

Report of the Board of Directors

Net income attributable to the Group up 22.6% to EUR 1,114 million.
Sevenfold increase in net income and fivefold growth in earnings per share since privatization in 1993.
Return on equity: 11.8% versus 10.4% in 1997.
Dividend per share: EUR 1.50 (EUR 2.25 including the tax credit).
Total dividend: EUR 327.7 million.
Payout rate: 29% versus 25% in 1997.

Nineteen ninety-eight was an excellent year for Banque Nationale de Paris. After rising 55% in 1997, net income attributable to the Group expanded by a further 23% to EUR 1,114 million, representing seven times the net income for 1993, the privatization year. Over the same period, earnings per share have expanded fivefold, to reach EUR 5.16 in 1998. These results reflect a deep-rooted improvement in the performance of all the Group's businesses. Income was boosted by more favorable economic conditions in France and the high level of activity on the equity markets, which helped to offset the impact of financial market turbulence and the substantial allowances set aside in response to worsening conditions in certain emerging markets.

Net banking income rose 9.6% to EUR 7,366 million, including organic growth of 7.8%. Fee income continued to expand, advancing 12.3% on 1997 to 34.1% of net banking income versus 33.5% the previous year, while value added to capital was 8.3% higher. Operating expenses increased 7.5%, reflecting the growth in retail banking business outside the euro countries and the development of the global customers and markets business, while the domestic banking division's operating expenses eased back 0.2%. Gross operating income reached EUR 2,347 million, up 14.6% on 1997 or 14.4% like-for-like. The operating efficiency ratio stood at 68.1% versus 69.5% the previous year. Additions to allowances amounted to EUR 1,203 million, an increase of 16%. The total includes EUR 290 million in new allowances concerning the "sensitive" countries of Asia, EUR 219 million related to Russia and a EUR 133 million⁽¹⁾ increase in general allowances for country risks. Disposals and write-downs of long-term investments, nonrecurring items, other income and expenses and the Group's share of earnings of companies carried under the equity method added EUR 454 million to earnings, raising net income before tax to EUR 1,598 million, an increase of 27.6% compared with 1997.

(1) Excluding the effect of divestments and securizations.

After deducting corporate income tax of EUR 431 million, up 41%, consolidated net income before minority interests came to EUR 1,167 million and net income attributable to the Group stood at EUR 1,114 million, in both cases 23% higher than the previous year.

Domestic Banking

The Domestic network posted strong revenue and earnings growth in 1998. With average outstanding loans of EUR 62.3 billion, the network's market share held firm compared with 1997 at 10.6%. Total sources of funds expanded 10.7% to EUR 105.3 billion.

One of the key developments of the year was the return to growth in outstanding loans, especially home loans, which rose 4.5% to EUR 17.4 billion. BNP's strategic focus on expanding the portfolio of consumer loans led to a strong rise in market share to 8.4%. Consumer loans outstanding at the end of 1998 totaled EUR 4.1 billion, up 9.8% on the year-earlier figure. In the area of savings products, the drive to promote sales of life insurance products and mutual funds yielded increases of 18% and 18.5% respectively in the value of customer funds invested in these products. In 1998, BNP was France's leading distributor of mutual funds, with sales in excess of EUR 4.4 billion. BNP's constant commitment to controlling risks, coupled with improved economic conditions, helped to limit additions to allowances to EUR 241 million.

Revenues generated by the Domestic network expanded 2.2% to EUR 3,435 million. Fee revenue accounted for 42.4% of the total, reflecting the successful launch of a number of innovative products. Efficiency gains drove a further 0.3% decline in operating expenses, contributing to a 14.8% rise in gross operating income to EUR 652 million. The French subsidiaries' gross operating income climbed 3.7% to EUR 203 million. Total gross operating income of

the Domestic Banking division came to EUR 855 million, up 12% on 1997.

BNP's policy of managing human resources actively and responsibly led to the recruitment of 1,000 school-leavers and graduates in 1998. In the years to come, this policy will support BNP's drive to expand its operations in France and other euroland countries, building on its ability to develop innovative products and its technological leadership in new distribution channels.

Retail Banking outside euro countries

BNP subsidiary Bank of the West has been merged with First Hawaiian Bank to create BANCWEST, a banking group serving the West of the United States with 213 branches and 800,000 customers. With 45% of the capital, BNP is BANCWEST's reference stockholder. BNPI, which is now over 97%-owned by BNP, is the other cornerstone of the Group's Retail Banking operations outside euro countries, with operations in the Mediterranean, the Indian Ocean and the French Overseas Areas.

The Retail Banking operation outside euro countries is building a position as a strategic business and key growth driver within the Group. In 1998, its net banking income grew 22% to EUR 733 million and gross operating income rose at the same rate to EUR 281 million.

The business will be developed in the years to come. Following the acquisition of BBL's interest in Société Financière pour l'Outre-Mer, BNP will hold 74% of the capital of this company, which holds stakes in eleven African banks including the BICIs.

Global Customers and Markets

Global Customers and Markets division net banking income rose 18.7% to EUR 2,554 million and gross operating income climbed 15.1% to EUR 897 million. These results reflected the strong performance of the division's high value-added businesses which are the key focus of its development effort:

- BNP confirmed its leadership of the French export financing market and its ranking among the world's ten largest providers of financing for international trade. In 1998, BNP was selected as arranger for 120 structured financing operations. Gross operating income from specialized finance activities rose 9.1%.

- The equities origination and brokerage business was strengthened by the acquisition of Pasfin (Italy), Ekachart (Thailand), Alliance (Singapore) and the teams of Peregrine (greater China and India) and Prudential Bache (Australia). Results from equity derivatives trading once again rose sharply in 1998 and the fixed income and currency trading businesses resisted well against market turbulence. Total gross operating income from financial activities surged 45.0% despite last year's crisis in the financial markets.

- The international private banking and asset management business continued to grow. The acquisition of exclusive control over UEB will expand and enhance BNP's presence in Switzerland, while asset management units have been created in Argentina, Brazil and Japan. In 1998, the business increased its gross operating income by 14.9%.

BNP's commitments in the countries hit by the financial crisis were further scaled down in 1998. Excluding trade-related finance which, by definition, carries lower risks, commitments came to EUR 558 million in Russia, EUR 471 million in Brazil and EUR 2,830⁽¹⁾ million in the "sensitive" countries of Asia, where BNP's total commitments have been cut significantly since the crisis broke out. In 1998, substantial additions were made to allowances for credit losses in these countries, including EUR 290 million for the "sensitive" countries of Asia, EUR 219 million for Russia and EUR 133 million for country risks in other countries. Total allowances for country risks came to EUR 2,315 million at year-end 1998, above the year-earlier figure. These allowances are significantly in excess of the amount required based on the Group's internal risk rating system.

Efficient Information Systems

Modern and efficient information systems play a vital role in keeping costs down, supporting innovation and helping the Group to adapt to changes in the competitive environment. BNP's successful switch to the euro demonstrated the Group's ability to use its technical infrastructure to serve its business objectives. The ISO 9002 certification obtained in February 1999 testifies to the quality of the information systems that support its operations.

The Bank's IT teams are currently preparing for the Year 2000. As of 31 December 1998, the status of the Year 2000 project was considered satisfactory.

(1) including loans to private clients - EUR 198 million.

The BNP Group since 1993: far-reaching modernization to create value for stockholders, employees and customers

Since its privatization, BNP has undergone a massive transformation.

Average return on equity, after income appropriation, has risen from 2.2% to 11.8%, placing BNP at the forefront of French banks in terms of profitability. Stockholders who purchased BNP shares at the time of its privatization have doubled the value of their investment in the last five years.

In the five years since privatization, BNP's policy of managing human resources actively and responsibly has led to the recruitment of 3,600 new employees in France, while staff turnover has created 8,800 vacancies. Over 3,500 employees have received training to allow them to take up new customer-facing positions. BNP's human resources policy has enabled the Bank to cope effectively with the elimination of certain positions due to increasing computerization and organizational changes by reducing the total workforce in France from 39,600 persons to 34,400 without any forced layoffs.

Constant profitability gains have allowed BNP to apply motivating compensation policies. Between 1993 and 1998, total payments under incentive and profit-sharing plans increased sevenfold. The number of staff participating in employee share issues has steadily increased, from 28% of the workforce in 1996 to 38% in 1997 and 57% in 1998.

BNP has also extensively reorganized its operations to enhance customer service.

Domestic Banking sales teams have been expanded by 16% and are increasingly specialized in specific customer segments. A research and innovation department with over 200 staff has been created to offer new products and services. The branch network is adapting constantly to changing customer needs. A quality program has been launched and results are assessed regularly by means of performance indicators and satisfaction surveys.

BNP has also set up dedicated teams to serve global customers throughout the world. Teams responsible for relations with major international customers have been organized by industry and a similar organization has been set up for institutional customers and banks. The international private banking teams have been strengthened and structured to provide a global service. Lastly, lines of business have been set up to offer these

customers international expertise in the various high value-added products and services offered by the Bank.

Outlook

With a capital adequacy ratio of 10.4%, including a Tier 1 ratio of 6.4%, stockholders' equity of EUR 11 billion at year-end 1998, a reserve for general banking risks of EUR 1 billion and an allowance for sectoral risks –not allocated to any specific risks– of EUR 218 million, BNP's balance sheet is particularly healthy. The Group intends to meet the earnings growth objectives set in the BNP 2002 business plan through controlled development of the business. Priority will be given to achieving rapid organic growth, but BNP will remain open to external growth opportunities that are compatible with its core values.

At the Annual Stockholders' Meeting, the Board of Directors plans to recommend a 40% increase in the dividend to EUR 1.50 per share, representing a total payout of EUR 2.25 including the *avoir fiscal* tax credit of EUR 0.75. If approved, the total dividend will amount to EUR 327,733,200, up 44% on the previous year. The dividend will be paid as from 21 May 1999, in cash only.

Twenty resolutions will be tabled at the combined Annual and Extraordinary Stockholders' Meeting of 4 May 1999.

The first twelve resolutions will be put to the vote at the Annual Stockholders' Meeting:

- The first resolution concerns approval of the balance sheet at 31 December 1998 and the statement of income for the year then ended. Before the resolution is put to the vote, the reports of the Board of Directors and the Auditors will be read out to the meeting.
- The second resolution concerns the appropriation of 1998 net income, including the payment of a dividend. BNP SA's net income for the year amounted to FRF 7,070,704 thousand (EUR 1,077,835 thousand). Including unappropriated retained earnings of FRF 1,327,025 thousand (EUR 202,304 thousand) brought forward from the prior year, total income to be appropriated comes to FRF 8,397,729 thousand (EUR 1,280,226 thousand). The recommended dividend amounts to EUR 327,733 thousand, representing EUR 1.50 (FRF 9.84) per share. Including the *avoir fiscal* tax credit of EUR 0.75 (FRF 4.92), the total payout per

share will be EUR 2.25 (FRF 14.76). If approved, the dividend will be paid as from 21 May 1999.

An amount of FRF 12,916 thousand will be transferred to the legal reserve and FRF 3,425,338 thousand will be appropriated to the special long-term capital gains reserve and retained earnings, leaving FRF 2,809,685 thousand in unappropriated retained earnings to be carried forward to next year.

- In the third resolution, stockholders will be invited to approve the agreements governed by Sections 101 to 106 of the Companies Act. Before the resolution is put to the vote, the Auditors' special report will be read out to the meeting.
- In the fourth resolution, the Board of Directors is seeking a 5-year authorization to issue bonds, subordinated notes, perpetual or not, or other debt securities with a maximum aggregate face value of EUR 6 billion or the equivalent in foreign currency. The proceeds from the issues would be used to finance the Company's development.
- The fifth resolution concerns an authorization to be given to BNP to purchase up to 10% of its shares on the open market. The maximum purchase price would be set at EUR 120 per share and the minimum sale price would be EUR 50.

The purchases would be carried out to stabilize the BNP share price. Alternatively, shares could be acquired for allocation or sale to employees, or in order to be cancelled at a later date, or for sale or transfer, or in connection with the Company's financial management and investment policies. The authorization would be given for a period of eighteen months.

- The sixth, seventh, eighth, ninth, tenth and eleventh resolutions concern the ratification of the appoint of Bernhard Walter as director, the re-election of Bernhard Walter, Jacques Friedmann, Jacques Henri Wahl and René Thomas and the election as directors of Jean-Marie Messier (to replace Jean Gandois, who is due to retire at the Annual Meeting) and François Grappotte.
- The twelfth resolution concerns the fees to be awarded to members of the Board of Directors.

The other eight resolutions are subject to the quorum and majority voting rules applicable to Extraordinary Stockholders' Meetings.

- In the thirteenth resolution, the Board of Directors is seeking an authorization to issue shares and share equivalents, with pre-emptive subscription rights. The aggregate par value of direct or secondary share issues would be limited to EUR 500 million (FRF 3.28 billion). The aggregate face value of the debt securities would be limited to EUR 7.5 billion (FRF 49.20 billion).

- In the fourteenth resolution, the Board of Directors is seeking an authorization to issue shares and share equivalents without pre-emptive subscription rights. The securities could be issued in payment for securities of one or several other companies quoted on a regulated market that are tendered to an exchange offer made by the Company. In particular, the authorization could be used to issue shares in the case where either or both of the public exchange offers made by BNP for Société Générale and Paribas are taken up by the two banks' stockholders.

The aggregate par value of shares issued under this authorization would not exceed EUR 2.4 billion (FRF 15.74 billion). If BNP's offers for Société Générale and Paribas are not taken up by the two banks' stockholders, the above ceiling will be reduced to EUR 600 million (FRF 3.94 billion) and if either one of the two offers is not taken up by the stockholders of the bank concerned, the ceiling will be reduced to EUR 1,500 million (FRF 9.84 billion).

The aggregate face value of debt securities issued under this authorization would be limited to EUR 7.5 billion (FRF 49.2 billion).

- In the fifteenth resolution, the Board of Directors is seeking an authorization to increase the capital to a maximum of EUR 600 million (FRF 3.94 billion) by capitalizing retained earnings.
- The sixteenth resolution concerns an authorization to be given to the Board of Directors to carry out any of the issues covered by the above three resolutions while the Company is the target of a takeover bid.
- The seventeenth resolution places a blanket ceiling of EUR 10 billion (FRF 65.59 billion) on issues of debt securities and EUR 2.4 billion (FRF 15.74 billion) on share issues carried out under the above authorizations.

The proceeds from the issues could be used to finance the Company's development or external growth operations. Alternatively, the securities could be issued in connection with a public exchange offer, as mentioned above.

- In the eighteenth resolution, the Board of Directors is seeking a 26-month authorization to cancel shares acquired under the fifth resolution. The maximum amount by which the capital could be reduced under this authorization in any given 24-month period would be 10%.
- The nineteenth resolution concerns the amendment of article 5 of the bylaws dealing with legal and statutory disclosure thresholds. Under the amended article, any group of stockholders owning at least 2% of the capital or voting rights—as opposed to 5% currently—would be entitled to apply for shares corresponding to undisclosed interests to be stripped of voting rights.
- The twentieth resolution concerns the granting of the necessary powers to carry out legal publication and other formalities.

Appendixes to the Report of the Board of Directors⁽²⁾

Consolidated income

The BNP Group's consolidated income statements for the years 1994 to 1998 are presented below:

	1998	1997	1996	1995	1994	% Change in 98/97
(In millions of euros)						
Net banking income	7,366	6,718	6,022	5,749	5,993	9.6
Operating expense and depreciation	(5,019)	(4,670)	(4,369)	(4,300)	(4,409)	7.5
Gross operating income	2,347	2,048	1,653	1,449	1,584	14.6
Net addition to allowances for credit risks and country risks	(1,203)	(1,034)	(578)	(844)	(1,124)	16.3
Net operating income	1,144	1,014	1,075	605	460	12.9
Gains (losses) on disposals of long-term investments, net of provisions	478	363	(107)	1	(19)	31.6
Non-recurring non-operating expenses	(132)	(233)	(257)	(126)	(45)	n.a.
Share of earnings of companies carried under equity method	124	124	82	5	97	(0.1)
Amortization of goodwill	(16)	(16)	(13)	(13)	(19)	1.9
Pretax income	1,598	1,252	780	472	474	27.6
Income taxes	(431)	(304)	(150)	(179)	(205)	41.4
Consolidated net income	1,167	948	630	293	268	23.1
Net income attributable to Group	1,114	909	588	272	253	22.6

Consolidated net income for 1998 totaled EUR 1,167 million and net income attributable to the Group came to EUR 1,114 million, up 23.1% and 22.6% respectively compared with 1997. The year-on-year growth reflects the sustained, large-scale improvement in the earnings performances of the various Group businesses. Income was

boosted by more favorable economic conditions in France and the high level of activity in the equity markets, which helped to offset the impact of financial market turbulence and the substantial allowances set aside in response to worsening conditions in certain emerging markets.

Net banking income

Net banking income climbed 9.6% in 1998 to EUR 7,366 million.

	1998	1997	1996	1995	1994	% Change in 98/97
(In millions of euros)						
Value added to capital ⁽¹⁾	4,855	4,482	4,053	3,959	3,994	8.3
Commissions and other ⁽¹⁾	2,511	2,236	1,969	1,790	1,999	12.3
Net banking income	7,366	6,718	6,022	5,749	5,993	9.6

(1) economic definitions.

Domestic Banking revenues expanded 2.3% to EUR 3,829 million. Revenues of the domestic branch network rose 2.2% to EUR 3,435 million, helped by a EUR 97 million increase in commission revenue.

Retail Banking revenues outside euro countries totaled EUR 733 million, an increase of 22% including the contribution of First Hawaiian Bank consolidated over the

last two months of the year. Based on a comparable structure and at constant exchange rates, the year-on-year increase came to 7.2%.

Global Customers and Markets revenues climbed 18.7% to EUR 2,554 million. Based on a comparable structure and at constant exchange rates, revenues rose 16.7%.

(2) The percent changes shown in this document have been calculated on the basis of data expressed in million French francs; as a result, they may be

slightly different from the percent changes obtained using data expressed in million or billion euro.

Net banking income	In millions of euros	% Change (98/97)
Global customers	884	10.7
Specialized finance	281	10.1
Financial activities	1,095	28.0
Asset management	194	33.4
Equity portfolio income	100	2.3
Global Customers and Markets	2,554	18.7

All businesses improved on their prior-year performance and in the case of the Global Customers business, revenue growth was accompanied by strict control over risk-weighted assets.

Commissions

						% Change in
(In millions of euros)	1998	1997	1996	1995	1994	98/97
On securities transactions	735	590	515	423	618	24.6
On customer transactions and other	578	481	425	337	351	20.4
On payment systems	355	319	299	285	266	11.1
On life/endowment insurance	126	130	112	109	83	(3.7)
Commission income ("BAFI" definition)	1,794	1,520	1,351	1,154	1,318	18.0
Other ⁽¹⁾	717	716	618	636	681	n.a.
Total commissions and other	2,511	2,236	1,969	1,790	1,999	12.3

(1) These figures essentially correspond to income that is not recorded as commissions according to "BAFI" criteria but which is economically related to commissions (such as foreign exchange commissions, software sales and re-invoiced expenses), including net expenses (EUR 26 million in 1998) recorded under "other operating income and expenses".

Operating expense and depreciation

						% Change in
(In millions of euros)	1998	1997	1996	1995	1994	98/97
Salaries and employee benefits, including profit-sharing	3,085	2,895	2,732	2,689	2,717	6.6
Other operating expense	1,601	1,454	1,323	1,314	1,369	10.1
Depreciation, amortization and provisions	333	321	314	297	323	3.8
Operating expense and depreciation	5,019	4,670	4,369	4,300	4,409	7.5

Total operating expense and depreciation rose 7.5% between 1997 and 1998. Expense trends between the various divisions were uneven.

Domestic Banking operating expense and depreciation eased back 0.2%. Since 1993, these costs have been cut by 5% or 11% in real terms, excluding the effects of inflation. BNP is continuing to implement its policy of gradually

scaling down employee numbers, based on natural wastage and voluntary departures. The number of employees was reduced by 1,035 persons between the beginning and the end of 1998. At 31 December 1998, the domestic branch network had 29,653 full-time equivalent employees. Adjustments reflected increasing computerization, organizational improvements and greater emphasis on expanding the sales force.

Number of Group employees

Full-time equivalent employees						% Change in
at 31 December	1998	1997	1996	1995	1994	98/97
Domestic Banking	31,882	32,917	34,092	35,203	36,049	(3.1)
BNP France	29,653	30,754	31,984	33,094	33,961	(3.6)
French subsidiaries	2,229	2,163	2,108	2,109	2,088	3.0
Global Customers and Markets and Retail Banking outside euro countries	21,443	16,671	15,913	15,693	15,505	28.6
In France	1,748	1,618	1,623	1,620	1,579	8.0
French subsidiaries	1,215	1,069	816	790	757	13.7
French overseas areas	1,079	1,142	1,157	1,209	1,244	(5.5)
Outside France	17,401	12,842	12,317	12,074	11,925	35.8
Europe	4,334	3,636	3,507	3,527	3,565	19.2
The Americas	6,634 ⁽¹⁾	3,331	3,204	3,144	3,021	99.2
Asia/Pacific	3,031	3,288	2,554	2,338	2,267	(7.8)
Africa/Middle East	3,402	2,587	3,052	3,065	3,072	31.5
Other	2,961	2,832	2,757	2,704	2,915	4.6
Total	56,286	52,420	52,762	53,600	54,469	7.4

(1) including the 5,000 employees of BANCWEST.

Operating expense and depreciation of the Retail Banking business outside the euro countries rose 22.0% to EUR 451 million. The increase was partly due to the first-time consolidation of First Hawaiian Bank, which has 3,170 employees, and costs generated by First Hawaiian Bank's merger with Bank of the West.

Global Customers and Markets operating expense and depreciation climbed 20.7%, reflecting the first-time consolidation of UEB and the cost of strengthening teams and IT and other resources, mainly at BNP Arbitrage, BNP Gestions, BNP Cooper Neff and BNP PrimeEast.

Higher gross operating income in all three divisions

Gross operating income by division	1998	1997	% Change in
(In millions of euros)			98/97
Domestic Banking division	855	764	12.0
Domestic network	652	568	14.8
Domestic subsidiaries	203	196	3.7
Retail Banking outside the euro countries	281	231	22.0
Global Customers and Markets	897	780	15.1
Global customers	338	318	6.3
Specialized finance	144	132	9.1
Financial activities	232	160	45.0
Asset management	85	74	14.9
Equity portfolio income	98	96	2.5
Other activities	314	273	14.5
Total BNP Group gross operating income	2,347	2,048	14.6

Gross operating income totaled EUR 2,347 million, an increase of 14.6% compared with 1997 and including organic growth of 13.2%. The contributions of the various divisions were as follows:

- 36.4% from Domestic Banking, which generated gross operating income of EUR 855 million, up 12.0% on 1997 (including 14.8% for the network and 3.7% for the subsidiaries);
- 12.0% from Retail Banking outside euro countries, with gross operating income 22% higher at EUR 281 million;
- 38.2% from the Global Customers and Markets division, with gross operating income of EUR 897 million, representing an increase of 15.1% attributable to 45% growth in income from financial activities and the sound performance of the international network;
- 13.4% from Other Activities, including EUR 126 million in interest arrears collected on loans to Kenya and Côte d'Ivoire, which were entirely offset by an addition to allowances for credit risks and country risks in the same amount. In 1997, similar operations were recorded for a total amount of EUR 0.2 billion.

Analysis of gross operating income of the international and French overseas areas network (all lines of business), according to geographic area

1998		
	In millions of euros	In percent
Europe (excluding France)	196	22.7
The Americas	329	38.0
Asia/Pacific	195	22.6
Africa/Middle East	110	12.7
French Overseas Areas	35	4.0
Total	865	100.0

Gross operating income of the international network (all lines of business) totaled EUR 865 million in 1998, up 5.4% on the previous year. The breakdown between the various continents is relatively even. The larger

contribution of the Americas reflects the operations of BANCWEST in the west of the United States, which is steadily expanding its retail banking network.

Net additions to allowances for credit risks and country risks

						% Change in
(In millions of euros)	1998	1997	1996	1995	1994	98/97
Allowances for specific risks	796	604	701	889	1,093	31.8
Domestic banking	241	366	521	728	715	(34.1)
Five Asian countries	299	90	—	—	—	x 3.3
Country risks and equivalents	407	430	(123)	(45)	31	(5.4)
Five Asian countries	(9)	370	—	—	—	n.a.
Additions to allowances for credit risks and country risks	1,203	1,034	578	844	1,124	16.3
Five Asian countries	290	460	—	—	—	(37.1)
Russia	219	—	—	—	—	—
Domestic banking	241	366	521	728	715	(34.1)

Net additions to allowances for credit risks and country risks totaled EUR 1,203 million in 1998 versus EUR 1,034 million the previous year, representing an increase of EUR 169 million or 16.3%.

During 1998, allowances to cover risks in five Asian countries—South Korea, Indonesia, Malaysia, the Philippines and

Thailand—were raised by EUR 290 million. At 31 December 1998, total allowances for risks in these countries stood at EUR 743 million. Out of the total, 51% corresponds to allowances for specific risks and 49% to allowances recorded as a precautionary measure to cover a potential deepening of the crisis in this zone.

Consolidated net income

Consolidated net income amounted to EUR 1,167 million. Net income attributable to the BNP Group rose 22.6% to EUR 1,114 million, representing seven times net income for 1993, the year of the Bank's privatization. Return on equity,

calculated by dividing average stockholders' equity after income appropriation by net income for the year (in both cases excluding minority interests), stood at 11.8% in 1998 versus 10.4% in 1997 and 2.2% in 1993.

Net income of BNP SA

	1998	1997	1996	1995	1994	% Change in 98/97
(In millions of euros)						
Net banking income	5,483	5,206	4,626	4,619	4,837	5.3
Operating expense and depreciation	(3,782)	(3,688)	(3,511)	(3,496)	(3,586)	2.6
Gross operating income	1,701	1,518	1,115	1,123	1,251	12.1
Net additions to allowances for credit risks and country risks	(973)	(839)	(306)	(481)	(793)	15.9
Non-recurring non-operating items and other	367	(409)	(496)	(346)	(208)	n.a.
Pretax income	1,095	270	313	296	250	x 4
Net income	1,078	320	362	271	201	x 3

The significant increase in BNP SA's net income in 1998 stems from the restructuring of its interest in Bank of the

West, which was accounted for as a share-swap in the parent company's accounts.

Appropriation of income

The Board of Directors is recommending that the Annual Stockholders' Meeting to be called to approve the 1998 accounts appropriate net income for the year of EUR 1,077,921,835.15, plus unappropriated retained earnings brought forward from the prior year in an amount of EUR 202,303,677.68, representing total income available

for appropriation of EUR 1,280,225,512.83, as follows:

- appropriation to the legal reserve: EUR 1,969,063.14;
- appropriation to other reserves and carryforward as unappropriated retained earnings: EUR 950,523,249.69;
- distribution of a total dividend of EUR 327,733,200.00.

Appropriation of income for 1998 (in euros)

Debit		Credit	
Legal reserve	1,969,063.14	Unappropriated retained earnings brought forward from prior year	202,303,677.68
Balance available for distribution:		Net revenue for the year less operating expense, depreciation provisions for general risks and commitments and other expenses	1,077,921,835.15
Other reserves	522,189,463.48		
Dividends	327,733,200.00		
Unappropriated retained earnings	428,333,786.21		
Total	1,280,225,512.83	Total	1,280,225,512.83

(In millions of euros)	1998	1997	1996	1995	1994	1993
Net income attributable to the Group	1,114	909	588	272	253	155
Total net dividend	328	228	171	106	93	84
Payout rate	29.4%	25.0%	29.0%	38.9%	36.7%	54.2%
Number of shares outstanding at 31 December ⁽¹⁾	218,410,671	213,244,188	207,434,993	192,183,938	190,046,159	184,008,556
Earnings per share (EUR)	5.16	4.31	2.85	1.42	1.36	1.01
Net dividend per share (EUR)	1.50 ⁽⁴⁾	1.07 ⁽³⁾	0.82	0.55 ⁽²⁾	0.49	0.46

(1) Including nonvoting shares in 1993.

(2) Paid on 192,904,218 shares, including the 720,280 new shares created on 27 February 1996 following the public tender offer for BNP España.

(3) Paid on 213,245,588 shares, including the 1,400 new shares with rights from 1 January 1997 subscribed under the 1995-2002 stock option plan.

(4) Paid on 218,488,800 shares, including the 78,129 new shares with rights from 1 January 1998 subscribed under the 1994-2001 and 1995-2002 stock option plans.

Subject to approval by the Annual Stockholders' Meeting, the net dividend per share (excluding the dividend tax credit) will amount to EUR 1.5, up 40% on the previous year's dividend.

Consolidated balance sheet analysis

The following table shows changes in the various balance sheet items over the last 5 years:

	1998	1997	1996	1995	1994	% Change in 98/97
(In billions of euros, at 31 December)						
Interbank and money market items	115.3	114.7	108.7	86.6	74.3	0.6
Customer loans	148.7	135.4	121.0	114.0	111.5	9.8
Securities portfolios	27.6	26.4	28.4	20.6	17.8	4.8
Other assets	30.8	31.6	23.0	19.2	15.2	(2.7)
Tangible and intangible assets	2.4	2.1	2.6	2.6	2.6	13.2
Total assets	324.8	310.2	283.7	243.0	221.4	4.7
Interbank and money market items	108.1	101.9	95.0	77.9	68.0	6.1
Customer deposits	118.0	109.4	97.2	88.1	79.8	7.8
Bonds and negotiable debt instruments	36.7	36.6	38.9	41.3	42.2	0.3
Other liabilities	38.8	41.2	34.1	19.3	15.2	(6.1)
Allowances for liabilities and charges	2.9	2.2	1.9	1.8	1.8	34.7
Subordinated debt	8.3	8.2	6.8	5.6	5.5	0.6
Reserve for general banking risks	1.0	1.0	1.0	1.3	1.3	1.3
Stockholders' equity (after income appropriation)	11.0	9.7	8.8	7.7	7.7	12.8
Total liabilities and stockholders' equity	324.8	310.2	283.7	243.0	221.5	4.7

Total consolidated assets at 31 December 1998 came to EUR 324.8 billion, up 4.7% on the year-earlier figure. The main year-on-year changes in consolidated balance sheet items were as follows:

Assets

- Total customer items expanded by 9.8% to EUR 148.7 billion, representing 45.8% of total assets versus 43.6% at 31 December 1997. Growth was driven by an increase in the customer loan portfolios of BANCWEST CORP. and BNP France and it also reflected a higher volume of resale agreements. BNP's credit risks on highly-leveraged institutions are not material.

- Interbank and money market items held firm, the increase in resale agreements and the portfolio of Treasury bills and money market securities having offset a decline in interbank loans and other interbank items.

Liabilities

- Interbank items rose 6.1% to EUR 108.1 billion, reflecting growth in repurchase agreements.
- Customer deposits expanded 7.8% to EUR 118.0 billion. Year-on-year growth was attributable to the higher volume of deposits at BANCWEST CORP. (due to a change in group structure), BNP France, BNP New York and UEB Geneva.

Stockholders' equity

Changes in capital stock

Changes in capital stock, 1992 to 1998	Number of shares	Capital stock (in FRF)
At 31 December 1992	70,739,443	3,536,972,150
1993		
Two-for-one stock-split and reduction in the par value of the shares from FRF 50 to FRF 25	141,478,886	3,536,972,150
Exercise of subscription warrants for nonvoting shares issued in 1990	12,048,924	301,223,100
Exercise of rights to subscribe to common and nonvoting shares issued in 1993	30,480,746	762,018,650
At 31 December 1993	184,008,556	4,600,213,900
1994 ⁽¹⁾		
Payment of the dividend in the form of shares of the company	1,685,603	42,140,075
Capital contribution of shares of Compagnie Financière Gamma	4,352,000	108,800,000
At 31 December 1994	190,046,159	4,751,153,975
1995		
Payment of the dividend in the form of shares of the company	2,137,779	53,444,475
At 31 December 1995	192,183,938	4,804,598,450
1996		
Stock-for-stock public tender offer for BNP España	720,280	18,007,000
Payment of the dividend in the form of shares of the company	1,675,995	41,899,875
Stock-for-stock public tender offer for CIP	12,202,336	305,058,400
Private placement reserved for staff members	652,444	16,311,100
At 31 December 1996	207,434,993	5,185,874,825
1997		
Stock-for-stock public tender offer for BNPI	1,315,122	32,878,050
Payment of the dividend in the form of shares of the company	3,574,073	89,351,825
Private placement reserved for staff members	920,000	23,000,000
At 31 December 1997	213,244,188	5,331,104,700
1998		
Issuance of shares on exercise of stock options	7,141	178,525
Stock-for-stock public tender offer for BNP "I"	1,702,410	42,560,250
Payment of the dividend in the form of shares of the company	2,176,932	54,423,300
Private placement reserved for staff members	1,280,000	32,000,000
At 31 December 1998	218,410,671	5,460,266,775
1999		
Issuance of shares on exercise of stock options	78,129	(in euros)
At 5 January 1999	218,488,800	873,955,200

(1) The Special Stockholders' Meeting of 7 December 1994 voted to convert nonvoting shares into common shares.

At 31 December 1998, BNP SA had capital stock of FRF 5,460,266,775 represented by 218,410,671 common shares with a par value of FRF 25. The shares are fully paid and are held in registered or bearer form, at the stockholders' discretion, subject to compliance with applicable laws and regulations. None of the shares carry double voting rights.

Increases in the number of shares in issue during 1998 were as follows:

- creation of 1,702,410 new shares in connection with the stock-for-stock public tender offer for BNPI (29 June 1998),

- payment of part of the 1997 dividend in shares, entailing the creation of 2,176,932 new shares (29 June 1998),
- private placement of 1,287,141 new shares, reserved for staff members (29 June 1998).

As of 5 January 1999, following the exercise of additional stock options, the conversion of the capital into euro and the rounding up of the par value of shares to EUR 4, BNP SA's capital stock stood at EUR 873,955,200 represented by 218,488,800 common shares.

Stockholders' equity

(In millions of euros, at 31 December after income appropriation)	1998	1997	1996	1995	1994	% Change in 98/97
Consolidated stockholders' equity, BNP Group share	9,927	9,001	8,469	7,415	7,342	10.3
Minority interests	1,064	744	287	337	350	42.9
Consolidated stockholders' equity, including minority interests	10,991	9,745	8,756	7,752	7,692	12.8

Consolidated stockholders' equity, including minority interests, totaled EUR 11 billion at 31 December 1998, up EUR 1,246 million compared with the year-earlier figure. The Group's share of consolidated stockholders' equity came to EUR 9.9 billion, representing a year-on-year increase of EUR 926 million as follows:

- EUR 258 million corresponding to share issues carried out during the year and EUR 786 million in 1998 undistributed

earnings appropriated to reserves, partially offset by

- the EUR 118 million negative impact of exchange rate fluctuations and other movements.

Minority interests in reserves increased by EUR 320 million, primarily reflecting the EUR 438 million impact of the restructuring of the Group's interest in the BANCWEST CORP. sub-group.

Capital adequacy ratios

Cooke ratio

At 31 December	New Cooke ratio			Former Cooke ratio			
In billions of euros and %	1998	1997	1997	1996	1995	1994	1993
Risk-weighted assets	180.23	181.87	177.56	172.16	155.82	147.83	157.54
Tier 1 and Tier 2 capital							
Tier 1	11.6	10.5	10.5	9.3	8.6	8.5	8.8
Tier 2	7.2	7.9	7.1	6.4	5.6	5.9	6.2
Total Tier 1 and Tier 2 capital	18.8	18.4	17.6	15.7	14.2	14.4	15.0
Tier 1 and Tier 2 ratio	10.4%	10.1%	9.9%	9.1%	9.1%	9.8%	9.5%
Tier 1 ratio	6.4%	5.8%	5.9%	5.4%	5.5%	5.7%	5.6%

The BNP Group's Cooke ratio (calculated on the revised basis taking into account market risks) stood at 10.4% at 31 December 1998 versus 10.1% at year-end 1997. The significant improvement is attributable to:

- the EUR 1.7 billion (1%) reduction in risk-weighted assets. Market risks remained broadly stable but credit risks declined. Changes in Group structure (Bank of the West / First Hawaiian, UEB, Banque du Caire et de Paris) resulted in an increase in credit risks, which was more than offset by the effect of currency translation and a significant decrease in credit risks (mainly corporate exposures) on a like-for-like basis.
- the EUR 0.4 billion (2.2%) growth in regulatory capital. Tier 1 capital expanded by EUR 1.1 billion, in line with the increase in book equity, while repayments of subordinated debt and other movements trimmed EUR 0.7 billion from Tier 2 capital.

Capital adequacy ratio

At 31 December 1998, the ratio of available regulatory capital to required regulatory capital for the BNP Group, calculated in accordance with the rules and instructions for the application in France of the European Council Directive on the capital adequacy of investment firms and credit institutions stood at 129% (123% in 1997) excluding Tier 3 capital (123% in 1997) and 136% (130% in 1997) including Tier 3 capital.

BNP also complies with the standards for the control of major risks, the liquidity ratios (102% at 31 December 1998) and the stockholders' equity and long-term capital ratios (99.7% at 31 December 1998). The Group entities that are registered as banking institutions comply with regulatory liquidity requirements.

Year 2000 project

The entire BNP Group organization in France and abroad is committed to ensuring that the change of millennium does not have an adverse impact on customers or stockholders. The Year 2000 project was launched over two years ago and progress is being monitored at the highest level of Group management. The organization structure set up to manage the changeover to the euro and the work performed on that project have considerably facilitated implementation of the Year 2000 project. The project is not confined to internal operations but also includes reviewing and validating interfaces with the main customers, suppliers and other

external partners, as well as with all national and international interbank systems.

The BNP Year 2000 project is being implemented in four phases:

- the first phase—which has been completed—involved identifying all systems and operations potentially at risk from the millennium bug and planning corrective measures. During this phase, processes were classified as high, medium or low priority. All processes related to customer services, interbank transactions, risk management and internal financial and management information are considered of critical importance and were therefore classified as high priority.
- the second phase consists of adapting applications and hardware to make them Year 2000-compliant. In the last twenty years, BNP has used a coding system which is not affected by the change of millennium and this helped to limit the work involved. The Bank's IT production processes have been awarded ISO 9002 certification, testifying to its success in controlling Year 2000 risks.
- the third phase is the sign-off phase. Numerous series of tests are being performed, including aging tests performed by simulating the processing of transactions at sensitive dates beyond the Year 2000, to ensure that the millennium bug has been completely eliminated, as well as an overall validation.
- the fourth and final phase consists of reinstalling the Year 2000-compliant applications.

The Bank has deployed the necessary resources to successfully complete the project. Out of the total budget of EUR 335 million set aside for the Euro and Year 2000 projects, EUR 84 million are specifically earmarked for the Year 2000 project. Costs incurred up to 31 December 1998 represented nearly 55% of the total budget. During the year, a total of 1,000 people, including 500 IT experts, worked on the Euro and Year 2000 projects.

The project is currently running to schedule. As of 31 December 1998, 80% of critical applications were Year 2000-compliant. The first half of 1999 will be devoted to testing and signing off hardware, most of which had been adapted by year-end 1998. Between April and September 1999, BNP will participate in the testing of national market systems and

a final test of global market systems is scheduled to take place in June 1999. During the second half of the year, the plans developed to deal with any residual Year 2000 problems will be validated. Within the BNP Group, a “dress rehearsal” is scheduled to take place in September 1999, along the same lines as for the changeover to the euro. This exercise will allow the Bank to assess its level of Year 2000 preparedness but will not provide absolute assurance that no problems will arise with the change of millennium, because much depends on the state of preparedness of external partners.

Alongside BNP’s internal Year 2000 project, action is being taken to assess the level of preparedness of the main customers, correspondents and suppliers. Letters have been sent to all suppliers requesting confirmation that their products and services are Year 2000-compliant and proposing appropriate support. BNP is also taking steps to ensure that customers are aware of the risks arising from the millennium bug and are taking appropriate action to deal with them. Questionnaires have been sent to the main large corporate customers, banks and other institutions to determine the status of their Year 2000 projects. The situation of other businesses and members of the professions is also being assessed, based on their replies to the 10 questions contained in the “Year 2000 mission” checklist. In the network, account managers are contacting customers to discuss Year 2000 issues. Lastly, specific tests are being conducted with the main customers and suppliers, to test the compatibility of data received by the Bank.

The Year 2000 project represents a mammoth task of critical importance. The BNP Group started work on the project well ahead of the 31 December 1999 deadline, and while its success cannot be guaranteed, every effort has been made to ensure that the project was conducted as efficiently as possible. As was the case for the Euro project, staff throughout the organization are using this opportunity to establish methodologies and tools that will be of benefit for many years to come, via cross-functional projects, the testing process and the modernization and streamlining of hardware and software assets.

Internal control system and risk management

In 1998, the BNP Group took further action to enhance its system of internal controls in order to optimize

the management of the risks inherent in its operations. The system is based on four main principles that underlie the Bank’s organization:

- **Hierarchy**—The director of each head office division defines his internal control system in coordination with the Bank’s other entities. He must ensure that it functions correctly and monitor effectively the activities for which he is responsible.
- **Separation of functions**—This principle applies primarily to departments that originate transactions and the administrative departments that settle the transactions. Separation of functions ensures ongoing, independent monitoring of business.
- **Delegation**—This is the fundamental concept on which the Bank’s decision-making framework is based. Each delegator must monitor the implementation of his decisions.
- **Instructions**—Printed copies of the Bank’s general policy, procedures, and controls are distributed throughout the entire BNP Group.

The BNP Group has created an internal control framework. It is organized according to eight risk families⁽³⁾ and four monitoring levels, and takes existing supervisory and service relationships between BNP Group entities into account. It defines each individual’s internal control responsibilities in the form of rules and regulations that state the scope and types of responsibilities delegated, the organization of monitoring procedures, and reporting requirements for each risk family.

The internal control system is run by a bank officer in charge of coordination and monitoring, and it is evaluated by the Management Audit and Inspection division, which reports directly to the Chairman and Chief Executive Officer. A specific unit has been set up to assist the bank officer responsible for internal control coordination and monitoring.

The key missions of this unit are to:

- regularly update the internal control framework;
- promote and facilitate consideration by the various divisions and departments of action to be taken to adapt

(3) Credit and counterparty risks, market risks, operational risks (accounting risks, administrative risks and IT risks), commercial risks (including the risk of damage to the Bank’s reputation), legal and tax risks and human resources risks.

their internal control systems to take account of changes in the types of business conducted, regulatory changes and the use of new technologies and new financial instruments;
- verify that procedures consistently contribute to meeting the aims and objectives of the internal control system.

The various divisions and departments have significantly enhanced their systems of internal control by issuing more clearly-worded delegations of responsibilities, creating or updating procedure databases and progressively developing monitoring tools by risk family. This effort will be stepped up in 1999.

The BNP Group's internal control system, which is a major tool guiding all of the company's decision-makers, takes into account French Banking Commission (CRB) regulation 97-02, effective 1 October 1997.

Principles and Organization of Risk Management

Through its banking and trading activities, BNP is exposed to various types of risk: credit risk, counterparty risk, market risk, liquidity risk, transformation risk, and operational risk (accounting, administration, IT).

BNP has created, and continually improves upon, a set of standards and procedures intended to identify, measure, and manage its various risks. This system operates according to three demanding principles: strict separation between sales and risk analysis, individual responsibility for lending decisions, and attribution of the financial consequences of decisions to the operational entities that make them. All of the Bank's entities take part in control procedures and work together to ensure strict compliance, particularly of ceilings imposed on profit centers. New activities and major changes to existing activities are presented to Group senior management so that the most significant risks can be accurately identified and the appropriate standards and procedures implemented.

Strategic Direction

In 1998, BNP set up a Risk Policy Committee which works alongside the General Management Credit Committee and the Market Risks and Activities Committee.

The Risk Policy Committee is responsible for defining risk policies and determining crisis management strategies. It makes decisions, when necessary, concerning the strategies to be followed by the Committees and managers responsible for commitments and market risks in order to deal

with situations potentially leading to an escalation of risks. To this end, the Committee reviews not only the risks involved and the business implications, but also the potential impact on the Bank's net banking income and financial communication.

The Committee is headed by the Chairman and Chief Executive Officer of BNP. Its members include the Chairman of the Market Risks and Activities Committee and the directors of the BFI-Risks and Risk Policy and Industry Research divisions.

Banking Activities

Responsibility for managing the Bank's commitments rests with its two core business divisions: Domestic Banking and International Banking and Finance.

Decision-Making Authority and Chain of Command

The Chairman and Chief Executive Officer delegates authority, with the faculty of subdelegating to the directors of the two core business divisions. Delegations are defined according to customer category, credit rating, and in some cases, business sector.

Subdelegations are organized in such a way that lending decisions rest solely with head office divisions for banks and sovereign borrowers, and with specialized units, which report to the two core business divisions, for certain operations requiring specific techniques or expertise (such as international commodity finance, specialized finance, and structured finance).

Any staff member vested with the authority to commit the Bank has the right and the obligation to reduce the amount of credit granted to a customer if he feels that the risk is deteriorating and warrants a reduction, even if the credit file does not fall within his powers

The General Management Credit Committee is the decision-making authority for commitments whose amount exceeds the delegation given to the directors of the two core business divisions. This Committee, headed by the Chief Operating Officer, has permanent members (including the director of the Risk Policy and Industry Research division, who holds veto power, as well as the directors of the two core business divisions), non-permanent members, representatives of the Management Audit and Inspection division, the Legal and Tax Affairs division, and credit application "sponsors". This Committee meets at least twice a week.

The General Management Impaired Credits Committee is the decision-making authority for impaired credits –allowances, waivers, write-offs–whose amount exceeds the delegation given to the directors of the two core business divisions, currently EUR 0.4 million. This Committee, headed by the Chairman and Chief Executive Officer of BNP, has permanent members (including the director of either the Legal and Tax Affairs unit or the Special Affairs and Collection unit, as well as the director of the Risk Policy and Industry Research division, or their representatives), non-permanent members (including representatives of the Management Audit and Inspection division), and application “sponsors”. This Committee meets once a month.

In the specific area of country risks, the office of the Chairman delegates authority to officers of the International Banking and Finance division. This delegation is limited to a ceiling that is set as a function of a country’s risk rating. Decisions concerning amounts above that ceiling are made by the General Management Credit Committee.

General Procedure for Granting Loans

Decisions pertaining to new originations must take into account all of the BNP Group’s commitments to the borrower or its group, regardless of whether the commitments were made by one of BNP’s divisions or subsidiaries. Under the principle of separation of powers, a relationship manager must always justify his position before a credit analyst or risk censor. In all cases, both parties may decide of a common accord to seek arbitrage at a higher hierarchical level.

The Bank conducts a comprehensive risk analysis for all lending decisions and rates borrowers according to probability of default. The complete rating system applies to corporations and banks. A simplified system is used for self-employed professionals, and credit scoring is used as a decision-making aid for individuals.

There are six distinct categories of healthy risks, two of which are considered “sensitive” or “préoccupant” (to be watched) under certain circumstances or special assessments. There are also two categories of impaired assets: the first includes doubtful loans (such as receivables in arrears, whether or not destined to be provisioned) and all receivables that warrant allowances; the second corresponds to receivables in the process

of collection and applies to customers with which the Bank has broken off commercial relations, having reverted to the status of simple creditor.

Country-risk ratings come under the responsibility of the International Banking and Finance division, which cooperates closely with the Economic Research division. During bi-annual assessments the frequency of which may be altered as needed the Bank rates all countries with which it has relations.

The Risk Policy and Industry Research division, reporting to the office of the Chairman, designs the methods used to identify and measure the risks the Bank incurs in banking and trading activities. This same division participates in commitment decisions in three ways: its prior consent is mandatory for applications falling under the responsibility of the General Management Credit Committee and for applications coming from a certain number of business sectors, whether or not they are presented to the Credit Committee, and it may also be consulted by BNP’s various units, to assist with specific decisions or help define the Bank’s lending policies.

General Procedure for Monitoring Loans

BNP monitors its loans at different levels, as defined by its general internal control procedure.

The first level concerns the profit centers. They monitor operations carried in their books, conduct periodic checks, and watch for warning signals that determine the Bank’s reaction to major events that affect the security of its commitments.

Domestic branches and international subsidiaries and branches follow exactly the same procedures. International units also take into account local practices and banking regulations applicable in the countries in which they operate.

Every day, branches receive a list of customers that have exceeded their limits. Every month the Bank prepares an operations summary of each customer account, containing such information as highest overdraft and frequency of credit limit overruns, which it forwards to the branches. Every quarter, all branches are required to prepare a list of commitments that may be downgraded and a list of impaired assets. Depending on the warning indications he receives, the director of the entity

concerned, or his hierarchical superior, decides whether or not to change the customer's risk rating.

All commitments are reviewed by the qualified authority every eighteen months (for the best ratings) or every year (for other ratings). For example, the General Management Credit Committee periodically reviews all commitments for which it is responsible.

Once a customer is rated "préoccupant" or impaired, it is specifically monitored by a dedicated account manager, with or without the assistance of either the Legal and Tax Affairs or the Special Affairs and Collection unit depending on the size of the commitments.

The collection channel in France is run and monitored by the Special Affairs and Collection unit, which operates directly or delegates its authority to the domestic network and domestic subsidiaries or to outside service providers if needed.

Commitments classified as impaired assets are reviewed annually by the qualified authority. For example, once a year, the General Management Impaired Credits Committee examines all affairs involving commitments of more than EUR 15 million.

At the second level, the credit risk departments of the Domestic Banking and International Banking and Finance divisions perform periodic on-site or remote checks to ensure that any authority they have subdelegated is being used correctly.

The third level is ensured by the Risk Policy and Industry Research division, in order to identify excessive concentrations of risk.

The fourth level is handled by the Management Audit and Inspection division, which reports directly to the Chairman and Chief Executive Officer. The purpose of this monitoring level is to ensure that General Management directives are applied correctly, to evaluate the risks incurred on missions it undertakes and the coherence of the risk management system at the various BNP entities.

General Procedure for Reporting Risks

The management information reports submitted to Group General Management include a risk report analyzed by rating and by type of customer. These schedules are produced on a monthly basis by the Domestic Banking

division and on a quarterly basis by the International Banking and Finance division. Risk monitoring statements covering corporate groups, banks, and specific economic sectors are prepared to enable General Management to monitor developments affecting them. Every half-year, the General Management "Préoccupant" Credits Committee, which is headed by the Chief Operating Officer of BNP and whose operation is analogous to that of the General Management Credit Committee, examines all commitments rated as "préoccupant". Every half-year, the General Management Impaired Credits Committee examines all commitments rated as "doubtful" as well as those in the process of collection.

Trading Activities

The main risks the Bank incurs and manages as part of trading activities are risk of counterparty default, risk of loss on balance-sheet and off-balance sheet instruments due to market price fluctuations, liquidity risk and operational risks.

BNP continues to implement Group of Thirty recommendations concerning the management of risks related to derivatives traded over the counter, valuing positions and reporting revenues related to these risks, measuring these risks (counterparty risks and price risks incurred on exposure to interest rates, exchange rates, equities, options, etc.), and the major operational aspects of managing these risks. The main recommendations apply to two aspects of trading activities:

Separation of Functions

BNP has made this an operating principle for all activities that incur risk. There is a complete separation of functions and responsibilities between sales staff and risk analysts, as well as between trading rooms, on the one hand, and the persons responsible for performing controls, the administrative departments that settle completed transactions, and the accounting departments that monitor the accounts, on the other hand. Risk control, which is carried out independently of the Capital Markets unit's worldwide lines of business, created several years ago, has developed into a system based on four basic levels of internal monitoring:

- **At the first level**, monitoring is carried out by the middle office (Business Monitoring), which is responsible for detailed reporting on utilizations and reports to the General Secretariat of the International Banking and Finance division.

- **At the second level**, monitoring is entrusted to the Market Risks Monitoring Unit, a specialized department of the International Banking and Finance division that centralizes market risks, conducts on-site inspections to ensure compliance with limits set by trading room managers and the dispatch of various reports to the appropriate hierarchical levels, centralized reporting (now weekly but soon daily, once the Bank has installed its internal model), auditing, and field support.
- **At the third level**, monitoring is ensured both by the Risk Policy and Industry Research division, which identifies, defines, and measures trading activity risks the same as it does for banking activity risks, and by the Market Risks and Activities Committee (the general authority supervising the BNP Group's market risks), which defines BNP Group policy concerning trading activities, validates market risk identification methods and measurement standards proposed by the Risk Policy and Industry Research division and market risk monitoring procedures, and sets limits for each main business category. Members of the Market Risks and Activities Committee are representative of all of the Bank's functional and operational expertise, so that its decisions apply to the entire BNP Group, and the Risk Policy and Industry Research division acts as secretary for its meetings.

The Market Risks and Activities Committee, which is headed by an advisor to the Chairman and CEO meets twice a month.

- **At the fourth level**, monitoring is entrusted to the Management Audit and Inspection division, which ensures the coherence and performance of every type of monitoring procedure and regularly reports to the office of the Chairman.

This separation of functions, between departments that incur risks and those in charge of administration and risk monitoring, prevails at all entities and at all levels of the Bank's worldwide lines of business. Staff members in charge of monitoring market risks report locally to both their director and the Market Risks Monitoring Unit. Back offices and accounting departments report to the General Secretariat of the International Banking and Finance division, which acts as central coordinator. In this way, administrative and operational risks can be identified and handled in the appropriate manner. Since BNP organized

its capital market activities into worldwide lines of business, managers have received real-time information on positions taken by the various profit centers.

The separation of functions, combined with the appropriate reporting systems, enables the Bank's General Management to stay abreast of risks incurred and all noteworthy events, on a regular and objective basis.

Risk Limits

In accordance with Group of Thirty recommendations, the Bank imposes aggregate and individual risk limits that correspond to measurements and that are clearly understood by management and traders alike.

- **Counterparty risk authorizations are monitored globally, by counterparty.** The Capital Markets unit, with its worldwide lines of business, has not been delegated authority concerning risk of loss on the Bank's counterparties, with the exception of specific authority concerning the most solvent equity and debt securities issuers. The head office divisions and profit centers in charge of relations with counterparties submit their requests at the appropriate decision-making level. Authorized credit lines are determined within the general framework of credit risk control.

BNP's computer system, which can handle more than 180,000 operations in progress, nearly 31,000 authorizations, and roughly 28,000 counterparties, is capable of performing global centralization and continuous monitoring of authorized credit utilizations. It can centralize counterparty risk authorizations, monitor trading room and site operations and positions, calculate counterparty risk utilizations (including risks related to issuers and delivery), manage overruns and abnormalities, directly or indirectly mark trades to market, and generate reports on capital market operations from trading room and site back offices in order to satisfy regulatory requirements (regulation 95-02 and the EU Capital Adequacy Directive or "CAD").

In order to ensure that its derivatives transactions are legally secure, BNP's policy is to sign legal agreements (using either the ISDA or AFB model), which allow it to use netting in the event of default by a counterparty, thereby significantly mitigating counterparty risk. The Group will only trade in long-term or highly volatile derivatives with the most creditworthy

counterparties. As of 31 January 1999, BNP had signed multi-product agreements with 388 of its 500 most significant counterparties, which accounted for 92.5% and 96%, respectively, of outstanding off-balance sheet commitments at that date.

- **BNP places aggregate risk exposure and operational limits on market risks.** Once a year, the Market Risks and Activities Committee gives the office of the Chairman a recommended amount of general market risk limit authorizations for the Group's capital market activities for the year. That amount is also broken down according to type of business and risk class: exposure to interest rates, exchange rates, equities, options, and commodities. It also informs the office of the Chairman of the profitability targets allocated to the units engaged in capital market activities, to help them assess the level of risk implied by these targets.

The Market Risks and Activities Committee ensures that limit authorization requests correspond to a satisfactory balance and diversification of market risks, particularly among the largest financial markets and the regions in which the Bank's capital market units and sites operate. As part of the decision-making process, it weighs the Bank's expertise in the proposed risk areas, its monitoring and reporting logistics, and profitability statistics and forecasts for the risks proposed.

The office of the Chairman is responsible for making decisions concerning the raising of limits and their allocation, in excess of the discretionary authority delegated to the President of the Market Risks and Activities Committee.

Twice a year, the Market Risks and Activities Committee submits a report on the utilization of market risk authorizations to the office of the Chairman, who relays the information to the Board of Directors.

- **The Market Risks and Activities Committee exercises general supervision over market risks.** Every month it monitors the use and results of general market risk authorizations. It analyzes market risk authorization use by each site and worldwide line of business and it checks up on secondary monitoring performed in the trading rooms. Once a month, the Market Risks and Activities Committee also examines significant gains and losses declared by sites and worldwide line of business.

Among other things, the rules for reporting significant gains and losses contain thresholds above which gains and losses must be reported as soon as they are detected, the Bank entities to which reports must be submitted, the conditions under which these entities may issue instructions to the reporting site, if necessary, and the nature of supporting information needed to explain the gains or losses reported.

Significant gains and losses declared to the Market Risks and Activities Committee must be classified under one of the following four categories: those related to ordinary trading activities which undergo more or less sizable variations caused by fluctuations in risk factors; those, related to model risk, resulting from a methodological error caused by a lack of applicable standard or the incompatibility between an existing standard and the prevailing situation in the markets; those related to personnel risks, caused by dysfunctions such as limit overruns and noncompliance with established procedures; and those, related to operational risks, such as those inherent in accounting, administrative, and computer systems.

Credit and Counterparty Risks

Credit Risks

Failure by a borrower to meet its obligations exposes the Bank to a risk of loss, referred to as credit risk. The loss is potential when default has not occurred; it materializes when the borrower defaults. The probability of default and subsequent variations may be measured in terms of factors that are specific to the borrower (e.g., financial condition, quality of management, competitive environment) and that are used to ascertain the actual risk of default.

BNP currently measures its credit risk on a transaction, company, portfolio of companies, or business sector on a conservative basis that only reflects its exposure to the transaction, company, portfolio of companies, or business sector, in other words, the total amount of credit utilizations (temporary bank overdrafts and financing commitments), off-balance sheet commitments and confirmed lines of credit given.

The "RECORD" program will be used as from the end of 1999 to assess credit risk more accurately. It will first be applied to business customers of the Domestic Banking division (SMEs and professionals), followed by major corporations and other customer categories. This program, which complies with internal control requirements, is a management aid for use in identifying yield/risk optimization

parameters and a management tool used to assess risk of concentration and measure business performance.

Credit risk coverage

By applying credit risk management principles and organization, BNP maintained the high quality of its assets in 1998.

Specific Risks

Provisioning of specific risks in France and abroad amounted to 53% of exposure at year-end 1993 (the privatization year). At year-end 1998 that figure stood at 63%.

Coverage of all⁽¹⁾ of the BNP Group's doubtful specific risks

In billions of euros, at 31 December	1998	1997	1996	1995	1994	1993
Doubtful loans outstanding	9.7	9.4	9.7	9.6	10.5	10.4
Allowances ⁽²⁾	6.1	6.0	6.1	5.8	5.7	5.5
Total coverage	63%	64%	63%	60%	54%	53%

(1) Including credit risks (receivables, securities and off-balance sheet commitments) on customers (including real estate risks) and credit institutions.

(2) Excluding the reserve for unforeseeable sectoral risks.

Doubtful specific risks amounted to EUR 9.7 billion, or 6.3% of gross customer loans outstanding at year-end 1998, compared with 6.7% at year-end 1997 and 8.5% at year-end

1993. The ratio of allowances for specific risks to gross customer loans stood at 4.0% compared with 4.2% at year-end 1997.

Ratio of doubtful specific risks to consolidated gross customer loans

In billions of euros, at 31 December	1998	1997	1996	1995	1994	1993
Gross customer loans	154.5	141.7	127.2	119.9	117.6	121.9
Doubtful specific risks as a percentage of gross customer loans	6.3%	6.7%	7.6%	8.0%	8.9%	8.5%
Allowances for specific risks as a percentage of gross customer loans	4.0%	4.2%	4.8%	4.8%	4.8%	4.5%

Country Risks

In 1998, the Bank regularly reassessed its risk in several emerging countries, in light of the worsening economic conditions in the countries concerned.

At 31 December 1998, total allowances for country risks amounted to EUR 2.3 billion, compared with EUR 2.2 billion at year-end 1997, including EUR 361 million related to five Asian countries (Indonesia, Thailand, the Philippines, South Korea and Malaysia) versus EUR 370 million one year earlier.

Last year's debt restructuring operations in Côte-d'Ivoire and Kenya did not have any impact on 1998 net income.

Balance Sheet Strength

Reserve for general banking risks. The reserve for general banking risks set up in 1993 in compliance with French Banking Commission regulations,

amounted to EUR 1,038 million at 31 December 1998. The EUR 13.6 million increase compared with year-end 1997 corresponds to additions to the reserve by subsidiaries of the international network.

Pensions and benefits. The various BNP Group units are committed to pay statutory or contractual benefits, such as pensions and seniority bonuses, to staff members. In addition, the Bank is encouraging voluntary departures or early retirement among eligible staff members in France. The allowances set up to cover these benefits amounted to EUR 643 million at 31 December 1998.

Allowance for unforeseeable sectoral risks. Since 1994, the BNP Group has maintained an allowance in its balance sheet to cover sectoral risks that might arise. At 31 December 1998, the allowance for unforeseeable sectoral risks totaled EUR 218 million. No portion of this allowance is allocated to cover any specific risks.

Counterparty Risk

In capital market business, counterparty risk is the risk of loss caused when a counterparty fails to honor an obligation. It is considered a credit risk when the counterparty's principal obligation is the repayment of a loan. Delivery-versus-payment risk occurs when the Bank has honored its side of an obligation without being able to determine whether the counterparty has done the same.

The Bank manages these two types of counterparty risk in the same way as credit risk, though it uses a specific procedure for monitoring delivery-versus-payment risk that entails breaking down transaction flows with each counterparty according to maturity.

By holding negotiable securities (mainly stocks and bonds), the Bank incurs another type of counterparty risk: issuer risk, which is the risk of loss caused by market price fluctuations reflecting factors specific to an issuer, such as its business sector and the markets' perception of its creditworthiness. BNP measures issuer risk continuously by marking to market the inventory of the issuer's securities and its forward positions in those securities. Once the internal market risk model is in use, for the purpose of measuring issuer risks BNP will also be able to take into account factors such as circumstantial considerations related to business sector or geographical location, liquidity of securities, or risk of credit rating downgrade or default, that could affect the issuer.

Capital market transactions with counterparties lead to funds flows that are either certain or conditional between the Bank and its counterparties. The amount and direction of those flows depend on the prices of the underlying instruments.

Contingent credit risk is the Bank's risk of loss when a counterparty defaults and market prices move in the Bank's favor in the interval between contract execution and default. The Bank is thus deprived of future funds flows which, when marked to market, give the instantaneous replacement value of the transaction. Contingent credit risk may be measured at any moment as the replacement value of the transaction plus add-ons reflecting market price movements between the time of valuation and the time of possible default. BNP currently values add-ons for each instrument and as a function of market price volatility over the time remaining until the contract matures or expires.

The widespread use of multi-product master-agreements

for netting all of the Bank's positions, counterparty by counterparty, has raised the need for tools that are more effective than the measurement method based on add-ons, which have the advantage of being product-specific but also the drawback of being static and difficult to aggregate.

BNP has developed the "Valrisk" project to measure contingent credit risk. Valrisk generates a risk profile for the interval between the valuation date and the expiration of the longest transaction outstanding, in real time and for each counterparty.

The Valrisk model is currently undergoing live testing by the Interest Rate Derivative Group (IRDG) line of business for banking counterparties and will be rolled out in 1999 to the entire Fixed Income-Foreign Exchange line of business and then to the Equities line of business.

Market Risk

BNP measures its market risks in terms of a Value at Risk (VaR) known as "RNP" (notional risk of loss) which is defined as sensitivity (of a position, portfolio, book, etc.) to market volatility. It represents the maximum potential loss determined based on the type of position (currency, interest rate, equity) and high adverse volatility assumptions. BNP's current in-house RNP model uses five years of underlying data to estimate the impact of these extreme adverse market fluctuations on the Group's interest rate, foreign exchange, and equity positions over a five-day holding period, assuming a 95% confidence level. It also examines the underlying data of the previous twelve months to determine whether volatility, measured according to the same criteria, has not varied in even greater proportions during this shorter period.

A limited set of significant fluctuation coefficients is considered for each risk class, determined on a very broad basis (e.g., short- and long-term interest rates; euro-zone currencies, other freely floating currencies, and centrally administered currencies).

In order to ensure effective risk management during major crises, the Bank performs historical simulations on its notional risks of loss.

Under the "Internal Model" project for measuring market risks, BNP is pursuing the methodological shift from RNP to a new definition of Value at Risk (VaR) based on a one-day holding period and a 99% confidence level which, unlike RNP, can be used to compare and aggregate market risks. Market risk measurement will reflect both uncertainty in

risk factors, over which the Bank's management has no control, and the Bank's exposure to that uncertainty, which management can control by applying limits and allocating total capital to specific trading activities. Thus, BNP will measure its market risks through a combination of two criteria: actual risk incurred through exposure to uncertainty in risk factors, and maximum authorized risk deriving from management decisions. The order of magnitude of uncertainty in risk factors makes the difference between actual risk and risk exposure. This difference of magnitude ensures that the internal model's measurement of exposure to risk is coherent with its measurement of the risk itself, in compliance with French Banking Commission (CRB) Regulation 97-02 concerning internal controls. On the one hand, management must authorize a maximum amount of uncertainty, and on the other, it must continuously measure actual uncertainty prevailing in the markets. VaR expresses an amount and the probability of losing that amount in an environment defined in terms of various parameters. In its in-house model, BNP defines three different sets of conditions to describe the environment:

- one for expected risk, which refers to all yields and correlations observed;
- another for risk exposure, which refers to yields and correlations defining a maximum authorized dispersion;
- a third for analyzing stress scenarios (unexpected risk), which refers only to yields observed under extreme market conditions and is used to define an extreme degree of dispersion beyond which the Bank may not commit itself.

RNP or VaR limits for interest rate, foreign exchange, and equity positions and for each currency are applied to each book and trader at each decision-making center. Each site is also given volume position limits, which are easier to monitor on a daily basis. Additional rules for second-order risks (such as decorrelation between two similar but not identical instruments) round out the limit framework. BNP uses a scenario-based method to perform specific checks on options due to the complexity of the non-linear risks they present. For reasons of conservatism, all authorizations for market risk limits, representing in the aggregate the general market risk limit, as imposed by the office of the Chairman based on a proposal by the Market Risks and Activities Committee and presented to the Board of Directors, are currently spread over the various books without taking any offsetting correlations into account.

At 31 December 1998, the general market risk limit was EUR 890 million. During the year, actual market risks averaged EUR 480 million, representing around 54% of the maximum allowed.

Asset/Liability Management

The Asset and Liability Management department's mission is to manage market risks in connection with the management of the BNP Group's structural financial risks. Its role includes identifying the transactions and market risks associated with banking operations, establishing an Internal Transfer Rates system and match-funding major balance sheet items accordingly. It is responsible for the Bank's funding and liquidity and for managing cash flows and residual market risks. Although its primary objective is not to maximise profits, it is organized in a way that allows its results to be measured.

Three high level ALM committees have been set up:

- The Domestic Banking ALM Committee, responsible for transformation and match-funding decisions concerning major balance sheet items related to the commercial banking business and for managing the related interest rate risks. The Committee monitors the results of its policy, as well as profits and losses arising from residual market risks (marginal mismatches and implicit options) managed directly by the ALM department.
- The International Banking and Finance ALM Committee, responsible for managing a proprietary portfolio. In accordance with its standard methods and procedures. This activity is carried out under the supervision and within the limits set by the Market Risks and Activities Committee, in accordance with its standard methods and procedures.
- The Control and Finance ALM Committee, responsible for making funding and liquidity decisions, verifying their implementation and monitoring all of BNP's regulatory ratios.

In 1998, demand for credit on the part of non-financial sector customers grew at roughly the same rate as customer deposits, resulting in a good match between these assets and liabilities. Asset/liability management therefore focused primarily on restructuring maturities to reduce the sensitivity of earnings and equity.

Management of Liquidity Exposure

The BNP Group's funding requirements were largely unchanged compared with 1997. The modest growth in funding needs in France was offset by a reduction in the needs of the international networks.

The proceeds from new medium- and long-term debt issues were used primarily to offset repayments of existing borrowings. Total funding raised by new issues came to EUR 1.1 billion, including just under EUR 0.46 billion worth of subordinated debt. Half of the total was denominated in French francs or other "in" currencies and half in US dollars. No preferred share issues were carried out during the year.

The Group held firm to its prudent mismatch policy, helped by the extreme stability of its sources of funding. BNP France's demand, savings and time deposits come from more than 10 million accounts held by individuals and companies.

Liquidity is also provided by liquid assets such as demand deposits, Treasury bills, securities received under repurchase agreements, negotiable certificates of deposit, government securities, and stocks and bonds in various currencies. The Group's strong financial condition ensures it easy access to the capital markets on excellent terms.

Management of Interest Rate Exposure

BNP takes into account all balance sheet and off-balance sheet operations, including forwards and options, in its analysis of interest rate risk. The Asset/Liability Management division defines methodological rules applicable throughout the Group for the matching of assets and the related refinancing and also manages the "interest rate book" for BNP France banking and proprietary transactions.

Interest rate risk on French franc operations in the domestic network is a structural feature of universal banking, which consists in transforming part of customer deposits into medium- and long-term loans to individuals and corporations.

The balance sheet profile of customer items changed significantly in 1996 and 1997. By contrast, in 1998 the flow of customer funds into home savings and passbook deposit accounts slowed although there was further strong growth in demand deposits.

For the first time in three years, outstanding fixed rate loans increased significantly, despite the continued high volume of

early repayments. Growth was driven primarily by home loans.

These developments fuelled a lengthening of the average maturity of customer loans while the average maturity of liabilities was only slightly longer. In order to reduce the sensitivity of stockholders' equity, the Asset/Liability Management division adjusted the maturity profile of interest rate hedges for transactions in French francs and the other "in" currencies.

Interest rate exposure on transactions denominated in "out" currencies is limited. Changes in interest rates have a similar impact on both assets and liabilities which are generally indexed to the same official rates. Fixed rate foreign currency debenture issues are generally swapped to eliminate interest rate risks.

Management of Net Foreign Exchange Position

Foreign exchange positions related to the results of foreign subsidiaries and branches that can be repatriated are now managed on a centralized basis by the Asset/Liability Management division which sets up monthly hedges.

In 1998, the BNP Group's net foreign exchange position was unchanged compared with the previous year.

Operational Risk

At BNP, operational risk covers administrative, accounting, and computer risks, as well as the risk of fraud, which the Bank's internal control framework classifies as staff-related.

Controls over operational risk are performed at four levels:

- **First level controls** are performed on an on-going basis either by the person responsible for data input or automatically by means of programmed controls.
- **Second level controls** are performed periodically either on-site or using remote supervision techniques, based on the Critical Supervision Points ("PSF") system. The PSF system comprises a limited number of compulsory controls covering major risks and evolve in terms of the areas of focus and the methodologies used, based on local management's assessment of needs.
- **Third level controls** consist of functional controls to verify compliance with the standards and procedures issued by the staff divisions.

- **Fourth level controls** are performed by the Management Audit and Inspection division as part of its standard internal audit program or at the time of specific audits carried out following customer complaints or where a fraud has been detected during second or third level controls.

Banking Activities

In 1997, the Domestic Banking-Domestic Network division validated qualitative procedures based on locating and implementing basic checkpoints, local audit plans based on the “KEOPS” (kit for assessing on-site operations) methodology used by both the Domestic Banking division and the Management Audit and Inspection division, and consolidated reporting per operating group and network division and by the Domestic Network division.

Controls over the activities of the International Banking and Finance division are performed by an internal audit department reporting to division management, which conducts audits both in Paris and at the foreign sites. BFI-Audit has produced methodological guidelines defining the information to be submitted by the foreign sites to division headquarters at periodic intervals. The reports contain information about the organization of the local internal audit department and the audits carried out during the reporting period. BFI-Audit also performs controls over the local internal auditors’ controls, in order to ensure that the Critical Supervision Points have been covered, in particular by reviewing reports on incidents exceeding a certain potential loss threshold.

Trading Activities

Operational risk control is based on several principles: accountability of the hierarchy, written procedures describing monitoring channels and audit trails, continuous rationalization of processing software, a system for reporting and handling incidents, and inspection assignments by the specialized audit departments.

The monthly reports to the Market Risks and Activities Committee identify significant losses and gains resulting from an operational risk (see below).

All of BNP’s banking and computer organization teams, from the Organization and Information Systems division (which plays a general role) to the Systems and Back Office

Engineering departments of the International Banking and Finance division (in charge of organizing execution services), help ensure the security of procedures. These entities have undertaken a major quality certification program that is now in progress. As the foreseeable part of operational risk is to be considered as an operating expense, this program will enable BNP to look into the possibility of insurance coverage.

Due to rapid changes occurring in the markets, continuous adjustments must be made to control systems, report procedures, and computer applications in order to put these principles into operation. BNP develops new products and businesses taking operational risk into account.

Model Risk

BNP defines model risk as the risk of losses that results from incorrect use of price calculation, mark-to-market, position hedging or risk management tools, affecting the reliability of the models produced using these tools or the analyses performed based on the models.

In 1998, the Risk Policy and Industrial Research division was given the task of defining and implementing an in-house general model risk management methodology, representing a third level internal control, starting with the model risk associated with capital market activities.

During the year, the Risk Policy and Industrial Research division “model risk” team produced an overall quantitative estimate of the impact of model risks on capital market activities and performed a technical assessment of several models used by the Equity and Fixed Income lines of business.

The team’s short-term goal is to use the above information to perform an estimate by line of business of the extent of the capital market activities’ exposure to model risk based on highest exposure strategies.

Its medium-term objective is to set up maintenance and research programs to detect any erosion of quality and take into account the latest data. The team will also establish research and development management procedures for these models and, if necessary, modify the provisioning system for model risks.

Business and results of BNP'S main domestic subsidiaries

Banque de Bretagne

In millions of euros	% Change								
	1998	1997	1996	1995	1994	98/97	97/96	96/95	95/94
Customer loans									
(average outstandings)	941	881	817	775	656	6.8	7.9	5.4	18.1
Originations	257	276	211	222	233	(6.8)	30.7	(4.9)	(4.7)
Customer deposits									
(average balances)	838	790	743	742	659	6.0	6.3	0.2	12.5

Banque de Bretagne, which will celebrate its 90th anniversary in 1999, is the oldest-established regional bank in Brittany. The bank has 620 staff and 68 branches, 62 of them in Brittany. Following the takeover of CIC by the Crédit Mutuel group, it is the last remaining privately-owned non-mutual regional bank.

The bank has always remained loyal to its roots, and has made a significant contribution to the development of the region. According to a February 1998 Dun & Bradstreet survey, Banque de Bretagne was still the leading banker to the region's smaller businesses, in an over-banked market dominated by the mutuals.

As well as being a local retail bank on a human scale, Banque

de Bretagne offers all the services of a large bank via its association with BNP subsidiaries such as BNP Lease, BNP Gestions, Natio-Vie and Médiforce.

In 1998, the bank pressed ahead with the modernization of its branch network. Some branches were refurbished or repositioned, while fifteen new ATMs were installed and two new branches opened.

Banque de Bretagne has stand-alone IT systems, which made a smooth transition to the euro. The bank's reputation for innovation was maintained with the introduction of a credit scoring system that enables branches to make immediate decisions on applications for consumer credit.

BNP Lease

In millions of euros	% Change							
	1998	1997	1996	1995	98/97	97/96	96/95	
Credits outstanding at 31 December	8,308	8,043	7,819	7,464	3.3	2.9	4.8	
Inc. equipment	3,724	3,396	3,241	3,125	9.7	4.8	3.7	
Inc. real estate	3,233	3,265	3,257	3,178	(1.0)	0.2	2.5	
Originations	3,081	3,030	2,816	2,629	1.7	7.6	7.1	
Inc. equipment	1,947	1,693	1,564	1,387	15.0	8.2	12.7	
Inc. real estate	316	398	315	523	(20.4)	26.4	(39.9)	

Pro forma BNP Bail + Crédit Universel, excluding Arius and Europcar Lease.

The 28 May 1998 merger between BNP subsidiaries BNP Bail and Crédit Universel to form BNP Lease has given the Group a big advantage at a time of intense competition and restructuring in the leasing sector.

BNP Lease can now offer retail and corporate customers a complete range of financing solutions: loans; operating leases; finance leases for equipment, real estate and energy projects; long-term vehicle rental (via Europcar Lease), and flexible short-term and long-term management and financing of computer equipment (via Arius). BNP Lease is a powerful player, well positioned in highly competitive markets where a dynamic and thoroughly professional approach is the key to success.

1998 saw strong domestic demand and a 6%–7% rise in corporate productive investment.

Credits originated by BNP Lease during the year topped EUR 3 billion, up 1.7% on the previous year. Operating leases and equipment finance leases were 15% higher in a favorable market. Lending slipped by 13%, mainly in the extremely competitive car loans market. Real estate and energy project finance leases, which saw strong growth in 1997 (including two big leases worth EUR 86.9 million), were adversely affected as borrowers waited for the vote on the proposal in the Finance Act to lower capital transfer taxes in 1999. This business reported a 20.4% decline in 1998, with some large deals postponed until 1999.

Total credits outstanding (excluding doubtful loans) advanced by 3.3% to EUR 8.3 billion, with trends by sector mirroring the year-on-year change in origination volumes.

Meunier Promotion

In millions of euros	% Change										
	1998	1997	1996	1995	1994	1993	98/97	97/96	96/95	95/94	94/93
Commercial and industrial real estate	396	155	145	240	390	145	x 2.5	6.8	(39.4)	(38.5)	n.a.
<i>including client representation contracts</i>	396	149	101	218	264	79	x 2.7	47.7	(53.7)	(17.2)	n.a.
Residential real estate	251	155	79	79	154	162	61.7	97.3	(0.6)	(48.4)	(5.1)
Revenues of real estate partnerships	647	311	224	319	544	306	x 2.1	38.6	(29.8)	(41.3)	77.5

Results for 1998 confirmed Meunier's position as one of France's leading real estate developers, in both:

- residential real estate, with starts on 2,000 units and revenues of EUR 251 million;
- commercial and industrial real estate, launching 110,000 m² of office programs and generating revenues of EUR 396 million –at zero financial risk, because Meunier operates via client representation contracts, and hence bears only the technical risk.

The Meunier group continued to expand its property management business through specialized subsidiaries, which manage office and apartment buildings for owner-investors, as well as condominium owners' associations.

All the group's activities played a part in returning Meunier to a good level of profitability.

BNP Gestions

In millions of euros	1998	1997	1996	% Change
Fund management	33.8	27.0	26.7	25.2
Institutional management	35.2	28.8	25.5	22.6
Private asset management under management contract	16.6	12.8	10.4	30.7
	85.6	68.6	62.6	25.0

BNP's domestic institutional and fund management activities, carried on through the BNP Gestions subsidiary, employ 260 staff in France and reported satisfactory results in 1998.

The quality of our asset management skills was once again reflected in the performance of our products, and acknowledged by the *Corbeille Long Terme* award from *Mieux Vivre Votre Argent* magazine and the *Laurier d'Or*

award from *Investir* magazine for 5-year global management. The globalization of the business continued, with eight new mandates obtained from central banks and major international investors.

Total assets under management by the BNP Group, including Natio-Vie and private asset management, amounted to nearly EUR 85.6 billion at end 1998, 25% higher than at the previous year-end.

Natio-Vie

In billions of euros	% Change								
	1998	1997	1996	1995	1994	98/97	97/96	96/95	95/94
Assets under management at 31 December	23,071	20,134	15,682	11,972	9,098	14.6	28.4	31.0	31.6
Premiums written (including ASSU-VIE)	2,970	4,468	3,627	3,177	2,450	(33.5)	15.3	14.1	29.7
Number of policies (thousands)	1,550	1,490	1,390	1,320	1,244	4.0	7.2	5.3	6.1
Market share:									
Global	4.3%	5.7%	5.1%	4.9%	4.0%				
Branch network	7.5%	9.3%	8.6%	8.6%	7.1%				

1998 was a year of consolidation for Natio-Vie, with the amount of savings collected dipping in the wake of tax changes. Nonetheless, Natio-Vie improved profits and strengthened its balance sheet.

There was strong growth of 44% in sales of individual unit-linked contracts, thanks to the launch of attractive new products (*MultiPEP*, *Floréal* and *Europhonie*), which enabled large numbers of investors to tap into the fine performance of the stock markets.

A low volume of withdrawals and a relatively high level of funds collected led to healthy growth of 15% in assets under management, which stood at EUR 23.1 billion at year-end.

Natio-Vie reported a sharp rise in net income of 17.3% to EUR 72.4 million, and further strengthened its balance sheet. The capitalization reserve and the reserve for policyholders' shares in profits together now represent two-thirds of total equity, more than double the 1995 level.

These reserves, together with substantial unrealized capital gains, provide assurance that policyholders will continue to enjoy satisfactory returns in the future.

Natio-Vie is to launch a top-up healthcare insurance scheme in 1999, a further diversification following the move into death benefit and group retirement policies.

Banexi

	1998	1997	1996	1995	1994
Number of companies in the equity portfolio at 31 December	293	362	380	362 ⁽¹⁾	566
Portfolio valuation (In millions of euros)	733	705	675	716	572
Excluding funds managed for clients	579	579	542	592	471
Investments during the year (In millions of euros)	112	110	58	357	100
Number of M&A deals	66	62	57	72	84

(1) After deconsolidation of BNP Développement and inclusion of CFJPE.

Banexi operates in both fields of merchant banking: equity investment and fund management on the one hand, and financial advisory/mergers and acquisitions on the other.

During 1998, Banexi completed a reorganization program aimed at ensuring the independence of third-party private equity management activities, now handled by its subsidiary BNP Private Equity.

In mid-1998, BNP Private Equity launched its first venture capital fund, Banexi Ventures 2, which raised EUR 61 million. This is to be followed in 1999 by the launch of a general development fund and two specialized funds: a telecoms fund, and a mezzanine fund. The aim is to treble the amount of assets under management.

As sponsor, Banexi supports each new fund by subscribing 20%-30% of the capital raised, and also by investing directly when justified by the size of the investee company.

Despite the attractiveness of new listing opportunities –in particular the *Nouveau Marché* of the *Paris Bourse*– Banexi managed to invest slightly more than in 1997. Of the total of EUR 112 million invested, EUR 90.5 million went into industrial sectors, with the emphasis mainly on the telecoms, agribusiness and automotive sectors. The remaining EUR 21.5 million was invested in a variety of unlisted investment funds.

Hands-on portfolio management resulted in a reduction in the number of holdings, and the realization of EUR 75.8 million of capital gains on the disposal of assets worth EUR 124.4 million.

The financial advisory and M&A business increased its market share, against a backdrop of strong growth in deal

activity and tough competition from Anglo-Saxon banks.

With 66 done deals worth an estimated EUR 13.6 billion, Banexi reaffirmed its leading position in terms of number of deals and advanced from sixth to fourth place in the rankings based on volumes.

Notable assignments in 1998 included advising the shareholders of Comptoirs Modernes in connection with the takeover by Carrefour, preparing the valuations of France Télécom (for the second tranche of the privatization) and of Alstom (for the stock market flotation), and advising Vivendi on its merger with Havas.

BNP Factor

BNP Factor provides BNP's corporate customers with factoring expertise in France and abroad. The company handles commercial debt recovery for businesses, plus partial or total refinancing, and underwrites debts where customers' clients default. These services are enhanced by innovative computer and on-line services.

From this year, BNP Factor has been running the BNP Group's factoring worldwide business line. It has also signed a commercial co-operation agreement with a German factor and a UK factor.

In 1998, the highly concentrated and competitive French factoring market continued to expand rapidly, with similar growth to 1997 (20%).

Working closely with the branch network, which refers most of its business, BNP Factor once again posted a sharp increase in revenues, with accounts receivable purchased from small businesses up 34%. At the end of the year, there were nearly 1,200 active contracts.

Volume of accounts receivable in millions of euros and annual growth rate:

	1994	1995	1996	1997	1998
In millions of euros	931	1,505	1,664	2,125	2,373
% growth ⁽¹⁾	—	62	11	28	12

(1) BNP Factor was set up in 1994.