solomon Island

BSP - Niue

- BSP Bank branches
- BSP Rural branches

chairman's report

Kostas Constantinou, OBE, Chairman

In 2010, BSP has continued to achieve steady improvements in its financial results despite major challenges presented by a year which commenced with a significant level of uncertainty as to the extent and impact of the general recovery from the Global Financial Crisis, uncertainties regarding the prospects of the PNG LNG project, and ended with significantly lower short term market interest rates.

Some of the bank's achievements over the year were:

- After tax net profit of K283 million, an increase of 10% on the after tax net profit of K257 million reported in 2009;
- Dividend payments totalling K248 million were made to shareholders comprising K182.4 million full dividend for 2009 (at 4 toea per share) and K65.6 million interim dividend for 2010 at 1.37 toea per share;
- New equity of approximately K143.6 million raised through IFC's investment in BSP;
- Regulatory capital ratios maintained at levels complying with the regulator's definition of "well capitalised";
- Return on equity of 27.4%, despite increased expenditure and investment in a major operational transformation exercise, and increased capital base from the IFC's equity investment transaction;
- Growing impetus of activities connected with the implementation of the bank's transformation strategy in the core PNG businesses; whilst work continues on various projects, progress indicates that some key programmes in the areas of customer segmentation, product development, process automation, operational risk, and management information systems, will be finalised in 2011.
- Net growth in customer deposits of K426 million to K7,186 million with market share of 51.4% in Papua New Guinea; and total group deposits at K7,985 million;
- Loans and advances increased by net K420 million to K3,384 million with market share of 50.4% in Papua New Guinea; total gross loans of the group is K4,250 million;
- Opening of the new Motukea Branch, 24th September 2010, and the commencement of pilot branches of BSP Rural;
- The introduction of ATMs in the Solomon Islands and additions to the Fiji ATM fleet to strengthen electronic banking service delivery channels in the Pacific Islands;
- Continued commitment to community-oriented activities resulting in 77 local community projects delivered by bank staff in PNG, Fiji and the Solomon Islands, worth in excess of K920,000.

The growth in assets and liabilities reflects not only continuing stable organic business growth of BSP in PNG and its Pacific Island operations. During the year, the bank raised approximately K143.6 million through an issue of new equity to International Finance Corporation, with the anticipated partnership in technical and expertise activities already commencing during the year. The bank also issued Fiji dollar denominated convertible notes in Fiji, with associated proceeds K22.9 million.

As mentioned in the highlights section, BSP's capital base remains in the "well capitalised" status as defined by the home regulator, the Bank of Papua New Guinea. Group Capital adequacy is 23.6%, an increase from the 22.1% level as at year-end 2009, reflecting the strong growth in BSP total balance sheet.

The maintenance of capital at sufficient levels to accommodate growth as well as to provide a cushion against business risks in the Pacific is central to the long term strategy and planning of the BSP Group. The IFC equity issue during 2010 is a part of this strategy, following on from the 2009 K75.5 million capital raising through an inaugural issue of term subordinated notes in PNG.

BSP continues at the forefront of the development of electronic banking facilities in the Pacific region. In 2010, BSP introduced SMS banking to the Fiji market, following on from the introduction of the service in PNG in 2009. There are now over 100,000 users in PNG and Fiji subscribed to this product. During the year 23 new ATMs were installed in PNG, along with GPRS EFTPOS machines in selected locations. There were 11 ATMs commissioned in the Solomon Islands, and in Fiji, the ATM fleet was increased to 84, making BSP's the largest fleet in Fiji.

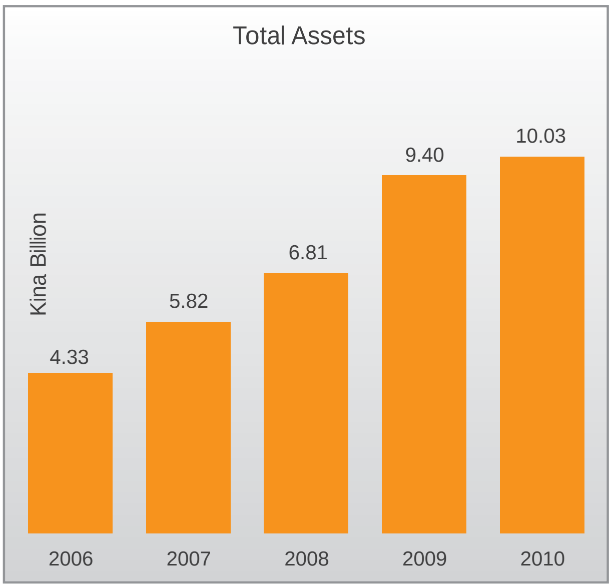
The PNG economy showed resilience during the global financial crisis, and in a year where a slow global recovery commenced, credible growth has been achieved on the back of key natural resource projects reaching build stage, or increasing production capacity, and aided by recovering commodity prices.

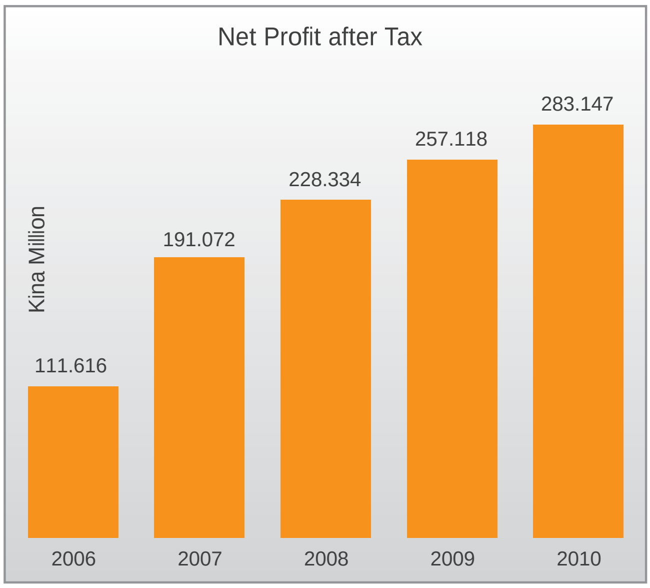
Key economic data in 2010 included:

- GDP growth estimate of 8.5%;
- Inflation of 7.5%;
- Stable maintenance of monetary policy by Bank of PNG with the Kina Facility Rate maintained at 7% during 2010;
- Foreign reserves increased to US Dollars 3,047 million (K7,925 million) at the end of 2010 representing approximately 10 months import cover and 14 months non-mineral import cover;

Whilst the country's macro-economic indicators are quite healthy, BSP's business environment in PNG continues to be characterised by abnormal risks in relation to general security, an increasingly competitive labour market compounded by a stressed education system, high communications costs by global standards, and sub-optimal standards of electricity supply. In recent years, a shortage of office and residential infrastructure in the major urban centres has developed, and this has led to a rapid escalation of rental costs. In 2010, the bank's PNG operations was affected for four days by industrial action where one of the main items under discussion was accommodation allowances. How successfully the country deals with these and other wider social issues in the context of the potential positive economic impacts of major mining and gas projects, will be critical for business in PNG.

The Solomon Islands and Fiji economies remained more subdued during the year. In the Solomon Islands the economy remains heavily reliant on timber and fish exports and in the mining sector, Allied Gold has made a significant investment, taking over the operations of the Gold Ridge Mining Limited.





The RAMSI assistance programme continues to be beneficial to the economy. Fiji's sugar industry still requires major capital rejuvenation and faces continued difficulty following the discontinuation of the EEC market support. Its tourism industry however shows signs of a return to normality, with visitor numbers and hotel bookings increasing in 2010, following the 2009 flooding and cyclones which adversely affected tourist numbers and the associated inflows from this sector. Nevertheless business confidence remains positive, the liquidity position has improved, and BSP's growth expectations are sound.

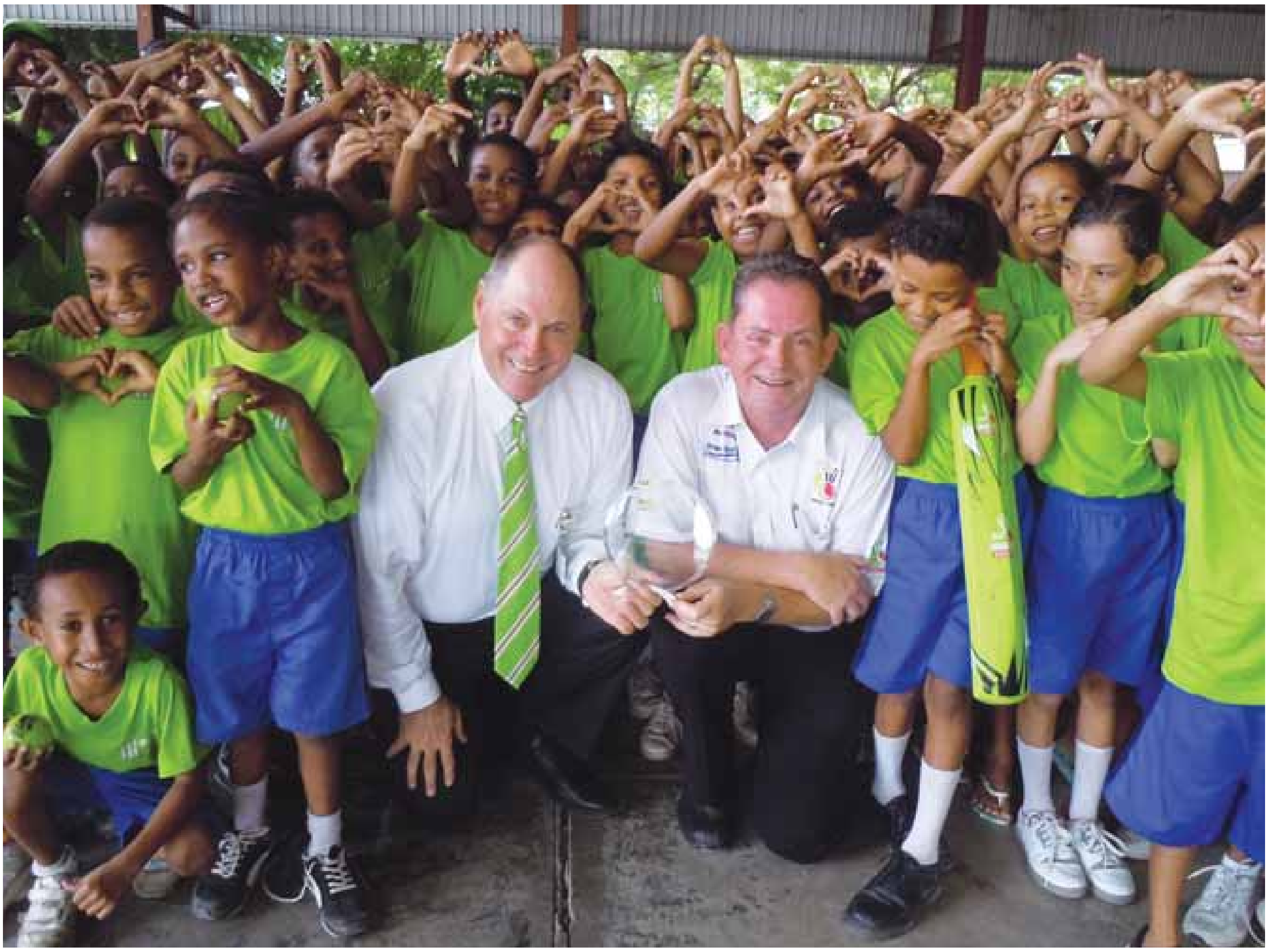
The major equity investment by IFC in BSP is a very strong endorsement of the group's underlying strategy and unique trading position in the Pacific, and its very real capability to be a major institution in the financial systems and emerging Pacific nation markets.

I thank all staff and the executive who have taken on the added responsibilities of implementing and participating in the BSP transformation programme, as well as maintaining their duties to ensure the bank and group's usual business is carried on smoothly. The commitment and dedication shown throughout 2010 is to be commended, and has enabled the bank to achieve solid results under challenging circumstances. With their continued support the bank will be well placed to cultivate opportunities in the future.

In February 2011, Noreo Beangke stepped down as Chairman of Bank of South Pacific Limited after 18 years of dedicated service. During the term of Mr Beangke's leadership, BSP has grown rapidly, especially with the acquisition and merger of PNGBC in 2002, and of the former Colonial Group in Fiji in 2009. My fellow Board members and I join the staff and executive of BSP in expressing our sincere gratitude for his chairmanship of BSP over the years, and his contribution generally to PNG business in that time. Mr Beangke continues as a non-executive Director of BSP.

To all shareholders and my fellow Board members – I acknowledge with thanks your ongoing support. I look forward to reporting another year of achievement by BSP in 2011.

Kostas Constantinou, OBE
Chairman



BSP CEO Ian Clyne with Bill Leane at the launch of BSP School Kriket Programme 2011, Port Moresby March 2011

Sport for life

Abigail Tere-Apisah, PNG Tennis Champion on US circuit

a brief history of BSP

1957

The bank commenced operations on 1 May 1957 in Port Moresby as a branch of the National Bank of Australasia Limited.

1974

Operations were later expanded to several centres and on 17 May 1974 the company was incorporated as Bank of South Pacific Limited, a wholly owned subsidiary of the Australian parent, with a paid-up capital of K2.00 million.

1980

In April 1980 and August 1981, a total of 300,000 ordinary fully paid shares of K1.00 were issued to the public in Papua New Guinea, thus increasing the paid-up capital to 2,300,000 fully paid K1.00 shares.

1993

On 24 August 1993, the nationally owned company, National Investment Holdings Limited (NIHL) acquired the 87% shareholding held by National Australia Bank. On 25 October 1993, 100% ownership of the bank was achieved by NIHL, which later changed its name to BSP Holdings Limited.

1995

In December 1995, BSP Holdings Limited completed a successful capital raising of K2.70 million by way of a Convertible Note Issue. The holding company took up an additional 2,700,000 fully paid shares of K1.00 in Bank of South Pacific Limited, increasing the issued capital to K5,000,000.

1998

In October 1998, BSP Holdings Limited raised K12.90 million through a Rights Issue of shares at K3.00. During December 1998 BSP Holdings Limited went into voluntary liquidation and its shareholders now hold shares in Bank of South Pacific Limited.

2001

In 2001 the Privatisation Commission, on behalf of the Government of Papua New Guinea, offered for sale a 51% interest in the Papua New Guinea Banking Corporation (PNGBC) through a competitive trade sale process. The company participated in this process by lodging a bid whereby it proposed to effect the acquisition of PNGBC by way of an amalgamation under the Companies Act rather than through a sale and purchase.

2002

Following an appraisal of all bids lodged in relation to the acquisition of PNGBC, the commission agreed to accept the company's bid. The company, the commission and the PNGBC executed the amalgamation deed in December 2001 which provided for the implementation of the amalgamation. The amalgamation was completed on 9 April 2002.

2003

The company's shares were listed on the Port Moresby Stock Exchange on 27 August 2003.

2004

In 2004, the company returned a profit after tax of K86.65 million up from the K39.98 million result in 2003. As at 31 December 2004, shareholders' equity reached K255.63 million. During 2004, the bank acquired the Niue Branch operations of Westpac Banking Corporation.

2005

In November 2005, Standard & Poors (S&P) issued an inaugural credit rating for BSP. The rating was B+ Stable, consistent with the S&P sovereign rating for Papua New Guinea.

a brief history of BSP

2005

2005 saw continued strong financial performance and balance sheet growth. Profit after tax increased to K99.22 million. Total assets increased to K2.95 billion and shareholders' equity grew to K308.30 million. Market capitalisation reached K1.40 billion. During this year, Capital Stockbrokers Limited was acquired and renamed BSP Capital Limited.

2006

Strong balance sheet growth with total assets reaching K4.33 billion and a 12.50% increase in after tax profit to K111.62 million continued the strong growth and financial performance during 2006.

2006

On 18 December 2006, a BSP branch was established in Suva, Fiji following the acquisition of the Habib Bank Ltd interests in Fiji.

2007

The acquisition of the National Bank of Solomon Islands Ltd was completed during April 2007. Now rebadged as a branch of BSP, it has the largest branch network in the Solomon Islands.

2007

Outstanding performance continued during 2007. Total assets increased to K5.80 billion, after tax profit increased by 71% to K191.07 million and market capitalisation to K3.28 billion. Expense to income ratio reduced to 39.40%.

2008

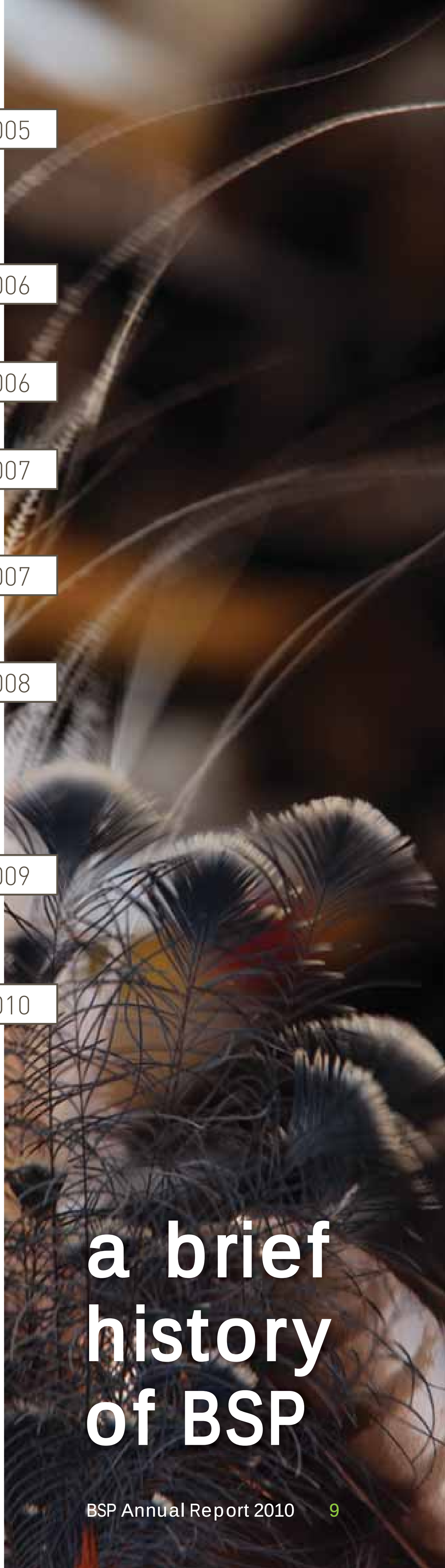
Performance was strong for the year despite the broader effects of downturn in the global economy beginning to impact the PNG economy in the last half of the year. After tax profit continued to grow, with an increase of 19% over the prior year, despite the BSP Capital CDO provisioning of K50 million. Strong balance sheet growth continued despite these effects with total assets increasing by 17% to K6.8 billion and capitalisation increasing by 33% to K4.3 billion.

2009

BSP posted sound results as the global economic downturn continued, increasing after tax results by 13%; BSP acquired the National Bank of Fiji and Colonial Fiji Life Insurance Limited from Commonwealth Bank of Australia, contributing K1.2 billion to assets growth of K2.6 billion.

2010

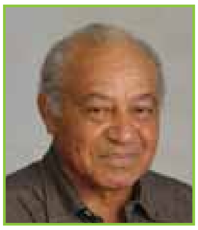
Solid results achieved as the global economy starts a slow recovery from the Global Financial Crisis, positively impacting PNG's resource-based economy. BSP's group profit increases 10% to K283.1 million, and assets reach K10.0 billion; IFC makes significant equity investment for 10% shareholding in BSP.



board of directors

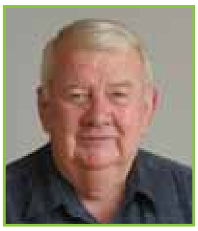
Kostas Constantinou, OBE
Chairman
Director since April 2009.
Appointed Chairman February 2011.
Kostas Constantinou is a prominent business figure in Papua New Guinea, holding a number of high level public sector and private sector appointments. He is a Chairman of various companies, including Airways Hotel & Apartment, Lamana Hotel Limited, Lamana Development Limited, Hebou Constructions and Alotau International Hotel. He is a Director of Heritage Park Hotel, Honiara, Gazelle International Hotel and Grand Pacific Hotel, Fiji. Kostas is a Director of two other listed companies: Oil Search Limited and Airlines PNG Limited. He is Deputy President of Employers Federation of Papua New Guinea, Honorary Consul for Greece in Papua New Guinea and Trade Commissioner of Solomon Islands to Papua New Guinea.

Ian B Clyne
Chief Executive Officer
Director since December 2008.
Ian Clyne was appointed as Chief Executive Officer by the Board of Bank South Pacific Limited on 17 October 2008. He has had a distinguished career in banking and finance; his most recent appointment was Executive Vice President and Managing Director, ING Bank Slaski Group, Poland. During his career Mr Clyne, a Bachelor of Business graduate from the Curtin University, Perth, Western Australia, has held senior banking appointments in Australia, PNG, Pakistan, Hong Kong/ China, France, UK, Singapore, Indonesia, Italy, and Poland, during a career with the Indosuez Bank, ING Barings and Lippo Bank. Prior to embarking on an international banking career, Mr Clyne worked in Papua New Guinea with Nambawan Finance Limited and Indoniu Finance during 1980 - 1986.

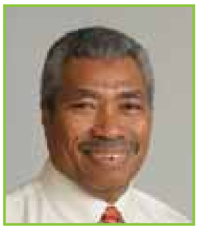


Tom Fox, OBE, BEc
Deputy Chairman
Non-executive Director
Director since June 1993.
Thomas Fox is currently an Executive Director of Kramer Group Limited. He holds a Bachelor of Economics Degree from the University of Papua New Guinea. He commenced his career with the Reserve Bank of Australia, and gained wide experience in senior management roles within semi-government institutions, and private sector companies, which included serving as the Managing Director of the Investment Corporation of Papua New Guinea for 8 years. His other current directorships include, PNG Sustainable Infrastructure Ltd, Capital Life Insurance Company Ltd. Mr Fox is also a a trustee for the Institute of National Affairs, and a foundation member and fellow of the PNG Institute of Directors.

Noreo Beangke, BA (Ec)
Non-executive Director
Director since August 1993.
Chairman May 1994 to February 2011.
Noreo Beangke holds a Bachelor of Economics Degree from the University of Papua New Guinea. Mr Beangke is also Chairman of PNG Coffee Exports Ltd, and a Director of New Guinea Islands Produce Ltd and Credit Corporation (Fiji) Limited.

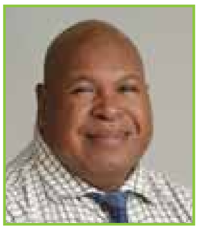


John Jeffery
Non-executive Director
Director since June 2001.
John Jeffery had a long and successful career in Australia before moving to Papua New Guinea in 1986 to take up a position at Madang-based James Barnes PNG Limited. Mr Jeffery's directorships include Chairman NASFUND and The Tower Ltd. He also continues to serve as President of the Employers' Federation of PNG and is a founding member of the PNG Institute of Directors Inc.

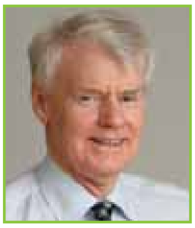


Gerea Aopi, CBE, MBA
Non-executive Director
Director since April 2002.
Gerea Aopi has achieved several tertiary degrees in Papua New Guinea, and a Masters of Business Administration from the University of Queensland. His career began with the PNG Development Bank and progressed through a variety of positions to Managing Director. He currently holds the position of General Manager, PNG with Oil Search Limited. Mr Aopi is also currently a director of Steamships Trading Company Limited, POMSox Ltd, Niu Marsh Ltd, Endeavour Properties Ltd and is the Chairman of Telikom (PNG) Ltd and Chairman for Independent Public Business Corporation.

Dr Ila Temu, PhD, MEc
Non-executive Director
Director since 2003.
Dr Temu achieved a distinguished academic career with the University of Papua New Guinea, the National Research Institute, the Australian National University and the University of California, Davis USA where he was awarded his Ph D. Dr Temu entered the private sector during 1996 when he was appointed Managing Director, Mineral Resources Development Company. From 2000 to 2008, Ila held senior positions in Placer Dome, including Country Manager, Tanzania. Since 2008, Ila has been Director of Corporate Affairs for Barrick's Australia Pacific Region. He is a member of the Management Group for the PNG Incentive Fund and an executive member of the Employers' Federation of Papua New Guinea.



Sir Nagora Bogan, KBE, LLb
Non-executive Director
Director since 2003.
Sir Nagora Bogan graduated with a Bachelor of Law from the University of Papua New Guinea in 1978. In 1992 Sir Nagora was appointed Commissioner General of the PNG Internal Revenue Commission. In 1996, he was appointed as PNG's Ambassador to the United States with accreditation as Ambassador to Mexico and High Commissioner to Canada. In 2002 Sir Nagora became a private business entrepreneur. He is Chairman and CEO of In Touch Media Ltd, a multimedia/ record label company, Chairman of the Board of POSF Limited and Director on several private company boards. Sir Nagora received his knighthood during 1997 in recognition of his distinguished public service.



Lyle Procter, MEc, FFin
Non-executive Director
Director since July 2004.
Lyle Procter has been a career central banker, having spent 36 years with the Reserve Bank of Australia. He also spent several years with the Australian Department of Foreign Affairs. Since retiring from the Reserve Bank Mr Procter has worked as a consultant to the International Monetary Fund, Washington, and the Asian Development Bank, Manila. He has also worked privately as a consultant to the Australian banking industry, and in several South-East Asian countries. Other current directorships include Sun Hung Kai and Co. Ltd and Quality HealthCare Asia Ltd.

John Kapi Natto, BA, B Ed Hons
Non-executive Director
Director since 2006.
John Kapi Natto graduated from Hobe Sound Bible College, Florida USA in 1989 with a Bachelors Degree in Education and also graduated from University of Papua New Guinea with a Bachelor of Education (Honours) Degree in 1991. He is currently the Managing Director of Kutubu Security Services Ltd which provides total security services to the Oil Search operations in Kutubu, SHP. Mr Natto is the Chairman of Namo'aporo Landowners Association Inc and Petroleum Resources Kutubu Ltd.

chief executive officer's report

Introduction

I take great pleasure and pride in reporting to shareholders that BSP Group has achieved another record result. Our net profit after tax increased by K26.0 million to K283.1 million, a 10.1% improvement on BSP's 2009 result. As stated in our Chairman's Report, this performance was characterised by continued sound growth in terms of Total Deposits – 6.6% to K7,984.6 million, and Net Loans 12.4% to K4,091.3 million.

BSP Group's Total Balance Sheet now exceeds K10 billion.

This result has been very creditable when one considers the uncertainties faced by the banking and business sectors as the world's economies have started to slowly recover from the adversities of the Global Financial Crisis (GFC). In PNG, BSP's local challenges were highlighted by a significant decline in money market yields during the year, which placed pressure on bank margins, and the flow on effects on the financial system and its processes of government expenditures relating especially to the large mining and gas projects.

A significant amount of time and effort was devoted by BSP to Capital and Liquidity Management and operational risk controls, to mitigate as much as possible any additional risks associated with these exceptional business trends. Whilst PNG has benefited from the recovery and stability in mineral, oil and gas, and general commodity prices, the country faces the uneasy prospect of managing an economy that is likely to be two-paced as the LNG project develops towards production stage in the next couple of years, and beyond.

As part of our capital planning strategy, BSP launched a "Convertible Notes" issue in the first half of 2010 in Fiji to raise Fiji dollar liquidity to support our expanding Fiji operations, and to encourage Fiji equity participation in BSP in line with our Pacific expansion strategy. This followed the first ever subordinated note issue by a bank in PNG in the prior year. The Convertible Notes are listed and traded on the South Pacific Stock Exchange. In July 2010, BSP also successfully negotiated the issue of new equity to the International Finance Corporation, raising K143.6 million. The transaction by IFC was one of its major equity investment deals for 2010, and enables BSP to access international technical expertise in the banking and finance industry. The technical benefits of this partnership have already started to be drawn on, with IFC demonstrating its skill and support for the BSP Rural initiative and also the conceptual design of a mobile banking solution.

From an investor's perspective, all BSP's key performance indicators remain sound. These include a return on equity of 27.4%, earnings per share of 5.9 toea, and a cost income ratio of 54%. The costs associated with the restructuring of the recently acquired Colonial Fiji business are included in this result.

At the end of 2010, the market capitalisation of BSP was approximately K3,782 million.

The Bank and Transformation

The bank has continued to progress with the implementation of its transformation strategy. In 2010, the agreed BSP strategy and the supporting SBU strategies were reviewed and refinements made as appropriate, to take into account evolving circumstances. BSP is truly a "forward looking" institution, progressing along its chosen path of change and modernisation. The important strategic agenda still remains, namely:

- Firstly, to position BSP to be able to fully participate in the increased economic activity that will accompany the PNG LNG project;
- Secondly, to significantly improve BSP's general banking service levels in terms of products, processes, systems and improve overall staff training levels and ultimately improve "customer service" levels;

- Finally to ensure that BSP has the financial and operational structure and ability to support the continuation of our Pacific expansion strategy.

The progress on transformation and modernisation activity in 2010 is demonstrated by achievements including:

- The re-design of financial and management reporting structures and systems and databases to reflect modern commercial business, segment and related product structures and improve business performance analysis; a restructured general ledger has been brought into production in February 2011;
- Segmentation reflected in the organisation of customer relationship management activities, strengthening the focus on the customer's needs for total banking solutions;
- Implementation of improved processes and systems in connection with account opening, which will continue throughout the branch network in 2011;
- Completion of a number of initiatives to move BSP's information technology and communications management onto a more controlled and automated environment;
- Opening of the first BSP Rural agencies, complete with electronic banking infrastructure and systems;
- The installation of upgraded or new systems applications in different parts of the business for more efficient and controlled processes, including budgeting and forecasting, operational risk management, credit processing with capital allocation model, and account reconciliations; processes are continuously being monitored and improved as applications become more embedded in the organisation, and training more specific;
- Implementation of a best practice Human Capital Management system, for more efficient processing of employee-related data, more automated human resource management tasks, including payroll and training;
- In Fiji, the newly acquired subsidiary immediately set about expanding its ATM fleet and introducing SMS banking, where by the end of 2010, BSP had the largest ATM fleet in that country.

The path to modernisation often requires the acceptance of concepts previously unknown, the adoption of practices previously unobserved, and the test of success is often against new benchmarks. BSP is committed to a rapid adoption and high quality application of new improved concepts, systems and practices, so external consulting firms and resources are being deployed to assist our people in BSP, who undoubtedly have the most important ingredient, the willingness and intellectual capacity to learn new things and apply them successfully in the business.

One year on, the BSP brand is now an extremely well recognised brand in PNG, the Solomon Islands, and Fiji. BSP is now clearly the Number "One" bank in PNG, ultimately the Pacific.

BSP continues to take a leading role in supporting community and sporting projects in the countries in which it operates. BSP's commitment to give back to the local communities has been amply shown through a number of initiatives at corporate as well as branch level. Some K920,000 worth of community project value was injected into communities in which the bank operates in PNG, Solomon Islands and Fiji. This was typically in the form of school equipment provision and classroom refurbishments, hospital and aid post repairs, water tank installation, market and public area clean-ups, and support of equipment and funding for various charity organisations, as well as participation by staff in natural environment conservation events.

In 2010, BSP launched its "Go-Green" initiative, where on selected dates, schools were sponsored to clean up their grounds and to participate in the clean up of public areas. BSP's community presence is not simply an opportunity to build good relations with the customers who support it, it is a way to demonstrate a philosophy of responsible citizenship, the value of public and community property, and it results in needed tangible benefits. The focus of BSP's community initiatives and participation is very much on children and youth programmes in education, health and sport. Our young people are the future of our nation and deserve support and encouragement. In 2010, the BSP School Tennis programme was attended by almost 21,000 children, when rolled out to 58 schools in 13 centres. BSP's association with youth and sport has also been successfully extended through the BSP School cricket programme in PNG's schools. Delivered by Cricket PNG, the programme had reached more than 50,000 children by the end of 2010, and was recognised by the International Cricket Council, as the Best Cricket Development Programme globally in 2010.

BSP's "love your bank" slogan is associated with our communities' programmes around PNG and the Pacific. A campaign during 2010 inviting the public to submit original ideas and imagery depicting the BSP slogan attracted a significant number and variety of entries, with the top prize awarded to a carving of the new BSP logo in the style of a PNG storyboard.

Products and Services

BSP SMS banking, launched in 2009 now has almost 80,000 users in PNG and 27,000 in Fiji. BSP's ATM network continues to grow, reaching 174 ATMs in PNG, 80 in Fiji, and 11 in the Solomon Islands. In 2010, the number of electronic banking transactions reached 96 million in PNG, more than doubling the 2009 total, and over 105 million including Fiji. The strategy to reduce branch overcrowding by the continued expansion of our ATM and EFTPOS network, is augmented by the launch of GPRS-enabled machines. In 2010 Mastercard could be accepted by BSP machines, following Visa card acquiring in 2008. In 2010, mobile phone top-ups for Digicel and Be-Mobile were made available through ATMs, and Digicel top-ups on SMS. These types of developments underline BSP's commitment to being the leader in electronic banking services in PNG and the Pacific.

Fraud continues to be a serious operational risk for BSP, and the specialist operational risk unit has commenced the appropriate analysis of existing and new business processes and also instituted improved risk identification and reporting regimes. With part of our "modernisation" strategy being to significantly reduce operational risks, the training of our people to recognise and mitigate risk, in a co-ordinated way, as well as to appreciate the consequences, is of critical importance. BSP has a "Zero" tolerance policy regarding staff frauds and has ensured that all fraud cases are reported to the police, and those involved are charged and dismissed. Corruption is not just a BSP problem, but a general business and community problem. It is seriously impacting all levels of PNG society and restricts economic development, especially in terms of expanding services to the less developed communities.

The Group and Pacific

Following the acquisition of the Colonial Group in Fiji from the CBA in 2009, BSP is now truly a Pacific bank. The Banking and Life insurance operations in Fiji are now being completely segregated to effectively manage the performance of these distinct parts of the investment in Fiji.

The Life insurance business could not be sold in 2010, and it remains a part of the BSP Group. BSP has revised its medium term strategy for this business, and will ensure it is well managed and contributes positively to the group and also policy holders.

In January 2011, a decree was passed by the government in Fiji, enabling the conversion of the banking operations – National Bank of Fiji – from a subsidiary company to a branch of BSP. The Board and management are currently working to effect the re-structure.

BSP Fiji still has the largest branch network, and recently its ATM network became the largest ATM network in Fiji. BSP is now the largest retail bank in Fiji.

BSP continues to work on the Pacific expansion strategy. Potential targets continue to be identified, and research is ongoing, but no specific transactions were formally initiated in 2010.

The Years Ahead

The commitment to the transformation of BSP into a 21st century bank remains. The ability of BSP to modernise and effectively perform its function as one of the most important financial institutions in PNG and the Pacific, will have a direct bearing on the value created for all stakeholders – shareholders, customers and employees.

The bank is being "re-engineered" with this single goal in mind. Initiatives for new and improved products, customer service processes, technology platforms and communications systems are proceeding with a growing sense of urgency. Some of the progress on transformation initiatives I have highlighted earlier in this report.

2010 has been a year in which the focus has been to refine the organisation's structure and develop, or where necessary, acquire the required expertise to begin implementation, and to build the capacity in BSP to absorb the major change.

In 2010, new branches have been opened in Porgera and Motukea. Vision City and Harbour City are scheduled to come into service this year. Our ATM network will continue to expand to about 250 in PNG, and 120 in Fiji . Eleven ATMs were commissioned in the Solomon Islands in 2010, and increases are also being considered for 2011. Electronic banking and SMS banking will continue to be further expanded in Fiji and Solomon Islands.

BSP will continue to look for interesting and strategically valuable expansion opportunities in the Pacific.

Conclusion

BSP's future is bright and positive, but it has set itself a very aggressive target of implementing and completing a very large portfolio of "Transformation" and "Modernisation" programmes in a relatively short timeframe. When the intended outcomes are achieved, BSP will be a bank characterised by: better product offers, service levels and access to banking services for customers; more efficient processes supported by improved training and resulting in greater job satisfaction; career opportunities and rewards for employees; and the translation of these for our shareholders into stronger profitability, and increasing shareholder value.

BSP remains committed to this "Transformation" and "Modernisation" path, and the drive to perform and achieve exists.

I sincerely thank all BSP Executives, Management and Staff for their efforts in 2010, combining their usual business tasks with new opportunities presented in the building of the new BSP for the future

Ian B Clyne
Chief Executive Officer/Director


WE ARE FOR THE GOODTIMES
AND BAD

2010 strategic business unit review

The daily execution of the bank's business operations is the responsibility of the strategic business units (SBUs), Retail Bank, Corporate, Treasury, Paramount Banking, Credit and Risk, Human Resources, Operations, and Finance and Planning.

Highlights of each SBU performance in 2010 include:

Retail Bank

The Strategic Business Unit (SBU) Retail Bank services the loan, deposit and transactional banking requirements of the personal and small business segments of the bank across its combined and still expanding network of 65 branches in Papua New Guinea, Solomon Islands, Fiji and Niue. The electronic banking component of this network also continues to grow and now includes almost 200 ATMs and more than 3000 EFTPOS devices in PNG. The electronic banking network in the Solomon Islands and Fiji has also grown considerably.

Retail PNG
2010 Highlights

The process of "modernisation and transformation" commenced in 2009 continued during 2010, resulting in improved revenues. Retail Bank's net revenues before the allocation of overheads increased when compared to the 2009 figures and the number of retail customers grew by 5% during 2010.

Increased transactional activity and revenues were achieved through a number of initiatives including the expansion and upgrade of EFTPOS devices and the enhancement of the bank's SMS banking product.

New EFTPOS terminals using GPRS communication protocols were introduced to replace older and slower technology. At larger EFTPOS merchant sites, IP communication protocols were introduced improving transaction authorisation times even further.

A number of enhancements were made to the bank's SMS banking product and these resulted in the customer base for this product increasing by 100%.

The number of ATM locations increased during 2010 and a programme of replacing older ATM's with more modern equipment continued.

Changes to the organisational structure of Retail Bank introduced during 2009, have resulted in better controls and communication and these contributed to improved service to our clients and growth outcomes.

Notwithstanding the increase in customer numbers achieved during 2010, Papua New Guinea remains largely unbanked due to communication and access difficulties in rural PNG. With the expansion of mobile phone communications across PNG in the past 18 months, new cost effective means of providing basic banking services have emerged. To take advantage of these developments and achieve greater outreach, BSP launched a new agency network under the name of BSP Rural. A pilot was set up in October 2010 and agencies established in Kwikila, Daulo and Lufa. Expansion of this agency network will commence in 2011.

2011 Challenges

During 2011, Retail Bank will continue to focus on improving our customer service, enhancing the functionality of electronic channels, expanding the electronic banking network into rural PNG and stimulating the use of these channels.

In early 2011, the bank's Internet banking channel will be upgraded and several new features launched to provide easy access and improved convenience for Internet banking customers.

Further enhancements will be made to our SMS banking channel and these, together with the expansion of the BSP Rural network, are expected to bring considerable numbers of previously unbanked people into the formal banking system.

The volume of card transactions will be further stimulated with the continuing expansion of ATMs and EFTPOS, as part of our strategy to increase points of pay.

New products and service delivery points to meet the needs of the High Net Worth Individuals (HNWI) will be launched in the first quarter of 2011 providing a premier level of banking service under the label of BSP First.

Corporate

Corporate forms a major part of BSP's Wholesale banking operations, together with Paramount Banking SBU.

From an overall perspective, the Corporate business continued to contribute strongly to the financial performance of BSP. Corporate's lending book increased by 16% in 2010, and this trend included the acquisition of several new clients. The growth trend is slightly below the system growth indicators published by the Bank of Papua New Guinea, and this is largely because a strategic and responsible approach has been taken by the bank to vigilantly monitor the quality of its loan book especially at a time of strong economic activity. This impacts BSP's market share position, which has decreased from 51.5% in 2009 to 50.4% at the end of 2010.

During 2010, a key Transformation initiative implemented by the Corporate Strategic Business Unit was its new customer segmentation model. This model now segments the client relationships being managed by this business into Strategic, Large Corporate, Mid-Corporate and Small Business categories, based on turnover. Much work has been undertaken to classify client relationships into the various segments. Allied to this initiative was the development of strategic plans for existing relationships, and for segment growth.

As part of the bank's strategy to position itself to be able to offer competitive services to clients and prospects involved in the increasing LNG sector and support industries, the Corporate team became heavily involved in the bank's PNG LNG project work. Several international companies participating in the PNG LNG project have developed relationships with BSP, and these will hopefully be expanded in the future.

Product development work was commenced by BSP Corporate, to complement the segmentation and client planning exercises. Client profiles have been developed, leading to the identification of potential gaps in the product offer and service levels. New products are being considered, as well as revised packaging of existing products. The product development effort will help to modernise BSP's relationship with its clients, extending the bank's capacity to build relationships with corporate clients outside the traditional lending products, as and when required. Product knowledge is being expanded to improve cross-selling sales and service capability.

In 2010 and continuing into 2011, there is intense activity in progress around the infrastructure to support product development and repackaging. Changes to the physical service environment are being made, product information and training delivery has been expanded and strengthened, and contracts and other documentation are under revision, to achieve a 2011 market roll out.

The extension of corporate banking business capabilities beyond the management of traditional lending relationships, to sell and support other banking products, should help diversify business opportunities for both clients and BSP. BSP's Corporate and Retail businesses are also jointly developing a strategy on cross-selling to corporate customers, using BSP's expansive branch network to touch all levels of corporate clients' points of representation across PNG.

The growth of BSP's corporate business in Fiji is a priority initiative for the bank in the region, and opportunities presented by cross-border clients in the region will be an area receiving increasing attention.

The Internet banking service has been reviewed and is being redesigned; the implementation of the new improved version is expected in mid 2011. This solution will advance BSP's on-line offering to a level comparable to that of major banks in the region.

In terms of systems and processes, a more modern pricing model has been deployed in Corporate banking in 2010. In tandem with the customer profitability model, the model will align risks, resources and effort with returns. The Customer Profitability Model has been reviewed and upgraded to allow the measurement of customer relationship performance across several dimensions.

The Corporate SBU aspires to be better than its competitors in the Corporate banking business on a range of measures including reputation, asset quality, market share, profitability, client satisfaction, innovation, and corporate responsibility. In 2011 and beyond, BSP's Corporate banking will accelerate its shift from a historically reactive service provider, to a proactive sales and service oriented business.

Treasury

The BSP Group operates in three very different environments, each with particular characteristics. What they have in common is that every one of them is small in the international context, with a small number of market participants, and a still developing foreign exchange market.

The bank remains very liquid, especially in PNG. BSP is currently discussing with BPNG how the Repurchase facility can be expanded to enhance overall market liquidity, promote an inter-bank money market and support a secondary bond market in the future.

While the size of BSP Alco's investment portfolio remained unchanged, the yield decreased as interest rate levels dropped in PNG. The amount of liquidity pouring into the market in 2010 forced rates down. Rates were not maintained at levels commensurate with inflation. This affected returns. However, the intrinsic value of the portfolio was promoted by long term assets at high interest rates. Maturing issues were replaced by shorter term paper, thereby reducing the duration and risk in anticipation of a future upturn in interest rates.

BSP PNG's Treasury managed to increase both market share and income from foreign exchange activities despite tightening margins and fierce competition. While some large multinationals were initially hesitant to expand the volume of foreign exchange with BSP, IFC's shareholding clearly enhanced BSP's standing as a counterparty resulting in a significant increase in turnover. A senior treasury marketing officer was recruited, and developed a Treasury marketing plan for 2011. This initiative will assist the bank with cross-selling to our customer base.

Exchange rate volatility sometimes favoured importers and benefitted exporters at other times. Unmatched foreign exchange positions caused by this volatility are managed through market risk management methods which tightly control the 'value at risk' exposure of BSP Treasury.

Paramount Banking

Paramount Banking is an integral division of Bank South Pacific managing K3.4b or over 45% of the bank's liability portfolio. The demands from our high value clients for better service compounded with competition from other banks for market share will continue to challenge the liability portfolio dominance currently enjoyed in Paramount Banking. Therefore strategies and objectives initiated in 2010 will continue in 2011.

The momentum of the LNG Project and related/spin off benefits to the wider community, Provincial Governments including Land owners and various sub contractors provides the opportunity for growth. Therefore we need to continue to refine service delivery mechanisms with emphasis on strengthening our relationship with high value clients.

We will continue to improve facilities at Paramount Banking Centres for clients including expanding services to new locations for clients' convenience. (eg Harbour City developments). Paramount Banking, together with Corporate and BSP Capital will strengthen relationships with high value clients.

The expected seasonal inflow of funds into the Paramount portfolio in the latter months of 2010 was below levels normally witnessed in prior years, and this has resulted in a slower annual growth trend in Paramount's deposit portfolio, compared to prior years. Recent announcements by the Central Bank have referred to a strategy whereby certain government trust funds could be retained by the Central Bank as part of an overall approach to the management of system liquidity, interest rates and inflation. This strategy has implications for Paramount's deposit portfolio, and will be addressed through the Paramount Banking SBU medium term business strategy and plan, for 2011 and beyond.

Highlights for the year 2010 included:-

- Continuing enhancement of our strategic partnership with the National Government and Donor Aid groups by leveraging opportunities with BSP's continually expanding electronic banking services and network in PNG.
- Continuing support for the National Government with its District Services Improvement Programme.

PNG Executive Team

Standing Left to right: Chris Beets (General Manager Treasury), Aho Baliki (General Manager Paramount Banking), Ian Mason (General Manager BSP Capital), Giau Duruba (General Manager Human Resources), Frans Kootte (General Manager Retail Bank)
Sitting: Left to right: Robin Fleming (Chief Risk Officer), Ian B Clyne (Chief Executive Officer), Johnson Kalo (Chief Financial Officer)

Credit and Risk

Credit and Risk Strategic Business Unit was engaged in much transformational activity during 2010, in addition to core business unit functions.

Transformation activity involved functional participation in projects sponsored by Credit and Risk Business Units, project involvement at a steering committee level and also as stakeholders in individual projects sponsored by other strategic business units. Operational Risk, Credit, and Audit contributions to this activity were substantial during the year and much of this work was undertaken by key subject matter experts within each of these business units.

Highlights of the individual business units in Credit and Risk are summarised below. Notwithstanding that Audit and Legal report to the CEO, their respective business highlights are included in the Credit and Risk Report for 2010 for purposes of completeness.

Credit

2010 continued the consistent loan growth achieved over recent years. With the exception of mid-size corporate customers, growth was achieved in all customer segments, led by the large corporates driven by continued capital expenditure in the Mining and Resource, Transport and Communication, and other infrastructure sectors.

The diversification of loans across key economic sectors will continue to be closely monitored to ensure no significant concentration risks develop that may impact the stability of the asset performance. The construction and development work of the PNG LNG project will continue to support growth in economic activity in all customer segments.

Performance of the loan portfolio remains sound with no major negative performance indicators evident. While delinquency and loss rates have increased marginally compared to the prior year, key delinquency and past due ratios are better than developing economy benchmarks.

Lending Policies and Procedures are reviewed on an ongoing basis with significant process changes made during 2010, focused on improving controls and reporting moving the bank towards compliance with best practice credit risk management standards. The last of the transformation project initiated changes approved by the Board are in the implementation phase for imbedding in the network during Quarter 1 2011.

Integration of the credit function in the Fiji operations is continuing to ensure standard business policies and practices are maintained across the group's operations and are expected to be completed in 2011.

Credit Inspection

Credit Inspection was established as a separate business unit in 2009. As a result of internal resource issues associated with transformation projects, the scheduled broad credit inspection of the corporate portfolio was curtailed in the second half of the year. To ensure that the lending portfolio remained subject to a credit review, PPB, a specialist recovery, insolvency and re-construction firm based in Australia, was again engaged to undertake a targeted credit file review for BSP.

In 2011, the credit inspection business unit will recommence its schedule of credit file reviews and portfolio analysis. This will involve site visitation/inspection of all wholesale business units across PNG, Solomon Islands and Fiji, with off-site/centralised inspection of selected retail business units. Credit Inspection may also undertake ad-hoc inspections based on specific factors, such as industry concentration or local economic factors.

Reports will be tabled at the completion of each review, which will detail not only asset quality, procedural accuracy and remedial actions required, but also provide some credit analysis/writing guidelines to portfolio managers.

Asset Management

A strong property market assisted with buoyant recoveries associated with mortgagee sale activities for non peforming loans. 2010 saw a marked reduction in volumes of loans being transferred to non performing and this could be attributed to the tighter assessment of loan applicants and increased early detection awareness.

Court litigations continue to be adversely affected by delays within the legal system. This affects only a small number of non performing loans. The bank pursues litigatiion where considered commercially viable or necessary to preserve the integrity of the bank's recovery rights.

Operational Risk

Since its separation from Audit in late 2009, the Operational Risk Department has employed its efforts on strengthening the overall risk management capability of BSP through the embedding of the Operational Risk Management Framework (based on the Basel II Standardised Approach Model) across the bank.

A key element of this exercise was fostering a risk culture throughout the bank. This was and continues to be a critical step as it sets the foundation for all components of the risk and control environment, provides improved discipline, integrity and ethical values.

Other risk initiatives undertaken during 2010 include:

- Mapping of the key internal processes, identifying the key risks and mitigating controls;
- Identification of the top 20 enterprise-wide risks across the bank;
- Development of monitoring tools (key risk indicators) to assist management better monitor their operational risks;
- Improvement of monitoring and analysis of non-lending related losses across the Retail Bank network, resulting in the reduction in operational losses;
- Assistance for Executives and Senior Management with analysis and regular reporting of operational risk issues;
- Implementation of the Anti-Money Laundering (AML) Norkom software to better monitor suspect and fraudulent transactions;
- Development of the Magique risk database to improve the capturing of risk assessment, loss and incident data in a centralised manner;
- Refinement of the management control attestations completed on half-yearly basis;
- Enhancement of the process in investigating fraudulent transactions;
- Provision of training to staff on the technical aspects of Operational Risk;
- Regular operational risk, anti-money laundering and fraud awareness workshops across the bank;
- Creation of the Business Continuity and Social and Environmental Management units within Operational Risk; and
- Separation of the BSP Fiji Audit and Risk in late 2010 to further strengthen the overall risk management capability of the Country Branch and creation of the Risk and Compliance Officer role in Solomon Islands.

Audit

Following the restructure of the Audit & Risk Business Unit late in 2009, where three separate business units were created – Audit Business Unit; Operational Risk Business Unit and Credit Inspection Business Unit – the Audit Business Unit continued with its 'modernisation' exercise during 2010.

The goal of this exercise is to accommodate and strengthen the bank's ongoing corporate governance principles in providing specialised and enhanced risk management and audit functions across all of the jurisdictions that it operates within.

The acquisition of the Colonial Group operations in Fiji has resulted in the creation of two internal audit teams based in Suva during the second half of 2010 – one in the Bank business and one in the Life Insurance business. They will be fully functional from early 2011.

BSP now has independent internal audit functions in Solomon Islands, Fiji and PNG with these various teams reporting, through the Head of Internal Audit, functionally to the Board Audit Risk and Compliance Committee (BARCC) in Port Moresby and administratively to the Chief Executive Officer (via the respective Country Managers).

PricewaterhouseCoopers (PwC) were also engaged in 2010 to assist review, and update the bank's audit processes, procedures (methodology) and technology. In conjunction with this, an exercise was also initiated to review the capabilities of the audit staff and to develop training and coaching plans to upskill the staff across all of the audit teams. Phase II of this exercise will continue during 2011.

In its endeavours to strengthen the corporate governance principles in the BSP Group, the Board Audit Risk and Compliance Committee also approved the recommendation to create several Branch Audit Officer positions at its meeting in October 2010. The Branch Audit Officers will be based permanently, from early 2011, in designated Port Moresby, Lae and Mt Hagen branches undertaking their independent audit tasks and reporting directly to the Head of Internal Audit.

Along with the initiative in 2009 to create Regional Audit Officer positions based in Mt Hagen, Lae and Kokopo, the Audit Business Unit will now have the ability to provide a more comprehensive and proactive audit coverage to ensure that the branches (and business units) are complying with the bank's internal controls, policies and procedures.

During 2011, the continued rollout of audit and risk software and other audit technology to Fiji and Solomon Islands will also complement the work PwC is assisting the bank with, regarding the ongoing standardisation of audit fieldwork (workpapers) and audit reports across the various audit teams.

Legal Services

Legal Services department maintained effective service standards in respect of compliance with POMSOX and SPSE reporting requirements, BPNG regulatory requirements, corporate compliance requirements, and also board secretarial functions within the bank. The department continued with its carriage of in house legal matters and internal legal advice to departments within the bank. Work was commenced on the creation of a compliance section within Legal Services to more effectively manage and monitor compliance functions across the bank.

Human Resources

The Human Resources Strategic Business Unit (SBU) provides support services to all strategic business units with the following core People Capital Management service functions;

- Recruitment and Selection
- Training and Development
- Performance and Benefits Management.
- Succession Planning

The HR SBU implemented a number of strategic initiatives in 2010 under the Transformation Programme.

These are;

- Introduction of the Staff Selection and Policies Manual to improve the recruitment function and training of business unit managers to use these tools and procedures to recruit best fit candidates.
- Conducting New Account Opening process training using Fast Path throughout the branches within Papua New Guinea, to improve quality of customer data and service levels of branches.
- Revamping of the Performance Management System (PMS) and training for all the managers and supervisors within Papua New Guinea Operations.

  We also introduced a new bonus scheme linked to the Performance Management System
- Introduction of the Human Capital Management system to improve the management of personnel data in the bank. The employee and manager self service modules of this system will be introduced in the second quarter of 2011.
- Prepared job profiles in the new format for the generic positions in the bank and used these revised job profiles to re-grade all the positions in the bank. The exercise also resulted in amendments to the salary structure to maintain competitiveness in increasingly competitive sectors of the labour market.

In 2010 we experienced some marginal improvements in the HR metrics we normally benchmark our performance against. The staff turnover was at 7.4% which is below the normal 10% rate experienced in the last two years. This is an excellent outcome compared to PNG standards and the LNG impact. Total headcount for 2010 was 3720.

Total training man-days increased marginally to 8366 compared to 7568 in 2009. A large portion of these was for back to basics training in Retail Bank operations.

Operations

The Operation SBU contains the following Business Units:

- Branch Operations
- International Operations
- Channel Operations
- Lending Support
- Information Technology
- Project Management Office
- Support Services
- Security Services
- Intranet/Documentation

The plan formulated in 2009 to establish a "Pacific Operations Centre" in Port Moresby by 2012 continued to take shape. Building plans also feature an independent data centre facility in a new Port Moresby location with a DR facility contained within the premises of the Pacific Operations Centre.

With the rapid growth of BSP's ATM fleet across PNG, Solomon Islands and Fiji in recent years, the economics of the ATM channel and its operations continue to change. The demands on the operational support activities have increased significantly, attributable largely to the geographically diverse and remote locations in the BSP ATM network. Given that this network is expected to grow further in coming years, BSP has started a review of its ATM supply and operational support requirements, aiming in 2011 to determine and formalize appropriate arrangements internally and with external parties, where appropriate.

New branches were opened in Motukea and Porgera plus work commenced for the Vision City Branch. Work started for bank premises in Ravalien Haus, including the initial BSP First outlet that is a model for further premier locations. These activities represent significant steps forward in BSP's goal to provide the best service to customers. In the area of ATMs there was a significant step forward with the rollout of a management facility for all of BSP's ATMs; this allows remote monitoring of ATMs to check their status and cash availability and is a significant productivity tool for the bank. The electronic data storage system BizeDocs project continued its implementation with a major step forward being the elimination of printing system reports in each branch; branch reports are now available in an electronic format and bank users can annotate their comments on to the electronic version, saving time and money by eliminating printing of reports.

There were multiple important IT achievements during the year. 2010 saw MasterCard and Pulse network transactions acquired at BSP ATMs. MasterCard transactions are now also acquired at POS devices. Westpac cards are also acquired at BSP ATMs which means that BSP now acquires Visa, MasterCard, Pulse, Westpac PNG and ANZ PNG cards across ATM and POS channels. A significant productivity tool was launched assisting the Operations area to reconcile internal accounts; this tool provides automated reconciliation of most (85-90%) entries, leaving a smaller number for manual investigation. Credit and Risk were assisted by the implementation of the Norkom Anti-Money Laundering system; this provides compliance to international monitoring standards to detect suspected money laundering activities. BSP Rural is an important new channel to extend the bank's distribution to provide banking facilities in remote areas. IT enabled this initiative by providing the facilities for BSP Rural to operate in their remote locations. This initiative both supports BSP's social responsibility and provides tangible benefits to customers who no longer need to make long, difficult and expensive visits to regional towns and cities for their banking needs.

Transformation is the name of the programme of work initiated by the bank to change the way we work with technology. Many years ago the bank invested in an internationally recognised core banking system. Now we want to do more with the system and instead of replacing it, with all the time and money that would take, BSP decided it would be more efficient and provide a better return on investment to rediscover the core banking system than to replace it. The Transformation Programme achievements in 2010 were:

- Created a new Chart of Accounts with a structure that supports the bank's new Market Segmentation strategy and provides the platform for improved financial reporting.
- Implemented Phase 1 of Customer Information File Cleanup activities for Corporate and Paramount Banks. This implemented the BSP standard for retention of customer data in the CIF and addressed incomplete data in customer records. This was done jointly with the initiative to address BSP's Market Segmentation Programme.
- Implemented Phase 1 of reviewing the BSP Lending processes, products and fees for the Corporate Bank. This increased efficiency and reduced risk. Manual fees were automated wherever possible.
- Reviewed BSP Fees for the Retail Bank to automate the collection of fees wherever possible.
- Launched a streamlined customer / account opening tool FASTPATH that provides higher productivity and more accurate data collection. This was successfully launched in the Retail Bank with plans to extend it to other businesses.
- Implemented testing tools within the IT Department that fundamentally changed the productivity of the bank's Testing Services team. Since the tools have been used the Testing team has been recognised by international stakeholders as one of the best teams they have encountered. While the testing tools revealed this level of expertise, it couldn't happen without the intellectual capital residing in Testing Services to start with.
- Implemented a market leading software management tool for the IT Department to control programming source code. This aligns the bank with international standards of source and object code management.

Finance and Planning

The bank has taken a major transformation and modernisation project driven through individual Strategic Business Units (SBU). In alignment with Bank and Group Strategy, the SBUs developed projects to improve their customer service levels both internally and externally, improve efficiency and maximise productivity. Finance and Planning initiated its share of projects primarily to improve manual processes; improve efficiency and retrieve accurate and timely data.

Finance and Planning's major projects were:

- The ICBS General Ledger Restructure - the General Ledger Restructure Project was taken to achieve several key objectives.
    - Improve financial reporting capabilities to help management better understand the financial position and performance of individual business units and dimensions within the organisation.
    - Implement a Chart of Accounts and reporting structures within the bank's General Ledger to provide better support for the bank's market segmentation strategies.

  The work to effect the ICBS General Ledger Restructure was performed in 2010, and the restructure was successfully implemented on the 4th of February 2011.
- More automated Budget and Forecasting tool to streamline and simplify processes, minimise error, and improve timeliness.

The new budgeting tool moves BSP along the path to:

- Integrated financial and operational planning in one system.
- Faster budget cycle time, increased budget accountability.
- More ability to analyse budget data and greater data accuracy and version control.

- Customer Profitability and Activity Based Management Models – revisions were made to the analytical reporting applications that model business processes to determine cost, profitability and drivers. These models support informed decisions that streamline processes, deliver revenue growth and reduce costs across the organisation.

- Establishment of a Procurement Function – to address sustainable procurement programmes aiming at reducing costs, increased efficiencies, and risks/mitigations.

The SBU also underwent a restructure in 2010.

Risk management and compliance aspects of the businesses are managed by a functional area called Governance and Risk. This section monitors and reviews the risk management processes, the risk profile and the processes for compliance with prudential regulations and standards and other regulatory requirements. This section also works closely with the bank's Operational Risk Management (ORM) to address issues highlighted in the annual audit reviews.

The Financial Planning and Control function of the SBU was divided into two sections, of which, one section focuses on Internal Management Reporting and Budget/ Forecast Cycles while the other section provides more financial analysis and financial information. This organisation supports, process initiatives to realise the SBU's vision to be an essential business partner who provides reliable and credible information and advice to our stakeholders to drive better performance.

Finance and Planning produced four Business Controllers who are placed in other Strategic Business Units to meet the Management Reporting requirements of the SBUs and its business units. Improvements to Management Report formats are being developed for businesses.

Maintaining skilled and well versed staff continues to be a challenge given the high demand for finance and accounting staff in PNG and the Pacific.

Going forward, Finance and Planning aims to drive an analytical culture in BSP, to inform business decisions.

Deputy General Managers

Left to right: Bob DeBrouwere (Human Resources), Lew Kenah (Retail Bank), Paul Russell (Paramount Banking), Rob Mantel (Finance) (Absent) Daryl Balchin (Security)

Corporate Governance

BSP has adopted an approach to Corporate Governance that is underpinned by its core values of Integrity, Leadership, People, Professionalism, Quality and Teamwork. This approach is supported by a comprehensive framework of Corporate Governance principles and policies. The BSP Board has demonstrated its commitment to developing and maintaining a standard of corporate governance that seeks to match global practice.

The Board ensures that it complies with the requirements of BSP's home exchange, Port Moresby Stock Exchange ("POMSOX"). It also closely monitors developments in corporate governance principles and practice within Australia and has benchmarked itself against:-

1. ASX Corporate Governance Council "Corporate Governance and Best Practice Recommendations"
2. Australian Prudential Regulatory Authority Prudential Standard APS 510
3. Standard Australia AS 8000-2003 Good Governance Principles

BSP is mindful of the advantages of demonstrating to investors that its corporate governance standards meet the requirements expected of companies listed in countries such as Australia. This Corporate Governance Statement therefore compares BSP's corporate governance practices to the ASX Corporate Governance Council and Best Practice Recommendations.

BSP manages in excess of half the banking market in Papua New Guinea, and is predominantly owned by institutions and individuals in Papua New Guinea. The Board, management and staff of BSP are very much aware of their responsibilities to the people of Papua New Guinea. The set of Corporate Governance principles developed by BSP is intended to provide a framework that will help to ensure that BSP deals fairly and openly with all its stakeholders – shareholders, customers and staff alike.

BSP publishes its corporate governance practices on its website. This is available at www.bsp.com.pg in the shareholders section.

1. The Board Of Directors

a) Role and Responsibility of the Board

The roles and responsibilities of the Board are defined in the Board Charter. This document also details the matters reserved for the Board and matters that have been delegated to management. The Board, with the support of its committees, is responsible to the shareholders for the overall performance of the company including its strategic direction; establishing goals for management; and monitoring the achievement of those goals with a view to optimising company performance and increasing shareholder value.

Key functions of the Board include:

- overall strategy of the company, including operating, financing, dividends, and risk management;
- appointing the Chief Executive Officer and setting an appropriate remuneration package;
- appointing General Managers and setting appropriate remuneration packages;
- appointing the Company Secretary and setting an appropriate remuneration package;
- endorsing appropriate policy settings for management;
- reviewing Board composition and performance;
- reviewing the performance of management;
- approving an annual strategic plan and an annual budget for the company and monitoring results on a regular basis;
- ensuring that appropriate risk management systems are in place, and are operating to protect the company's financial position and assets;
- ensuring that the company complies with the law and relevant regulations, and conforms with the highest standards of financial and ethical behaviour;
- acquisitions and disposals material to the business;
- establishing authority levels;
- Directors' remuneration via the Remuneration and Nomination Committee;
- selecting, with the assistance of the Audit, Risk and Compliance Committee, and recommending to shareholders, the appointment of external auditors;
- approving financial statements.

A number of these responsibilities have been delegated by the Board to various committees. The committees and their responsibilities are detailed below under Board Committees.

The Board has delegated to management responsibility for:

- developing the annual operating and capital expenditure budgets for Board approval, and monitoring performance against these budgets;
- developing and implementing strategies within the framework approved by the Board, and providing the Board with recommendations on key strategic issues;

- appointing management below the level of General Manager and preparing and maintaining succession plans for these senior roles;
- developing and maintaining effective risk management policies and procedures;
- keeping the Board and the market fully informed of material developments.

b) Membership, expertise, size and composition of the Board

The Corporate Governance Principles affirm that the majority of the Board should be independent. As is typical of small financial markets generally, in Papua New Guinea, there are very considerable demands on the relatively small numbers of people with the skills and experience to fill the demanding role of Non-executive Director on the Boards of the Nation's larger corporate institutions. In these circumstances it is inevitable that a number of the Non-executive Directors of BSP will also have roles on the Boards, or in Senior Management, of institutions that may be significant shareholders in, or substantial customers of, the bank. Directors of BSP are meticulous in handling situations where there could potentially be conflicts of interest, by declaring their interests in advance, and absenting themselves from any consideration of matters where a conflict might arise. The bank's Corporate Governance Principles require Directors to disclose any new Directorships and equity interests at each Board meeting.

The maximum number of Directors, as prescribed by the Constitution approved by shareholders, is ten. At the date of this report there are ten Directors, with nine Non-executives designated as independent, plus the Chief Executive Officer. Under the Constitution, at each annual general meeting one-third of the company's Directors, in addition to any Director appointed during the year, excluding the Chief Executive Officer, must offer themselves for re-election by the shareholders. Normally, Non-executive Directors are expected to serve a maximum of four three-year terms, dating from the AGM at which the newly elected Director is first confirmed by shareholders. This provision has effect from the date the bank took its present form, following the merger of BSP with the Papua New Guinea Banking Corporation in April 2002. The Board will apply this provision with a degree of flexibility should it be necessary to ensure appropriate continuity, bearing in mind the particular circumstances of the Papua New Guinea market.[1]

The Board has a broad range of skills, experience and expertise that enables it to meet its objectives. Details of the Directors' business backgrounds and experience are provided on pages 10 and 11.

1 For example, to avoid a situation where a number of Directors would otherwise be approaching retirement date at around the same time, or to recognise circumstances when suitably qualified candidates may not be immediately available.

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

Nominees of the Board and/or shareholders must meet the "fit and proper person" criteria established by the Bank of Papua New Guinea before they can take their place on the Board. The Board does not accept that any office bearer and/or employee of an institutional shareholder, by virtue only of his/her position within that organisation, have an automatic right to be appointed to the Board.

On joining the Board, new Directors will be provided with a comprehensive orientation programme.

c) Role and selection of the Chairman

The Chairman is elected by the Directors every two years and holds the position for a maximum of three terms. His role includes:

- ensuring all new Board members are fully aware of their duties and responsibilities;
- providing effective leadership on the company's strategy;
- presenting the views of the Board to the public
- ensuring the Board meets regularly throughout the year, and that minutes are taken and recorded accurately;
- setting the agenda of meetings and maintaining proper conduct during meetings;
- reviewing the performance of Non-executive Directors.

The Chairman is not permitted to occupy the role of Chief Executive Officer.

Kostas Constantinou, OBE, who sits on the Board as an independent Non-executive Director, is the current Chairman.

d) Director independence and Conflict of Interest

Directors are determined to be independent if they are judged to be free from any material or other business relationship with the bank that would compromise their independence. Prior to appointment, Directors designated, are required to provide information to the

Board for it to assess their independence.

In assessing the independence of Directors, the Board will consider a number of criteria including:

- the Director is not an executive of the bank;
- the Director is not a substantial shareholder of the bank or otherwise associated directly with a substantial shareholder of the bank;
- the Director has not within the last three years been a material consultant or a principal of a material professional adviser to the bank or a group member, or an employee materially associated with the service provided;
- the Director is not a material supplier to or customer of the bank or other group member, or a material consultant to the bank or other group member, or an employee materially associated with the material supplier or customer;
- the Director has no material contractual relationship with the bank or other group member other than as a Director of the bank;
- the Director is free from any interest and any business or other relationship which could, or could reasonably be perceived to, materially interfere with the Director's ability to act in the best interests of the bank.

This information is assessed by the Board to determine whether on balance the relationship could, or could reasonably be perceived to, materially interfere with the exercise of the Director's responsibilities. Materiality is assessed on a case-by-case basis.

As noted earlier, the Board is cognisant of the need to avoid conflicts of interest and it has in place policies and procedures for the reporting of any matter, which may give rise to a conflict between the interests of a Director and those of the company. These arrangements are designed to ensure that the independence and integrity of the Board are maintained.

The Bank of Papua New Guinea sets prudential limits on loans to "associated persons ": Bank South Pacific fully complies with these requirements.

Financial Note 31, Related party transactions, on pages 94 - 96, provides details of Directors' interests.

e) Meetings of the Board and attendance

Scheduled meetings of the Board are held at least every two months, and the Board meets on other occasions as necessary to deal with matters requiring attention. Meetings of Board Committees are scheduled regularly during the year. The Board has a policy of rotating its meetings between locations where the company has a significant presence. On these occasions the Board also visits company operations and meets with local management and key customers.

The Chairman, in consultation with the Chief Executive Officer, determines meeting agendas. Meetings provide regular opportunities for the Board to assess BSP management of financial, strategic and major risk areas. To help ensure that all Directors are able to contribute meaningfully, papers are provided to Board members one week in advance of the meeting. Broad ranging discussion on all agenda items is encouraged, with healthy debate seen as vital to the decision making process.

Financial Note 32, Directors' and Executive remuneration, on pages 98 - 100, provides attendance details of Directors at Board meetings during 2010.

f) Review of Board Performance

The Remuneration and Nomination Committee reviews the processes by which the Board regularly assesses its own performance in meeting its responsibilities. It is intended to extend the assessment of the Board as a whole to include an assessment of the contribution of each individual Director. The Board is cognisant of the need to continually identify areas for improvement; to ensure that it meets the highest standards of corporate governance; and for the Board and each Director to make an appropriate contribution to the company's objective of providing value to all its stakeholders. The performance review is conducted annually, and may involve assistance from external consultants.

g) Board Access to Information and Advice

All Directors have unrestricted access to company records and information and receive regular detailed financial and operational reports to enable them to carry out their duties. The General Managers make regular presentations to the Board on their areas of responsibility. The Chairman and the other Non-executive Directors have the opportunity to meet with the Chief Executive Officer and the General Managers for further consultation, and to discuss issues associated with the fulfilment of their roles as Directors.

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

2. Board Committees

a) Board Committees and Membership

The Board has established two committees whose functions and powers are governed by their respective charters. These committees are the Audit Risk and Compliance Committee, and the Remuneration and Nomination Committee.

Membership of the committees and a record of attendance at committee meetings during the year is detailed in table below. Remuneration details are provided in Financial Note 32 on page 98.

Membership of Board Committees as at 31 December 2010

	Board Audit Risk and Compliance Committee	Remuneration and Nomination Committee
John Jeffery	5/7 Chair	
Nagora Bogan	3/7	
Gerea Aopi	4/7	
Tom Fox	6/7	Chair 4/4
Noreo Beangke		2/4
Ila Temu		4/4

b) Committee Charters

The Committee Charters are available in the shareholders information section of the BSP website www.bsp.com.pg

c) Committee Structure

Committee members are chosen for the skills, experience and other qualities they bring to the committee. At the next Board meeting following each committee meeting, the Board is given a report by the Chairman of the respective committee and minutes of the meeting are tabled.

The Audit Risk and Compliance Committee is comprised of three Non-executive Directors, a majority of whom should be independent, and who are duly appointed by the Board. The Chairman of the Audit Risk and Compliance Committee must be one of the independent Directors, other than the Chairman of the Board. Each member should be capable of making a valuable contribution to the committee and membership is reviewed annually by the BSP Board.

The Remuneration and Nomination Committee comprises three Non-executive Directors, the majority of whom should be independent, and who are duly appointed by the Board. The Chairman of the Remuneration and Nomination Committee must be one of the independent Directors, other than the Chairman of the Board. Each member should be capable of making a valuable contribution to the committee, and membership is reviewed annually by the BSP Board.

A review of the performance of committee members forms part of the Board's performance review.

d) Board Audit Risk and Compliance Committee

The Audit Risk and Compliance Committee is delegated by the Board with responsibility for reviewing and monitoring the:

- integrity of the financial statements and the financial reporting and audit process;
- external auditor's qualifications, performance and independence;
- performance of the internal audit function of the bank;
- performance of the operational risk function of the bank;
- systems of internal control and management of all risks;
- systems for ensuring operational efficiency and cost control;
- systems for approval and monitoring of expenditure including capital expenditure;
- processes for monitoring compliance with laws and regulations (both in Papua New Guinea and overseas);
- implementation of Board decisions by management and making recommendations to the Board for the appointment of the external auditor;
- annual internal audit plan and its ongoing review.

In the course of fulfilling its mandate, the committee meets with both the internal and external auditors without management present.

i. Annual Financial Statements

The Audit Risk and Compliance Committee reviews the annual financial statements to determine whether they are complete and consistent with the information known to committee members and to assess whether the financial statements reflect appropriate accounting principles. In particular it:

- pays attention to complex and/or unusual transactions;
- focuses on judgmental areas, for example those involving valuation of assets and liabilities; provisions; litigation reserves; and other commitments and contingencies;
- meets with management and the external auditors to review the financial statements and the results of the audit;
- reviews the other sections of the Annual Report before its release and considers whether the information is understandable and consistent with members' knowledge about the bank and its operations;
- satisfies itself as to the accuracy of the financial accounts, reconciles them with management accounts presented to the committee, and signs off on the financial accounts of the bank before they are submitted to the Board.

ii. External Audit

The Audit Risk and Compliance Committee is responsible for making recommendations to the Board on appointment and terms of engagement of BSP external auditors. The selection is made from appropriately qualified companies in accordance with Board policy. The Board submits the name of the recommended appointee to shareholders for ratification. In line with the policy of the Bank of Papua New Guinea, the signing partner in the external audit firm must be rotated at least every three years.

The committee reviews annually the performance of the external auditors and makes recommendations to the Board regarding the continuation or otherwise of their appointment, consistent with the Bank of Papua New Guinea's Prudential Standard No. 7/2005 – External Auditors, while ensuring their independence is in line with Board policy.

There is a review of the external auditor's proposed audit scope and approach, to ensure there are no unjustified restrictions. Meetings are held separately with the external auditors to discuss any matters that the committee or the external auditors believe should be discussed privately. The external auditor attends meetings of the Audit Risk and Compliance Committee at which the external audit and half yearly review are agenda items.

The committee ensures that significant findings and recommendations made by the external auditors are received and discussed promptly, and that management responds to recommendations by the external auditors in a timely manner.

The duly appointed external audit firm may not be engaged by the company to provide specialist consultancy services relating to financial, strategic and /or taxation matters.

The external auditor is invited to the Annual General Meeting of shareholders and is available to answer relevant questions from shareholders.

The Bank of Papua New Guinea Prudential Standards provide for a tri-partite meeting between BPNG, the external auditors, and the bank, if required.

iii. Internal Audit

The Audit Risk and Compliance Committee approves, on the recommendation of management, the appointment of Head of Internal Audit. The committee meets regularly with Head of Internal Audit.

Reviews are undertaken of the scope of the work of the internal audit function to ensure no unjustified restrictions or limitations have been placed upon the Audit and Risk Departments. The Audit Risk and Compliance Committee also reviews the qualifications of internal audit personnel and endorses the appointment, replacement, reassignment or dismissal of the internal auditors.

An independent review by an expert consultant is made regularly as to the effectiveness of the internal audit and risk function. These reports are presented to the Board Audit Risk and Compliance Committee, and the Board.

The Audit Risk and Compliance Committee meets separately with the internal auditors to discuss any matters that the committee, or the internal auditors, believe should be discussed privately. The Internal Auditor has direct access to the Audit Risk and Compliance Committee and to the full Board. The committee ensures that significant findings and recommendations made by the internal auditors are received and discussed promptly, and that management responds to recommendations by the internal auditors on a timely basis.

Internal Audit meets with the external auditors half yearly, to review the scope and findings of internal audit's annual audit plan, and the extent of the external audit plan, having regard to internal audit's findings.

iv. Compliance

The Audit Risk and Compliance Committee reviews the effectiveness of the systems for monitoring compliance with all legal and regulatory obligations

Believe

- to place confidence
or faith in the truth

and the Constitution of the bank. It also reviews the results of management's investigation and follow-up (including disciplinary action) of any fraudulent acts, or non-compliance.

The committee obtains regular updates from management and the bank's legal officers regarding compliance matters, and satisfies itself that all regulatory compliance matters have been considered in the preparation of the financial statements.

Reviews of the findings of any examinations by regulatory agencies are undertaken and the Chairman of the Board Audit Risk and Compliance Committee has the right to approach a regulator directly in the event of a prudential issue arising.

v. Risk Management

The committee's role in the bank's risk management processes are detailed in 3(b).

e) Board Remuneration and Nomination Committee

The Remuneration and Nomination Committee has been established to assist the Board in fulfilling its oversight responsibilities in respect of Board and Senior Executive Management selection, appointment, review and remuneration.

The responsibilities of the Remuneration and Nomination Committee are:

- oversee the selection and appointment of a Chief Executive Officer and recommend an appropriate remuneration and benefits package to the full Board;
- determine and review appropriate remuneration and benefits of Directors for recommendation to the full Board, and subsequently to the shareholders;
- identify and maintain a clear succession plan for the Executive Management Team, ensuring an appropriate mix of skills and experience as well as appropriate remuneration and benefits packages are in place and reviewed regularly;
- ensure that the Board itself maintains an appropriate mix of skills and experience necessary to fulfil its responsibilities to shareholders while maintaining a world class Corporate Governance regime;
- receive and endorse positions/titles recommended by the Chief Executive Officer from time to time as applying to designated Senior Executive Management positions;
- review the procedures in place to ensure that all new Senior Executive appointees are adequately qualified and experienced, and that proper recruitment procedures are followed;
- review and make recommendations to the Board on the appointment and terms and conditions of employment to all Senior Executive Management positions;
- review and approve all termination arrangements for such Senior Executives;
- review transactions between the company and any of the Directors or relevant Senior Executives;
- review and make recommendations to the Board on employee remuneration and benefits' policies and practices generally;
- engage external consultants as and when deemed appropriate to benchmark remuneration packages for Executives and Senior Management;
- review Board performance, tenure, and succession planning.

The Board has in place a review process, led by the Chairman, that involves a peer review of performance based on a broad range of criteria. A performance review was performed in 2010 and early 2011.

3. Risk Management

a) Approach to Risk Management

The bank's Risk Management activities are aligned to the achievement of the bank's Objectives, Goals and Strategy. The Board, in consultation with the Executive Committee, determines the bank's risk appetite and risk tolerance. These benchmarks are used in the risk identification, analysis and risk evaluation processes. BSP distinguishes the following major risks:

Credit Risk - The potential for financial loss where a customer or counter party fails to meet their financial obligation to the bank.

Market Risk - The potential financial loss arising from the bank's activities in financial, including foreign exchange, markets. More detailed commentary on financial risk management is provided in the Notes to the Financial Accounts.

Liquidity Risk – The risk of failure to adequately meet cash demand in the short term without incurring financial losses.

Interest Risk - Risk to earnings from movement in interest rates.

Operational Risk - The risk of loss resulting from inadequate or failed internal processes, people, or from external events, including legal and compliance risk.

The bank's Asset and Liability Committee monitors market risk, interest risk, and liquidity risk, and the Credit Committee monitors credit risk. Operational risk is monitored by the Operational Risk Committee, including the maintenance of a risk register system that has been implemented across the bank. The Executive Committee and the Board overview the highest tier of risks within these risk registers.

The bank's risk management policy ensures that the bank has in place acceptable limits for the risks identified by the bank's employees. The risk management approach encompasses the following:

- defining the types of risks that will be addressed by each functional or policy area (i.e., credit risk, interest rate risk, liquidity risk, operational risk, etc.);
- ensuring that mechanisms for managing (identifying, measuring, and controlling) risk are implemented and maintained to provide for organisation-wide risk management;
- developing information systems to provide early warning, or immediate alert, of events or situations that may occur, or already exist, that could create one or more types of risk for the bank;
- creating and maintaining risk management tools, including those requested by the Board, such as policies, procedures, risk registers, controls and independent testing, personnel management and training, and planning;
- instituting and reviewing risk measurement techniques that Directors and management may use to establish the bank's risk tolerance, risk identification approaches, risk supervision or controls, and risk monitoring processes;
- developing processes for those areas that represent potential risks;
- establishing appropriate management reporting systems regarding these risks so individual managers are provided with a sufficient level of detail to adequately manage and control the bank's risk exposures.

b) Risk Management Roles and Responsibilities

The Board accepts responsibility for ensuring it has a clear understanding of the types of risks inherent in the bank's activities. Therefore, responsibility for overall risk management in BSP is vested with the Board. However every employee from Executive Management to the newest recruit has a responsibility and a part to play in the process.

There is a formal system of financial and operational delegations from the Board to the Chief Executive Officer, and from the Chief Executive Officer to the General Managers. These delegations reflect the bank's risk appetite, and are cascaded down to managers who have skills and experience to exercise them judiciously.

The Board defines the accountabilities (including delegated approval/control authorities/limits) and reporting/monitoring requirements for the risk management process. The severity of risks identified in the risk identification, analysis and evaluation processes, and noted in the Strategic Business Unit Risk Registers, is used to determine the approval/ control authorities/ limits. The Board reviews these risk limits annually along with an annual review of the bank's significant risks.

The Board has adopted guidelines, with the help of management analysis, covering the maximum loss exposure the bank is able and willing to assume. These guidelines are detailed in the bank's Risk Policy and Procedures Manual which has been externally reviewed and approved by the Board.

The Board has also delegated to the Audit Risk and Compliance Committee responsibility for overview of loss control and for overseeing the risk management function.

The Board Audit Risk and Compliance Committee is responsible for providing regular reports and recommendations to the Board on the risk management activities of the bank, especially relating to risk issues that are outside of the authority of the bank's Executive Committee to approve.

The bank's Executive Committee is responsible for deliberating on risk management issues which are outside of the delegated authorities/ limits of the Credit Committee, Asset and Liability Committee (ALCO) and General Managers, with escalation of these issues to the Audit Risk and Compliance Committee, and the Board itself, in case of need.

c) Management Assurance

The Board is provided with regular reports about BSP's financial condition and its operating performance. Annually, the Chief Executive Officer and the Chief Financial Officer certify to the Board that:

- the financial records of the bank have been properly maintained and that they accurately record the true financial position of the company;

- the financial statements and notes meet all appropriate accounting standards;
- there are sound systems of risk management and control that are operating effectively.

Additionally, all General Managers provide bi-annual statements attesting that:

- they have assessed and documented the risks and internal control procedures in their Strategic Business Unit;
- they have identified any changes in business, operations and computer systems and the risks that may arise from those changes;
- the risk management and internal compliance and control systems are appropriate and operating efficiently and effectively;
- any weaknesses in the risk management and internal compliance and control systems have been identified and remedial action taken.

4. Ethical Behaviour

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

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

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

BSP is committed to a culture in which it is safe and acceptable for employees, customers and suppliers to raise concerns about poor or unacceptable practices, irregularities, corruption, fraud and misconduct

The bank has adopted a whistle-blowing policy that is designed to support and encourage staff to report in good faith matters such as:

- unacceptable practices;
- irregularities or conduct which is an offence or a breach of laws of Papua New Guinea (actions and decisions against the laws of Papua New Guinea including non-compliance);
- corruption;
- fraud;
- misrepresentation of facts;
- decisions made and actions taken outside established BSP policies and procedures;
- sexual harassment;
- abuse of Delegated Authorities;
- misuse of company assets;
- disclosures related to miscarriages of justice;
- health and safety risks, including risks to the public as well as other employees;
- damage to the environment;
- other unethical conduct;
- failure to comply with appropriate professional standards;
- abuse of power, or use of the bank's powers and authority for any unauthorised purpose or personal gain;
- breach of statutory codes of practice.

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

Further, Directors and management may only trade in the securities of the company, subject to the foregoing insider trading restrictions, during each of the eight weeks following the announcements of half yearly profit and yearly profit or the date of issue of a prospectus. Management should discuss proposed share trades with the Chief Executive Officer in advance, who in turn will keep the Chairman of the Board appraised of management activities. Directors should discuss proposed share trades with the Chairman in advance.

In addition, Directors and management must not trade in any other entity if inside information on such entity comes to the attention of the Director or management by virtue of holding office as an Officer of the bank.

5. Market Disclosure

The bank's continuous disclosure regime is fundamental to the rights of shareholders to receive information concerning their securities. The most important aspect of the bank's shareholder communication policy is to comply with the continuous disclosure regime and to implement best practice disclosure policy.

Market announcements are posted to BSP's website immediately after release to the market. All market announcements made by the bank since its listing in August 2003 are currently available on the website.

Where BSP provides financial results' briefings to analysts or media, these briefings are published on the website as soon as possible after the event. In any event, no material information which has not been previously released to the market is covered in such briefings. The material upon which the briefing is based (such as slides or presentations) is released to the market prior to the briefing.

The bank's insider trading rules are important adjuncts to the continuous disclosure regime in ensuring that shareholders are given fair access to material information regarding securities. BSP seeks to limit the opportunity for insider trading in its own securities through its continuous disclosure policies and the dealing rules applying to its employees and Directors.

6. Shareholder Communications

BSP Code of Conduct requires its employees to act with high standards of honesty, integrity, fairness and equity in all aspects of their employment with the bank.

With this in mind, BSP commits to dealing fairly, transparently and openly with both current and prospective shareholders using available channels and technologies to communicate widely and promptly. The bank commits to facilitating participation in shareholder meetings, and dealing promptly with shareholder enquiries.

Our shareholder communication policy is built around compliance with disclosure obligations and aspiring to be at the forefront of best practice in disclosure. Our framework for communicating with shareholders is to concisely and accurately communicate:

- our strategy;
- how we implement that strategy; and
- the financial results consequent upon our strategy and its implementation.

The bank uses shareholder forums such as the Annual General Meeting, and group meetings with larger shareholders, within disclosure policies, to communicate financial performance and strategies.

7. Remuneration

BSP remuneration policy for senior management is comprised of a fixed component and an at risk component that is a combination of short term rewards and long term incentives. The remuneration packages of General Managers and the Chief Executive Officer are approved by the Remuneration and Nomination Committee, and details are provided by the committee to the Board.

Fixed remuneration of senior management is reviewed at the time of contract renewal taking into account the nature of the role, the pay position relative to comparable market pay levels, and individual and business performance.

The "at risk" component of the remuneration package is a performance based Executive Management Share Option Plan (EMSOP). This plan is structured to provide senior management with the incentive to deliver sustained growth in value for shareholders. Performance hurdles are incorporated in the EMSOP and senior staff are selected to participate based on their annual performance, potential, and the business need to retain critical skills.

Further information about the EMSOP is provided in Note 27 to the Annual Accounts on pages 88 - 91. Under PNG tax law individuals who participate in the EMSOP are responsible for any related taxation liabilities.

Non-executive Directors are remunerated on a fixed basis within an aggregate Directors' fee pool approved periodically by shareholders. The shareholders last approved a pool of K1.00 million in May 2006. During 2010, K1.00 million of the pool was utilised (2009: K0.73 million).

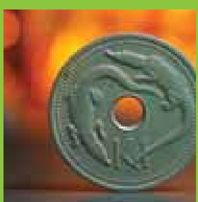
A table of fees paid to Directors during 2010 is produced on page 98. Non-executive Directors are not paid any retirement or superannuation benefits, nor do they participate in any share option programmes.

historical summary 2010

Profit and Loss (K'000)	2005[2]	2006	2007	2008	2009	2010
Net interest income	161,804	209,581	276,872	377,100	473,969	544,002
Non interest income	144,174	134,531	202,510	243,828	251,743	410,973
Bad and doubtful debt (expense)/recovery	3,968	1,311	4,345	(11,353)	(15,020)	(20,581)
Other operating expenses	(167,265)	(178,573)	(188,871)	(229,599)	(335,146)	(522,827)
Operating Profit	142,230	166,850	294,856	379,976	375,546	411,566
Impairment of non-current asset	-	(1,775)[3]	(10,373)[4]	(50,000)	2,372	-
Profit before tax	142,230	164,518	283,571	328,798	378,143	410,804
Income tax (expense)	(43,006)	(52,902)	(92,499)	(100,464)	(121,025)	(127,657)
Profit/(loss) after tax	99,224	111,616	191,072	228,334	257,118	283,147
Dividends (toea)						
Dividends paid per share[5]	1.00	1.40	1.60	2.20	2.20	5.37
Balance Sheet (K'000)						
Net loans and advances	873,538	1,163,252	1,550,271	2,343,844	3,638,562	4,091,297
Total assets	2,952,458	4,333,666	5,819,549	6,807,868	9,397,821	10,027,290
Deposits	2,542,935	3,773,805	5,055,917	5,782,020	7,493,779	7,984,657
Capital	308,300	396,295	571,700	744,254	934,097	1,134,397
Performance Ratios						
Return on Assets	3.4%	3.1%	3.8%	3.6%	3.2%	2.9%
Return on Equity	32.2%	31.7%	39.5%	34.7%	30.6%	27.4%
Expense/Income	54.6%	51.9%	39.4%	45.0%	46.0%	54.7%
Key Prudential Ratios						
Capital adequacy	29.4%	25.9%	29.0%	22.8%	22.1%	23.6%
Liquid Asset Ratio	56.2%	51.4%	50.3%	47.5%	50.1%	43.0%
Leverage ratio	9.6%	7.5%	9.2%	10.4%	9.1%	10.5%
Exchange Rates (One (1) PNG Kina buys):						
US Dollar	0.3230	0.3300	0.3525	0.3735	0.3700	0.3785
AUS Dollar	0.4400	0.4171	0.3999	0.5396	0.4127	0.3724

(Source – Bank of Papua New Guinea Quarterly Economic Bulletin)

2 From 2005 onwards, statistics are consolidated for Bank of South Pacific and its subsidiaries
3 Impairment of goodwill on acquisition of net assets of Habib Bank Ltd, Fiji Operation, Dec 2006
4 Impairment of remaining goodwill in respect of acquisitions of Capital Stockbrokers Ltd (2005), Habib Bank Ltd - Fiji Branch (2006) and National Bank of Solomon Islands (2007)
5 Dividend per share has been adjusted for 1/10 share split 2008. In 2010, BSP paid a full and final dividend for the 2009 year in July, and an interim dividend for 2010 year, in November.



overseas branches and subsidiaries

Overseas Branches and Subsidiaries

Summary Financial Information
All amounts are expressed in K'000

	Total Asset	Total Liabilities	Turnover	Net Profit After Tax
Solomon Islands	311,221	246,599	27,377	17,119
Fiji Branches	149,666	139,532	3,289	(143)
Fiji Subsidiaries	1,645,966	1,453,547	218,897	10,727
Niue	3,988	5,119	400	(323)
BSP Capital	21,212	8,480	3,484	(3,854)

Overseas Branches

2010 Highlights

Fiji
The results of the bank in Fiji are subdued primarily because of the impact of the margin restriction imposed by the Reserve Bank of Fiji during 2010, which removed an estimated FJ$10m of net interest income from profit.

Since successfully acquiring the Colonial Bank from CBA in December 2009, BSP now operates the largest branch and ATM network in Fiji and has the largest customer account base. The number of home and personal loans written by the bank now exceeds the number written by all the other banks in Fiji combined.

During 2010, effort was focused on the growth of the bank's low-cost deposit base in Fiji. This was facilitated by the introduction, in early 2010, of an attractive suite of innovative Electronic Banking products delivered to urban and rural communities through SMS banking, ATM and EFTPOS channels.

Improved functionality and greater outreach through these channels will continue during 2011. The bank will also launch Internet banking in Fiji in early 2011. This will complement the bank's Electronic Banking offering and to allow the bank to compete more robustly in the high net worth, Corporate and Small Business markets.

Meanwhile, the bank is well placed as a facilitator of payments throughout Fiji, through alliances established during 2010 with Western Union, and in support of the e-wallet initiatives of the Fiji Telcos, Digicel, Vodafone and TFL.

Solomon Islands
The bank continues to maintain the largest branch banking network and the only agency network in the Solomon Islands. Our strong retail base has been used to leverage several electronic banking initiatives designed to improve customer service and increase card usage.

The bank now has 12 ATMs operating and an EFTPOS channel was introduced late in 2010. The number of Kundu Card customers using the ATM and EFTPOS channels has growing rapidly during 2010 and is currently growing at 10% month on month.

Internet banking was launched for business banking clients mid December and usage of this product also continues to grow strongly.

In 2011, focus will be on the further expansion of the EFTPOS channel including merchant acquisition and interchange with other banks. The introduction of SMS banking is also scheduled for 2011.

To accommodate the growth in electronic banking delivery channels our existing retail banking department was restructured to segregate front office sales and service from our back office operational processing

BSP Capital Limited

BSP Capital continued its transformation process in 2010. Some of these achievements included:

- A complete divisionalisation of the business, separating the Funds Management, Sharebroking and Nominee/Custodian functions of the business, enabling better reporting and governance in the management of compliance and operational risk. IFC is one prominent organisation that now uses our custodial services;
- Building our Funds Management team to full strength, with specialist personnel now on board to ensure that we are able to vie for the business of the largest financial institutions with sizeable investment portfolios in the country. In that regard, at the end of 2010, we were successful in tendering for the management of part of the portfolio of Nambawan Super Ltd, a K3 billion fund.
- Our Corporate Research Department is the only organisation in PNG putting out quality research on local companies, and their research now goes out to an electronic list in excess of 4,000 subscribers, so much so that we now have Asian Fund Managers who seek our research;
- As a 62.5% shareholder in the Port Moresby Stock Exchange, we were instrumental in bringing in KPMG to review the entire operational structure of POMSoX. This has led to another transformation project being launched in late 2010, which will see POMSoX in 2011, as an organisation who through a revamp of systems and processes, will aim to gain membership of the World Federation of Exchanges, an elite group currently comprised of 52 Stock Exchanges from around the world.

In 2010, we consolidated all facets of our business arms, ensuring that BSP Capital emerged as an efficient, fully resourced, professional and totally compliant division of the BSP Group of Companies. We are in the final stages of going live with both our Stockbroking, Funds Management and fully integrated Back Office computer systems, which should see further cost and labour efficiencies in our day-to-day operations.

Our Equities and Corporate Advisory Divisions were very active in 2010. We are now fielding enquiries from the Asian sector, who with the current LNG activity, see PNG very much as an emerging market, for the channelling of investment funds. In 2010, we were instrumental in brokering a deal between Interoil and Energy World Corporation in terms of provision of a viable alternate power source for Interoil's LNG operations.

Our Funds Management business has seen a complete turnaround in 2010, with our appointment as an additional Manager of Nambawan Super Ltd. We are poised to acquire clients from other sectors of the finance markets in PNG, and are well placed to pursue the management of the substantial investment streams which will flow to landowner companies participating in the current LNG project.

The 2011 year will be a challenging one, where BSP Capital will need to consolidate on the achievements of 2010, and convert that into a highly professional, functional and profitable operation, unfettered by the legacy issue of the Global Financial Crisis in late 2008.

Colonial Fiji Life Limited

Overview

Following the decision to retain the Fiji Insurance Business the focus has been on separating the management of the business from the bank and setting the necessary platform for future growth. A new Managing Director and two new Independent Directors with extensive international industry experience have been appointed to the Boards of the Insurance Companies. An experienced professional also accepted the position of Appointed Actuary. The appointments of these very experienced professionals to these key positions have been well received in the market. The majority of the other key management positions were also filled.

Rebranding of the businesses to reflect its new BSP ownership is currently being finalised for launch in the first half of 2011.

Financial Performance

The Insurance Group NPAT for 2010 was $4.7m, $0.9m above budget. After adjustment for non-operating items NPAT was $5.1m, $1.3m above budget. Life insurance sales grew by 16%. However overall insurance new business remained inline with the previous year.

Fiji Political and Economic Climate

Fiji's political situation remains uncertain. There is a proposed amendment to the current constitution, with an emphasis on electoral reform and the timeline for a newly elected government is 2014.

The Reserve Bank of Fiji Economic Review for December 2010 indicated that there was some improvement noted in Fiji's economic conditions. Data showed a pick-up in private consumption while investment activity continues to be restrained. The tourism and gold industries performed strongly, while lower output was noted in the sugar industry.

The environment remains challenging.

Insurance Market

The life insurance market is dominated by endowment products. There are two major players. BSP Group's life insurance market share on in-force premium basis was at 61% at the end of 2009. Health insurance has been very competitive with four active competitors. Competition is very strong from our Life competitor which has been successful in the sale of a single premium product. Focus in 2011 will be on the review of our products and the development of our Distribution Channels. These are critical to sustaining and further improving our market leadership position.

Strategic Initiatives

A full strategic review by KPMG has commenced in February 2011. The review will evaluate growth potential and future options for the Insurance Businesses in Fiji and set the necessary groundwork for the formulation of Strategic and Business Plans.

Other key initiatives already underway include:

- Product review for both the Life and Health businesses, including detailed research into the market and competitor products and services
- Further development of our Agency distribution channel with clear strategies for recruitment, training and development and implementation of cost effective incentive schemes.
- Re-launch of sales through the BSP banking network and other non traditional sales channels
- Review of the Investment Assets covering the performance of Private Equity Portfolio and the Investment Mandate.
- Commencement of ground work on the replacement of our insurance core and support information systems.

Fiji Bank Executives

Standing left to right: Ronesh Dayal (Chief Financial Officer), Ravindra Singh (General Manager Human Resources), Ms Alvina Ali (General Manager Legal and Compliance), Paul Littlefair (Chief Operating Officer). **Seated left to right:** Greg Watson (General Manager Retail Banking), Howard Politini (General Manager Microfinance, Government and Community Relations), Kevin McCarthy (Country Manager Fiji), Cecil Browne (General Manager Corporate and International), Haroon Ali (Chief Risk Officer).

The Solomon Islands team

Back Row: Alphonse Taoti (Manager Information Systems), Peter Lemon (Manager Human Resources), Janet Marau (Manager Banking Operations), Mark Corcoran (Country Manager), Vincent Misi (Assistant Accountant), Rob Bochman (Manager Relationship Banking), Edward Uma (Financial Controller) **Front Row:** Rose Murray (Manager International Operations), Tupou Halofaki (Manager Retail Banking Services), Laurish Pio (Senior Audit Officer), Lynn Taoti (Manager Credit Administration)

Life Management Teams

Left to right: Mosese Ratakele (General Manager Properties), Michael Collins (Chief Operating Officer), Ms Adrienne Ali, Malakai Naiyaga (Managing Director Life), Pramesh Sharma (General Manager Investments).

directors' report

For the Year Ended 31 December 2010

The Directors take pleasure in presenting the Financial Statements of Bank of South Pacific Limited and its subsidiaries (Company and the Group) for the year ended 31 December 2010. In order to comply with the provision of the Companies Act 1997, the Directors Report is as follows:

Principal activities

The principal activity of Bank of South Pacific Limited and the Group is the provision of commercial banking and finance services throughout Papua New Guinea and the Pacific region. BSP is a company listed on the Port Moresby Stock Exchange (POMSoX), incorporated under the Companies Act of Papua New Guinea, and is an authorised bank under the Banks and Financial Institutions Act of Papua New Guinea. The Bank and the Group are licensed to operate in the Solomon Islands, Fiji Islands and Niue. The registered office is at Douglas Street, Port Moresby.

Review of operation

For the year ended 31 December 2010, the Company's profit after tax was K276.570 million (2009: K257.738 million profit). The Group's profit after tax was K283.147 million (2009: K257.118 million).

Dividends

An interim dividend of K65.585 million was declared and paid on the 15th November 2010 by the Company in respect of the half year ended 30 June 2010 (2009: K182.374 million full and final dividend was paid on 8th July 2010 in respect of the year ended 31 December 2009).

Directors and officers

The following were Directors of the Bank of South Pacific Limited during the year ended 31 December 2010:

Mr K Constantinou, OBE	Sir N Bogan	Mr J G Jeffery	Dr I Temu
Mr G Aopi	Mr I B Clyne	Mr J K Natto	
Mr N N Beangke	Mr T E Fox	Mr C C Procter	

Details of Directors' tenure and Directors and executives' remuneration during the year are provided in Note 32 of the Notes to the Financial Statements.

The Company Secretary is Mrs Mary Johns.

Independent Audit Report

The financial statements have been audited and should be read in conjunction with the independent audit report on page 104. Details of amounts paid to the auditors for audit and other services are shown in Note 5 of the Notes to the Financial Statements.

Donations

Donations made by the Company during the year amounted to K316,983 (2009: K282,976).

Interests Register

Transactions recorded in the Interests Register are disclosed in Note 31 of the Notes to the Financial Statements.

Change in accounting policies

No changes in accounting policies occurred during the year.

For, and on behalf of, the Directors.

Dated and signed in accordance with a resolution of the Directors in Port Moresby this 04th day of March 2011

Kostas Constantinou, OBE
Chairman

Ian B Clyne
Chief Executive Officer/Director

Statement by the Directors

For the year ended 31 December 2010

The Directors declare that:

a) in the Directors' opinion, there are reasonable grounds to believe that the Company and the Group will be able to pay their debts as and when they become due and payable; and

b) in the Directors' opinion, the attached financial statements and notes thereto are in accordance with the PNG Companies Act 1997, including compliance with accounting standards and give a true and fair view of the financial position and performance of the Company and the Group.

Additional Statutory Information

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

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

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

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

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

Dated and signed in accordance with a resolution of the Directors at Port Moresby this 04th day of March 2011.

Kostas Constantinou, OBE
Chairman

Ian B Clyne
Chief Executive Officer/Director

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statement of comprehensive income

For the year ended 31 December 2010

All amounts are expressed in K'000	Note	Group 2010	Group 2009	Bank 2010	Bank 2009
Interest income	1	646,044	582,862	576,481	576,954
Interest expense	1	(102,042)	(108,893)	(80,390)	(106,746)
Net interest income		**544,002**	**473,969**	**496,091**	**470,208**
Fee and commission income	2	152,058	108,809	145,581	106,030
Other income	3	258,915	142,934	155,075	125,623
Net operating income		**954,975**	**725,712**	**796,747**	**701,861**
Bad and doubtful debts (expense)/recovery	4	(20,581)	(15,020)	(19,112)	(16,376)
Other operating expenses	5	(522,828)	(335,146)	(375,174)	(308,684)
Operating profit		411,566	375,546	402,461	376,801
Impairment of non-current assets		-	2,372	-	2,372
Share of loss from Associates accounted for using the equity method	14(a)	(762)	225	(364)	(1,209)
Profit before tax		**410,804**	**378,143**	**402,097**	**377,964**
Income tax expense	6(a)	(127,657)	(121,025)	(125,527)	(120,226)
Operating profit/(loss) after tax from ordinary activities		**283,147**	**257,118**	**276,570**	**257,738**
Other comprehensive income					
Exchange difference on translation of foreign operations/subsidiaries	28	2,739	(7,076)	2,242	(6,862)
Net value gain on revaluation of share options	28	657	(249)	657	(249)
Net movement in asset revaluation	28	-	37,623	-	37,628
Other comprehensive income for the year, net of tax		**3,396**	**30,298**	**2,899**	**30,517**
Total comprehensive income for the year		**286,543**	**287,416**	**279,469**	**288,255**
Earnings per share - basic and diluted (toea per share)	34	5.9	5.6	5.8	5.7

The attached notes form an integral part of these financial statements.

statement of financial position

For the year ended 31 December 2010

All amounts are expressed in K'000	Note	Group 2010	Group 2009	Bank 2010	Bank 2009
ASSETS					
Cash and balances with Central Bank	15	1,042,029	996,393	744,280	796,197
Treasury & Central Bank bills	16	2,280,816	2,325,713	2,280,816	2,305,708
Amounts due from other banks	17	302,061	191,888	295,028	186,655
Loans and advances to customers	18	4,091,297	3,638,562	3,276,747	2,860,022
Properties held for sale	19(a)	-	9,011	-	-
Property, plant and equipment	19(b)	364,154	282,246	312,024	243,302
Assets subject to operating lease	19(c)	77,480	86,024	77,480	86,024
Other financial assets	20	1,521,915	1,512,569	1,318,174	1,331,311
Investment in associates	14	54,456	47,733	12,563	1,417
Investment in subsidiaries		-	-	215,517	226,201
Intangibles	13	16,158	21,333	-	-
Investment properties	19(d)	74,816	70,990	-	-
Deferred tax asset	21	64,968	52,603	52,569	41,210
Other assets	22	137,140	162,756	80,114	88,680
Total assets		**10,027,290**	**9,397,821**	**8,665,312**	**8,166,727**
LIABILITIES					
Amounts due to other banks	23	23,638	26,594	29,497	12,202
Amounts due to customers	24	7,984,657	7,493,779	7,185,575	6,759,626
Subordinated debt securities	25(b)	75,525	75,525	75,525	75,525
Other liabilities	25(a)	683,993	670,955	150,424	202,260
Provision for income tax	6(b)	30,484	109,691	28,513	103,377
Deferred tax liabilities	21	30,166	31,881	31,792	31,881
Other provisions	26	64,430	55,299	54,642	45,778
Total liabilities		**8,892,893**	**8,463,724**	**7,555,968**	**7,230,649**
SHAREHOLDERS' EQUITY					
Ordinary shares	27	461,633	318,014	461,633	318,014
Retained earnings	28	588,977	553,912	578,372	551,625
Other reserves	28	83,787	62,171	69,339	66,439
Total shareholders' equity		**1,134,397**	**934,097**	**1,109,344**	**936,078**
Total equity and liabilities		**10,027,290**	**9,397,821**	**8,665,312**	**8,166,727**

The attached notes form an integral part of these financial statements.

statement of changes in shareholders' equity

For the year ended 31 December 2010

Bank

All amounts are expressed in K'000	Note	Share capital	Reserves	Retained Earnings / (Accumulated losses)	Total
Balance at 1 January 2009	27&28	318,014	35,922	394,461	748,397
Net profit	28	-	-	257,738	257,738
Final dividend paid for 2008	28	-	-	(100,305)	(100,305)
Deferred income 2009		-	-	(269)	(269)
Other comprehensive income	28	-	30,517	-	30,517
Balance at 31 December 2009	**27&28**	**318,014**	**66,439**	**551,625**	**936,078**
Net profit	28	-	-	276,570	276,570
Dividend paid	28	-	-	(247,959)	(247,959)
Deferred income 2010		-	-	(1,864)	(1,864)
Issue of ordinary shares	27	143,619	-	-	143,619
Other comprehensive income		-	2,900	-	2,900
Balance at 31 December 2010	**27&28**	**461,633**	**69,339**	**578,372**	**1,109,344**

Group

All amounts are expressed in K'000	Note	Share capital	Reserves	Retained Earnings / (Accumulated losses)	Total
Balance at 31 December 2009	27&28	318,014	62,171	553,912	934,097
Net profit	28	-	-	283,147	283,147
Dividend paid	28	-	-	(247,959)	(247,959)
Deferred income 2010		-	-	(1,864)	(1,864)
Prior year adjustments		-	-	1,741	1,741
Issue of ordinary shares	27	143,619	-	-	143,619
Equity component of convertible notes		-	18,218	-	18,218
Other comprehensive income		-	3,398	-	3,398
Balance at 31 December 2010	**27&28**	**461,633**	**83,787**	**588,977**	**1,134,397**

The attached notes form an integral part of these financial statements.

statement of cash flow

STATEMENT OF CASH FLOW
For the year ended 31
December 2010

		Group		Bank	
All amounts are expressed in K'000	Note	2010	2009	2010	2009
CASH FLOW FROM OPERATING ACTIVITIES					
Interest received		645,728	584,859	573,599	579,318
Fees and other income		437,135	249,399	300,015	232,578
Interest paid		(109,337)	(116,142)	(80,807)	(101,732)
Amounts paid to suppliers and employees		(482,970)	(327,522)	(323,839)	(300,651)
Operating cash flow before changes in operating assets	**33**	**490,556**	**390,594**	**468,968**	**409,513**
Decrease/(increase) in loans		(429,305)	(535,954)	(435,838)	(532,554)
Decrease/(increase) in bills receivable and other assets		866	28,679	866	(26,047)
(Decrease)/increase in deposits		488,179	920,295	425,949	961,889
(Decrease)/increase in bills payable and other liabilities		8,192	(126,547)	(26,886)	62,175
Net cash flow from operations before income tax		**558,488**	**677,067**	**433,059**	**874,976**
Income taxes paid	6(b)	(220,415)	(101,403)	(213,771)	(101,372)
Net cash flow from operating activities		**338,073**	**575,664**	**219,288**	**773,604**
CASH FLOW FROM INVESTING ACTIVITIES					
Decrease/(increase) in government securities		176	(281,094)	38,029	(273,963)
Expenditure on property, plant and equipment		(136,744)	(32,747)	(104,118)	(27,822)
Proceeds from disposal of property, plant and equipment		6,020	2,472	1,987	1,184
Proceeds from disposal of interest in former associate		100	-	100	-
Proceeds from other investments		34,338	-	-	-
Movement in share trading activities		749	3,575	-	-
Additional funding in associate		-	(800)	-	(800)
Additional funding in subsidiary		641	-	(10,000)	-
Net cash flow on acquisition of branch		(371)	8,622	(371)	(180,100)
Net cash flow from investing activities		**(95,091)**	**(299,972)**	**(74,373)**	**(481,501)**
CASH FLOW FROM FINANCING ACTIVITIES					
Issue of share capital	28	143,983	-	143,619	-
Proceeds from subordinated debt securities/convertible notes	25&11	22,395	75,525	-	75,525
Client management trust		(4,795)	(6,745)	-	-
Dividends paid	28	(247,959)	(100,305)	(247,959)	(100,305)
Net cash flow from financing activities		**(86,376)**	**(31,525)**	**(104,340)**	**(24,780)**
Net increase/(decrease) in cash and cash equivalents		**156,606**	**244,167**	**40,575**	**267,323**
Effect of exchange rate movements on cash and cash equivalents		2,159	(3,135)	(1,414)	(3,135)
Cash and cash equivalents at the beginning of the period-subsidiary		-	213,466	-	-
Cash and cash equivalents at the beginning of the year		1,161,687	707,189	970,650	706,462
Cash and cash equivalents at the end of the year	**30**	**1,320,452**	**1,161,687**	**1,009,811**	**970,650**

The attached notes form an integral part of these financial statements.

environment

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accounting policies

For the year ended 31 December 2010

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

A Basis of presentation and general accounting policies

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

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

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

B Consolidation

The consolidated financial statements incorporate the assets and liabilities of all controlled entities of the Bank and the Group as at 31 December 2010, and their results for the year then ended.

Controlled entities are those over which the Group has the power to govern financial and operating policies, generally accompanied by a shareholding that commands the majority of voting rights, and are commonly referred to as subsidiaries.

Subsidiaries are accounted for at acquisition under the purchase method of accounting, where:

- acquisition cost is measured at fair value of assets acquired, equity issued, liabilities assumed and any directly attributable costs of the transaction;
- identifiable net assets are recorded initially at acquisition, at their fair values;
- any excess of the acquisition cost over the relevant share of identifiable net assets acquired is treated as goodwill, and any deficiency is recognised directly in the statement of comprehensive income;
- All intercompany transactions and balances are eliminated.

C Investment in Associates

Associates are entities over which the Group has significant, but not controlling influence, generally accompanied by a shareholding conferring between 20% - 50% of voting rights.

In the consolidated financial statements, these investments are accounted for under the equity method, where:

- The investment is initially recognised at cost;
- The Group's share of profits or losses are recognised in the statement of comprehensive income.

For the year ended 31 December 2010

D Derivative financial instruments and acceptances

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

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

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

E Revenue

Interest income and expense

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

Interest income includes coupons earned on inscribed stock, accrued discount and premium on Treasury and Central Bank bills.

Short term insurance contracts

These contracts are the Term Life, Medical and Travel policies sold and underwritten by Colonial Health Care (Fiji) Limited.

These contracts protect the Group's customers from the consequences of events such as death, medical emergency or loss on travel. Guaranteed benefits paid on occurrence of the specified insurance event are either fixed or linked to the extent of the economic loss suffered by the policy holder. There are no maturity or surrender benefits.

For all these contracts, premiums are recognised as revenue (earned premiums) proportionally over the period of coverage. The portion of premium on in-force contracts that relates to unexpected risks at the balance sheet date is reported as the unearned premium liability. Premiums are shown before deduction of commission.

Claims and loss adjustment expenses are charged to income as incurred based on the estimated liability for compensation owed to contract holders or beneficiary. They include direct and indirect claims settlement costs and arise from events that have occurred up to the balance sheet date even if they have not yet been reported to the Group. The Group does not discount its liabilities for unpaid claims. Liabilities for unpaid claims are estimated using the input of assessments for individual cases reported to the Group and statistical analyses for the claims incurred but not reported, and to estimate the expected ultimate cost of more complex claims that may be affected by external factors (such as court decisions).

Long term insurance contracts

These contracts insure human life events (for example death or survival) over a long duration. They protect the Group's customers from the consequences of events such as death, disability or critical illness. Guaranteed benefits paid on occurrence of the specified insurance event are fixed or linked to the level of bonus declared to the contract holder. Most of the policies have maturity and surrender benefits.

For the year ended 31 December 2010

E Revenue (continued)

For all these contracts, premium are recognised as revenue when they become payable by the contract holder. Premiums are shown before deduction of commission.

Approximately 90% of the above contracts in the Group's portfolio contain a Discretionary Participation Feature (DPF). This feature entitles the holder to receive, as a supplement to generated benefits, additional benefits or bonuses.

A liability for contractual benefits that are expected to be incurred in the future is recorded when the premiums are recognised. The statutory liability is based on LPS 3.04 Capital Adequacy Standard issued by the Australian Prudential Regulation Authority and is calculated in a two-step process.

Firstly a base policy liability is calculated in a way that allows for the systematic release of planned profit margins as services are provided to policy owners and the revenues relating to those services are received (Margin on Service methodology). Services used to determine profit recognition include the cost of expected insurance claims and the allocation of future bonuses. The liability is generally determined as the present value of all future expected payments, expenses, taxes and profit margins reduced by the present value of all future expected premiums and take into consideration projected future bonuses. The liabilities are recalculated at each balance date using best estimate assumptions. These assumptions are revised regularly and adjusted for actually experience on claims, expense, mortality and investment returns.

The base policy liability is the recalculated to arrive at a statutory policy liability, based on assumptions which anticipate more adverse experience than the best estimate experience. Allowance is made for future bonuses (if any) in line with these adverse assumptions. The statutory policy liability is calculated as follows:

For policies with a Discretionary Participation Feature the maximum of:

- the base policy liability calculated on adverse assumptions and with the use of discretions
- the base policy liability calculated on best estimate assumptions including policy holder retained earnings
- the current surrender value

For other businesses the maximum of:

- the base policy liability calculated on adverse assumptions and with the use of discretions
- the current surrender value, or unearned premium reserve

The statutory policy liability is then increased by the solvency margin required under the Insurance Act 1998.

F Fee and commission income

Fees and commissions are generally recognised on an accrual basis when the service has been provided. All other risk related fees that constitute cost recovery are taken to income when levied. Non-refundable front-end loan fees are capitalised and deferred over the expected term of the financial instrument.

For the year ended 31 December 2010

G Borrowing expenses

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

H Loans and provisions for loan impairment

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

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

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

I Goodwill

Goodwill represents the excess of the cost of any acquisition over the acquirer's interest in the fair value of the identifiable assets and liabilities acquired as at the exchange transaction. Goodwill is reported in the statement of financial position as an intangible asset.

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

J Computer systems development costs

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

helping

- develop skills for life

BSP proudly supports Papua New Guinea Swimming Inc (PNGSI)

For the year ended 31 December 2010

K Property, plant and equipment

Land and buildings are measured at fair value. Fair value is determined on the basis of regular independent valuation prepared by external valuation experts, based on discounted cash flows or capitalisation of net income (as appropriate). The fair values are recognised in the financial statements of the consolidated entity, and are reviewed at the end of each reporting period to ensure that the carrying value of land and buildings is not materially different from their fair values.

Any revaluation increase arising on the revaluation of land and buildings is credited to the asset revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense in profit or loss, in which case the increase is credited to the Statement of Comprehensive Income to the extent of the decrease previously charged. A decrease in carrying amount arising on the revaluation of land and buildings is charged as an expense in statement of comprehensive income to the extent that it exceeds the balance, if any, held in the asset revaluation reserve relating to a previous revaluation of that asset.

Depreciation on revalued buildings is charged to profit or loss. On the subsequent sale or retirement of a revalued property, the attributable revaluation surplus remaining in the asset revaluation reserve, net of any related deferred taxes, is transferred directly to retained earnings.

Depreciation is provided on property, plant and equipment, including freehold buildings but excluding land. Depreciation is calculated on a straight line basis so as to write off the net cost or other revalued amount of each asset over its expected useful life to its estimated residual value. Leasehold improvements are depreciated over the period of the lease or estimated useful life, whichever is the shorter, using the straight line method. The estimated useful lives, residual values and depreciation method is reviewed at the end of each annual reporting period.

The following basis and method of depreciation is used:

Class of asset	Method	Rate
Property (excluding land)	Straight line basis	2 - 3% pa
Plant and equipment	Straight line basis	10 - 25% pa
Equipment under operating lease	Straight line basis	20% pa

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

L Leases

Bank is lessee

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

Bank is lessor

Finance leases are included in Loans and Advances to Customers (Note 14) and are accounted for under the finance method whereby income is taken to account over the life of the lease in proportion to the outstanding investment balance.

For the year ended 31 December 2010

L Leases (continued)

Assets subject to operating leases are separately disclosed in the statement of financial position, according to the nature of the asset. These assets are stated at cost less accumulated depreciation. The assets are depreciated on a straight line basis over the life of the operating lease. Lease income is recognised on a straight line basis over the term of the lease.

M Cash and cash equivalents

For the purpose of the Cash Flow Statement, cash and cash equivalents comprise notes and coins, and balances due to and from other banks.

N Provisions

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is vitually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

O Employee benefits

A liability is required for benefits accruing to employees in respect of wages and salaries, annual leave, long service leave when it is probable that settlement will be required and they are capable of being measured reliably.

Liabilities recognised in respect of employee benefits expected to be settled within 12 months, are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Liabilities recognised in respect of employee benefits which are not expected to be settled within 12 months are measured as the present value of the estimated future cash outflows to be made by the consolidated entity in respect of services provided by employees up to reporting date.

Post employment benefits - defined contribution plans

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

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

For the year ended 31 December 2010

P Income tax

Current tax

Current tax is calculated by reference to the amount of income taxes payable or recoverable in respect of the taxable profit or tax loss for the period. It is calculated using tax rates and tax laws that have been enacted or substantively enacted by reporting date. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

Deferred tax

Deferred tax is accounted for using the balance sheet liability method. Temporary differences are differences between the tax base of an asset or liability and its carrying amount in the statement of financial position. The tax base of an asset or liability is the amount attributed to that asset or liability for tax purposes.

In principle, deferred tax liabilities are recognised for all taxable temporary differences. Deferred tax assets are recognised to the extent that it is probable that sufficient taxable amounts will be available against which deductible temporary differences or unused tax losses and tax offsets can be utilised. However, deferred tax assets and liabilities are not recognised if the temporary differences giving rise to them arise from the initial recognition of assets and liabilities which affects neither taxable income nor accounting profit.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period(s) when the asset and liability giving rise to them are realised or settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by reporting date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax for the period

Current and deferred tax is recognised as an expense or income in the statement of comprehensive income, except when it relates to items credited or debited directly to equity, in which case the deferred tax is also recognised directly in equity.

Q Investments

Investments are classified into the following categories: held for trading, held-to-maturity and available-for-sale. Trading reflects active and frequent buying and selling, and financial instruments held for trading generally are used with the objective of generating a profit from short-term fluctuations in price or dealers margin. Investments with fixed maturity that the management has the intent and ability to hold to maturity are classified as held-to-maturity. Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, are classified as available-for-sale; Management determines the appropriate classification of its investments at the time of the purchase.

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

BSP has a year round programme of community service

Official opening BSP Rural Branch: Daulo, Eastern Highlands Province. BSP CEO Ian Clyne and Mr Lars Thunell, Executive Vice President & CEO of International Finance Corporation at launch celebrations.

For the year ended 31 December 2010

R Foreign currency

The financial statements of the Company are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of these financial statements, the results and financial position of the Company are expressed in Papua New Guinea kina, which is the company's functional and presentation currency.

In preparing the financial statements, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rate of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Foreign operations

On consolidation, the asset and liabilities of the consolidated entity's overseas operations are translated at exchange rates prevailing at the reporting date. Income and expense items are translated at the average exchange rates for the period unless exchange rates fluctuate significantly. Exchange differences arising, if any, are recognised in the foreign currency translation reserve, and recognised in profit or loss on disposal of the foreign operation.

S Share capital

Share issue costs

External costs directly attributable to the issue of new shares are deducted from equity net of any related income taxes.

Dividends on ordinary shares

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

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

Share options

The fair value of the employee services received in exchange for the grant of options is recognised as an expense. The total amount to be expected rateably over the vesting period is determined by reference to the fair value of the options determined at the grant date, excluding the impact of any non-market vesting conditions (for example profitability). Non-market conditions are included in assumptions about the number of options expected to become exercisable or the number of shares that the employee will ultimately receive. This estimate is revised at each balance sheet date and the difference is charged or credited to the statement of comprehensive income, with a corresponding adjustment to equity. The proceeds received on exercise of the options net of any directly attributable transactions costs are credited to equity.

For the year ended 31 December 2010

T Asset Impairment

At each reporting date, the Bank and the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Bank and the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Goodwill, intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually and whenever there is an indication that the asset may be impaired. An impairment of goodwill is not subsequently reversed.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the reversal of the impairment loss is treated as a revaluation increase.

U Non-current assets held for sale

Non-current assets (and disposal groups) classified as held for sale are measured, with certain exceptions, at the lower of carrying amount and fair value less costs to sell.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the asset (or disposal group) is available for immediate sale in its present condition subject only to terms that are usual and customary for such a sale and the sale is highly probable. The sale of the asset (or disposal group) must be expected to be completed within one year from the date of classification, except in the circumstances where sale is delayed by events or circumstances outside the company's control and the company remains committed to a sale.

V Comparatives

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

Wisdom

- utilizing knowledge,
experience and common sense

financial risk management

For the year ended 31 December 2010

A Bank operations, risks and strategies in using financial instruments

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

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

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

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

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

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

B Capital adequacy

The Bank and the Group is required to comply with various prudential standards issued by the Bank of Papua New Guinea (BPNG), the official authority for the prudential supervision of banks and similar financial institutions in Papua New Guinea. One of the most critical prudential standards is the capital adequacy requirement. All banks are required to maintain at least the minimum acceptable measure of capital to risk-weighted assets to absorb potential losses. The BPNG follows the prudential guidelines set by the Bank of International Settlements under the terms of the Basel Accord. The BPNG revised prudential standard 1/2003, Capital Adequacy, prescribes ranges of overall capital ratios to measure whether a bank is under, adequately, or well capitalised, and also applies the leverage capital ratio. In all months, the Bank and the Group complied with the prevailing prudential requirements for total capital and leverage capital. As at 31 December 2010, the Bank and the Group's total capital adequacy ratio and leverage capital ratio satisfied the capital adequacy criteria for well-capitalised. The minimum capital adequacy requirements as set out under the standard are: Tier 1 8%, total risk base capital ratio 14% and the leverage ratio 6%.

For the year ended 31 December 2010

B Capital adequacy (continued)

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

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

The Bank and the Group's capital adequacy level is as follows:

		Balance sheet / notional amount		Risk-weighted amount	
All amounts are expressed in K'000		2010	2009	2010	2009
Balance sheet assets (net of provisions)					
Currency		1,042,029	999,683	-	-
Loans and advances		4,091,297	3,638,562	3,977,693	3,239,995
Investments and short term securities		3,802,731	3,838,282	-	-
All other assets		1,091,233	921,294	863,830	692,030
Off-balance sheet items		1,220,614	1,200,968	503,154	416,132
Total		11,247,904	10,598,789	5,344,677	4,348,157
		Capital (K'000)		Capital Adequacy Ratio (%)	
Capital Ratios		**2010**	**2009**	**2010**	**2009**
a) Before YTD profits included in Tier 1 Capital					
	Tier 1 capital	768,769	598,310	14.4%	12.6%
	Tier 1 + Tier 2 capital	1,261,714	1,054,789	23.6%	22.1%
b) After YTD profits included in Tier 1 Capital					
	Tier 1 capital	1,051,916	855,428	19.7%	18.0%
	Tier 1 + Tier 2 capital	1,261,714	1,054,789	23.6%	22.1%
c) Leverage Capital Ratio – Before YTD profits included in Tier 1 capital				7.7%	6.4%
d) Leverage Capital Ratio – After YTD profits included in Tier 1 Capital				10.5%	9.1%

For the year ended 31 December 2010

C Credit risk and asset quality

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

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

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

Large credit exposures are also monitored as part of credit risk management. These are classified as the largest 25 individual accounts or groups of related counter-parties. As at 31 December 2010, the 25 largest exposures totaled K1.410 billion, accounting for over 62.9% of the Bank and 49.9% of the Group's total loan portfolio (2009: K997 million, accounting for over 58.1% and 26.4% respectively).

The Bank of Papua New Guinea has maintained a revised prudential standard for asset quality since October 2003. The revised standard specifies more detailed criteria for the classification of loans into various grades of default risk and corresponding loss provision levels as a consequence of those gradings. Since its introduction, the Bank and the Group has complied with the requirement at all times.

Credit related commitments

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

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

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

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

For the year ended 31 December 2010

C Credit risk and asset quality (continued)

Economic sector risk concentrations

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

All amounts are expressed in K'000	2010	%	2009	%
As at 31 December				
Commerce, finance and other business	1,661,184	41	1,855,439	51
Private households	882,512	22	463,963	13
Government and Public Authorities	116,041	3	8,214	-
Agriculture	334,157	8	260,051	7
Transport and communication	426,733	10	276,230	8
Manufacturing	261,464	6	397,624	11
Construction	409,206	10	377,041	10
Net loan portfolio balance	4,091,297	100	3,638,562	100

D Liquidity risk

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

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

Short-term mismatch of asset and liability maturity at 31 December 2010.

The maturity profile of material Assets and Liabilities as at 31 December 2010 is shown in the following schedule. The mismatching of maturity of assets and liabilities indicates an apparent negative net "current" asset position. However, as stated in the preceding paragraph, mismatched positions are established and managed to achieve profit opportunities that arise from them, particularly in a normal yield curve environment. Accordingly, this mismatched maturity position is considered manageable by the Bank and the Group, and does not impair the ability of the Bank and the Group to meet its financial obligations as they fall due. The Directors are also of the view that the Bank and the Group is able to meet its financial obligations as they fall due for the following additional reasons:

- The Bank and the Group complies with the Minimum Liquid Asset Ratio ("MLAR") and Cash Reserve Requirement ("CRR") set by the regulatory authority, the Bank of Papua New Guinea ("BPNG"). The MLAR is the minimum ratio of liquid assets to total customer deposits considered by the regulator as sufficient to support exceptional liquidation by depositors, of their funds. The requirement to hold a minimum of 25% of the value of total customer deposits in the form of prescribed liquid assets was reduced to zero percent by the BPNG in September 2010. As at 31 December 2010, the Bank and the Group's Liquid Asset Ratio was approximately 42.96% (2009: 50.14%).

Happiness

- feeling, showing satisfaction or expressing joy

For the year ended 31 December 2010

D Liquidity risk (continued)

- The CRR specifies that a bank must hold an amount equal to 4% of its total customer deposits in the form of cash in an account maintained at the BPNG. The Bank and the Group complies with this daily requirement on an ongoing basis. The balance of the CRR account is shown in Note 15, Cash and Balances with Central Bank, and Note 30, Cash and cash equivalents.

Maturity of assets and liabilities

All amounts are expressed in K'000

As at 31 December 2010	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Assets						
Cash and Central Bank assets	1,042,029	-	-	-	-	1,042,029
Treasury & Central Bank bills	645,146	736,200	899,470	-	-	2,280,816
Due from other banks	302,061	-	-	-	-	302,061
Loans and advances	759,077	415,204	604,353	1,477,824	834,839	4,091,297
Investments	-	-	238,103	349,642	934,170	1,521,915
Total assets	**2,748,313**	**1,151,404**	**1,741,926**	**1,827,466**	**1,769,009**	**9,238,118**
Liabilities						
Due to other banks	23,638	-	-	-	-	23,638
Due to customers	6,366,940	960,024	539,647	35,471	82,575	7,984,657
Other liabilities	679,884	30,587	-	-	75,525	785,996
Other provisions	18,239	34,451	-	-	27,136	79,826
Total liabilities	7,088,701	1,025,062	539,647	35,471	185,236	8,874,117
Net liquidity gap	**(4,340,388)**	**126,343**	**1,202,279**	**1,791,995**	**1,583,773**	**364,001**
As at 31 December 2009	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Total**
Total assets	3,574,405	619,864	1,072,174	1,856,863	1,541,819	8,665,125
Total liabilities	6,840,446	989,886	443,656	23,799	165,937	8,463,724
Net liquidity gap	**(3,266,041)**	**(370,022)**	**628,518**	**1,833,064**	**1,375,882**	**201,401**

E Operational risk

Operational risk is the potential exposure to unexpected financial or non-financial losses arising from the way in which the Bank and the Group conducts its business. Operational risk is managed through formal policies, documented procedures, business practices and compliance monitoring.

An operational risk management function is responsible for the maintenance of these policies, procedures, practices and monitoring the organisation's compliance with them. The Operational Risk Committee coordinates the management process across the organisation.

An independent internal audit function also conducts regular reviews to monitor compliance with policy and regulatory environment and examines the general standard of control.

For the year ended 31 December 2010

F Foreign exchange risk

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

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

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

All amounts are expressed in K'000

As at 31 December 2010	USD	AUD	EURO	PGK	Other	Total
Assets						
Cash and Central Bank assets	1,458	1,168	38	735,408	303,957	1,042,029
Treasury & Central Bank bills	-	-	-	2,280,816	-	2,280,816
Due from other banks	35,389	227,480	956	26,120	12,116	302,061
Loans and advances	47,249	2,376	-	3,227,122	814,550	4,091,297
Investments	-	-	-	1,318,174	203,741	1,521,915
Other assets	-	-	-	751,187	37,985	789,172
Total assets	**84,096**	**231,024**	**994**	**8,338,827**	**1,372,349**	**10,027,290**
Liabilities						
Due to other banks	-	-	-	(29,497)	5,859	(23,638)
Due to customers	(107,559)	(157,174)	(2,099)	(6,916,467)	(801,358)	(7,984,657)
Other liabilities	-	-	-	(322,664)	(561,934)	(884,598)
Total liabilities	(107,559)	(157,174)	(2,099)	(7,268,628)	(1,357,433)	(8,892,893)
Net on-balance sheet position	**(23,463)**	**73,850**	**(1,105)**	**1,070,199**	**14,916**	**1,134,397**
Off-balance sheet net notional position	24,946	8,491	6,133	-	5,714	45,284
Credit commitments	-	-	-	1,220,614	-	-
As at 31 December 2009						
Total assets	66,725	93,605	4,135	7,890,756	1,342,600	9,397,821
Total liabilities	(117,692)	(120,373)	(789)	(6,945,999)	(1,278,871)	(8,463,724)
Net on-balance sheet position	**(50,967)**	**(26,768)**	**3,346**	**944,757**	**63,729**	**934,097**
Off-balance sheet net notional position	16,648	9,269	7,105	-	10,237	43,259
Credit commitments	-	-	-	1,111,273	-	-

For the year ended 31 December 2010

G Interest rate risk

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

Given the profile of assets and liabilities as at 31 December 2010 and prevailing rates of interest, a 1% increase in rates will result in a K0.297 million decrease in net interest income, whilst a 1% decrease in rates will result in a K0.274 million increase in net interest income.

Effective interest rates as at 31 December		
Amounts are expressed in % p.a.	**2010**	**2009**
Assets		
Cash and Central Bank assets	7.00	7.00
Treasury and Central Bank bills	3.50	7.05
Due from other banks	7.00	7.00
Loans and advances	12.50	13.30
Investments	9.70	9.50
Liabilities		
Due to other banks	7.00	7.00
Due to customers	3.00	3.00

For the year ended 31 December 2010

G Interest rate risk (continued)

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

All amounts are expressed in K'000

As at 31 December 2010	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non interest bearing
Assets						
Cash and Central Bank assets	-	-	-	-	-	1,042,029
Treasury & Central Bank bills	645,146	736,200	899,470	-	-	-
Due from other banks	302,061	-	-	-	-	-
Loans and advances	1,989,354	510,339	740,327	565,058	286,215	-
Investments	-	-	238,103	349,642	934,170	-
Other assets	-	-	-	-	-	789,176
Total assets	2,936,561	1,246,539	1,877,900	914,700	1,220,385	1,831,205
Liabilities						
Due to other banks	23,638	-	-	-	-	-
Due to customers	4,669,132	642,114	339,147	33,471	5	2,300,788
Other liabilities	-	-	-	-	75,525	809,073
Total liabilities	4,692,770	642,114	339,147	33,471	75,530	3,109,861
Interest sensitivity gap	**(1,756,209)**	**604,425**	**1,538,753**	**881,229**	**1,144,855**	**(1,278,656)**
As at 31 December 2009						
Assets						
Cash and Central Bank assets	-	-	-	-	-	996,393
Treasury & Central Bank bills	1,731,100	187,543	407,070	-	-	-
Due from other banks	191,888	-	-	-	-	-
Loans and advances	1,599,968	401,010	697,185	576,658	363,737	-
Investments	-	35,000	87,349	567,150	823,070	-
Other assets	-	-	-	-	-	732,700
Total assets	3,522,956	623,553	1,191,604	1,143,808	1,186,807	1,729,093
Liabilities						
Due to other banks	26,594	-	-	-	-	-
Due to customers	4,575,913	574,476	309,656	23,799	76,100	1,933,835
Other liabilities	-	-	-	-	75,525	867,826
Total liabilities	4,602,507	574,476	309,656	23,799	151,625	2,801,661
Interest sensitivity gap	**(1,079,551)**	**49,077**	**881,948**	**1,120,008**	**1,035,185**	**(1,072,568)**

For the year ended 31 December 2010

H Fair values of financial assets and liabilities

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

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

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

Forward exchange contracts outstanding at 31 December 2010, stated at the face value of the respective contracts are:

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

As at 31 December 2010		USD	AUD	EURO	GBP	Other	Total
Selling	FCY	16,795	-	-	4,760	-	-
	Kina	**43,855**	**-**	**-**	**19,716**	**-**	**63,571**
Buying	FCY	(15,742)	(29,013)	(400)	(3,200)	(82,975)	-
	Kina	**(43,376)**	**(75,030)**	**(1,487)**	**(2,030)**	**(4,160)**	**(126,083)**
As at 31 December 2009							
Selling	FCY	1,831	15,874	100	4,500	1,287	-
	Kina	**5,504**	**38,279**	**368**	**7,353**	**2,497**	**54,001**
Buying	FCY	(45,382)	(32,500)	(20)	(5,161)	-	-
	Kina	**(120,585)**	**(29,631)**	**(77)**	**(22,501)**	**-**	**(172,794)**

I Policy liabilities

Key assumptions used in determining this liability are as follows:

(i) Discount Rates

For contracts which have a Discretionary Participation Feature (DPF), the discount rate used is linked to the assets which back those contracts. For 31 December 2010 this was 5.49% per annum (30 June 2010: 5.41% per annum), based on 5 year government bond rate and expected earnings from the investment portfolio. For contracts without DPF, a rate of 4.04% per annum was used at 31 December 2010 (30 June 2010: 3.85% per annum). For Accident business a rate of 3.98% per annum was used at 31 December 2010 (30 June 2010: 5.62% per annum). These rates were based on the 5 year government bond rate in Fiji.

(ii) Investment and Maintenance Expenses

Future maintenance and investment expenses have been derived from budgeted expenses. Future inflation has been assumed to be 3.5% per annum (30 June 2010 3.5% per annum) for determining future expenses.

(iii) Taxation

The rates of taxation enacted or substantially enacted at the date of the valuation (i.e. 31%) are assumed to continue into the future.

The reduction in tax rates from financial year 2010 would have an immaterial impact on policy liabilities with any reduction in the liability materially offset by an increase in bonus rate.

For the year ended 31 December 2010

I Policy liabilities (continued)

(iv) Mortality and Morbidity

Projected future rates of mortality for insured lives are based on the Fiji Mortality Statistics performed in 1998. These are then adjusted by comparing with the Group's own experience. For 2010, the mortality rates used was 85% of the mortality statistics. Assumptions are reviewed based on annual experience studies. There have been no changes to mortality assumptions for the current year.

(v) Rates of Discontinuance

Best estimate assumptions for the incidence of withdrawal and discontinuance are based on the Group's experience and are reviewed regularly. Rates used for the long term insurance contracts are as follows:

	31 Dec 2010	30 Jun 2010
Whole of Life and Endowment Insurance	14%	14%
Term Insurance	16%	16%
Accident Insurance	13%	13%

(vi) Basis of Calculation of Surrender Values

Surrender values are based on the provisions specified in the policy contracts. There have been no changes to surrender bases during the period (or the prior periods) which have materially affected the valuation result.

(vii) Discretionary Participating Business

For most participating business, bonus rates are set such that, over long periods, the returns to contract holders are commensurate with the investment returns archieved on the pool of assets which provide security for the contract, together with other sources of profit arising from this business. Distributions are split between contract holders and shareholders with the valuation allowing for shareholders to share in distributions at a maximum allowable rate of 20% (30 June 2009: 20%). For business written 1995 and 1998 the shareholder receives 11% of distributions.

In applying the contract holders' share of profits to provided bonuses, consideration is given to equity between generations of policyholders and equity between generations of policyholders and equity between the various classes and sizes of contracts in force. Assumed future bonus rates included in the liability for the long term insurance contracts were set such that the present value of the liabilities equates to the present value of assets supporting the business together with assumed future investment returns, allowing for the shareholders right to participate in distributions.

Assumed future bonus rates per annum for the major classes of participating businesses range from 1.35% to 3.25% per annum (30 June 2010: 1.05% to 2.00% per annum).

Reinsurance

Contracts entered into by the Group with Reinsurers under which the Group is compensated for losses on one or more contracts issued by the Group, are classified as reinsurance contracts.

As the reinsurance agreements provide for indemnification by the Reinsurers against loss or liability, reinsurance income and expenses are recognised separately in the Income Statement when they become due and payable in accordance with the reinsurance agreements.

Reinsurance recoveries for claims are recognised as Reinsurance recoveries.

Fiji's rebranding commenced with BSP's Love Your Bank campaign in 2010. The "hand made heart" has been widely adopted by men, women and children throughout and has been adopted as a unique symbol of courage and positive vision for Fiji.

notes to the financial statements

For the year ended 31 December 2010

1 Net interest income

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Interest Income				
Cash and short term funds	1,339	1,167	1,339	1,167
Public Securities: Treasury bills and Inscribed stock	228,619	282,801	223,061	282,406
Loans and advances	412,260	298,196	351,531	293,106
Other	3,826	698	550	275
	646,044	582,862	576,481	576,954
Less:				
Interest Expense				
Customer deposits	90,202	103,555	68,550	101,408
Other banks	32	1,666	32	1,666
Subordinated debt securities	9,278	3,664	9,278	3,664
Other borrowings	2,530	8	2,530	8
	102,042	108,893	80,390	106,746
	544,002	**473,969**	**496,091**	**470,208**

2 Net fee and commission income

Fee and commission income				
Credit related	49,167	38,941	44,639	38,561
Trade and international related	143	165	143	165
Electronic banking related	13,449	8,735	13,449	8,735
Brokerage and fee income	1,957	1,996	-	-
Other	87,725	59,293	87,733	58,890
	152,441	109,130	145,964	106,351
Less:				
Fee and commission expenses				
Agencies	383	321	383	321
	383	321	383	321
	152,058	**108,809**	**145,581**	**106,030**

For the year ended 31 December 2010

3 Other income

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Foreign Exchange related	139,260	104,338	132,566	104,338
Net insurance premium income	89,074	6,621	-	-
Other	30,581	31,975	22,509	21,285
	258,915	**142,934**	**155,075**	**125,623**
Included in other income:				
Profit/(loss) on sale of fixed assets	1,166	1,184	498	1,184
Change in fair value of assets held through profit and loss	10,119	2,755	-	-
Foreign Exchange related income includes gains and losses from spot and forward contracts and translated foreign currency assets.				

4 Bad and doubtful debts (expense)/recovery

Bad debts recovered - net	34,479	29,498	31,690	29,584
Net charge to doubtful debts provision	(55,060)	(44,518)	(50,802)	(45,960)
	(20,581)	**(15,020)**	**(19,112)**	**(16,376)**

5 Other operating expenses

Administration	171,520	74,508	99,548	73,291
Auditors' remuneration	1,893	1,178	1,597	1,153
Computing	22,234	16,332	22,234	16,332
Depreciation	53,499	37,371	43,261	36,556
Amortisation of computer development	645	1,684	645	1,684
Non-executive Directors' costs	1,533	886	1,533	886
Non-lending losses	5,812	25,683	4,292	24,900
Fixed asset write off	645	1,397	645	1,397
Premises and equipment	33,069	37,953	30,331	37,953
Increase/(decrease) in policy liabilities	2,576	7,556	-	-
Claims, surrender and maturities	5,106	4,782	-	-
	298,532	**209,330**	**204,086**	**194,152**
Staff costs				
Defined contribution plans	7,836	4,236	5,011	4,236
Statutory benefit contributions	10,841	5,808	8,016	5,467
Wages and salaries	164,413	89,056	125,784	86,662
Other	41,206	26,716	32,276	18,167
	224,296	125,816	171,087	114,532
	522,828	335,146	375,173	308,684

For the year ended 31 December 2010

6(a) Income tax expense

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Current tax	142,609	128,170	142,328	127,783
Deferred tax	(20,438)	(13,463)	(20,607)	(14,045)
Current year	122,171	114,707	121,721	113,739
Prior year adjustments	5,486	6,318	3,806	6,487
	127,657	**121,025**	**125,527**	**120,226**
Tax calculated at 30% of profit before tax (2010: 30 %)	119,473	113,052	120,629	113,389
Tax calculated at 29% of profit before tax – subsidiary	3,828	842	-	-
Expenses not deductible for tax	2,601	2,050	1,092	1,398
Deductible expenses not recognised for accounting purposes	-	(1,049)	-	(1,049)
Net insurance income not subject to tax	2,211	2,974	-	-
Tax benefit not brought to account – subsidiary	(5,942)	(3,162)	-	-
Prior year under provision	5,486	6,318	3,806	6,487
	127,657	**121,025**	**125,527**	**120,226**
Further information about deferred taxes is presented in note 21.				

6(b) Income tax ecoverable / (provision for income tax)

Recoverable / (provision) comprise:				
At 1 January	(109,691)	(68,416)	(103,377)	(68,355)
Opening balance – subsidiary	-	(5,898)	-	-
Income tax provision	(142,609)	(128,170)	(142,328)	(127,784)
Tax benefit not brought to account – subsidiary	(5,942)	-	-	-
Expenses not deductible for tax	3,922	(1,398)	-	(1,398)
Deductible expenses not recognised for accounting purposes	-	1,049	-	1,049
Prior year over / (under) provision	12,890	(8,261)	12,890	(8,261)
Foreign tax paid	6,644	4,866	-	4,866
Tax payments made	204,302	96,537	204,302	96,506
At 31 December	**(30,484)**	**(109,691)**	**(28,513)**	**(103,377)**

7 Discontinued operations

Colonial Fiji Life Limited (CFLL) is no longer available for sale (available for sale in 2009). A full consolidation has been performed in 2010.

For the year ended 31 December 2010

8 Acquisition of associate/Available for sale investment

In November 2010, the Bank acquired 50% interest of Suva Central Limited from Colonial Fiji Life Limited(CFLL) a 100% subsidiary of Bank of South Pacific Ltd for a consideration of K12.563 million (Fiji dollars $8.5 million). Suva Central Limited is a company incorporated in the Fiji Islands. CFLL transferred the shares to Bank South Pacific. These shares were transferred at fair value and the carrying value of the investment is recorded at acquisition cost.

9 Acquisition of subsidiary

In March 2010, the Group acquired EMWAL Nominees Limited, a duly registered company incorporated in the Republic of Fiji Islands for a consideration of 2 Fiji Dollars (FJD). The EMWAL Nominees Limited was incorporated on 27 October 2006 as a shelf company. After the acquisition, it was renamed as BSP Convertible Notes Limited (BSP CN).

BSP CN is a special purpose vehicle incorporated in Fiji with limited powers under its memorandum and articles to facilitate the issue of convertible notes, BSP Fiji Class Shares and the loan to BSP, Fiji Branch of funds raised. 100% of the ordinary shares of BSP CN are beneficially owned by Bank of South Pacific Limited.

During the period, BSP CN issued convertible notes and raised FJD16.090 million (K23.5 million) at FJD5.25 per note. The notes attract a half yearly coupon of 7% and at maturity on 20 April 2013 will convert to Fiji Class Shares at the ratio of 10 shares for 1 Note. (See note 11)

In May 2010, BSP Rural, a wholly owned subsidiary of Bank of South Pacific Limited was incorporated. At 31 December 2010 it operated branches/agencies in three locations. These branches/agencies are operated on the Bank's core banking system and the cash used and deposits mobilised are the assets and liabilities of BSP. In this regard BSP Rural acts as an agent of Bank of South Pacific Limited.

10 Borrowings

On 23 June 2010, the Group signed a loan agreement with International Finance Corporation (IFC), a member of the World Bank Group to obtain a floating rate loan to the amount of US$30 million. As at 31 December 2010, the balance of the undrawn borrowing was US$30 million.

11 Convertible notes

On 20 April 2010, the Group issued 3,064,967 Fiji Dollars (FJD) denominated mandatory convertible notes through its wholly owned subsidiary BSP Convertible Notes Limited at an issue price of FJD5.25 (K7.30) per note. Each note entitles the holder to convert to ten (10) Fiji Class shares. On conversion all notes are redeemed for their face value and the proceeds of that redemption are applied as the subscription price for Fiji Class shares. Notes can only be redeemed in cash at the election of BSP CN Fiji with regulatory approval. The amount payable at redemption will be greater of the market value or face value of the note plus accrued interest.

The net proceeds received from the issue of the convertible notes have been split between the financial liability element and the equity component, representing the residual attributable to the option to convert the financial liability into equity of BSP CN Fiji, as follows:

For the year ended 31 December 2010

11 Convertible notes (continued)

	K'000
Proceeds of issue	22,394
Liability component of issue (note 25(a))	4,176
Equity component (note 28)	18,218

The equity component of K18,218 has been credited to equity (option premium on convertible notes) of BSP CN Fiji.

The liability component is measured at amortised cost. Interest payment of 7% per annum is payable twice yearly on 20 April and 20 October for a maximum of three (3) years. The accrued interest expense for the half year for the two-month period since the loan notes were issued was FJD220,084 (K306,310).

For the year ended 31 December 2010

12 CDO Provision

In 2008 and prior periods, BSP Capital Limited a subsidiary of the Bank, marketed certain collateralised debt obligation investment products issued or arranged by Lehman Brothers. The value of the notes was seriously impaired following the Global Financial Crisis of 2007-2008, particularly the demise of Lehman Brothers, which was the primary issuer or promoter in the majority of cases. Value remains subject to great uncertainty, because of the status of the issuer/promoter, and the general level of financial asset prices declined dramatically as the Global Financial Crisis developed, and because of the complex investment structures and contractual relationships causing difficulties in identifying the nature and quality of the assets underlying these instruments.

A K50 million asset impairment adjustment/provision in respect of these events was created as a prudent estimate of the cost to BSP Group of protecting against reputation risk and risk of financial loss. The balance as at 31 December 2010 is K3.226 million (2009:K6.860 million).

As at 31 December 2010 and up to the date of the release of these financial statements, K46.7 million of these losses have been realised.

13 Intangible asset

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Gross carrying amount	16,158	21,333	-	-
Impairment adjustment	-	-	-	-
	16,158	21,333	-	-

The Directors have determined that the carrying value of the goodwill arising on consolidation as a result of elimination of BSP investment in its subsidiaries is considered not materially impaired. The Directors also determined that these subsidiaries continue to trade profitably and the impairment adjustment does not indicate otherwise.

14(a) Investments in Associates

Name of Associates	Principal activity	Place of incorporation and operation	Proportion of ownership and voting power held	
			2010	2009
PNG Micro Finance Limited****	Micro finance	PNG	-	32%*
Suva Central Limited	Property rental	Fiji	50%*	50%*
Richmond Limited	Hotel operation	Fiji	61.3%**, 50%***	61%**, 50%***
Williams and Gosling	Freight forwarding	Fiji	27.7%	20.4%*

*both ownership and voting power held, **ownership, ***voting power held, ****disposed in 2010

For the year ended 31 December 2010

14(a) Investments in Associates (continued)

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Investment in associate	47,733	46,708	1,417	1,826
Disposal	(5,078)	-	(1,053)	-
Additional	12,563	800	12,563	800
Share of profit/(loss) for year ending December 2010	(762)	225	(364)	(1,209)
Net investment in associate	54,456	47,733	12,563	1,417
Summarised financial information of associates:				
Total assets	188,011	217,421	41,738	39,924
Total liabilities	(103,184)	(122,925)	(38,794)	(37,533)
Net assets	84,827	94,496	2,944	2,391
Net profit/(loss)	(1,536)	3,228	(1,138)	(3,779)
Share of associate's profit or loss:				
Share of associate's profit/(loss)	(762)	225	(364)	(1,209)

For the year ended 31 December 2010

14(b) Disposal of Investments in Associates

As at 31st December 2009, the Bank held a 32% interest in PNG Microfinance Limited and accounted for the investment as an associate. In May 2010, the Bank disposed its full interest in the associate to a third party for the proceeds of K100,000. This transaction has resulted in the recognition of a loss in profit or loss as follows;

	Total K'000
Proceeds of disposal	100
Less: Carrying value of investment at the date of sale	(1,053)
Loss recognised on disposal of associate interest	(953)

15 Cash and balances with Central Bank

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Notes and coins	278,484	233,722	173,626	152,762
Balances with Central Bank other than statutory deposit	258,688	401,872	155,271	378,016
Included in cash and cash equivalents	537,172	635,594	328,897	530,778
Statutory deposits with Central Bank	504,857	360,799	415,383	265,419
	1,042,029	996,393	744,280	796,197

16 Treasury and Central Bank Bills

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Treasury & Central Bank Bills - face value	2,312,609	2,357,862	2,312,609	2,337,857
Discount for interest receivable	(31,793)	(32,149)	(31,793)	(32,149)
	2,280,816	2,325,713	2,280,816	2,305,708

Treasury and Central Bank bills are debt securities issued by the Central Bank. These bills are classified as assets held for trading and carried at fair value.

17 Amounts due from other banks

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Items in the course of collection	259,586	84,874	259,586	84,874
Placements with other banks	42,475	107,014	35,442	101,781
Included in cash and cash equivalents	302,061	191,888	295,028	186,655

For the year ended 31 December 2010

18 Loans and advances to customers

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Loans originated by the Bank				
Overdrafts	680,475	614,085	615,482	566,655
Leases	174,171	182,142	174,171	182,142
Term loans	2,692,603	2,296,478	2,430,426	2,043,497
Mortgages	654,761	629,187	163,946	153,252
Policy loans	47,965	46,430	-	-
Gross loans and advances net of reserved interest	4,249,975	3,768,322	3,384,025	2,945,546
Less allowance for losses on loans and advances	(158,678)	(129,760)	(107,278)	(85,524)
	4,091,297	3,638,562	3,276,747	2,860,022
Allowance for losses on loans and advances				
Movement in allowance for losses on loans and advances:				
Balance at 1 January	129,760	50,496	85,524	50,496
Opening balance – subsidiary	-	42,382	-	-
New provision	39,847	23,581	30,000	22,225
Loans written off against provisions / (write back of provisions no longer required	(10,929)	13,301	(8,246)	12,803
Balance at 31 December	158,678	129,760	107,278	85,524
Loans and advances to customers includes finance lease receivables, analysed as follows:				
Investment in finance leases received				
Not later than 1 year	23,522	15,061	23,522	15,061
Later than 1 year and not later than 5 years	161,773	182,142	161,773	182,142
Later than 5 years	-	-	-	-
	185,295	197,203	185,295	197,203
Unearned future finance income	(11,124)	(15,061)	(11,124)	(15,061)
Net investment in finance leases	174,171	182,142	174,171	182,142
The net investment in finance leases is analysed as follows:				
Not later than 1 year	22,984	14,580	22,984	14,580
Later than 1 year and not later than 5 years	151,187	167,562	151,187	167,562
Later than 5 years	-	-	-	-
	174,171	182,142	174,171	182,142

For the year ended 31 December 2010

19(a) Properties held for sale

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Premises	9,011	9,011	-	-
Disposal	(9,011)	-	-	-
	-	9,011	-	-

For the year ended 31 December 2010

19(b) Property, plant and equipment

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
(i) Carrying value				
Capital works in progress	94,061	58,347	77,815	46,284
Premises	241,073	209,859	216,212	200,378
Accumulated depreciation	(59,398)	(32,781)	(41,357)	(32,107)
	181,675	177,078	174,855	168,271
Equipment	305,623	200,349	231,421	182,134
Accumulated depreciation	(217,205)	(153,528)	(172,067)	(153,387)
	88,418	46,821	59,354	28,747
	364,154	282,246	312,024	243,302
(ii) Reconciliations				
Capital WIP				
At 1 January	58,347	38,787	46,284	38,787
Opening balance – subsidiary	-	13,135	-	-
Additions	115,669	38,194	100,907	35,989
Transfers	(79,955)	(31,769)	(69,376)	(28,492)
At 31 December	94,061	58,347	77,815	46,284
Premises				
At 1 January	177,078	113,577	168,271	113,577
Opening balance – subsidiary	-	9,120	-	-
Additions	14,697	3,383	13,859	2,726
Disposals	(330)	(2,052)	(20)	(1,756)
Adjustments prior year	1,895	2,354	1,895	2,354
Revaluation Increases	-	57,141	-	57,141
Depreciation expense	(11,665)	(6,445)	(9,150)	(5,771)
At 31 December	181,675	177,078	174,855	168,271
Equipment				
At 1 January	46,821	22,684	28,747	22,684
Opening balance – subsidiary	-	17,614	-	-
Additions	76,672	25,652	55,517	24,494
Disposals	(5,330)	(3,157)	(2,888)	(2,600)
Adjustments prior year	3,545	6,410	3,545	6,410
Depreciation expense	(33,290)	(22,382)	(25,567)	(22,241)
At 31 December	88,418	46,821	59,354	28,747

For the year ended 31 December 2010

19(b) Property, plant and equipment (continued)

Freehold land and buildings carried at fair value

An independent valuation of the Bank's land and buildings was performed by GDA Pacific Valuers to determine the fair value of the land and buildings. The valuation, which conforms to International Valuation Standards, was determined by reference to capitalisation of the notional income stream approach on the Market Value basis. The effective date of the valuation is 9th October 2009.

The carrying amount of land and buildings had they been recognised under the cost model are as follows:

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Freehold land	11,467	11,461	11,467	11,461
Buildings	89,561	75,906	89,561	75,906
	101,028	87,367	101,028	87,367

19(c) Assets subject to operating lease

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
(i) Carrying value				
Aircraft	115,041	115,041	115,041	115,041
Accumulated depreciation	(37,561)	(29,017)	(37,561)	(29,017)
	77,480	86,024	77,480	86,024
Reconciliation				
Aircraft				
At 1 January	86,024	94,568	86,024	94,568
Depreciation	(8,544)	(8,544)	(8,544)	(8,544)
At 31 December	77,480	86,024	77,480	86,024
(ii) Future minimum lease payments				
Not later than one year	7,509	13,164	7,509	13,164
Later than 1 year and not later than 5 years	3,461	9,240	3,461	9,240
	10,970	22,404	10,970	22,404

19(d) Investment Properties

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Opening net book value	70,990	-	-	-
Opening net book value – subsidiary	-	79,703	-	-
Additionals and adjustments	5,038	298	-	-
Gain/Loss on Revaluation	(1,212)	-	-	-
Transfer to properties held for sale	-	(9,011)	-	-
At 31 December	74,816	70,990	-	-

For the year ended 31 December 2010

20 Other financial assets

Securities - held to maturity

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Inscribed stock - issued by Central Bank	1,499,615	1,491,431	1,318,174	1331,311
Financial assets carried at fair value through profit and loss:				
Equity securities	22,300	21,138	-	-
At 31 December	1,521,915	1,512,569	1,318,174	1,331,311

21 Deferred tax asset

Deferred taxes are calculated on all temporary differences under the liability method using an effective tax rate of 30% applicable from 1 January 2010 (2009: 30%). Deferred income taxes are recognised for tax losses carried forward only to the extent that realisation of the related tax benefit is probable. At 31 December 2010, the net benefit reflects the estimated future tax benefits at applicable income tax rates of the following:

Specific allowance for losses on loans and advances	8,173	15,332	7,951	9,760
General allowance for losses on loans and advances	24,543	19,669	24,233	15,897
Employee related provisions	11,896	9,531	10,336	7,878
Prepaid expenses	(253)	-	(253)	-
Other provisions	24,770	4,005	6,147	3,693
Depreciation and amortisation	(24,916)	(23,542)	(26,030)	(22,566)
Unrealised foreign exchange gains	(5,509)	(9,314)	(5,509)	(9,314)
Deferred expenditure	(3,902)	5,041	3,902	3,981
	34,802	20,722	20,777	9,329
The movements on the deferred income tax accounts are as follows:				
At 1 January	20,722	10,052	9,329	9,800
Specific allowance for losses on loans and advances	(7,159)	8,136	(1,809)	2,564
General allowance for losses on loans and advances	4,874	11,799	8,336	8,027
Employee related provisions	2,365	3,220	2,458	1,663
Depreciation and amortisation	(1,374)	(10,274)	(3,464)	(9,302)
Prepaid expenses	(253)	30	(253)	20
Other provisions	12,961	(1,786)	2,454	(1,929)
Unrealised foreign exchange gains	3,805	(5,455)	3,806	(5,455)
Deferred expenditure	(1,139)	5,000	(80)	3,941
At 31 December	34,802	20,722	20,777	9,329
Represented by:				
Future income tax benefit	64,968	52,603	52,569	41,210
Deferred tax liability	(30,166)	(31,881)	(31,792)	(31,881)
At 31 December	34,802	20,722	20,777	9,329

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21 Deferred tax asset (continued)

Taxable and deductible temporary differences arise from the following:

All amounts are expressed in K'000			Group - 2010				
	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Disposal	Subsidiary-opening balance	Closing balance
Gross deferred tax liabilities	(31,881)	9,767	(6,018)	5,915	(7,949)	-	(30,166)
Gross deferred tax assets	52,603	10,671	1,694	-	-	-	64,968
	20,722	**20,438**	**(4,324)**	**5,915**	**(7,949)**	**-**	**34,802**
			Group - 2009				
	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Disposal	Subsidiary-opening balance	Closing balance
Gross deferred tax liabilities	(17,094)	(271)	2,625	(17,141)	-	-	(31,881)
Gross deferred tax assets	27,146	13,734	-	-	-	11,723	52,603
	10,052	**13,463**	**2,625**	**(17,141)**	**-**	**11,723**	**20,722**

All amounts are expressed in K'000			Bank - 2010				
2010	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Disposal	Others	Closing balance
Gross deferred tax liabilities	(31,881)	9,767	(6,018)	4,289	(7,949)	-	(31,792)
Gross deferred tax assets	41,210	10,840	519	-	-	-	52,569
	9,329	**20,607**	**(5,499)**	**4,289**	**(7,949)**	**-**	**20,777**

			Bank - 2009				
	Opening balance	Current period P&L Movements	Adjustment brought forward	Revaluation & net addition	Disposal	Others	Closing balance
Gross deferred tax liabilities	(17,081)	(284)	2,625	(17,141)	-	-	(31,881)
Gross deferred tax assets	26,881	14,329	-	-	-	-	41,210
	9,800	**14,045**	**2,625**	**(17,141)**	**-**	**-**	**9,329**

For the year ended 31 December 2010

22 Other assets

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Items in transit and other assets	34,701	45,143	16,504	34,765
Accrued income	51,317	51,777	48,024	44,161
Intercompany account	-	-	2,896	-
Computer development costs	2,387	2,934	2,387	2,934
Outstanding premiums	25,710	23,566	-	-
Inventory	4,033	4,676	-	-
Prepayments	10,459	6,409	10,127	6,409
Accounts receivable	8,533	28,251	176	411
	137,140	162,756	80,114	88,680

23 Amounts due to other banks

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Items in the course of collection	23,638	26,594	29,497	12,202

24 Amounts due to customers

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Demand / current	6,141,624	5,471,424	5,747,076	5,106,154
Term	1,843,033	2,022,355	1,438,499	1,653,472
	7,984,657	7,493,779	7,185,575	6,759,626

25(a) Other liabilities

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Creditors and accruals	65,817	36,672	27,730	27,760
Items in transit and all other liabilities	138,265	186,071	122,694	174,500
Interest payable-convertible notes	4,176	-	-	-
Policy liabilities	446,754	423,258	-	-
Premiums received in advance	4,961	4,432	-	-
Outstanding claims	7,644	5,451	-	-
Claims incurred but not reported (IBNR)	1,678	1,624	-	-
Borrowings	14,698	13,447	-	-
	683,993	670,955	150,424	202,260

For the year ended 31 December 2010

25(b) Subordinated debt securities

At 31 December, there are K75.525 million of debt securities outstanding, expected to be settled more than 12 months after the balance sheet date. The notes were issued during 2009, with a maturity date in 2019, and interest is payable semi-annually at 11% per annum. They are valued at amortised cost. The Group has not had any defaults of interest or other breaches with respect to its debt securities in 2010.

26 Other provisions

	Group		Bank	
All amounts are expressed in K'000	**2010**	**2009**	**2010**	**2009**
Staff related	43,746	34,461	34,568	26,708
Provision for non lending loss	17,505	12,539	16,896	10,771
Provision for offshore creditors' GST	3,179	8,299	3,178	8,299
	64,430	55,299	54,642	45,778
Staff related provisions				
At 1 January	34,461	21,865	26,708	20,979
Provisions charge	62,168	17,202	57,613	7,440
Payouts	(52,883)	(4,606)	(49,753)	(1,713)
At 31 December 2010	43,746	34,461	34,568	26,708

27 Ordinary shares - Bank

Number of shares in '000s, book value in K'000	Number of Shares	Book Value
At 31 December 2008/1 January 2009	4,559,328	318,014
Issuance during the year	-	-
At 31 December 2009/1 January 2010	4,559,328	318,014
Issuance during the year	227,967	143,619
At 31 December 2010	4,787,295	461,633

On 30 July 2010, the Group issued to IFC Capitalisation Fund 227,966,436 shares at 63 toea per share for a total of subscription price of K143,618,855.

The issued capital of Bank of South Pacific Limited comprises ordinary shares. Following is a summary of principal shareholders as at 31 December 2010 and their respective percentage holdings.

For the year ended 31 December 2010

27 Ordinary shares - Bank (continued)

Major shareholders: % shareholding	2010	2009
Independent Public Business Corporation	17.61	23.49
Nominees Niugini Limited	11.07	11.63
Nambawan Super Limited	9.98	10.49
Petroleum Resources Kutubu Limited	9.64	10.12
Credit Corporation (PNG) Limited	8.04	8.43
National Superannuation Fund Limited	6.79	7.13
PNG Sustainable Development Programme Limited	6.12	6.43
IFC Capitalization (Equity) Fund LP	4.76	-
International Finance Corporation	4.76	-
PNG Teachers Savings and Loans Society Limited	3.73	4.01
Comrade Trustee Services	3.20	3.42
Tropicana Limited	1.04	1.09
	86.74	86.24
All Others	13.26	13.76
	100.00	100.00

Share Options - Executive Management Share Option Plan

An Executive Management Share Option Plan was established at the Annual General Meeting of 27 May 2004. The first tranche of options of 1,121,818 were exercised on 30 June 2006. These options were valued at Mark to Market. The second tranche of options of 1,481,818 were exercised on 30 June 2007.

On 1 July 2008, the Board under this plan, granted options over ordinary shares of Bank of South Pacific Limited to the executives only. These options were issued for nil consideration, are not transferable, and cannot be quoted on any stock exchange.

On July 2010, when the 2008 EMSOP expired, the executive management forfeited their right to exercise their options.

On July 2010, the Board granted 18,250,000 options over ordinary shares of Bank of South Pacific Limited to the executives only (taking into account the 10/1 share split in 2008). The options have a vesting period of 1 July 2012, and an exercise price of K0.65. The overriding exercise conditions of these options are performance hurdles.

The 2010 share options have been valued in compliance with IFRS 2 and classified as equity on the balance sheet.

notes to the financial statements

For the year ended 31 December 2010

27 Ordinary shares - Bank (continued)

Options 2010	Opening balance	Share split	Issued	Exercised	Forfeited	Others	Closing Balance
2008	8,000	-	-	-	8,000	-	-
2009	-	-	-	-	-	-	-
2010	-	-	18,250	-	-	-	18,250
Total	**8,000**	**-**	**18,250**	**-**	**8,000**	**-**	**18,250**
Weighted average exercise price	1.26		0.65		1.26		0.65

Options 2009	Opening balance	Share split	Issued	Exercised	Forfeited	Others	Closing Balance
2007	7,000	-	-	-	7,000	-	-
2008	8,000	-	-	-	-	-	8,000
2009	-	-	-	-	-	-	-
Total	**15,000**	**-**	**-**	**-**	**7,000**	**-**	**8,000**
Weighted average exercise price	0.91	-	-	-	0.505	-	1.26

For the year ended 31 December 2010

28 Reserves and retained earnings/(accumulated losses)

All amounts are expressed in K'000	Group 2010	Group 2009	Bank 2010	Bank 2009
Retained earnings				
At 1 January	553,912	394,367	551,625	394,461
Net profit for the year	283,147	257,118	276,570	257,738
Dividend paid	(247,959)	(100,305)	(247,959)	(100,305)
Deferred income and prior year adjustments	(123)	2,732	(1,864)	(269)
At 31 December	588,977	553,912	578,372	551,625
Reserves comprise:				
Revaluation reserve	68,776	68,776	68,776	68,776
Capital reserve	635	635	635	635
Equity component of convertible notes	18,218	-	-	-
Options reserve	1,968	1,311	1,967	1,311
General reserve	2,875	2,875	2,875	2,875
Exchange reserve	(8,685)	(11,426)	(4,914)	(7,158)
	83,787	62,171	69,339	66,439
Movement in reserves for the year:				
Revaluation reserve				
At 1 January	68,776	31,146	68,776	31,146
Asset revaluation	-	54,769	-	54,769
Deferred tax on asset revaluation	-	(17,139)	-	(17,139)
At 31 December	68,776	68,776	68,776	68,776
Capital reserve				
At 1 January	635	635	635	635
At 31 December	635	635	635	635
Options reserve				
At 1 January	1,311	1,560	1,311	1,560
Movement during the year	657	(249)	656	(249)
At 31 December	1,968	1,311	1,967	1,311
General reserve				
At 1 January	2,875	2,875	2,875	2,875
At 31 December	2,875	2,875	2,875	2,875
Exchange reserve				
At 1 January	(11,424)	(4,348)	(7,156)	(294)
Movement during the year	2,739	(7,076)	2,242	(6,862)
At 31 December	(8,685)	(11,424)	(4,914)	(7,156)

For the year ended 31 December 2010

29 Contingent liabilities and commitments

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Off balance sheet financial instruments				
Standby letters of credit	28,671	41,641	27,470	41,641
Guarantees and indemnities issued	286,409	(34,932)	281,407	(34,932)
Trade letters of credit	17,814	24,538	17,815	24,538
Commitments to extend credit	887,720	1,080,026	863,938	1,080,026
	1,220,614	1,111,273	1,190,630	1,111,273

Legal Proceedings

A number of legal proceedings against the Bank and the Group were outstanding as at 31 December 2010. No provision has been made as existing management information and professional advice indicate that it is unlikely that any significant loss will arise. Based on information available at 31 December 2010, the Bank and the Group estimates a contingent liability of K73.833 million (2009: K65.689 million) in respect of these proceedings.

Statutory deposits with the Central Bank

Cash reserve requirement - 4% of all amounts due to customers (2009: 3%)	363,680	360,799	274,206	265,419
Commitments for capital expenditure				
Amounts with firm commitments, and not reflected in the accounts	37,691	7,145	29,759	7,145
Operating lease commitments				
Not later than 1 year	11,449	7,991	7,578	7,991
Later than 1 year and not later than 5 years	20,718	60	7,049	60
Later than 5 years	20,904	92	-	92
	53,071	8,143	14,627	8,143

30 Cash and cash equivalents

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

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Cash and balances with Central Bank (note 15)	1,042,029	996,393	744,280	796,197
Due from other banks (note 17)	302,061	191,888	295,028	186,655
Due to other banks (note 23)	(23,638)	(26,594)	(29,497)	(12,202)
	1,320,452	1,161,687	1,009,811	970,650

For the year ended 31 December 2010

31 Related party transactions

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

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

A number of banking transactions are entered into with these related parties in the normal course of business, and include loans, deposits, property rentals, share transfers and foreign currency transactions. These transactions are carried out on commercial terms and market rates. For the year ended 31 December 2010, balances and transactions of accounts for Directors were as follows:

All amounts are expressed in K'000	2010	2009
Deposits		
Opening balances	21,758	14,623
Net movement	22,681	7,135
Closing balance	44,439	21,758
Interest paid	2,461	3,365
Loans and advances		
Opening balances	65,795	29,262
Loans issued	24,954	48,399
Interest	61	580
Charges	6,925	5,065
Loan repayments	(14,164)	(17,511)
Closing balance	83,571	65,795

Incentive-based transactions are provided for staff. Such transactions include marginal discounts on rates, and specific fee concessions. These incentives are mainly percentage-based on market rates and fees, and as such, staff accounts are always subject to underlying market trends in interest rates and fees. As at 31 December 2010, staff account balances were as follows:

All amounts are expressed in K'000	2010	2009
Housing loans	10,385	10,560
Other loans	14,381	10,503
	24,766	21,063
Cheque accounts	5,023	3,791
Foreign currency accounts	-	4
Savings accounts	3,338	2,725
	8,361	6,520

For the year ended 31 December 2010

31 Related party transactions (continued)

Interests Register

The following are transactions recorded in the interests register:

Name	Nature of Interest	
K. Constantinou, OBE	Director	Bank of South Pacific Ltd[1], BSP Capital Ltd[1], Airways Hotel & Apartments Ltd, Lamana Hotel Ltd, Lamana Development Ltd, Hebou Constructions Ltd, Heritage Park Hotel Ltd, Gazelle International Hotel, Airlines PNG Ltd, Oil Search Ltd, Alotau International Hotel, Kimbe Bay Hotel, Grand Pacific Hotel, Hotel Technical Services Ltd, CGA Properties Ltd, City Centre Development Ltd, Coastwatchers Court Ltd, Fairhaven No.57 Ltd.
	Shareholder	Airways Hotel & Apartments Ltd, Lamana Hotel Ltd, Lamana Development Ltd, Hotel Technical Services Ltd, C.G.A Properties, Fairhaven No.57 Ltd.
	Member	Australian Institute of Company Directors, PNG Institute of Directors.
T. E. Fox	Director	Bank of South Pacific Ltd[2], Teyo No.1 Ltd[5], Capital Life Insurance Company Ltd, BSP Capital Ltd.
	Shareholder	Teyo No.1 Ltd, Bank of South Pacific Ltd, Citigold Corporation Ltd, Marengo Gold Ltd, New Guinea Energy Ltd.
	Trustee/Member	Institute of National Affairs[8], PNG Institute of Directors.
I. B. Clyne	Director	Bank of South Pacific Ltd[9], BSP Capital Ltd, Capital Life Insurance Company Ltd, BSP Convertible Notes Ltd, BSP Rural Ltd.
	Member	Commercial Bankers Association.
J. G. Jeffery	Director	Bank of South Pacific Ltd, National Superannuation Fund Ltd[1,5], Employers Federation of PNG, Jayliss Ltd, City Pharmacy Ltd, Airlines PNG Ltd.
	Shareholder	Highlands Pacific Ltd, Oil Search Ltd, Jayliss Ltd[1].
G. Aopi	Director	Bank of South Pacific Ltd, Oil Search Ltd[7], Steamships Trading Co Ltd, POMSoX Ltd, Hirad Ltd, Marsh Ltd, Wahinemo Ltd, FM Morobe Ltd, CDI Foundation, Telikom PNG Ltd[1], Independent Public Business Corporation[1], BSP Capital Ltd.
	Shareholder	Oil Search Ltd[7], Lihir Gold Ltd, Hirad Ltd, Wahinemo Ltd, Highlands Pacific Ltd, Melanesian Trustees (ICPNG), Bank of South Pacific Ltd, Kumul Asset Management.
	Trustee/Member	Institute of National Affairs, Business Council of PNG.

For the year ended 31 December 2010

31 Related party transactions (continued)

Interests Register

The following are transactions recorded in the interests register:

Name	Nature of Interest	
Dr. I. Temu	Director	Bank of South Pacific Ltd, Tipi Enterprise Ltd, BSP Capital Ltd, PNG Ports Corporation[1].
	Shareholder	Telstra Ltd, Nautilus Minerals Niugini Ltd.
	Employee	Barrick Gold Ltd.
	Member	Divine Word University, Chamber of Mining & Petroleum.
Sir N. Bogan	Director	Bank of South Pacific Ltd, Nambawan Super Ltd[1,5], Coprez Communications Ltd[1], Coprez Holdings Ltd, Inventive Nook Ltd, James Cook Ltd, Niugini Cocoa Factory, In Touch Media Ltd[1], Ahi Holdings Ltd.
	Shareholder	Coprez Holdings Ltd, Inventive Nook Ltd, James Cook Ltd, Niugini Cocoa Factory, In Touch Media Ltd.
	Member	Evangelical Lutheran Church Finance Committee.
C. C. Procter	Director	Bank of South Pacific Ltd, Sun Hung Kai Ltd, BSP Capital Ltd, Allied Overseas Ltd.
J.K. Natto	Director	Bank of South Pacific Ltd, Petroleum Resources Kutubu Ltd[1], Kutubu Security Services Ltd[3], Welgris Fuel Distributors Ltd, Maxpro Security Services Ltd, Hekari Properties Ltd, Namo'aporo Landowners Association Inc[1], BSP Capital Ltd, Hevi Lift Ltd.
	Member	Australian Institute of Company Directors.
N. N. Beangke	Director	Bank of South Pacific Ltd, Credit Corporation (Fiji) Ltd, PNG Coffee Exports Ltd[1,5], Boroma Ltd, General Holdings Ltd[5], Credit Corporation(SI) Ltd, BSP Capital Ltd.
	Shareholder	Credit Corporation (PNG) Ltd[5], Boroma Ltd, Credit Corporation (Vanuatu).

[1]Chairman, [2]Deputy Chairman, [3]Managing Director, [4]Executive Director, [7]General Manager, [8]Councillor, [5]Company is shareholder of Bank of South Pacific Limited, or shareholder of company that is shareholder, [6]Companies have banking facilities with BSP, [9]Chief Executive Officer.

On 3 February 2011, K. Constantinou, OBE replaced N.N. Beangke as Chairman of Bank of South Pacific Limited.

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For the year ended 31 December 2010

32 Directors' and executive remuneration

Directors' remuneration

Directors of the Company received remuneration including benefits during 2010 as detailed below:

Name of Director	Meetings attended/ total held	Base emolument	Total remuneration 2010	Total remuneration 2009
K. Constantinou, OBE	10/10	69,521	69,521	60,900
N. N. Beangke	9/10	102,259	102,259	94,500
T. E. Fox	9/10	99,109	99,109	91,350
Dr. I. Temu	8/10	74,097	74,097	67,200
C. C. Procter	9/10	96,300	96,300	88,800
Sir N. Bogan	4/10	65,210	65,210	60,900
I. B Clyne*	10/10	-	-	-
J. G. Jeffery	9/10	87,300	87,300	79,800
G. Aopi	7/10	76,384	76,384	70,350
J. K. Natto	4/10	66,072	66,072	60,900

Directors Thomas Edova Fox, Sir Nagora Bogan and John Gordon Jeffery retired by rotation in accordance with Clause 15.3 of the Company's Constitution and being eligible, offered themselves for re-election by the shareholders on the 21st May 2010 Annual General Meeting.

Non-executive Board Members of the Board – Beangke, Fox, Temu, Procter, Constantinou, Aopi and Kapi Natto will receive an allowance of K46,324 as Board of Directors of BSP Capital Ltd which forms part of the Group.

*Managing Director/Chief Executive Officer receives no fees for his services as Director during the year.

For the year ended 31 December 2010

32 Directors' and executive remuneration (continued)

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

Remuneration K'000	2010 No.	2009 No.	Remuneration K'000	2010 No.	2009 No.	Remuneration K'000	2010 No.	2009 No.
100-110	16	12	310-320	-	1	490-500	2	1
110-120	14	3	320-330	-	1	500-510	2	1
120-130	3	3	330-340	1	3	510-520	1	-
130-140	2	3	340-350	-	1	530-540	5	1
140-150	2	9	350-360	-	-	540-550	1	-
150-160	3	4	360-370	1	-	560-570	4	2
160-170	9	1	370-380	1	1	570-590	1	-
180-190	8	4	380-390	2	2	590-670	5	1
190-200	4	1	390-400	-	1	670-700	3	1
210-220	1	2	400-410	1	1	750-790	2	-
220-240	5	-	410-420	2	2	790-800	-	-
240-250	-	-	420-430	-	3	810-830	2	1
250-260	-	1	430-440	1	-	830-850	-	1
260-269	2	-	440-450	2	2	850-860	-	-
270-280	-	-	450-460	-	3	920-930	-	1
280-290	2	-	460-470	2	1	930-1,020	2	2
290-300	1	-	470-480	1	2	1,220-1,260	-	-
300-310	-	-	480-490	1	-	1,540-2,230	2	1
Total							**119**	**80**

Executives' remuneration stated includes exercised options (refer to Note 27).

For the year ended 31 December 2010

32 Directors' and executive remuneration (continued)

Executive remuneration

The specified executives during the year were:

Ian B Clyne	Robin Fleming	Chris Beets
Johnson Kalo	Peter Dixon	
Aho Baliki	Hans Abma	
Frans Kootte	Giau Duruba	

Specified executives remuneration in aggregate (K'000)

	Primary			Post-employment					
	Salary	Bonus	Non-monetary	Super	Pre-scribed benefits	Other	Equity options	Other benefits	Total
2010	6,944	1,825	224	135	-	-	-	396	9,524
2009	4,778	1,539	100	130	-	-	-	133	6,680

33 Reconciliation of operating cash flow

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Reconciliation of operating profit/(loss) after tax to operating cash flow before changes in operating assets				
Operating profit/(loss) after tax	283,147	257,118	276,570	257,738
Add: Tax expense	127,657	121,025	125,527	120,226
Operating profit before income tax	410,804	378,143	402,097	377,964
Major non cash amounts				
Depreciation	53,499	37,371	43,261	36,556
Amortisation of deferred acquisition and computer development costs	645	1,684	645	1,684
Net (profit)/loss on sale of fixed assets	1,855	(1,184)	1,987	(1,184)
Gain on property revaluation	-	(2,372)	-	(2,372)
Sundry write off	-	32,372	-	32,372
CDO buy-back provision	-	-	-	-
Movement in forex income accrual	(2,760)	(3,135)	(1,414)	(3,135)
Movement in provision for doubtful debts	(17,739)	(16,645)	(19,112)	(16,376)
Movement in payroll provisions	7,731	(5,345)	7,731	(5,232)
Net effect of other accruals	36,521	(30,295)	33,773	(10,764)
Operating cash flow before changes in operating assets	490,556	390,594	468,968	409,513

For the year ended 31 December 2010

34 Earnings per share

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

	Group		Bank	
All amounts are expressed in K'000	2010	2009	2010	2009
Net Profit attributable to shareholders (K'000)	283,147	257,118	276,570	257,738
Weighted average number of ordinary shares on issue ('000)	4,787,295	4,559,328	4,787,295	4,559,328
Basic and diluted earning /(loss) per share (expressed in toea)	5.9	5.6	5.8	5.7

35 Segment information

Bank of South Pacific Limited and the Group comprises two segments, this being the provision of banking services and products and stock broking services. For management purposes, segment information determination is based on the risks involved with the provision of core banking services and products and the Bank and Group's management reporting system. The main business lines for management purposes are the core banking segments of Retail Bank, Wholesale Bank which includes Corporate and Paramount SBUs, insurance operations in Fiji, and BSP Capital's stock broking and fund management activities. The Bank of South Pacific Limited and Group's business segments operate in Papua New Guinea, Niue, Fiji and Solomon Islands. Inter segment adjustments reflects elimination entries in respect of inter segment income and expense allocations included funds transfer pricing.

Analysis by business segments:

Year ended 31 December 2010								
All amounts are expressed in K'000	Retail	Wholesale	Fiji Bank	Insurance	BSP Capital	Others	Adjust Inter Segment	Total
Revenue	365,498	524,599	91,893	89,074	3,772	336,957	88,886	1,500,679
Costs	(349,594)	(194,463)	(89,836)	(77,531)	(7,338)	(154,798)	(216,315)	(1,089,875)
Operating results	15,904	330,136	2,057	11,543	(3,566)	182,159	(127,429)	410,804
Income tax expense								(127,657)
Profit after tax								**283,147**
Year ended 31 December 2009								
	Retail	Wholesale	Fiji Bank	Insurance	BSP Capital	Others	Adjust Inter Segment	Total
Revenue	285,946	525,756	8,712	15,891	4,288	488,707	162,803	1,492,103
Costs	(298,797)	(277,597)	(6,441)	(15,259)	(7,012)	(112,556)	(396,298)	(1,113,960)
Operating results	(12,851)	248,159	2,271	632	(2,724)	376,151	(233,495)	378,143
Income tax expense								(121,025)
Profit after tax								**257,118**

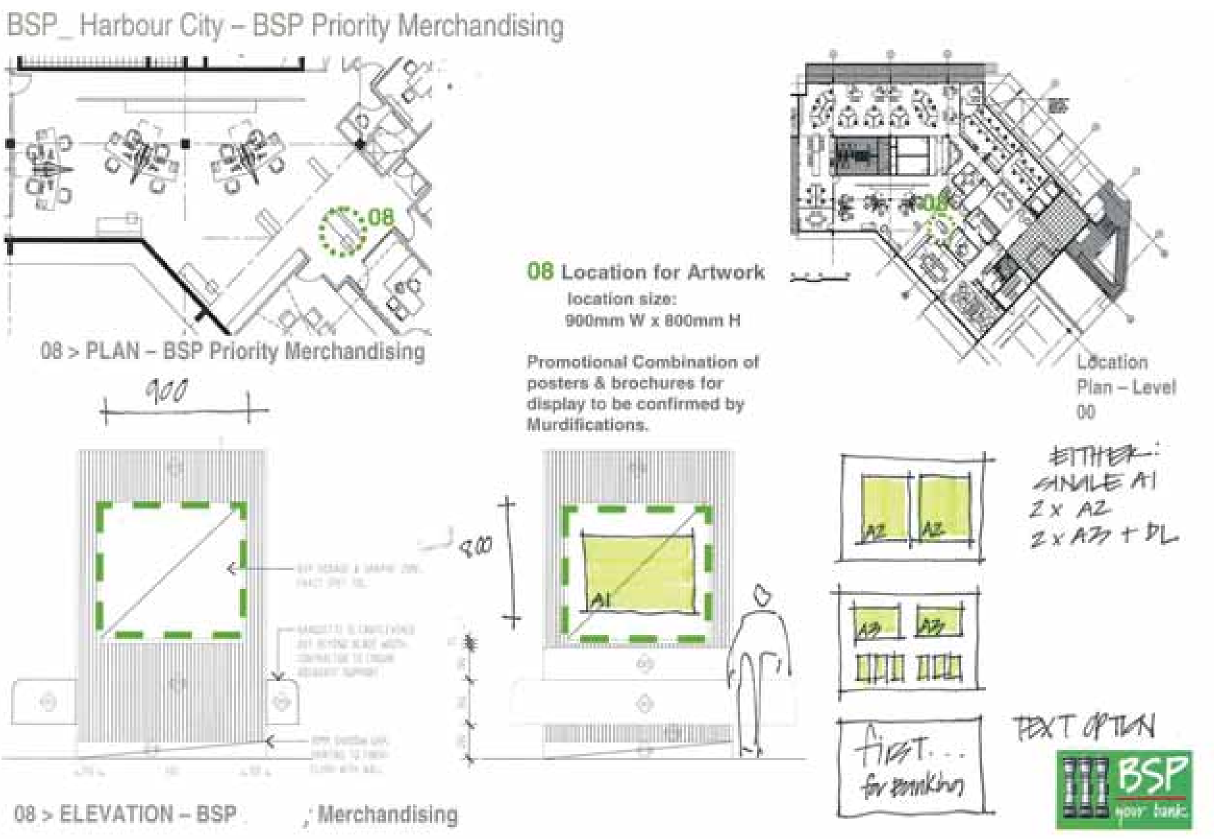
36 Events occurring after balance sheet date

Subsequent to balance date, on 4 February 2011, the government of Fiji passed a decree enabling the change in legislation of Fiji National Bank Ltd, to a branch of Bank of South Pacific Ltd. Any date before June 2011, may be elected as the effective date. The effective date of the decree is yet to be gazetted.

The decree provides for the vesting of National Bank of Fiji Limited t/a Colonial National Bank's (CNB) business and undertakings in Bank of South Pacific Limited (BSP), assignment and vesting of all of CNB's contracts, assets and liabilities to BSP, transfer of all CNB customer relationships to BSP and assumption of responsibility by BSP of all CNB employees.

The decree also provides for the release and discharge of CNB from all further actual or contingent liabilities and obligations in respect of the business to any person, deemed consent for the vesting of any CNB property, any transfer or security given to CNB, or any other right or benefit of CNB to BSP, continuation of any legal action by or against CNB, in the name of BSP and use of information given by any customer or any other person to CNB for its use in the business to be deemed to be information given to BSP for the same purpose.

It further provides for various other consequential matters, including admission of evidence by BSP, continued application of the Bankers' Books Evidence Act, directions to registrars to record entries and memorials in any relevant instrument, continuity of legal rights or accrued losses and taxation consequences.




WE ARE FOR STAYING HOME
AND GOING PLACES

Deloitte.

Deloitte Touche Tohmatsu

Deloitte Tower, Level 12
Douyglas Street
Port Moresby
PO Box 1275 Port Moresby
National Capital District
Papua New Guinea

Tel: +675 308 7000
Fax: +675 308 7001
www.deloitte.com/pg

Independent Auditor's Report to the Shareholders of Bank of South Pacific Limited and its subsidiaries

We have audited the accompanying consolidated financial statements of Bank of South Pacific Limited and its subsidiaries, which comprise the consolidated statement of financial position as at 31 December 2010, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flow statement for the year then ended on that date and notes comprising a summary of significant accounting policies and other explanatory information, and the directors' declaration.

Management's Reposiblity for the Financial Statements

The management of Bank of South Pacific Limited and its subsidiaries is responsible for the preparation and true and fair presentation of the consolidated financial statements in accordance with the International Financial Reporting Standards and other applicable laws and regulations. This responsiblity includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibitly

Our responsiblity is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statments. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statments, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion, and we have obtained all information required by us.

Audit Opinion

In our opinion,

a) the consolidated financial statements give a true and fair view of the financial position of Bank of South Pacific Limited and its subsidiaries as at 31 December 2010, and of the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards and applicable laws and regulations,
b) proper accounting records have been kept by Bank of South Pacific Limited and its subsidiaries.

Other Information

We do not provide any other sevices to Bank of South Pacific Limited and its subsidiaries.

Port Moresby, this 9th day of March 2011.

Deloitte Touche Tohmatsu

DELOITTE TOUCHE TOHMATSU

By: Suzaan Theron
Partner
Registered under the Accountants Act 1996

Member of
Deloitte Touche Tohmatsu

shareholder information

The following is a summary of pertinent issues relating to a shareholding in the Company. The Constitution of BSP may be inspected during normal business at the Registered Office.

Rights attaching to ordinary shares

The rights attaching to shares are set out in Bank of South Pacific Limited's Constitution and in certain circumstances, are regulated by the Companies Act 1997, the POMSoX Listing Rules and general law.
There is only one class of share. All shares have equal rights.

Other rights attached to ordinary shares include:

(a) General meeting and notices

Each member is entitled to receive notice of, and to attend and vote at, general meetings of BSP and to receive all notices, accounts and other documents required to be sent to members under BSP's constitution, the Companies Act or the Listing Rules.

(b) Voting rights

At a general meeting of shareholders every holder of fully paid ordinary shares present in person or by an attorney, representative or proxy has one vote on a show of hands (unless a member has appointed two proxies) and one vote per share on a poll.

A person who holds a share which is not fully paid is entitled, on a poll, to a fraction of a vote equal to the proportion which the amount paid bears to the total issue price of the share.

Where there are two or more joint holders of a share and more than one of them is present at a meeting and tenders a vote in respect of the share, the Company will count only the vote cast by the member whose name appears first in BSP's register of members.

(c) Issues of further shares

The Directors may, on behalf of BSP, issue, grant options over or otherwise dispose of unissued shares to any person on the terms, with the rights, and at the times that the Directors decide. However, the Directors must act in accordance with the restrictions imposed by BSP's constitution, the POMSoX Listing Rules, the Companies Act and any rights for the time being attached to the shares in any special class of those shares.

(d) Variation of rights

Unless otherwise provided by BSP's constitution or by the terms of issue of a class of shares, the rights attached to the shares in any class of shares may be varied or cancelled only with the written consent of the holders of at least three-quarters of the issued shares of that class, or by special resolution passed at a separate meeting of the holders of the issued shares of the affected class.

(e) Transfer of shares

Subject to BSP's constitution, the Companies Act and the POMSoX Listing Rules, ordinary shares are freely transferable.

The shares may be transferred by a proper transfer effected in accordance with the POMSoX Business Rules, by any other method of transferring or dealing with shares introduced by POMSoX and as otherwise permitted by the Companies Act or by a written instrument of transfer in any usual form or in any other form approved by either the Directors or POMSoX that is permitted by the Companies Act.

The Directors may decline to register a transfer of shares (other than a proper transfer in accordance with the POMSoX Business Rules) where permitted to do so under the POMSoX Listing Rules or the transfer would be in contravention of the law. If the Directors decline to register a transfer, BSP must give notice in accordance with the Companies Act and the POMSoX Listing rules, give the party lodging the transfer written notice of the refusal and the reason for refusal. The Directors must decline to register a transfer of shares when required by law, by the POMSoX Listing Rules or by the POMSoX Business Rules.

(f) Partly paid shares

The Directors may, subject to compliance with BSP's constitution, the Companies Act and the POMSoX Listing Rules, issue partly paid shares upon which there are outstanding amounts payable. These shares will have limited rights to vote and to receive dividends.

(g) **Dividends**

The Directors may from time to time determine dividends to be distributed to members according to their rights and interests. The Directors may fix the time for distribution and the methods of distribution. Subject to the terms of issue of shares, each share in a class of shares in respect of which a dividend has been declared will share in the dividend equally.

Each share carries the right to participate in the dividend in the same proportion that the amount for the time being paid on the share (excluding any amount paid in advance of calls) bears to the total issue price of the share.

Dividend payouts over the last seven years are disclosed in the schedule of Historical Financial Performance elsewhere in this Annual Report.

(h) **Liquidation**

Subject to the terms of issue of shares, upon liquidation assets will be distributed such that the amount distributed to a shareholder in respect of each share is equal. If there are insufficient assets to repay the paid up capital, the amount distributed is to be proportional to the amount paid up.

(i) **Directors**

BSP's constitution states that the minimum number of directors is three and the maximum is ten.

(j) **Appointment of directors**

Directors are elected by the shareholders in general meeting for a term of three years. At each general meeting, one third of the number of directors (or if that number is not a whole number, the next lowest whole number) retire by rotation. The Board has the power to fill casual vacancies on the Board, but a director so appointed must retire at the next annual meeting.

(k) **Powers of the Board**

Except as otherwise required by the Companies Act, any other law, the POMSoX Listing Rules or BSP's constitution, the Directors have power to manage the business of BSP and may exercise every right, power or capacity of BSP to the exclusion of the members.

(l) **Share buy backs**

Subject to the provisions of the Companies Act and the POMSoX Listing Rules, BSP may buy back shares in itself on terms and at times determined by the Directors.

(m) **Officers' indemnities**

BSP, to the extent permitted by law, indemnifies every officer of BSP (and may indemnify any auditor of BSP) against any liability incurred by the person, in the relevant capacity, to another person unless the liability arises out of conduct involving lack of good faith.

BSP may also make a payment in relation to legal costs incurred by these persons in defending an action for a liability, or resisting or responding to actions taken by a government agency or a liquidator.

Twenty largest registered fully paid ordinary shareholders

At the 31 December 2010, the twenty largest registered fully paid shareholders of the Company were:

		Share Held	%
1.	Independent Public Business Corporation	843,115,964	17.61
2.	Nominees Niugini Limited	530,105,100	11.07
3.	Nambawan Super Limited	477,805,052	9.98
4.	Petroleum Resources Kutube Limited	461,538,400	9.64
5.	Credit Corporation (PNG) Limited	384,819,211	8.04
6.	National Superannuation Fund Limited	325,051,165	6.79
7.	PNG Sustainable Development Programme Limited	293,027,664	6.12
8.	IFC Capitalization (Equity) Fund LP	227,966,436	4.76
9.	International Finance Corporation	227,966,436	4.76
10.	Teachers Savings and Loans Society Limited	178,673,659	3.73
11.	Comrade Trustee Services Limited	153,081,253	3.20
12.	Tropicana Limited	49,836,525	1.04
13.	Lamin Trust Fund	35,181,316	.73
14.	Credit Corporation (PNG) Ltd (CC Finance Ltd)	30,000,000	.63
15.	Solomon Islands National Provident Fund Board	28,286,854	.59
16.	Mineral Resources OK Tedi No. 2	26,000,000	.54
17.	Catholic Diocese of Kundiawa	21,656,880	.45
18.	Southern Highlands Provincial Government	20,000,000	.42
19.	Mineral Resources Star Mountains Ltd	19,757,982	.41
20.	Society of Divine Word	19,424,725	.41
	Other shareholders	434,000,563	9.08
		4,787,295,185	100.00

Distribution of shareholdings

At the 31 December 2010, the Company had 7,488 shareholders. The distribution of shareholdings is as follows:

Range (number)	Number of Shareholders	Number of Shares
1-1,000	1,177	871,238
1,001 - 5,000	4,145	9,033,676
5,001 - 10,000	898	6,642,257
10,001 - 100,000	993	27,175,536
100,001 and above	275	4,743,572,478
	7,488	**4,787,295,185**

Dividend reinvestment scheme

The Company has suspended its dividend reinvestment scheme.

Employee share scheme

The Company resolved on 27 May 2004 that a maximum of 1% of the total number of shares held in the Company may be allocated to employees each year at the discretion of the Board.

shareholder information

Interest in shares in the Bank

Directors hold the following shares in the Bank:

Director	Shares Held	%
T. E. Fox	5,080,581	0.11
Gerea Aopi	100,000	0.00

N. Beangke holds an indirect shareholding of 8,000,000 in the Company through a family trust, General Holdings Limited. This indirect shareholding represents 0.17% of the Company's issued capital.

Registered Office

Bank of South Pacific Limited
PO Box 78,
PORT MORESBY
National Capital District
PAPUA NEW GUINEA
Telephone: +675 322 9700

Share Registry

PNG Registries Limited
PO Box 1265,
PORT MORESBY
National Capital District
PAPUA NEW GUINEA
Telephone: +675 321 6377

Website

www.bsp.com.pg

Home Exchange for BSP Shares

Port Moresby Stock Exchange Ltd (POMSOX)
PO Box 1531
PORT MORESBY
National Capital District
PAPUA NEW GUINEA
Telephone: +675 320 1980

Home Exchange for BSP Convertible Notes

South Pacific Stock Exchange
GPO Box 11689,
SUVA
Fiji
Telephone: +679 330 4130

BSP CEO Ian Clyne with members of Cheshire disAbility Services PNG handover of new vehicles

BSP Board Of Directors

branch network

Senior Management

Chief Executive Officer
Ian B Clyne

General Manager Retail Bank
Frans Kootte

Chief Risk Officer
Robin Fleming

General Manager Treasury
Christopher Beets

General Manager Paramount Banking
Aho Baliki

General Manager Human Resources
Giau Duruba

Chief Financial Officer
Johnson Kalo

Branches	Phone Numbers
AITAPE Branch Manager Quillan Nongi	(675) 857 2042
ALOTAU Branch Manager Ben Umba	(675) 641 1284
BIALLA Branch Manager Marco Hamen	(675) 983 1095
BOROKO Branch Manager Anne Baniyamai	(675) 323 2288
BUKA Branch Manager Benjamin Kiwai	(675) 973 9042
BULOLO Branch Manager Joe Makinta	(675) 474 5366
COMMERCIAL CENTRE Manager Operations Madeleine Topelemu	(675) 325 5999
DARU Branch Manager Ivy David	(675) 645 9062
DOUGLAS STREET Branch Manager Wesley Hosea	(675) 321 2444
GOROKA Assistant Branch Manager Billy Veveloga	(675) 732 1633
KAINANTU Branch Manager Reuben Elijah	(675) 737 1065
KAVIENG Branch Manager Maureen Wanu	(675) 984 2066
KIMBE Branch Manager Misbil Alfred	(675) 983 5166
KIUNGA Branch Manager Norman Aser	(675) 548 1073

Branches	Phone Numbers
KOKOPO Branch Manager Albert Burua	(675) 982 9088
KUNDIAWA Branch Manager Albert Seri	(675) 735 1025
LAE Branch Manager Mary Kundi	(675) 473 9801
LAE COMMERCIAL Branch Manager Agnes Mark	(675) 473 9808
LAE MARKET Branch Manager Julie Warren	(675) 473 9606
LAE OPERATIONS CENTRE Branch Manager Eileen Goviro	(675) 473 9866
LIHIR Branch Manager Robinson Panako	(675) 986 4052
LORENGAU Branch Manager Karen George	(675) 470 9050
MADANG Branch Manager Cecilia Pasum	(675) 852 2477
MAPRIK Branch Manager Wendy Poka	(675) 858 1317
MENDI Branch Manager Joseph Was	(675) 549 1070
MORO Branch Manager Sibona Kema/Barry Namongo	(675) 275 5808
MT HAGEN Branch Manager Alex Kuna	(675) 542 1877
MOTUKEA Branch Manager Lina Popal	(675) 321 7701

Branches	Phone Numbers
POPONDETTA Branch Manager Joe Ururu	(675) 329 7171
PORGERA Branch Manager John Basanu	(675) 547 6900
PORT MORESBY Branch Manager Magai Kavailon	(675) 322 9790
RABAUL Branch Manager Bevilon Homuo	(675) 982 1744
TABUBIL Branch Manager Tony Waningu	(675) 548 9179
VANIMO Branch Manager Josephine Komoru	(675) 857 1209
WABAG Relieving Branch Manager Jerry Marie	(675) 547 1176
WAIGANI BANKING CENTRE Branch Manager Leslie Wagiam	(675) 300 9600
WAIGANI DRIVE Branch Manager Mathias Manowo	(675) 325 6788
WEWAK Branch Manager Annette Poka	(675) 856 2344
FIJI (Fiji) Country Head Kevin McCarthy	(679) 330 4011
BA (Fiji) Branch Manager Ropate Toroca	(679) 667 4599
CENTREPOINT (Fiji) Branch Manager Viviana Veisaca	(679) 334 2333
DOMINION HOUSE (Fiji) Branch Manager Susie Fesaitu	(679) 331 4400

Branches	Phone Numbers
LABASA (Fiji) Branch Manager Anand Nair	(679) 881 1888
LAUTOKA (Fiji) Branch Manager Josefa Tuitubou	(679) 666 2466
LEVUKA (Fiji) Branch Manager Meli Tamani	(679) 344 0300
NADI (Fiji) Branch Manager Salim Buksh	(679) 670 0988
NAMAKA (Fiji) Branch Manager Madhur Lata Kumar	(679) 672 8950
NAUSORI (Fiji) Branch Manager Rohit Kumar Sharma	(679) 347 8499
PACIFIC HARBOUR (Fiji) Branch Manager Ram Rattan	(679) 345 2030
PACIFIC HOUSE (Fiji) Branch Manager Rajesh Chand	(679) 331 4400
RAKIRAKI (Fiji) Branch Manager Reginald Kumar	(679) 669 4200
RENWICK (Fiji) Branch Manager Sara Kasaqa Petueli	(679) 330 4011
SAMABULA (Fiji) Branch Manager Losalini Mere Vuinakelo	(679) 338 7999
SAVUSAVU (Fiji) Branch Manager Praveen Chand	(679) 885 0199
SIGATOKA (Fiji) Branch Manager Davendran Pillay	(679) 650 0900
SUVA – CENTRAL (Fiji) Branch Manager Mohammed Arif	(679) 331 4400

Branches	Phone Numbers
TAVEUNI (Fiji) Branch Manager Marica Mara	(679) 888 0433
TAVUA (Fiji) Branch Manager Albertina Rose Lilo	(679) 668 1507
TOP TOWN NADI (Fiji) Branch Manager Irimaia Dru	(679) 670 5111
NIUE (Niue) Branch Manager Ann Pesamino	(683) 4220
SOLOMON ISLANDS (SI) Country Head Mark Corcoran	(677) 21874
AUKI (SI) Branch Manager Samuel Misi	(677) 40484
COMMERCIAL BANKING (SI) Branch Manager Rose Abana	(677) 23620
GIZO (SI) Relieving Branch Manager Tewia Laore	(677) 60539
HONIARA (SI) Branch Manager Michael Kahamana	(677) 21814
MUNDA (SI) Branch Manager Rebecca Hickie	(677) 62177
NORO (SI) Branch Manager Clotilda Londeka	(677) 61222
POINT CRUZ (SI) Branch Manager Rose Funa	(677) 21874
RANADI (SI) Branch Manager Joy Vave	(677) 39403

Corporate Responsibility and Marketing

Community Contribution

Environmental Responsibility

Sport for Life

Growing Responsibly

Changing Lives

Transformation

Marketing

Across Papua New Guinea and the South Pacific. We are your bank.

At BSP, we're much more than a bank, we are a real part of your community.

Every year we're helping by supporting hundreds of educational, environmental and sporting and charitable programmes to help a wide range of people on a local, regional, state and national level. As the only home grown bank in the South Pacific, we understand that we have the opportunity to make a difference where it matters most.

We are proud when asked what BSP stands for. Often comes the reply, "BSP stands for the bank that supports the people". We do. We are building a bank that listens to customers, is changing to meet the growing and unique needs of PNG and the South Pacific and to help people really get more out of life.

Community Contribution

A long term commitment to care and to contribute

BSP's commitment to give back to local communities is through a number of initiatives at corporate as well as branch level. K920,000 worth of community project value was injected into communities in which the bank operates in PNG, Solomon Islands and Fiji. This was typically in the form of school equipment provision and classroom refurbishments, hospital and aid post repairs, water tank installation, market and public area clean-ups, and support of equipment and funding for various charity organisations.

BSP's Community Programme is unique, working in partnership with communities to provide support for what's really needed in each area in which BSP operates.

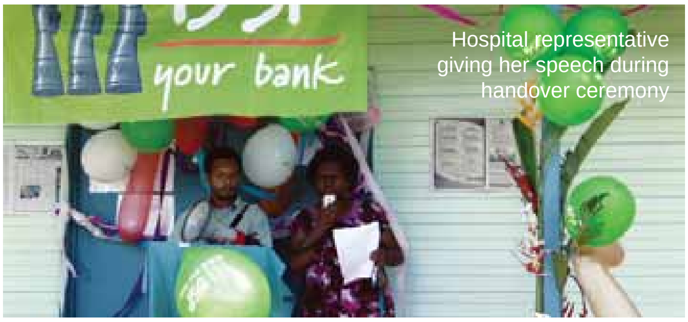

Aitape basketball court before refurbishment


Staff scrubbing and weeding grass from the court

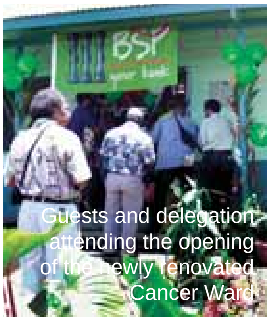

Newly completed basketball stand with BSP painted board

Aitape Branch

Basketball court refurbishment



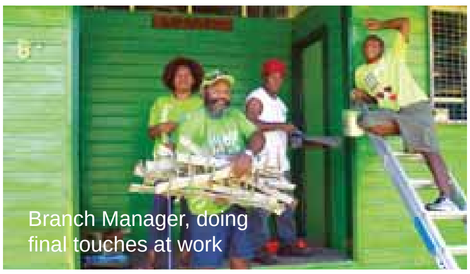
Hospital representative giving her speech during handover ceremony


Guests and delegation attending the opening of the newly renovated Cancer Ward

Alotau Branch

Renovation of Cancer Ward, General Hospital


Contractors at work on the Bialla High School library renovations


Branch Manager, doing final touches at work


Branch Manager, Mr Hamen conducting the handover ceremony

Bialla Branch

Renovation of School Library, Bialla High School

QUICK FACTS

- Every BSP branch designed their own community programme after discussion with their community.
- In 2010, 34 individual significant projects were completed across PNG.
- Each project involved major planning and time, including refurbishing health facilities, renovating schools, bringing healthcare to communities, installing water supply to schools.
- Thousands of local BSP men and women contributed, devoting their own time.


Staff cleaning and painting the ward


Desks, bins and chairs ready for donation to the ward

Boroko Branch

Renovation of Children's Ward, Port Moresby General Hospital

QUICK FACTS

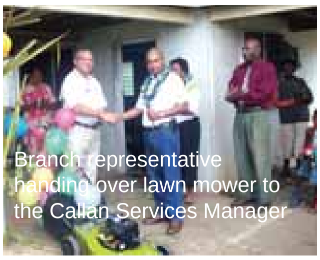
- Over K2 million committed by BSP to fund the projects and to help out communities across PNG in 2009/10.
- CEO Ian Clyne introduced the annual Community Programme in 2009. "BSP is 100% committed to the people of PNG.


Footpath shelter before cleaning, renovation and painting


Footpath shelter after renovation. New furnishings were also provided for the comfort of patients & families

Buka Branch

Buka General Hospital - painting of footpath shelters & Birthing Centre


Branch representative handing over lawn mower to the Callan Services Manager


Branch staff hand over goodies at ceremony 23rd July

Daru Branch

Construction of cement pathway in Callan Services Disabled Centre


Branch staff scrubbing down walls


Staff carrying new louvre windows for replacement of old and broken ones

Douglas Branch

Renovation Children's Paediatric Ward, Port Moresby General Hospital


School representatives receive the basketball equipment donated by BSP on the new court


Branch Manager Madeleine Topelemu takes a shot before declaring the court open at the handover ceremony.

Gordons Com Centre Branch

Erima Primary School - Construction of basketball court


Branch staff painting the rubbish drums


Painted rubbish drums lined up in front of Goroka Branch before being shipped to selected sites for installation

Goroka Branch

Goroka Town - Installation of rubbish bins


Kainantu Branch staff painting the classrooms


Branch project Manager Mark Posenu handing over the newly constructed desks to the school headmaster

Kainantu Branch

Tuempinka Primary School - repainting & supply of 50 desks


Kavieng Branch staff assembling and installing new medical equipment


Branch Manager Maureen handing over equipment to the doctor in charge of Kavieng General Hospital Surgical Ward

Kavieng Branch

Kavieng General Hospital - cleaning & new surgical ward equipment


Fully decorated vehicle loaded with desks ready for delivery


Branch staff load newly constructed desks on to delivery vehicle to deliver to the school

Kimbe Branch

Ruango Primary School - donation of classroom equipment

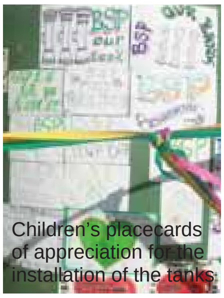

Branch staff happy following the handover ceremony


Fully completed and installed tanks for the school

Kiunga Branch

Kiunga Secondary School - Installation of 2 x 9000L Tuffa Tanks


Member for Kokopo - Dr Allan Marat speaking at the handover ceremony


Children's placecards of appreciation for the installation of the tanks


Mr Seri handing over water tanks to Headmaster of Pinorkwa Primary School

Kundiawa Branch

Installation of 2 Tuffa Tanks - Pinorkwa Primary School


The newly constructed and painted desks being displayed at the classroom painted in BSP colours

Kokopo Branch

Purchasing, painting and furnishing new classrooms, Kurapa Elementary School


The two installed Tuffa Tanks (incl water pump & plumbing accessories) providing much needed water to the school


Before the renovation, the dilapidated state of the old Cancer Ward


After - the fully renovated Cancer Ward

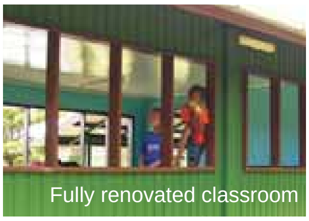
Lae Town & Lae Com Branches

Renovation of Cancer Ward - Angau Memorial Hospital & donation of 2 Tuffa Tanks


Students of Four Mile Primary School use the heart symbol to show their appreciation for the new water supply

Lae Market Branch

Four Mile Primary School - Installation of 2 Tuffa Tanks


Fully renovated classroom


Branch representative giving speech at the handover ceremony

Lihir Branch

Comprehensive renovation of Double Classroom - Londolovit Elementary School


Broken swings before refurbishment

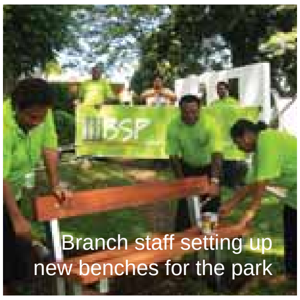

Swings and seating through the park were refurbished ready for public use

Lorengau Branch

Lorengau Town Authority refurbishment of the Lions Park


The monument fountain area before BSP renovation began


Madang Branch staff completing refurbishment including installation of solar power fountain


Branch staff setting up new benches for the park


Madang staff at handover ceremony show heart

Madang Branch

Modilon General Hospital - refurbishment of monument/rec area


Renovated double classroom ready for handover presentation


Students from Maprik Secondary School celebrate the opening of the new facilities


The renovated clinic ready for the handover ceremony


Branch Manager Mr David Wasape handing over keys to the doctor in charge for the newly renovated Mendi Urban Clinic

Maprik Branch

Renovation & Painting of double classroom - Maprik Secondary School

Mendi Branch

Mendi Urban Clinic Renovation


Branch staff at work painting the Mess Hall


Branch Manager Aila Steven handing over the renovated facility to school representative

Moro Branch

Renovation of school and installation of water tank, Waro Primary School


Branch staff complete finishing touches to renovated facilities and took time out to donate blood during the day


Branch staff complete installation of new equipment including televisions, coffee machines for patients and families

Mt Hagen Branch

Mt Hagen General Hospital - Renovation of TB Ward & rec facilities


BSP Staff clearing the site for the new toilet facility


Early stage of construction of the new toilet area

Popondetta Branch

Uganda Mathyrs Catholic School - construction of ablution block


Dr Pyakalyia receiving ultrasound hearing equipment from Branch Manager Magai Kavailon


Beds donated for the birthing centre


Staff showing heart at the presentation of equipment for the refurbishment

Port Moresby Branch

Gerehu Urban Clinic - General Clinic/Donation of equipment

Rabaul Branch

Police Station - cleaning, renovating, donation of office equipment & computer


Police station had been neglected for 15 years, and shown here before the works programme


Building after the completion of the renovation


Tap outlet that will receive water from the tank


Classroom receiving rainwater from the new tank

Tabubil Branch

Tabubil High School - supply of clean water and installation of Tuffa Tank


Classroom prior to being reconstructed


Handover ceremony


Children of Dasi Primary School show appreciation with a thank you


Staff at work rebuilding classroom facilities

Vanimo Branch

Dasi Primary School - Construction of classroom facilities and recreation area


Mobile squad building before work


Building exterior after renovation

Wabag Branch

Renovation of Wabag Mobile Squad Police Station - Wabag Town


Branch Manager Mr Wagiam handing over classroom key to school Head Teacher


Students show appreciation of new completed classrooms


School assembles to form BSP with renovated classroom in background

Waigani Branch

Renovation of classroom & teachers office at Wardstrip Primary School


Before renovation work

After renovation work

Wewak Branch

Major renovation of Wirui Clinic, Women & Children Antenatal Wing

Environmental Responsibility

Making the environment a consideration in everything we do.

BSP truly signalled it is a green bank by launching its environmental programme in 2010, introducing the Go Green initiative throughout the South Pacific.

It was the opportunity to start to change the way people care for their community and a way in which BSP can make a positive contribution by being part of a strategy to raise awareness to create a better, cleaner and healthier world.

More than 150,000 school children and people throughout PNG, Fiji, the Solomon Islands and Niue responded to an invitation to clean up their schools and communities in September and October - making it one of the biggest clean-up initiatives ever attempted. The clean-ups were held in conjunction with the worldwide event, “Clean up the World”. BSP has adopted the “Fix up, clean up and care for the environment” idea and believes “World improvement begins with me”. We can all play our part.

Go Green is a year round commitment to continue to work together to make a positive difference to the world in which we live.

The BSP team in Fiji have a year round programme of replanting and improving the environment

Governor of NCD Port Moresby, Powes Parkop leant a hand at the Clean Up events

BSP staff take part in the Go Green Clean Up the World Campaign

A Student at Sacred Heart Primary School in Hohola, Port Moresby happy to be part of Go Green

GO GREEN BSP

QUICK FACTS

- BSP is the only bank to wholly fund, organise and co-ordinate clean-up events in every territory in which it operates.
- Tonnes of waste was collected.
- 1000s of trees and mangroves have been planted since launch.
- Individual environmental events across the South Pacific continue year round.

We are part of a shift in the community towards the environment

Improving the environmental performance of our business is absolutely the right thing to do but it also makes good business sense.

As a business leader, we are committed to sustainable business practices. We are determined to conduct our operations in a manner that does not compromise the ability of future generations to meet their needs. BSP will continue our earth effort by challenging ourselves, our system and our partners.

Go Green

BSP's Go Green campaign was launched with the largest South Pacific wide Clean-Up events being held throughout Papua New Guinea, Fiji, the Solomon Islands and Niue.

More than 150,000 school children and people throughout the South Pacific, responded to an invitation by BSP, to clean up their schools and communities in September and October. PNG experienced one of the biggest clean-up initiatives ever attempted, solely funded and organised by BSP.

The programme was part of BSP's Go Green Campaign - celebrating its participation in the "Clean Up the World" campaign - a worldwide event.

Clean Up the World MEMBER 2010

In Port Moresby, BSP Chief Executive Officer, Ian Clyne and NCD Governor, Powes Parkop and his family, joined several school clean-ups in the city on Friday and community clean-ups on Saturday.

Governor Parkop said ideally everyone should "keep their environment clean and healthy everyday" and that is what the BSP Go Green initiative is all about – "keeping the environment free from litter and pollution".

The Governor congratulated BSP for their initiative and said it has set the pace for other corporate citizens, schools and members of the community to follow.

BSP CEO, Ian Clyne, said: "Unlike other Clean-Up Projects this is a programme developed in response to the community's desire for long-term solutions to environmental problems."

Ian Clyne continued, "Working in partnership with different sections of the PNG community, BSP's Annual Clean Up Days are part of an education programme."

"The primary aim of getting schools involved is to inspire children to care for the environment which means we are taking a step towards changing the future. It is important that we create a culture where everyone respects their environment and keeps it clean and healthy everyday," he said.

BSP will educate and raise community awareness of environmental issues and promote conversations on biodiversity and ecological sustainability.

An inaugural South Pacific wide event in 2010, the BSP Annual Clean-Up Days have already become the biggest annual volunteer event with a unique, whole of the South Pacific focus. Across the thousands of registered Clean-Up sites throughout the South Pacific, thousands of tonnes of rubbish were collected.

Ian Clyne comments: "World improvement is everybody's business. Your very presence on this earth means you will either positively or negatively impact the environment and therefore make the world a little better or a little worse.

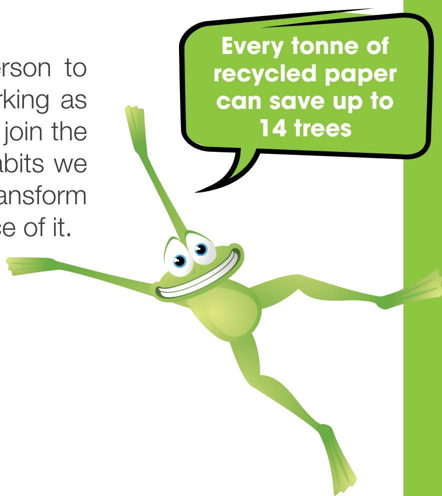
Each of us must ask ourselves: when we leave this world and our children's children move in, what will they find?

The underlying basic principle of BSP's Go Green Campaign is therefore, "World Improvement Begins With Me."

Obviously it is very hard for one person to change the whole world. But by working as a team and by encouraging others to join the team and change their destructive habits we all can make a difference. We can transform the world by cleaning up our little piece of it.


Honiara, Solomon Islands School Clean Up Day received overwhelming support


BSP Reef Rangers, Mangrove Replanting, PNG



Making the environment a consideration in everything we do

Improving the environmental performance of our business is absolutely the right thing to do but it also makes good business sense.

We have always strived to be an environmentally responsible business and we have made significant changes throughout the history of our operations as our understanding of environmental impacts has improved.

BSP believes that a business leader should also be an environmental leader and is therefore committed to sustainable business practices. We are determined to conduct our operations in a manner that does not compromise the ability of future generations to meet their needs. BSP will continue our earth effort by challenging ourselves, our system and our partners.

Our objectives are to:

- make the environment a consideration in everything we do;
- provide leadership for our branches, suppliers and customers and encourage them to be pro-active;
- seek programmes and partnerships that promote positive, environmental outcomes;
- ensure that we comply with all environmental laws and regulations;
- educate and improve the awareness of our employees and customers and work with our suppliers to obtain their commitment, cooperation and feedback and, where possible, bring about changes in behaviour;
- ensure that all staff are aware of their responsibilities and accountable for their actions/inaction;
- measure performance and through implementation and review of our programmes, actions and procedures, improve it.

What BSP is doing to re-use, reduce and recycle

When it comes to the operation of our branches and waste we are continuing to explore options to decrease our environmental impact. Our first priority is to reduce the resources and materials being used wherever possible.

Where we can't reduce our materials, our aim is to reduce waste to landfill. We continue to seek ways to incorporate reuse and recycling into our branches and we see this as one of our greatest opportunities for improvement.

The growth of our business means we are facing increasing challenges in regard to waste management. However, improvements are being made all the time. For example, the commitment to recycling within the territory of PNG has improved considerably our reliance on conventional disposal methods, decreasing the weight on non-recyclable -v- recyclable waste across the BSP network.

Currently under trial in several locations are LED (light emitting diodes) lighting energy-saving devices. The trial is proving positive with indicative energy savings of between 26 and 30 per cent.

Corporate offices recycle office and print paper and have introduced a suite of paperless initiatives.

We are part of a shift in the community towards the environment

Increasingly over the last few years, BSP has encouraged employees and their families and communities to avoid using plastic bags and has set a target to help reduce plastic bag usage.

To achieve this BSP has:

- provided a range of re-useable shopping bags to employees, their families and communities throughout the country;
- provided education awareness programmes on "Ways to Go Green";
- appointed a BSP Eco Ambassador to provide employees and the broader community with training and support on sustainability issues, helping to champion improvements in their workplace, homes and communities. It is BSP's intention to have at least one Eco Ambassador at every BSP branch throughout the South Pacific.

Fiji schoolroom - Go Green Annual School Clean Up events occurred throughout the country in October

Governor Powes Parkop Port Moresby NCD participated with many of the schools throughout Port Moresby on BSP Schools Clean Up Day

Adults and children participated in the Annual Clean Up Day's events

The Solomon Islands Annual Clean Up Day: wholly organised, run and funded by BSP

Doing what's right

Your trust is a precious asset to our business. Our goal is to preserve and build on it every day. That's why we work to do what is right in the community and integrate social and environmental priorities into our branches and relationships.

Corporate Responsibility

We give back to our communities.

We take seriously the responsibilities that come with being a leader. We help our customers build better communities, and leverage our size, scope and resources to help make the world a better place. We are committed to sustainable business practices and are determined to conduct our operations in a manner that does not compromise the ability of future generations to meet their needs.

BSP is growing and our challenge, and commitment, is to ensure this growth is responsible and sustainable.

QUICK FACTS

- 100s of tonnes of waste paper have been recycled by BSP in 2010.
- 30 percent saving in energy achieved by new low energy lighting installed in branches.
- 1000s of "Ways to Go Green" Fact Sheets have been distributed to customers, staff and the community.

BSP School Kriket won the International Cricket Council Award for Best Cricket Development Programme globally in 2010

Winner BSP School Kricket Programme

Sport For Life

The focus of BSP's community initiatives and participation is very much on children and youth programmes in education, health and sport. Our young people are the future of our nation and deserve support and encouragement.

We encourage children to 'never stop playing' by contributing to sporting organisations that develop kids' sports skills and provide opportunities for them to play. In 2009/2010, BSP invested more than K1 million into children's sporting related partnerships. As part of these sponsorships we support 650,000 children per year to lead active lifestyles.

BSP's association with youth and sport has also been successfully extended through the BSP School Kriket Programme in PNG's schools. Delivered by Cricket PNG, the programme had reached more than 50,000 children by the end of 2010, and was recognised by the International Cricket Council, as the Best Cricket Development Programme globally in 2010. For many provinces in PNG, this was the first time the game of cricket was played. This unique programme also invited girls to participate, with an overwhelming response of 50% females taking part.

BSP is very pleased to support Papua New Guinea Swimming Inc (PNGSI) that provides the infrastructure for thousands of children to learn to swim and participate in swimming competitions.

Investing in swimming enables PNG to develop the sport on both a national and international level. In addition to ensuring that the sport of swimming develops at a grassroots level, BSP is also pleased to support PNGSI's Aquatic Excellence Silver and Gold Target squad athletes.

In 2010, BSP continued its association with the Papua New Guinea Paralympic Committee. In addition to financial sponsorship and equipment BSP provided people to assist the country's paralympians, for the team in New Delhi, India.

The three-year sponsorship agreement to help PNG Paralympics ensures funding to help elite disabled athletes train and compete.


BSP CEO, Ian Clyne and players from PNG Tennis Association celebrate the K150,000 donation from BSP

Fiji: Heartening support in Fiji


BSP School Kriket won the International Cricket Council Award for Best Cricket Development Programme globally in 2010


BSP CEO, Ian Clyne showing a hands-on approach with BSP's interest in developing tennis


National Championship in Port Moresby

BSP presentation of K750,000 for the BSP School Kriket Programme to Bill Leane CEO Cricket PNG by CEO BSP Ian Clyne and Johnson Kalo, BSP VP


The BSP Tennis Programme teaches new skills and encourages health and fitness


PNG Paralympians doing us proud in India.

The Digicel Fiji Sevens co-sponsorship by BSP in Fiji has broadcast the BSP brand internationally

Changing Lives

Health In Focus

In 2010 BSP again joined forces with many health organisations with a focus on health and well being including the Business Coalition Against HIV/ AIDS (BAHA) to promote awareness of HIV/AIDS and assist with funds for support programmes. The HIV/AIDS epidemic is increasing in all sectors of life despite many efforts made to reduce the trend.

Miss BSP with a child at the Kimbe General Hospital

Handover by sponsors of the Cheshire disAbility Services PNG buses


Cheshire Homes disAbility Services PNG


BSP staff member donating blood


Rosemary Mawe, BSP delivers gifts to POM General Hospital over the New Year

Local Sponsorships

Hundreds of sporting clubs and associations across PNG and the South Pacific benefit from the support of their local BSP branch, sponsorship or staff volunteering. BSP managers and staff often team together across their province or in smaller regional or suburban groups to support their local sporting groups or education centre.

Events and organisations supported include:

Cheshire disAbility Services PNG
The Salvation Army
City Mission PNG
Cricket PNG
AFL PNG
PNG Squash
Papua New Guinea Paralympic Committee
PNG Tennis Association
PNGBSA
National Capital District Commission NCDC
Papua New Guinea Red Cross
Transparency International Papua New Guinea Inc
National Canoe & Kundu Festival Committee
The Institute of Internal Auditors PNG Chapter
Business Council of Papua New Guinea, Voice of the Private Sector
MEMBER
Clean Up the World MEMBER 2010

Growing Responsibly

The Group and The South Pacific

Following the acquisition of the Colonial Group in Fiji from the CBA in 2009, BSP is now truly a Pacific bank.

In Fiji, the newly acquired subsidiary immediately set about expanding its ATM fleet to 100 and introduced SMS banking, by the end of 2010. Similarly the ATM network was expanded to 11 in the Solomon Islands.

BSP Fiji has the largest branch network, and recently its ATM network became the largest ATM network in Fiji. BSP is now the largest retail bank in Fiji.

The BSP brand is extremely well recognised in PNG, the Solomon Islands, and Fiji. BSP is now clearly the Number "One" bank in PNG, ultimately the Pacific.

Launch of new ATM Vision City

How We Do Business Affects People Everyday

Products, Services and People

At BSP, we're committed to make banking a convenient and easy part of life. We understand that there's increasing need to save time and money. We're committed to improving our product offers, service levels and access to banking services for customers.

BSP was the first bank to launch SMS banking in PNG in 2009 and now almost 80,000 users in PNG bank anytime, anywhere - simply by using their mobile phone. This easy way to bank means there is no need to travel to a branch to bank. In Fiji, over 50,000 customers are finding this the better way to bank.

BSP's ATM network is the largest in the country - and continues to grow, with hundreds of ATMs throughout PNG. With selected sites featuring 24 hour/7 day a week banking, this offers another convenient way to access your money and suit your lifestyle.

The expanding network of EFTPOS now consists of over 3,300 locations - so banking is easier and more convenient than ever before.

BSP continues to find new innovative ways to make banking easier and more accessible for everyone. 1000s of BSP wireless Eftpos units feature throughout the South Pacific

A typical SMS banking promotion in Fiji which has contributed to the successful launch of the popular banking choice, with 50,000 + users

In Suva, Fiji BSP participated in the Showcase Event, a week to expose to the business community and general public new ways to bank, including SMS banking

In 2010, mobile phone top-ups for Digicel and Be-Mobile were made available through ATMs, and Digicel top-ups on SMS.

In 2010 Mastercard could be accepted by BSP machines.

In 2010 BSP launched BSP Rural - providing a service for those in remote locations previously disadvantaged by no available banking services. This unique service continues to expand , complete with electronic banking infrastructure and systems

These types of developments underline BSP's commitment to being the leader in electronic banking services in PNG and the Pacific.

At BSP we proudly encourage, train, mentor and develop talented people across the South Pacific. A career with the only home grown bank in the South Pacific region provides opportunities supported by improved training, resulting in greater job satisfaction; career opportunities and rewards for employees; and the translation of these for BSP shareholders into stronger profitability, and increasing shareholder value.

Official opening of BSP Rural, Daulo, Eastern Highlands Province. From BSP, Paul Thornton (Left) and CEO, Ian Clyne joined Mr Lars Thunell, the Executive Vice President and CEO IFC.

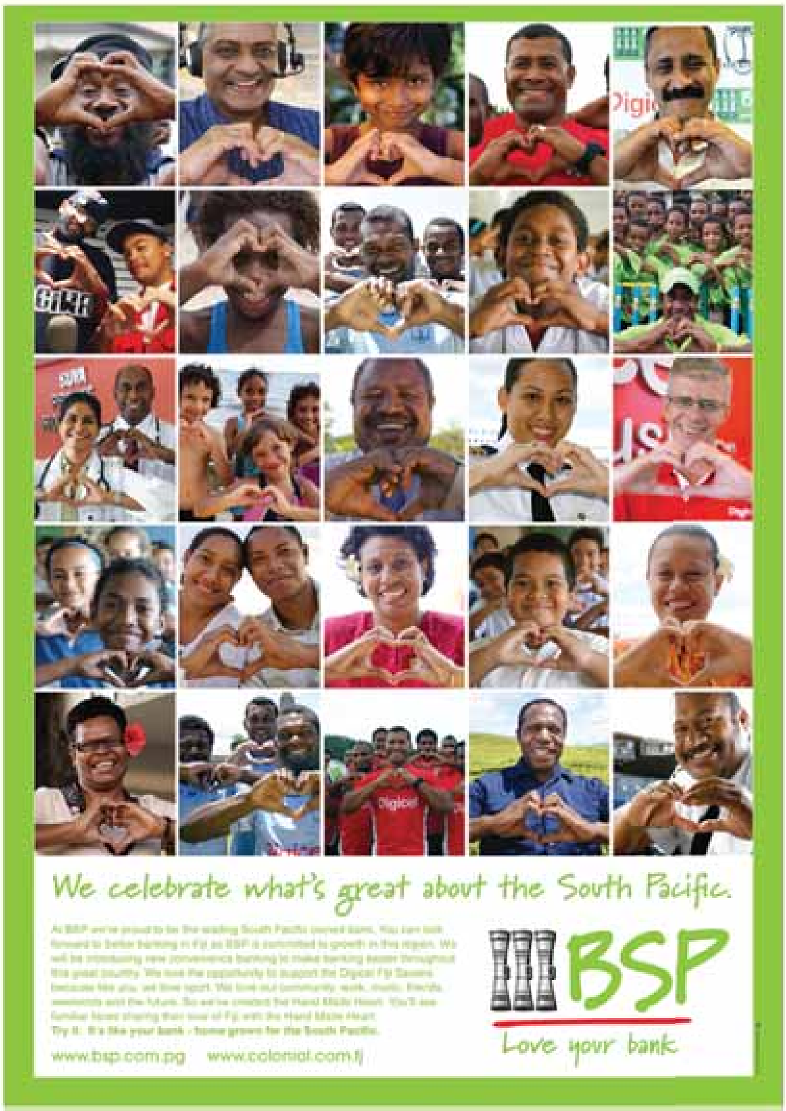
Digicel Fiji 7 co-sponsorship brought international exposure to the BSP brand. It was a strategic part of the launch of the BSP brand throughout Fiji.

BSP banner, displayed building length Central Street, Suva, Fiji throughout launch period 2010

launch activities Fiji 2010

Colonial Arcade BSP rebranding launch, Suva, Fiji

Launch Day Suva Central, Fiji



BSP Fiji Community Programme leader, Howard Politini and the BSP team deliver much needed sports equipment and gifts to Desbandhu Primary School, Fiji

Transformation

The Years Ahead

BSP is truly a “forward looking” institution, progressing along its chosen path of change and modernisation to transform into a 21st century bank, introducing initiatives for new and improved products, customer service processes and technology platforms.

In 2010, the Motukea Service Branch opened and in 2011 we have commenced operations at the new Pogera Branch, with Vision City, Harbour City, Arawa and Komo (containerised branches) coming into service this year. Our ATM network will continue to expand in PNG, Fiji and the Solomon Islands in 2011. Similarly, electronic banking and SMS banking will continue to be further expanded in Fiji and Solomon Islands.

BSP’s future is bright: characterised by our identifiable lively green colour, and determination to deliver better product offers, service levels and access to banking services for all.

Marketing

Communicating to our customers

In the past few years there has been increased stakeholder and community interest in our bank. BSP has invited this interest by creating a brand image that is deliberately bright, modern and innovative reflecting the bank's positive vision for the future.

There are three key areas in which BSP has positioned itself: *brand *community *convenience. The bank has deliberately highlighted its difference as a uniquely South Pacific grown and focused banking organisation. It has reinforced its commitment to social responsibility through its communications in relation to its community initiatives and it continues to expose its strategic direction and development as a 21st century banking organisation with infinite potential. Like all other aspects of the bank's business, BSP is energetic in delivery of its communications which include TV, radio, newspapers, magazines, outdoor billboards and posters, email, internet sites, social media. Increasingly BSP is developing educational materials to raise the level of financial literacy. It's another way BSP is working to ensure the community benefits most from the bank who is committed to service people at all levels throughout the South Pacific.


One Bank, Many Possibilities...
Corporate & International
Operational & Novated Leases
Foreign Exchange
Treasury
Term Deposits
Business Loans & Cheque Products
Merchant Solutions
Over 200 ATMs & Over 3300 EFTPOS Terminals
More ATMs in More Locations than any other Bank in PNG
Payroll & Internet Solutions
New breakthrough evolution Internet Banking Solution
Kundupei
Payroll Management
Everyday Banking Solutions
SMS, Internet & Mobile Services
ATM & EFTPOS
Visa Debit Cards
Kundu Card, Rural Banking
Western Union
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Banking is our business, we take it very seriously.
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KunduCard
Kundu Account
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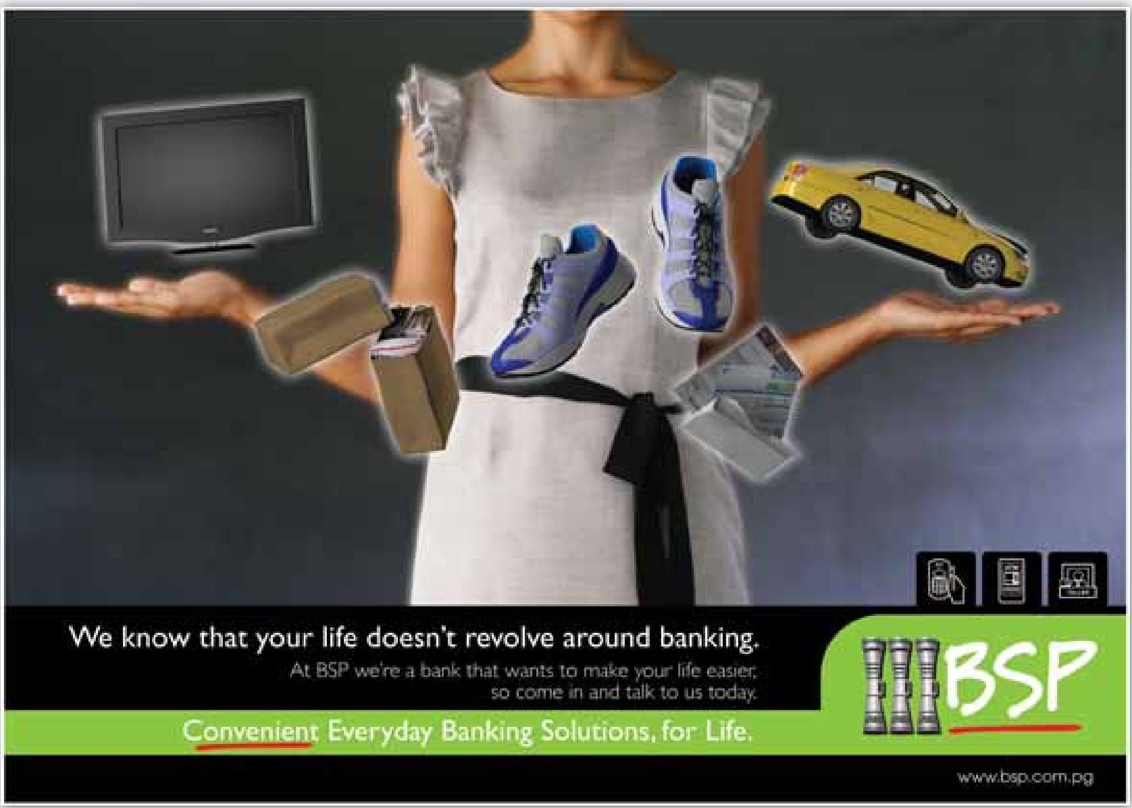
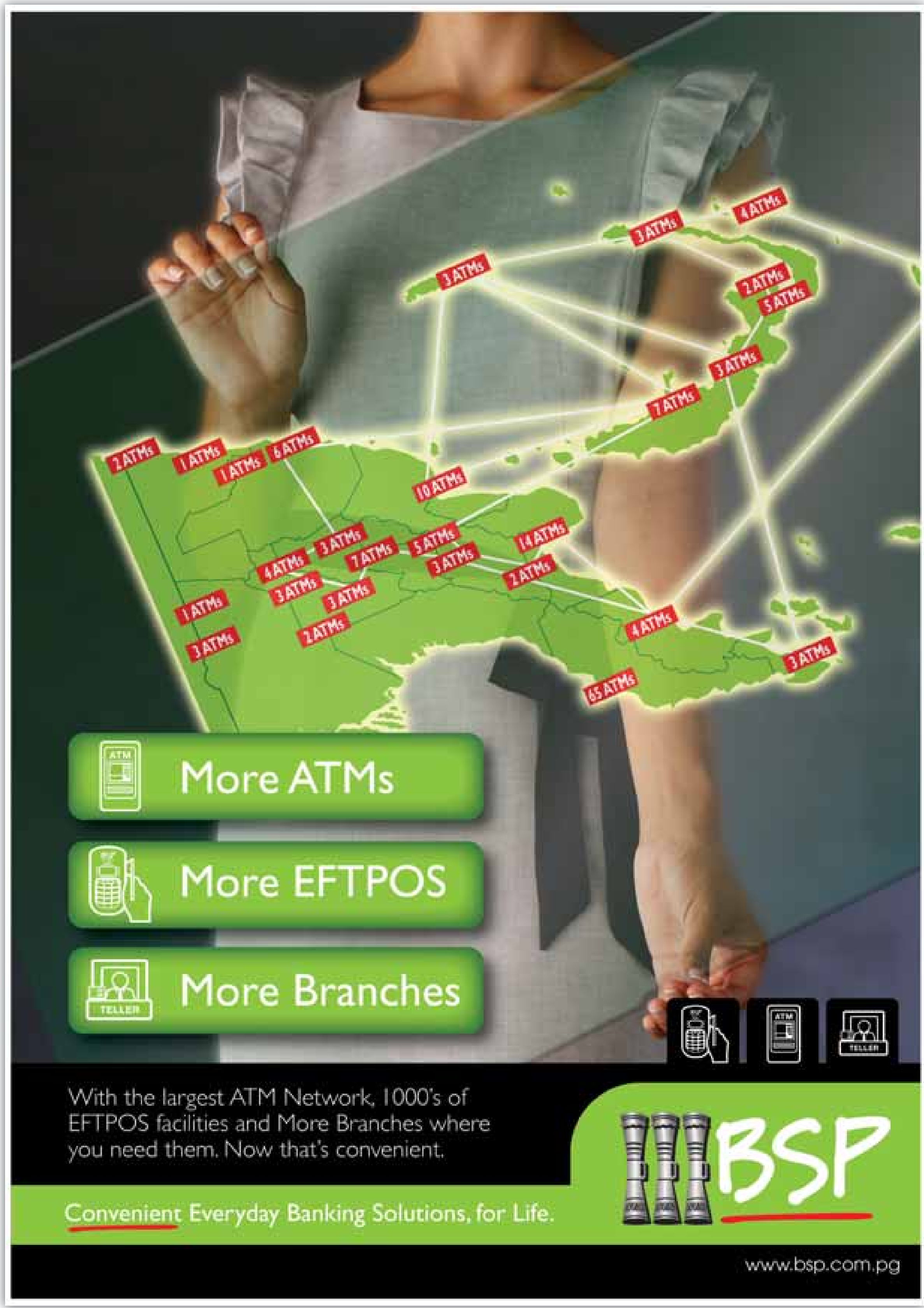
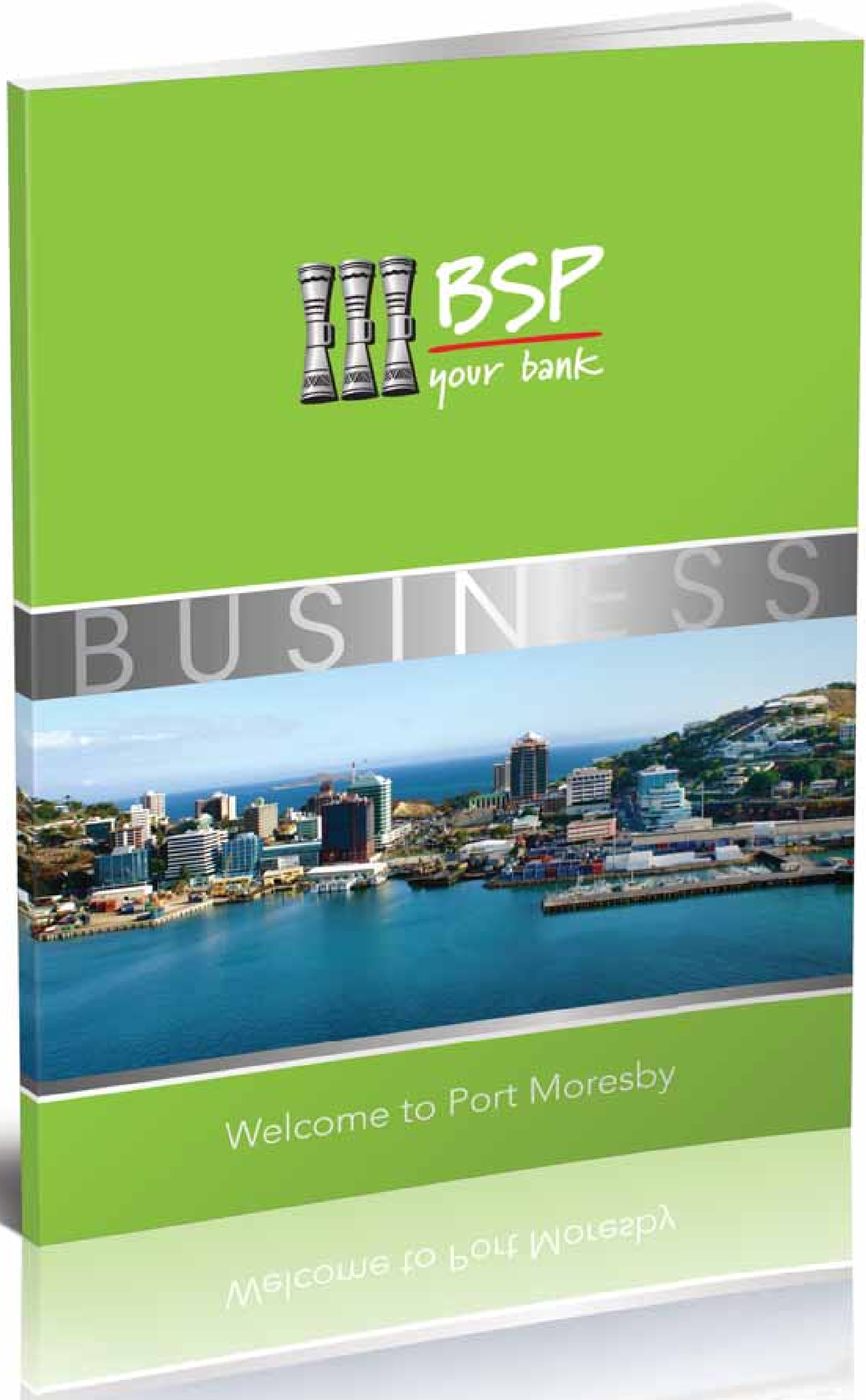
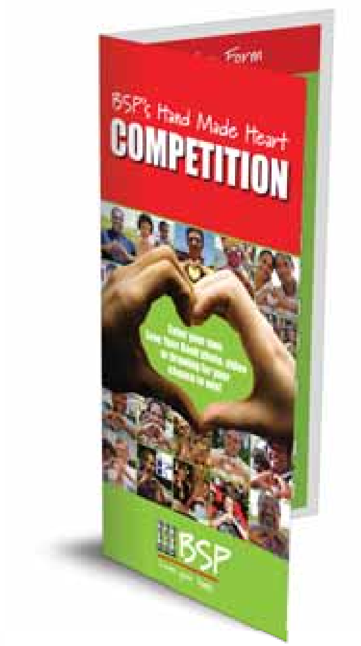
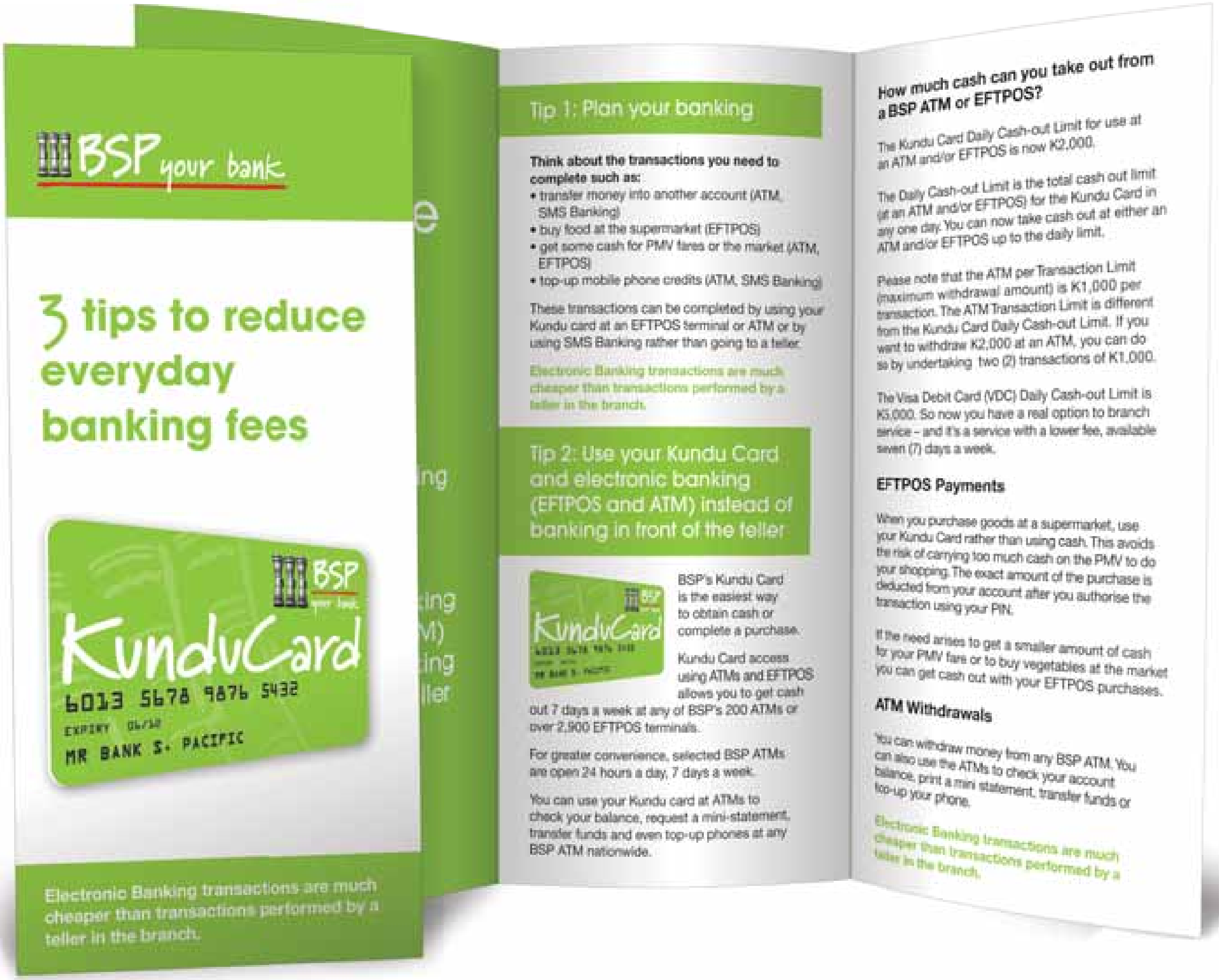

We know that your life doesn't revolve around banking.
At BSP we're a bank that wants to make your life easier,
so come in and talk to us today.
Convenient Everyday Banking Solutions, for Life.
BSP
www.bsp.com.pg


More ATMs
More EFTPOS
More Branches
With the largest ATM Network, 1000's of EFTPOS facilities and More Branches where you need them. Now that's convenient.
Convenient Everyday Banking Solutions, for Life.
BSP
www.bsp.com.pg


BSP
your bank
BUSINESS
Welcome to Port Moresby


BSP's Hand Made Heart
COMPETITION
BSP


Help keep Papua New Guinea clean
BSP


BSP your bank
3 tips to reduce everyday banking fees
BSP your bank
KunduCard
6013 5678 9876 5432
EXPIRY 06/12
MR BANK S. PACIFIC
Electronic Banking transactions are much cheaper than transactions performed by a teller in the branch.
Tip 1: Plan your banking
Think about the transactions you need to complete such as:
• transfer money into another account (ATM, SMS Banking)
• buy food at the supermarket (EFTPOS)
• get some cash for PMV fares or the market (ATM, EFTPOS)
• top-up mobile phone credits (ATM, SMS Banking)
These transactions can be completed by using your Kundu card at an EFTPOS terminal or ATM or by using SMS Banking rather than going to a teller.
Electronic Banking transactions are much cheaper than transactions performed by a teller in the branch.
Tip 2: Use your Kundu Card and electronic banking (EFTPOS and ATM) instead of banking in front of the teller
BSP's Kundu Card is the easiest way to obtain cash or complete a purchase.
Kundu Card access using ATMs and EFTPOS allows you to get cash out 7 days a week at any of BSP's 200 ATMs or over 2,900 EFTPOS terminals.
For greater convenience, selected BSP ATMs are open 24 hours a day, 7 days a week.
You can use your Kundu card at ATMs to check your balance, request a mini-statement, transfer funds and even top-up phones at any BSP ATM nationwide.
How much cash can you take out from a BSP ATM or EFTPOS?
The Kundu Card Daily Cash-out Limit for use at an ATM and/or EFTPOS is now K2,000.
The Daily Cash-out Limit is the total cash out limit (at an ATM and/or EFTPOS) for the Kundu Card in any one day. You can now take cash out at either an ATM and/or EFTPOS up to the daily limit.
Please note that the ATM per Transaction Limit (maximum withdrawal amount) is K1,000 per transaction. The ATM Transaction Limit is different from the Kundu Card Daily Cash-out Limit. If you want to withdraw K2,000 at an ATM, you can do so by undertaking two (2) transactions of K1,000.
The Visa Debit Card (VDC) Daily Cash-out Limit is K5,000. So now you have a real option to branch service – and it's a service with a lower fee, available seven (7) days a week.
EFTPOS Payments
When you purchase goods at a supermarket, use your Kundu Card rather than using cash. This avoids the risk of carrying too much cash on the PMV to do your shopping. The exact amount of the purchase is deducted from your account after you authorise the transaction using your PIN.
If the need arises to get a smaller amount of cash for your PMV fare or to buy vegetables at the market you can get cash out with your EFTPOS purchases.
ATM Withdrawals
You can withdraw money from any BSP ATM. You can also use the ATMs to check your account balance, print a mini statement, transfer funds or top-up your phone.
Electronic Banking transactions are much cheaper than transactions performed by a teller in the branch.

Sports gear for your school!
SCHOOL SPORTS PROGRAMME
Nominate your school today.
Supporting active lifestyles
BSP
Play sport, for life!

Sports gear for your school!
BSP
SCHOOL SPORTS PROGRAMME
Nominate your school today.
(Nominations close 31st March 2011)
Supporting active lifestyles
BSP is committed to improve the health and wellbeing of children. We encourage children to 'never stop playing' by Contributing to sporting organisations that develop kids' sports skills and provide opportunities for them to play. So we're providing a Sports Kit to schools throughout PNG for children so they can participate in football, soccer, netball, volleyball, basketball, cricket and tennis.
For details and to nominate your School visit BSP.com.pg/SchoolSportsProgramme
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Community programmes throughout Fiji reflect BSP's commitment to youth, education, sports, fitness and health. Children across the country love showing the BSP heart in thanks and appreciation.

notes

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Bank of South Pacific Limited