







## Good Corporate Governance

*As an effort to achieve its vision and missions and business strategy, BRI has and will consistently apply corporate governance based on Good Corporate Governance (GCG) principles, consisting of transparency, accountability, responsibility, independency, and fairness.*

### Good Corporate Governance Principles :

#### **Transparency :**

Transparent in decision making process and in disclosing relevant and material information on the company.

#### **Accountability :**

Clear functions, implementations and responsibilities in managing the bank effectively.

#### **Responsibility :**

Compliance to the regulations and sound banking principles.

#### **Independency:**

The bank is professionally managed without any conflicts of interest and undue influences or pressure from stakeholders contrary to the regulations and sound banking principles.

#### **Fairness:**

Fairness and equality in fulfilling stakeholders' rights stated in any agreement and regulations.

### Corporate Governance Implementation

#### **Code of Conducts**

In implementing GCG principles, BRI has developed some policies including code of conducts as a standard ethics for all employees.

The Code of Conducts is manifested in Corporate Culture, namely Integrity, Professionalism, Customer Satisfaction, Set a Good Example, and Human Resources Appreciations. Code of Conducts is dynamic and it will be reviewed based on business environment and developments

#### **Corporate Planning**

In supporting the implementation of GCG, BRI has developed corporate planning and control system. Corporate Planning is divided into short term (one year) planning presented as Annual Budget and Planning; medium term (three years) planning presented as Business Plan; and long term (five years) planning presented as Corporate Plan. Management is responsible for the execution of the planning and reports it to Annual General Meeting of Shareholders (AGM). The responsibility included evaluation of organization

structure, system and procedure, human resources, and company performance including internal audit function in each level of organization structure.

### Corporate Governance Guidance

As a guidance for the implementation of GCG, BRI has outlined Board Manual which clearly defines the duties and responsibilities of Board of Directors and Board of Commissioners. In addition to Board Manual, good corporate governance is also based on policies, rules/regulations and referring to GCG principles.

### Board of Commissioners' (BOC) Duties and Responsibilities

In accordance with the company's Articles of Association and relevant laws and regulations, the main duty of BOC is to be responsible for the oversight of corporate management performed by the Board of Directors. Commissioners may give advices to the Board in relation to the company strategy formulation and the corporate action plan and budget. Commissioners are also responsible for supervising the Board's performance and compliance with the company's Articles of Association and all laws and regulations.

Furthermore, Commissioners are obliged to undertake additional tasks as requested by the shareholders, upon General Meeting of Shareholders approval, such as the establishment of an Audit Committee for improving feasibility and quality control of the company's financial report. The accomplishment of all duties and responsibilities of Commissioners stated in the

Article of Association to be hold accountable before the AGM.

### The Composition of the BOC 31 December 2006

Name	Position
Bunator Sanim	President Commissioner/ Independent Commissioner
Mulia P Nasution*	Commissioner
Agus Pakpahan**	Commissioner
Sunarsip	Commissioner
B.S. Kusmuljono	Independent Commissioner
Baridjussalam Hadi**	Independent Commissioner
Aviliani	Independent Commissioner

### Commissioners Internal Meetings

Name	Attendance	Percentage
Bunator Sanim	29	85%
Mulia P Nasution*	5	15%
Agus Pakpahan**	6	18%
Sunarsip	27	75%
B.S. Kusmuljono	25	74%
Baridjussalam Hadi**	20	59%
Aviliani	26	76%

### Commissioners Meeting with Directors

Name	Attendance	Percentage
Bunator Sanim	10	83%
Mulia P Nasution*	2	17%
Agus Pakpahan**	4	33%
Sunarsip	11	92%
B.S. Kusmuljono	7	58%
Baridjussalam Hadi**	8	67%
Aviliani	9	75%

\*) Appointed at AGM on 30 May, 2006 and proposed resignation as of November 1, 2006

\*\*) Appointed at AGM on 30 May 2006

## Audit Committee

During the period of 2006, the Audit Committee had undertaken its functions, duties, and responsibilities in accordance with the Audit Committee Charter. In its meeting with working units, the Audit Committee through Commissioners asked several management subordinates to attend committee meeting and provide the necessary information.

The Audit Committee had increased the meeting frequency and extended the scope of the meeting with the management, particularly related to the work of Accounting and Financial Management, Technology and Information System, Internal Audit, Legal, Strategic Planning, and Human Resource Management, Compliance, Consumer Banking, and Risk Management.

## Members of Audit Committee

Name	Position
Aviliani	: Chairperson
Bunasor Sanim	: Member
Abdussalam Konstituanto	: Member
H.C. Royke Singgih	: Member
Dedi Budiman Hakim	: Member

## Attendance of Audit Committee

Name	Attendance	Percentage
Aviliani	Chairperson	100%
Bunasor Sanim	Member	100%
Abdussalam Konstituanto	Member	100%
H.C. Royke Singgih	Member	100%
Dedi Budiman Hakim	Member	100%

## Audit Committee's Meetings

No	Activities/Working Unit	Date	Agenda
1	Public Accountant PSS (E&Y)	12 January 2006 3 March 2006	Audit Planing for Year 2006 Report on Audit Result (exit meeting)
2	Credit Administration	24 January 2006 10 March 2006	Four Eyes Principle in loans decision Loans portfolio monitoring
3	Bank Indonesia	10 February 2006	Risk Based Audit (RBA) and human fraud
4	Strategic Planning	14 February 2006	Standard operating procedures on offline transaction
5	Compliance	13 April 2006	Know Your Customer Principles (KYC)
6	Internal Audit	9 May 2006 24 September 2006 14 November 2006 4 December 2006	Annual Audit Planning, Risk Based Audit, Strategic Business Partner and Auditors Competencies Evaluation on audit activities and audit findings for Quarter I and II 2006 Quality of findings, and audit report for Quarter III 2006 Developing IT audit method
7	Technology and Information System	16 May 2006 5 September 2006	IT Governance. Disaster Recovery Plan
8	Logistic	16 June 2006	Procurement
9	Human Resources Management	6 July 2006 10 September 2006 3 October 2006	Grading system and career path GCG self assessment Consumer Banking personnel
10	Consumer Banking	22 August 2006	Business Developing Strategies
11	Accounting & Financial Management	16 October 2006	Financial Report and Monthly financial report (LBU) to BI

## Audit Committee Report

To support the effectiveness in carrying out their duties and responsibilities, the Commissioners had formed an Audit Committee which comprises a chairperson and four members. The Chairperson and members of the Committee are independent parties and possess adequate expertise, background of knowledge, and experiences.

In 2006, The Audit Committee has performed some internal and external activities.

### 1. Internal Activities

- To prepare Audit Committee's work plans which are the realization of Audit Committee Charter
- To hold meetings with Internal Audit to discuss internal control system, audit findings especially which are considered high risk and may influence the bank business.
- To hold meetings with Accounting and Financial Management Division and other related Divisions to discuss the development of BRI's financial performance and other financial information.
- To hold meetings with other Divisions, such as the Human Resource Management Division, Legal Division, Technology and Information System Division, and Strategic Planning Division, Logistic Division, and Credit Administration Division to discuss issues related to the function of the work units related and the

performance of BRI.

- To hold regular (weekly) meetings with other committees in the Commissioners to discuss important issues related to the effectiveness of the Commissioners' functions, duties and responsibilities.
- To evaluate and to make written report to Commissioners on minute of meetings and assignments given to the Audit Committee.
- To attend internal workshops regarding GCG, performance evaluation & Internal Audit Communication Forum, and visit regional offices or branches in order to get direct information regarding the problem encountered by certain work units.
- To provide training material convened by Regional Audit Offices

### 2. External Activities

- To attend seminars related to Audit Committee's function such as The Institute of Internal Auditor (IAA) Indonesia Chapter, IKAI, and sharing vision for improving competencies and capabilities of Audit Committee.
- To have discussion with external Auditor, prior and after investigation regarding any findings on the bank's financial statement.
- To attend forum on commissioners for state owned banks.

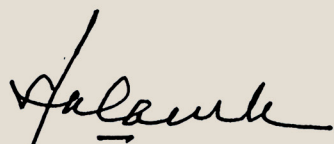
PT Bank Rakyat Indonesia (Persero) Tbk.  
Audit Committee



Aviliani  
Independent Commissioner/Chairperson



Burasor Sanim  
Independent Commissioner/Member



Abdussalam Konstituanto  
Member



H.C. Royke Singgih  
Member



Dedi Budiman Hakim  
Member

## Risk Monitoring Committee

Risk Monitoring Committee is a relatively new committee in the organization. This committee is formed based on Risk Monitoring Committee Charter. It has been formally in duty since February 2006, after having two additional non-commissioner members recruited externally (independent) who have received formal assignment on Commissioners Meeting on 28 December 2006.

### Tasks and Responsibilities of Risk Monitoring Committee

Risk Monitoring Committee maintains an effective relationship with Commissioners, Directors and its management, regulators and relevant parties. This committee must evaluate, regularly review, and give recommendation to Commissioners on bank's risk management policies. It also oversees main risks of the bank and ensures that the Board of Directors has the necessary actions to identify, measure, monitor, and control the risks.

The Committee evaluates and analyzes on Board of Directors' proposal regarding transactions and business activities beyond the BOD's authority, third parties financing and credit requiring Commissioners' consultation. It also evaluates, monitors and recommends Commissioners on Annual Budget and Planning, Business Plan and Corporate Plan.

### Members of Risk Monitoring Committee

Initial formation of the Risk Monitoring Committee consisted of :

Chairperson : Sunarsip (Commissioners)  
Members : B.S. Kusmuljono (Commissioners)  
Ridwan D. Ayub (Non Commissioners)  
Enjang Mukhtar (Non Commissioners)

To comply with the regulation stipulated by Bank Indonesia no. 8/4/PBI/2006 regarding Good Corporate Governance Implementation by Commercial Banks and based on Commissioners Meeting on 6 June 2006, the chairperson, Sunarsip (Commissioner), was replaced by Baridjussalam Hadi (Independent Commissioner).

### Composition of Risk Monitoring Committee as of 31 December 2006 :

Name	Position
Baridjussalam Hadi	: Chairperson
Sunarsip	: Member
Ridwan D. Ayub	: Member
Enjang Mukhtar	: Member

The Risk Monitoring Committee Charter stipulates that the Committee must have meeting at least once a month. However, to improve the quality of monitoring on risk management, there is an agreement that Committee meeting become a part of Commissioners meeting, with the number of meetings in 2006 was 35 meetings.

### Nomination and Remuneration Committee

The tasks of this committee is to recommend and assist Commissioners in outlining nomination and remuneration policies in accordance with the Article of Association and other related regulations. The proposal of remuneration and nomination of Commissioners and Directors must be approved by Annual General Meeting of Shareholders.

The Committee has five members chaired by an Independent Commissioner. Internal meeting should be held at least once in a month, while meeting with Human Resource Management Division and other related working units at least every three months. The meeting has its quorum if attended by more than 50% of its members.

Members of Nomination and Remuneration Committee as of 31 Desember 2006

Name	Position
B.S. Kusmuljono	Chairperson
Aviliani	Member
Agus Pakpahan	Member
Tuanmas Sinintaro	Member
Dwi Lilis Ernawati	Secretary

### Board of Directors' (BOD) Duties and Responsibilities

The duties and responsibilities of BOD are to manage the company in accordance with the Articles of Association. In practice, BOD is obliged to represent the company inside and outside the court. BRI has eight Directors, including the President Director, who undertake their

management duties in particular fields specified in the General Meeting of Shareholders.

### The Composition of the BOD

Based on the decision of General Meeting of Shareholders on 30 May 2006, the structure of the Board of Directors has undergone changes as follows:

#### The Period of 1 January - 30 May 2006

Name	Position
Sofyan Basir	President Director
Wayan Alit Antara	Deputy President Director
Ahmad Askandar	Director
Akhmad Amien Mastur	Director
Hendrawan Tranggana	Director
Ventje Raharjo	Director
Gayatri Rawit Angreni	Director

### Nomination and Remuneration Committee Meetings

No.	Date	Meeting Agenda
1	1 February 2006	<ul style="list-style-type: none"> <li>New organization structure of Human Resources Management Division</li> <li>Functional Work Plan of Human Resources Management Division</li> </ul>
2	14 February 2006	<ul style="list-style-type: none"> <li>Board of Director's organization structure and authority</li> </ul>
3	10 March 2006	<ul style="list-style-type: none"> <li>Management of Financial Institution Pension Funds</li> </ul>
4	2 May 2006	<ul style="list-style-type: none"> <li>Action plans for Internal Audit Findings</li> <li>Consultation on Executives Employees' tour of duty</li> <li>Evaluation on grading system implementation</li> <li>Incentive policy and Haj Pilgrim for BRI employees</li> </ul>
5	22 May 2006	<ul style="list-style-type: none"> <li>Proposal regarding <i>tantiem</i> for Directors, Commissioners and Secretary of Commissioners</li> <li>Distribution plan for remaining unexercised MSOP 1 and 2</li> </ul>
6	6 July 2006	<ul style="list-style-type: none"> <li>Premium allowance in salary system</li> <li>Evaluation on grading system implementation</li> <li>Definition of Executive Employees</li> </ul>
7	26 September 2006	<ul style="list-style-type: none"> <li>Evaluation on employees' tour of duty</li> <li>Evaluation and strategy to up grade employees' productivity</li> <li>Achievement of Human Resources Management Division 2006 target (budget and work plan) and work plan for 2007.</li> </ul>

#### The Period of 30 May - 31 December 2006

Nama	Position
Sofyan Basir	President Director
Sarwono Sudarto	Director of Operations
Abdul Salam	Director of Finance
Sudaryanto Sudargo	Director of Corporate
Sulaiman A. Arianto	Director of MSME
A.Toni Soetirto	Director of Consumer Banking
Lenny Sugihat	Director of Credit Risk Analysis
Bambang Soepeno	Compliance Director

#### Board of Directors Meeting

The Board regularly holds meeting to discuss policies and strategic actions of the company.

#### Board Meeting for the Period of 1 January - 30 May 2006

Name	Attendance	Percentage
Sofyan Basir	9	82%
Wayan Alit Antara	10	91%
Ahmad Askandar	11	100%
Akhmad Amien Mastur	10	91%
Hendrawan Tranggana	8	73%
Ventje Rahardjo	8	73%
Gayatri Rawit Angreni	10	91%

#### Board Meeting for the Period 30 May - 31 December 2006

Name	Attendance	Percentage
Sofyan Basir	17	89%
Sarwono Sudarto	19	100%
Abdul Salam	13	68%
Sudaryanto Sudargo	15	79%
Sulaiman A. Arianto	16	84%
A. Toni Soetirto	12	63%
Lenny Sugihat	18	95%
Bambang Soepeno	18	95%

#### Committee to Assist Board of Directors

In undertaking the duties, Board of Directors is assisted by Executive Committees, consisting of :

##### Risk Management Committee

The Committee was established in 2002. To adjust with the internal need, in 2006, the committee has undertake some actions including:

- To change the definition of Risk Management Working Unit, previously a working unit consisting of Risk Management and Compliance Division, Treasury Division, Credit Administration Division, to Risk Management Division
- To segregate the function of Operational working unit into Core Risk Taking Unit and supporting Risk Taking Unit
- To change the organization of Risk Management Committee
- To add members of Risk Management Committee such as Corporate Secretary, Human Resources Management Division, Logistic Division, Information System and Technology Division, Compliance Desk, Sharia Business Unit.

#### Assets and Liabilities Committee

The Assets and Liabilities Committee (ALCO) is responsible for managing assets and liabilities of BRI, including management of liquidity, interest rates, foreign exchange, investment, and maturity gap. ALCO meeting is at least once a month.



### Credit Policy Committee

The function of Credit Policy Committee is to approve loans as well as loan extension up to the limits approval authority of the Board of Directors in conjunction with Assets and Liabilities Committee.

### Information and Technology Steering Committee

The IT Steering Committee accounts for giving recommendations and determining the policy related to IT risks. This committee formulates the development of information technology and its strategies.

### Remunerations of Board of Directors and Board of Commissioners

The remuneration, *tantiem*, post service allowances for Board of Directors and Board of Commissioners must be approved by General Meeting of Shareholders.

Based on Annual General Meeting of Shareholders on 30 May 2006, remuneration and other benefits for Board of Directors and Board of Commissioners as follows :

- The salaries, honorarium paid to Commissioners' and Directors in 2006 is unchanged compared to the amount decided by Annual General Meeting of Shareholders dated May 17, 2005. The ratio of salaries of President Director, Deputy President Director, Director, President Commissioner, Commissioner and Secretary of Commissioner is 100%, 95%, 90%, 40%, 36% and 15% of President Director salary. Total salaries and allowance for Board of Directors and Board Commissioners is Rp16.92 billion.
- *Tantiem* for Board of Commissioners and Board of Directors was 0.52% of BRI net profit in 2005 or Rp19.80 billion with similar ratio of salary ratio as December 2005.

### Ownership of BRI's Share by Commissioners and Directors as of 31 December 2006

Name	Position	Number of Shares	Percentage to Total Shares
Sofyan Basir	President Director	3,115,500	0.0254
Sarwono Sudarto	Director	160,500	0.0013
Abdul Salam	Director	-	0.0000
Sudaryanto Sudargo	Director	181,000	0.0015
Sulaiman A. Arianto	Director	460,500	0.0037
A. Toni Soetirto	Director	-	0.0000
Lenny Sugihat	Director	630,000	0.0051
Bambang Soepeno	Director	120,000	0.0001

As of 31 December 2006, none of Commissioners owned BRI shares.

## Corporate Secretary

Corporate Secretary has played a wider role as a gate of information for externals. In order to have a transparent and accurate information to and from the public, and to avoid inconsistency in conveying information, Corporate Secretary has implemented one gate policy. Furthermore, in order to maintain the quality of information from and to the company, the Management implemented spokesperson policy.

As a communication gate to capital market, BRI has established Investor Relations under Corporate Secretary right after BRI went public.



Providing services to capital market community can be done through media of communication. Analyst meeting which is held quarterly, is a regular occasion to meet with analysts in Capital Market. BRI also receives company visit and hold conference call requested by local and foreign investors. During 2006, BRI has received company visit more than 160 times.

Another assignment for Investor Relations is to assist Board of Directors in investors meeting during road show/conference. Through road show, BRI management has met with more than 220 institutional investors. To provide up to date

information to capital market community, Investor Relations regularly publishes Financial Up-Date and Investor's Newsletter quarterly. Investor Relations maintains website ([www.ir-bri.com](http://www.ir-bri.com)) that is accessible for shareholders to obtain information.

## Internal Audit

In performing its duties, the Internal Audit uses Risk Based Audit (RBA) method. In this method, business processes and business units estimated to have significant risks affecting significantly company's objectives will be prioritized to be audited compared to the ones with less risks. In implementing RBA, the Internal Audit encourages and evaluates risk management implementation. To maintain the quality of audit result, the Internal Audit continuously undertakes quality improvement program, internally by undertaking Internal Review Program and externally through quality standardization assessment with international standard ISO 9001 2000.

Through Internal Review Program, all delivery channel of internal audit, at the Head Office and Regional Offices level are examined every year using scoring system. For ISO 9001 2000, the consultant will examine some delivery unit with ISO 9001 2000.

To comply with Bank Indonesia regulation, every three years, bank's Internal Audit must be reviewed by external auditor to assess its compliance to Standard of Internal Audit Function by Banks (SPFAIB). The review shows that BRI's Internal Audit has performed its function in accordance to standard and always makes necessary adjustment continuously toward best practice.

## Legal Support and Litigation

In safeguarding its operation, BRI carry out some preventive actions in legal aspect to mitigate risk related to legal risk. Some actions includes constructing Legal Manual consisting of Legal Manual on Procedure in legal case handling and cases compilation, Legal Manual on Delivery System, and Legal Manual on Credit.

In addition to the Legal Manual Construction, BRI also provides consultancy on legal aspect to all Regional Offices, Inspection Offices, and branches throughout Indonesia. The consultancy method is by examining the legal aspects of documents of credit, savings, personnel, logistics/fixed assets, and others.

By adhering the principles of providing optimum legal protection and minimizing financial losses, BRI Legal Division, with its internal staff or external lawyers is always ready to provide legal assistance in every legal cases.

## Procurements

To support BRI business, Logistic Division is responsible for logistic function including, planning, budgeting, procurement, payment and distribution, maintenance, and fixed assets administration.



BRI continuously develops its General Policy on Logistics (KUL) to guarantee procurement process is in accordance with GCG principles, to ensure that control and planning mechanism of procurement is based on the business need, priority scale, budget and efficiency.

As a public company required to deliver accurate and up to date information, BRI puts into consideration an accurate asset recording and reporting. More importantly, the developing of widespread networks requires BRI to updated its Logistic Information System (SIM-LOG) which had been implemented since 2003.





## Management Discussions and Analysis

*All BRI's products and services reflect commitments to Micro, Small and Medium Enterprises (MSMEs). Since its establishment, BRI has focused its business activities on developing Micro, Small, and Medium Enterprises (MSMEs).*

The commitment to MSME is clearly evident not only from the variety of products which are mostly dedicated to serve these segments but also from the composition of loans which is dominated by loans to these segments.

Saving products are including Simpedes (*Simpanan Umum Pedesaan*), a product provided to accommodate middle to lower income level people, for them to be able to have savings in bank. For those of wider range of society, BRI has introduced BritAma savings product.

In the loan side, BRI offers Kupedes (*Kredit Umum Pedesaan*) or General Rural Credit, which is the main product aimed at micro business entrepreneurs. Kupedes is used to finance investment as well as working capital, and for other purposes. Other than Kupedes, BRI offered varieties of commercial loans for small businesses and medium businesses. BRI also offers consumer loans which mainly consist of loans to employees with fixed income and some of

mortgage, loans for vehicle ownership and other consumer loan schemes.

The commitments and focus to MSMEs can also be seen in the loan portfolio composition, as described in the table below.

### Marketing and Customers Rely on the Extensive Network.

Extensive network is one of BRI's competitive advantages among banks in Indonesia. BRI has the largest network of more than 4,900 offices spread across Indonesia, in big cities and small towns as well as in rural areas.

To support the operational activities, up to end of December 2005, BRI had operated 982 ATMs (Automated Teller Machine). Cooperated with other banks through Link network, ATM Bersama, and ATM Prima, BRI card can be used in more than 20,000 ATMs. BRI has also cooperated with

### Composition of Loans by Business Segment

Business Segment	Percentage from Total Loan				
	2002	2003	2004	2005	2006
Micro	30.51%	30.55%	30.77%	30.17%	30.22%
Small Business	48.38%	50.22%	51.08%	50.42%	48.27%
- Small Commercial	24.19%	26.69%	28.01%	28.53%	27.05%
- Small Consumers	24.18%	23.53%	23.06%	21.90%	21.22%
Medium sized	3.69%	4.55%	4.59%	6.25%	8.22%
<b>Total Micro, Small and Medium</b>	<b>82.57%</b>	<b>85.31%</b>	<b>86.44%</b>	<b>86.83%</b>	<b>86.71%</b>
Corporate	17.43%	14.69%	13.56%	13.17%	13.29%

Cirrus and Maestro ATM network, enabled customers to use their ATM cards in all ATMs with Cirrus and Maestro logo, all over the world.

To provide a better service to customers, BRI is continually perfecting the ATM card by introducing BRI Card which can be used not only as an ATM card but also as a debit card so as to be useful in various transactions.

In order to improve company's image and to introduce BRI's products more widely, a lot of promotion activities and public communication had been done. The activities have proven to be effective for increasing the number of customers. BRI has around 40 million accounts, consist of 35 million deposit accounts and 5 million loan accounts.

## **Operational Performance Review**

### **Net Interest Income**

Net Interest Income (NII) by end of December 2006 was Rp13.79 trillion, or up 10.69% compared to end of December 2005 which was recorded at Rp12.46 trillion. The growth in NII was the result of the increase in interest income and investment, altogether with the increase in income from sharia financing, which reached Rp21.07 trillion or up by 22.12% from end of year 2005 of Rp17.25 trillion. The NII was also the result of a surge in interest expenses, reaching Rp7.28 trillion by end of December 2006, or a growth of 51.80% from end of year 2005 position of Rp4.80 trillion. Yearly NII reflected Net Interest Margin (NIM), which by end of December 2006 reached 11.17%, slightly below end of December 2005 position of 12.18%. Interest income was coming from loan expansions and improving loan quality, while the increase of interest expenses was caused both by increasing interest rate as well as a shift toward high cost

deposits in quarter 2 and quarter 3, following the trend in the interest rate at the time. As the result, cost of funds was creeping up, to reach 6.27% by end of December 2006

Contributions from Government Bonds in interest income was declining continually to be at 11.10% of total interest income by end of December 2006, from 12.62% by end of December 2005

### **Other Operating Income**

In 2006, other operating income increased significantly, to reach Rp1.51 trillion, from Rp956.25 billion in 2005, or grew 57.81%. The increase was largely rooted from marked to market value gains and sales of securities, including those of recapitalization and government bonds, amounted to Rp484.20 billion by end of December 2006 from Rp231.63 billion by end of December 2005, or an increased of 109.04%. The other source of income was commissions and other fees income, which reached Rp837.69 billion by end of December 2006, from Rp527.89 billion by end of December 2005, or grew 58.69%.

### **Allowance for Possible Losses on Earning Assets and Other Assets**

By end of December 2006, allowance for possible losses on earning assets and other assets was at Rp1.85 trillion, an increase from Rp400.83 billion recorded by end of December 2005. The surge was, among other things, caused by problem loans emerged after consecutive natural disasters occurred in recent years throughout Indonesia.

### **Other Operating Expenses**

In 2006, other operating expenses was declining by 0.45%, from Rp7.70 trillion by end of December 2005 to Rp7.67 trillion by end of

December 2006. The ratio of operating expense to operating income had also increased, from 70.83% by end of December 2005 to 74.38% by end of December 2006. The increase was largely stemmed from higher allowance for possible losses on earning assets and other assets.

### Profit

The success of maintaining the growth of net interest income in one side, and managing the cost on the other side, has resulted in the increase of net profit by 11.79%, from Rp 3.81 trillion for the year of 2005, to Rp4.26 trillion for the year of 2006.

## Financial Performance Review

### Assets

BRI's total assets by end of December 2006 reached Rp154.73 trillion, up 26.02% compared with end of December 2005 which was recorded at Rp122.78 trillion.

The components of assets were earning assets which constituted 85.48% of total assets, and non earning assets which constituted the remaining 14.52%. In 2005 the composition was 86.54% earning assets and 13.46% non earning assets.

Earning Assets include placement with Bank Indonesia and other banks, securities, Government recapitalization bonds, loans, receivables, and investments in stocks. Non earning assets include cash, current accounts with Bank Indonesia, premises and equipments, and other assets.

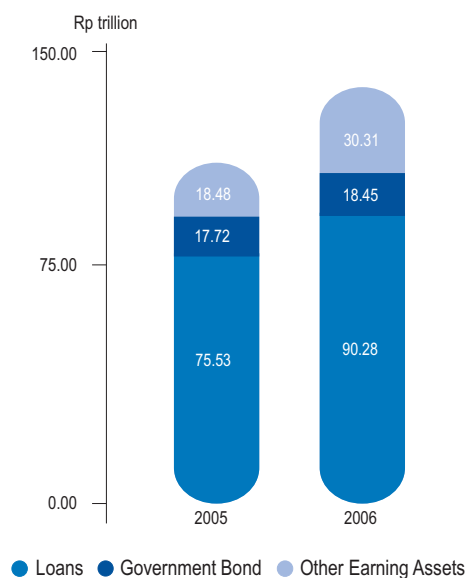
### Earning Assets

Total earning assets before provisions by end of

December 2006 was Rp139.04 trillion, or grew by 24.44% compared to the end of December 2005 which was at Rp111.73 trillion. The growth came mainly from loans which acquired 64.93% of total earning assets, a drop from 67.60% of total earning assets as of end of December 2005. The portion of Government Bonds was also declining, from 15.86% of total earning asset as of December 2005 to 13.27% by end of December 2006. As the consequences, the portion of other non earning assets, including *Sertifikat Bank Indonesia* (SBI = Central Bank Bill) was increasing from only 16.54% as of end of December 2005 to 21.80% as of end of December 2006.

The accumulation of Allowance for Possible Losses was also inched up, by Rp1.31 trillion became Rp6.79 trillion by end of December 2006.

### Growth and Composition of Earning Assets



### Loans

Loans, (including sharia financing) recorded a significant growth, from Rp. 75.53 trillion by end of December 2005 to Rp90.28 trillion by end of



December 2006, or grew by 19.53%. As much as 30.22% of total loans were disbursed as micro loans, 48.27% as small loans, 8.22% as medium sized loans and the remaining 13.29% were loans to corporation.

Small loans consist of Small Commercial Loans and Small Consumer Loans, which portion was 27.05% and 21.22% respectively. Summing up together, loans to micro, small and medium enterprises (MSMEs) grew 19.36%, from Rp65.59 trillion by end of December 2005 to Rp78.28 trillion by end of December 2006. The growth served as an indicator that the economy of small and medium businesses was improving during 2006.

#### Loans' Quality

Loans with category "Current" increased from Rp66.81 trillion by end of December 2005 to Rp80.29 trillion by end of December 2006, while loans with category "Special Mention" rose from Rp5.19 trillion to Rp5.65 trillion, while Non Performing Loans (NPLs) were also increasing from Rp3.53 trillion to Rp4.34 trillion in the same period. As such, the ratio of NPLs increased slightly, from 4.68% as of end of December 2005 to reach 4.81% as of end of December 2006.

The increasing NPLs was solely caused by rising NPLs in the Small Commercial Loans from 3.00% to 4.38%, while NPLs in other loan segments were decreasing : medium sized loans' NPLs declined from 7.48% to 5.87%, Corporate Loans from 16.93% to 13.55% and Micro Loans from 1.55% to 1.36%. However, net NPLs were improving from 1.92% by end of December 2005 to 1.29% by end of December 2006. To maintain comfortable cushion for the problem loans, related to series of disasters hit Indonesia and also to cover loss in some riot torn areas in recent years, coverage ratio was increased, from 153.09% by

end of December 2005 to 154.69% by end of December 2006.

#### Government Bonds

Declining interest rate occurred in the second semester of 2006 yielded an unrealized gain from Government Bonds holdings. The gains were sourced from increased market value of the Bonds, both from trading portfolio and from Bonds which were in Available For Sale (AFS) portfolio, each recorded gain of Rp609.91 billion and Rp190.34 billion respectively.

Government Bonds hold by BRI by end of December 2006 reached Rp18.44 trillion, increased 4.08% compare to end of December 2005 position of Rp17.72 trillion. As previously, Bonds with fixed rate dominated BRI's Government Bonds portfolio, amounted to Rp11.91 trillion or acquired 64.55% of total Government Bonds' holdings. The remaining of total Government Bonds' holdings or Rp6.54 trillion were in the floating rate. In the total assets, Government Bonds sit on 11.92% of total assets, a decline from end of December 2005 position of 14.43%



#### Third Party Funds

Third Party Funds (TPFs) were funds mobilized from the people in the form of demand deposits, saving deposits and time deposits. Included in the TPFs are sharia saving products such as

demand deposit *Wadiah*, saving deposit *Mudharabah* and time deposit *Mudharabah*. As of end of December 2006, TPFs successfully accumulated were Rp124.47 trillion, grew 28.26% compare with 2005's position of Rp97.05 trillion. TPFs were the major liabilities for BRI, as it constituted 90.29% of total liabilities.

Demand deposits were one of low cost funds which showed the highest growth in 2006. By end of December 2006 demand deposits amounted to Rp27.86 trillion, or grew 60.29% from previous year position of Rp17.38 trillion. As the result, the portion of demand deposits in total deposits jumped, from only 17.91% by end of December 2005 to reach 22.39% by end of December 2006. Savings, the other source of low cost funds, were recorded an increase, from Rp49.37 trillion as of end of December 2005 to Rp58.31 trillion as of end of December 2006, or grew by 18.10%. These increasing trends of both these two type of deposits lead to a bigger portion of low cost funds in total deposits, from 68.79% in 2005 to 69.23% in 2006. Subsequently, the portion of high cost funds of time deposits were declining, from 31.21% in 2005 to reach 30.77% in 2006 despite the increase of time deposits from Rp30.29 trillion as of December 2005 to Rp38.30 trillion in December 2006.

#### Subordinated Loans

Subordinated loans were intended to strengthen BRI's capital structure (especially tier II capital). Total subordinated loans by end of December 2006 reached Rp2.23 trillion, a decline from previous year position of Rp2.39 trillion.

BRI had issued two subordinated loans, which were *Subordinasi I* bond amounted to Rp500 billion and US Dollar denominated Subordinated Notes amounted to USD 150 million.

The *Subordinasi I* bond was issued on 9 January

2004, with a coupon of 13.50% for the first six years and 23.50% until the maturity date on 9 January 2014 with a call back option in the sixth year, on 9 January 2010.

The USD 150 million Subordinated Notes was issued on 25 September 2003, with a coupon of 7.75% during the first five years and 7.24% for the remaining years until its maturity date on 30 October 2013. The Notes hold callable option which can be exercised on 30 October 2008.

#### Equity

In end of December 2006 BRI's equity was at Rp16.88 trillion, increased by 26.40% compared to 2005's position which stood at Rp13.35 trillion. The increase in equity was mainly due to net profits accumulated during the period, amounted to Rp4.26 trillion, and from allocation of 2005's net profits as stipulated in BRI's Annual General Meeting of Shareholders in 2005.

#### Capital Adequacy

BRI's Capital Adequacy Ratio (CAR) by end of December 2006 reached 18.82%, jumped from 2005's position of 15.29%. The improving CAR was the benefits of BRI by being a bank with a strong focus to MSMEs. Bank Indonesia (BI) regulation (No 8/3/DPNP/2006 dated 30 January 2006) which changes the calculation of risk weighted assets, assigns an easing risk weight on loans to small businesses, mortgage and loans to civil servants and pensioners, loans which sit the biggest portion in BRI's loans portfolio. The changes of the risk weight are as follow :

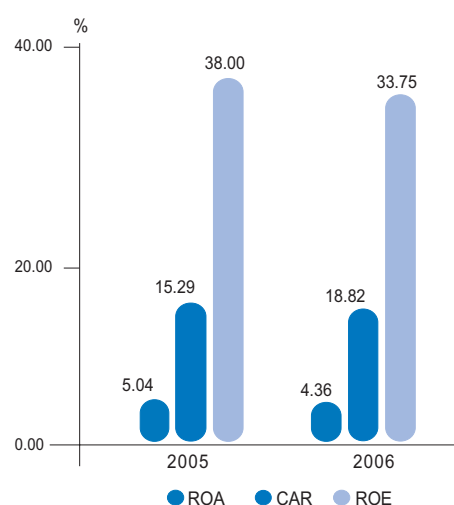
Type of Loan	Risk Weight	
	Previously	Now
Small Businesss Loan	100%	85%
Mortgage	50%	40%
Consumer Loan to Employees/Retirees	100%	50%

(Rp billion)		
Type of Equity	2005	2006
Tier I Equity	10,519	13,104
Tier II Equity	2,309	1,881
Placement	(66)	(70)
Total Equity Available	12,762	14,915
Total Risk Weighted Assets (RWA)	83,494	79,261
Capital Adequacy Ratio (CAR)	<b>15.29%</b>	<b>18.82%</b>

Return on Assets (ROA) before tax in 2006 reached 4.36%, a slight decrease from 2005's of 5.04%. Return on Equity (ROE) was also declining to 33.75%, from 38.00% in 2005. BRI's capital expenditures in 2006 was Rp280.17 billion, consist of Rp82.61 billion for IT expenditure and Rp197.55 billion for non IT expenditure. This was a significant decline compare to 2005

expenditure which recorded at Rp706.97 billion, consist of Rp368.11 billion IT expenditures and Rp338.87 billion non IT expenditures.

### Financial Ratios



### Bank Rakyat Indonesia :

#### The Largest and The Best Bank in Serving Micro, Small and Medium Enterprises (MSMEs) in Indonesia

As stipulated in the Corporate Plan 2003-2007, in 2006, BRI aimed to be the best and largest bank in serving micro, small and medium business in Indonesia. This target was the answer from the Bank to all the stakeholders, especially the shareholders for their trust on BRI, showed in BRI's IPO in 2003 which was recorded as one of the most successful IPO in Indonesia at the time.

An indicator that can serve as a sign of the achievement of the 2006 Corporate Plan target was the inclusion of BRI stock (BBRI) among blue chip stocks in the JSX. The steady and solid performance of BBRI was a reflection of investors' trust in BRI's fundamentals which derived from a consistent focus to micro, small and medium enterprises. BRI's microbanking even had been acknowledged as one of the best microbanking system in the world. The United Nations had chosen BRI's micro banking as an example of a healthy and commercially profitable microbanking practices.

Another indicator which showed that BRI is the best and largest bank in serving micro, small and medium businesses in Indonesia is the large number and well geographic spread of customers. As of end of December 2006, total accounts held by the Bank were more than 40 million accounts. This large number of customers was also a reflection of the Bank's success in undertaking financial intermediary activities, as it was also showed in the Loan to Deposit Ratio (LDR) which by end of December 2006 reached 72.53%, higher than banking industry's LDR of 61.54%. The acknowledgements were also coming from various prominent institutions, domestically and internationally, in the form of various awards received, in many assessments criteria.





## A Robust Risk Management

*BRI's activities always deal with risks related to its function as a financial intermediary. Therefore, business activities must be managed properly which enables BRI to avoid loss exceeding its capabilities.*

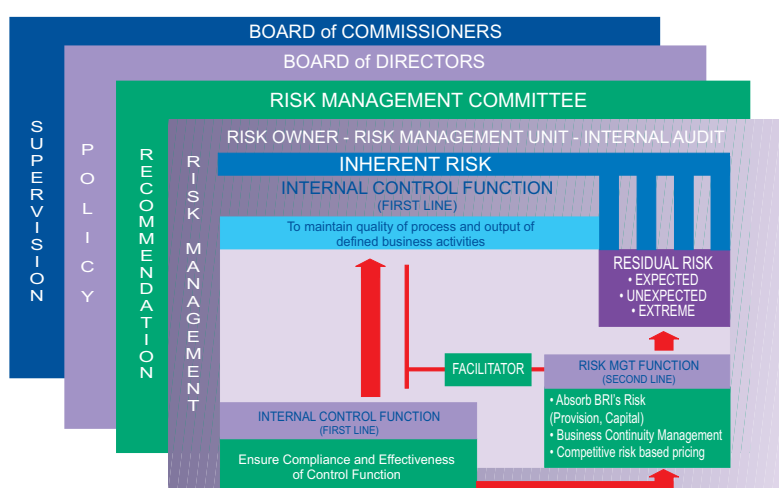
*Risk management plays an important role in achieving company objectives through two aspects which are protecting capital and optimizing risks and returns.*

### Risk Management Organization

BRI had established and implemented a holistic and integrated risk management to minimize potential losses. Risk management is undertaken by applying three lines of defense, including :

1. Risk Taking Units, serving as the first line of defense, is a unit responsible for internal control function that maintains the quality of output and business process in accordance with the policies and procedures. Risk Taking Unit directly controls inherent risk to minimize residual risk.
2. Risk Management Units, serving the second line of defense, is responsible for managing the risk to ensure that total risk exposure will not exceed the Bank's capital. Managing risks is undertaken through setting and monitoring risk limit.
3. Internal Audit, as the third line of defense, is responsible for ensuring the effectiveness of internal control at both risk taking unit and risk management unit as well.

The relationships of the three lines of defense can be described as follow :





## Risk Management General Policy and Strategy

Risk Management General Policy is the highest level of rules in the implementation of risk management in all BRI business activities, both for conventional banking and sharia banking. The policy governs risk management organization, risk management process (identification, measurement, monitoring and controlling), risk management integration, information, internal control system, risk management of new products and activities and contingency plans.

Board of Commissioners have the responsibility to actively oversee risk management in the Bank, including to approve and to evaluate General Policy of Risk Management, oversees Board of Directors responsibility on the implementation of risk management policy in accordance with the regulations.

Board of Directors have the responsibility of establishing a comprehensive written policy and strategy of risk management, setting risk limit, and implementing the policy of risk management and risk exposure of BRI.

Risk Management function is undertaken by Risk Management Division with three departments namely: Credit Risk Management Department, Market Risk and Integrated Risk Management Department, and Operational and Other Risk Management Department.

Board of Directors, assisted by Risk Management Committee (RMC) - the highest hierarchy in Risk Management System-, manage business risk exposure and establish Risk Management System in BRI. Board of Directors and RMC hold quarterly meeting.

To ensure that all business risks have been controlled properly and had been taken into account BRI's interests and objectives, Board of Directors set Risk Management Strategy including :

- Risk limit and parameter setting
- Planning and actions plan needed based on BRI risk profile in a certain period.

## Risk Profile

BRI evaluates its aggregate risk through self assessment process to produce a Risk Profile consisting of Inherent Risk (inherent risk in bank activities prior control implementation) and *Risk Control System* (control on inherent risks). Based

### RISK PROFILE FORMULATION



on the business complexity and size of Bank, risk evaluation is undertaken on eight types of risks namely credit risk, market risk, liquidity risk, legal risk, compliance risk and strategic risk on seven functions namely credit, treasury, trade finance, funding, operations and services, IT system, and support functions.

The self assessment show that the business risk as of December 2006 was *Low* with low *Inherent Aggregate Risk* and strong *Risk Control System*.

Risk Profile of Quarter IV 2006 as follow :

DESCRIPTION	RISK TYPE								Aggregate
	Credit	Market	Liquidity	Operations	Legal	Reputation	Compliance	Strategic	
<b>INHERENT RISK AGGREGATE</b>	2.23	1.00	1.33	1.18	1.14	1.07	1.43	1.82	1.40
<b>RISK CONTROL AGGREGATE</b>	1.38	1.30	1.13	1.88	1.38	1.38	1.25	1.50	1.40
<b>RISK COMPOSITE</b>	1.80	1.15	1.23	1.53	1.26	1.22	1.34	1.66	
<b>OVERALL RISK SCORE</b>									1.40

**NOTE :**

Scoring scale : 1 – 5

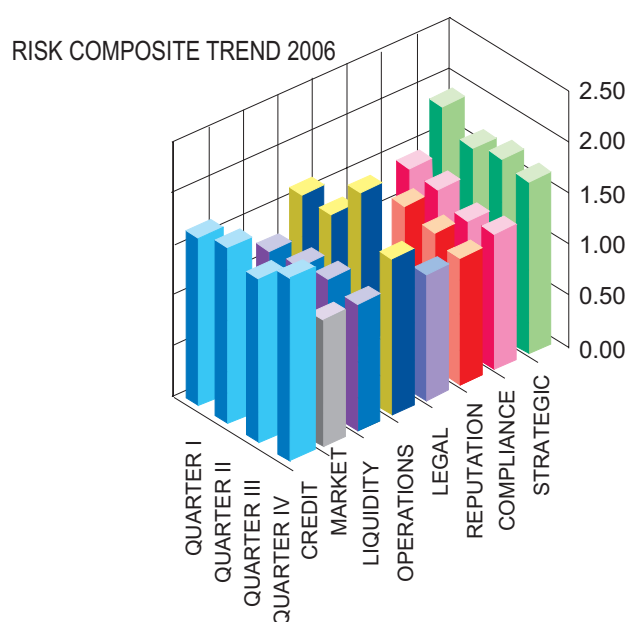
- Inherent Risk : Low (<2) Moderate (2 - 3.5) High (> 3.5)

- Risk Control : Strong (<2) Acceptable (2 - 3.5) Weak (> 3.5)

- Risk Composite : Low (<2) Moderate (2 - 3.5) High (> 3.5)

- Overall Risk : Low (<2) Moderate (2 - 3.5) High (> 3.5)

BRI's risk profile trend during 2006 for each risk type is stable as shown in the diagram below:



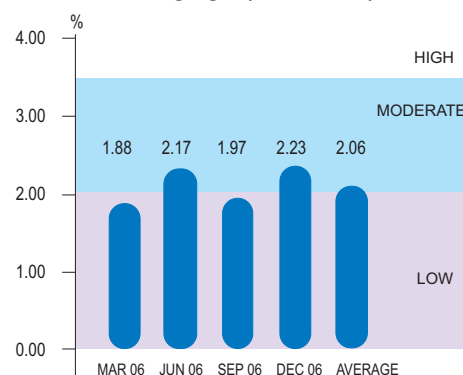


## Credit Risk

Credit Risk is the biggest component of risk portfolio, contributed 94.47 % of total credit and market risk (as of December 2006). Credit risk in product/receivables exposure are in form of lending or non-lending (placement, investment, and payable/other assets such as internal or external receivables)

In 2006, the average inherent risks based on risk profile self assessment, was moderate with Strong risk control system. Inherent risk in credit risk is monitored through some activities parameters in credit, trade finance, and treasury. Those are shown in the diagram as follows :

### Inherent Risk Agregat (Credit Risk)



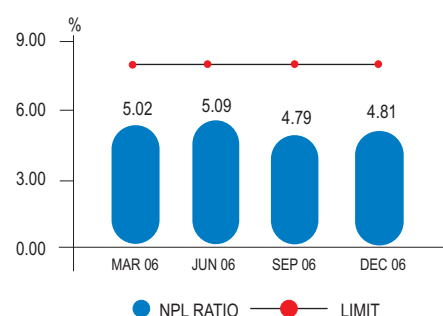
Credit risk from lending activities is monitored through some parameters such as Non Performing Loans (NPLs), credit concentration on 25 largest borrowers, 25 borrowers of highest NPLs, and provision ratio. Credit risk from trade finance activities is monitored through parameters such as NPLs on Export, NPLs on Import LC; while treasury activities are monitored through Net Performance Asset and outstanding concentration of three largest borrowers/issuers.

During 2006, credit risk profile from lending

activities has been maintained at below credit risk limit. Some parameters for monitoring credit risk are described below :

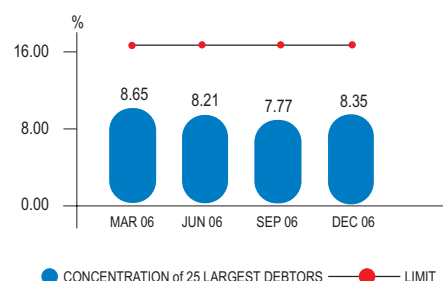
#### 1. NPLs ratio to total loans

Average NPLs in 2006 is 4.93%, far below the limit set at 8%.



#### 2. Credit concentration of 25 largest borrowers

Average outstanding of 25 largest borrowers to total outstanding is 8.24%, below the limit set at 15 %.



In anticipating Basel II implementation, BRI is developing credit risk's measurement complying to Basel II framework. BRI has formed Project Office Credit Risk Basel II whose assignments including preparing the implementation of credit risk management using Standardized Approach and Internal Rating Based Approach.

## Market Risk

Market Risk is risk from adverse movements in market variables in portfolio held by BRI that could incur losses. Market variables consist of interest rate and exchange rates.

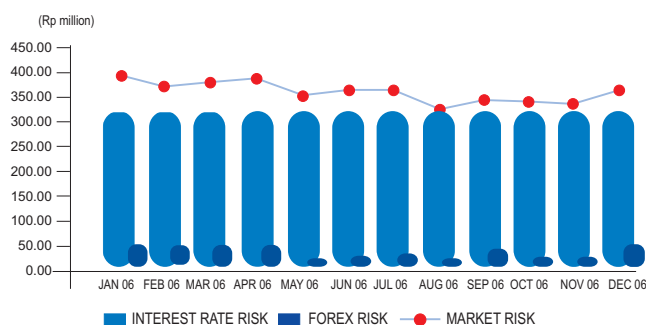
The scopes of market risk management include treasury activities, investment in marketable securities and money market, investment in other financial institutions, funding activities (in form of lending), financing activities, securities issuance, and trading. This also includes activities based on sharia principles.

Using Standardized Approach, the measurement of market risk (consists of interest rate risk and exchange rate risk) shows that monthly average of capital allocated to cover market risk is Rp366 billion or approximately 2.5% of total equity.

marketable securities in trading book exposed to interest rate risk.

Sensitivity analysis on repricing gap position with 3-5% increase in interest rate gave no significant impact on BRI's Net Interest Income (NII) and capital. Stress testing performed in December 2006 on interest rate repricing gap, showed that BRI profit will be in distress if the interest rate increase to 57% from current market risk which were around 9.5%.

Monthly average of capital allocated to cover exchange rate risk both in trading book and banking book, is 10% of capital allocated to cover market risk. The low percentage of capital allocated to cover exchange rate is due to daily average of Net Open Position (NOP) maintained at 3%-5%, far below the maximum NOP of 20%. BRI has conducted a simulation of Value at Risk



In 2006, capital allocated to cover market risk was stable with declining trend due to prudent policy by diversifying the trading portfolio and most of it was in low risk government bonds. Market risk capital in 2006 is mostly for covering

(VaR) using variance covariance with confidence level at 99% and 1 day holding period. The result of VaR on interest rate risk of trading book position (Trading and Available for Sale) and VaR exchange rate risk in trading book and banking book) as follows :

(Rp billion)				
Description	Mar'06	Jun'06	Sep'06	Dec'06
VaR Interest Rate Risk	82.48	80.07	87.44	93.91
VaR Exchange Rate Risk	7.74	5.76	3.26	8.01



Overall market risk profile at BRI is quite low because BRI always maintains NOP and maturity/repricing gap at a moderate level, hence, there will be little impact on NII and BRI capital.

### **Operational Risk**

The rapid development in banking industry escalates the complexity of risks in banking activities. Consequently, there is a need of good corporate governance and adequate risk management process based on the size and complexity of BRI activities.

Operational risk is a risk resulting from inadequate or failed internal process, people and system or from external events, which will affect BRI operations.

Risk identification process is undertaken on each function and operations activities of BRI,

consisting of seven functions namely credit, funds, treasury, trade finance, operations and services, IT system, and support. Identification result on these functions is an important information for BRI in evaluating and establishing risk profile of BRI.

During 2006, operation risk profile coming from inherent risk and risk control system demonstrates that aggregate risk inherent in operational risk was at the level between low and moderate. Meanwhile, aggregate risk control system lied between strong and acceptable.

In order to lower risk composite of control system, BRI currently is improving framework, governance, and operational risk management infrastructure including the implementation of Incident Management to record all incidents in daily operation of BRI in order to reduce the dependency from Internal Audit data.

### **Risk Management on new products/activities**

Risk management on new products and/or activities is a phase that has been done in developing new products and activities. This phase is to minimize unexpected risk in providing new product and activities.

Risk Management working unit is responsible for reviewing the risk management in new products and activities proposal, ensuring the readiness of BRI in providing this new products and activities and recommending its risk management to Compliance Director.

In 2006, BRI has performed risk evaluation on credit card, Financial Institution Pension Funds (DPLK) and SMS Banking.

### **Business Continuity Management (BCM)**

BCM is an integrated part in the organization to cope with the intensifying competition, automated business process, increasing business

complexity, the capabilities of bank in providing continues service, and the ability of bank in adapting regulation changes especially internal business interruption risk management.

Some of new initiatives such as preparing work plan of Business Continuity Management will be completed in 2007.

### **Risk Management Certification**

The success of risk management also lies on the capabilities of individuals assigned in risk taking unit, risk management, and supporting unit. In order to improve the quality of the human resources and to comply with the Bank Indonesia Regulation, in 2006, there were 501 BRI executives already possess Level One Risk Management Certificate and 119 of them possess Level Two Risk Management Certificate.

In the future, BRI will increase number of employees to join the Risk Management Certification Program and increase the level of risk management certification.