

Treasury and Financial Markets

THE TREASURY AND FINANCIAL MARKETS business line looks after the short and long-term financing of the Group and enables clients of the Group's commercial business lines to be offered a vast range of capital market products.

In view of the extent and quality of its bond issues, the majority with AAA ratings, Dexia occupies a recognized position on the international capital markets.

In 2004, Dexia was classified in fourth place for local authority bond issues.

This business line is also active on its own account, in particular through the management of a bond portfolio the credit quality of which is excellent and the risk profile low.





**EUR 28.9
billion**

**Total amount of long-term bonds
issued by Dexia in 2004**

—

**EUR 43.9
billion**

**Total amount of the credit
spread portfolio**

—

AAA

**More than 65% of bonds
issued by Dexia have
an AAA rating**

—

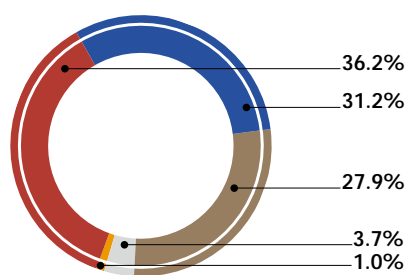
4th

**Dexia is classified
in fourth place
for local authority
bond issues in euro**

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Presentation and business review

CREDIT SPREAD PORTFOLIO QUALITY



- AAA
- A
- AA
- BBB
- Non-investment grade

BREAKDOWN BY ISSUER IN 2004

(in billions of EUR)

Dexia Municipal Agency ⁽¹⁾	8.5
Dexia Crédit Local	3.3
Dexia Bank Belgium	1.2
Dexia BIL	0.7
Dexia Crediop	5.4
Dexia Hypothekenbank Berlin	9.8
Total	28.9

(1) Dexia Municipal Agency is a registered company of the Dexia Group which issues mortgage bonds (collateralized bonds with first-quality assets).

The primary objective of the Treasury and Financial Markets business line is to provide support for the Group's other business lines and also to operate as a full-fledged profit center.

Treasury and Financial Markets makes short-term money market products and long-term funding available to the Group in order to bolster the growth of its balance sheet.

Demonstrating constant ability to innovate, Treasury and Financial Markets teams develop a broad range of capital market products (fixed income, structured products based on interest rates, foreign exchange, securitization) for the clients of the Group's commercial business lines (local governments, corporate investors, private and retail banking customers and fund managers), but also for its own institutional customers (banks, insurance companies) which are monitored by specialized salesmen delivering a tailor-made service.

These teams also manage a bond portfolio (credit spread portfolio), which helps assure Dexia of a high degree of liquidity and generates a large portion of earnings in this business.

Long-term funding

In 2004, the Group issued long-term bonds in the amount of EUR 28.9 billion (versus EUR 21.5 billion in 2003), with an average life of slightly more than 7 years.

The Group continued to benefit from its AAA-rated issuers – Dexia Municipal Agency and Dexia Hypothekenbank Berlin – to meet its funding requirements. Total AAA-rated covered bond issues amounted to EUR 18.3 billion in 2004, with an average life of 8 years.

Credit spread portfolio ⁽¹⁾

This portfolio has been built up over time as a source of income and also serves as a liquidity buffer that provides flexibility for long-term funding programs.

Short-term paper, previously managed by the money market team, was transferred to the credit spread portfolio in 2004 in the amount of slightly more than EUR 5 billion. At the end of 2004, the portfolio managed EUR 43.9 billion. On a pro-forma basis, the total outstanding was down EUR 1.6 billion, mainly owing to the depreciation of the US dollar vis-à-vis the euro, due to the fact that half of the portfolio is composed of in USD-denominated assets.

At the end of 2004, the average life of the portfolio was 5.3 years. The portfolio can boast of good credit quality (more than 95% is rated A or higher).

The portfolio is mainly invested in floating rate notes and asset swaps, with exposure to financial institutions (49%), asset-backed securities (29%), sovereign and local government issues (20%) and corporate borrowers (2%).

Money market

The basic objective of this activity line is to meet the Group's short-term funding needs by using various instruments such as commercial paper programs both USD and EUR denominated, certificates of deposit (CD) programs, the inter-bank market and repurchase agreements (REPO). Outstanding commercial paper and certificates of deposit totaled EUR 23.6 billion at the end of 2004 (versus EUR 21.0 billion at the end of 2003). The second objective is the management of the Group's liquidity in the main currencies and of its short-term interest rate positions.

Fixed income

This activity mainly involves the origination and syndication of bond issues for local government clients, as well as for the Group. For example, Dexia Capital Markets⁽²⁾ acted as joint lead manager for the Region of Catalonia (EUR 500 million) and as joint book-runner and joint lead manager for several Italian local governments, including issues for the City of Rome (EUR 400 million) and the Region of Abruzzi (EUR 250 million). In 2004, Dexia ranked fourth for local governments bonds issued in euro. In 2003, Dexia was twelfth on the list.

Financial engineering and derivatives

This activity line targets two objectives: on the one hand, the development of structured products for clients of the Group's commercial business lines (local authorities and their affiliates as well as private individuals) and, on the other, the management of trading and hedging positions on interest rates and equity derivatives. An example would be the development of inflation-related products for large local governments in Europe and shareholding plans for corporate clients in Belgium.

Foreign exchange

This activity line supplies Group's clients (mainly fund managers and corporate clients) with products in both cash and derivatives markets. It provides solid backing for the clients of Dexia Fund Services, for whom optimized market tools were developed in 2004.

Securitization

Exploiting skills developed in the United States in the securitization of commercial mortgage loans, Dexia has developed securitization in Europe, mainly focusing on public finance applications. The Group acts as adviser and/or arranger for this type of transactions. For example, in 2004, Dexia was the sole arranger of a real estate securitization program for an Italian region.

Securities brokerage

This activity aims at providing the Group's institutional clients (banks, insurance companies, asset managers, companies and so on) with a high-quality service for their transactions involving the purchase and sale of shares and share derivatives. Research capacity and reliability in execution are the key elements of this service provided in Paris, Brussels, Luxembourg and Spain (via Bancoval).

(1) The credit spread portfolio is a proprietary trading bond portfolio designed to generate a stable credit margin. This portfolio is managed without any exposure to interest rate risk.

(2) Dexia Capital Markets is a brand name used in the capital markets to promote Dexia's name in different compartments.

Financial results of the business line

The analysis hereafter is based on the underlying data (i.e. excluding nonrecurring items) for this business line, in order to allow a better understanding of the fundamental trends of the business line. Items considered nonrecurring are detailed in the financial results on pages 62 and 63.

Treasury and Financial Markets had a very good year, in progression when compared to the previous year (gross operating income up 11.9% in one year, and up 15.3% at constant exchange rate) despite a high level in 2003, boosted by one-off items. This good performance was achieved thanks to increasing revenues and decreasing operating expenses.

This business line reported a 9.0% growth in earnings for the full year 2004 on the previous year (+12.4% at constant exchange rate). **Net income** for the full year stood at EUR 283 million.

Main contributors are the credit spread portfolio, representing 63% of total business line's earnings, followed by money market activities (17%) and financial engineering and derivatives (8%).

Revenues for the full year 2004 amounted to EUR 531 million, up 4.2% (or +6.5% at constant exchange rate). This is a very good performance, recalling that 2003 revenues were boosted by capital gains accounted

for following the closure of proprietary management activities (EUR 12 million in the first quarter of 2003). Provisions were reversed in the bond portfolio in the context of tightening spreads that took place in 2004.

Costs were reduced by 8.5%, to EUR 177 million for the full year 2004. This results from the downsizing of some activities and the positive effects of the integration at Dexia Bank Belgium, causing, among other, reallocations of central overheads which were, this year, more favorable to the business line.

Gross operating income amounted to EUR 354 million for the full year (+11.9% and +15.3% at constant exchange rate).

The **cost-income ratio** improved in 2004, and reached 33.4% for the full year against 38.0% in 2003.

Corporate income tax amounted to EUR 89 million for the full year 2004, up 51.1% in one year. This significant increase is explained by both better operating income, and by the regularization in the tax treatment, in the past, of derivative products, resulting in a EUR 13 million charge accounted for in the fourth quarter of 2004.

Return on economic equity⁽¹⁾ (ROEE) improved and stood at 31.6% in 2004.

(1) Net income before minority interests as a percentage of allocated equity at the end of the period.



UNDERLYING STATEMENT OF INCOME ⁽¹⁾

(excluding nonrecurring items)

(in millions of EUR)	2003	2004	Evolution
Revenues	510	531	+4.2%
- Net interest and related income	479	492	+2.7%
<i>of which interest on EEA ⁽²⁾</i>	53	48	-9.5%
- Net commissions and other income	31	39	+26.3%
- Technical and financial margin of insurance activities	0	0	n.s.
Costs	(194)	(177)	-8.5%
Gross operating income	316	354	+11.9%
Cost of risk	5	21	x4.2
Operating income	321	374	+16.6%
Net gains & recoveries on long-term investments	0	0	n.s.
Corporate income tax	(59)	(89)	+51.1%
Income from equity-accounted companies	0	0	n.s.
Net income before minority interests	262	285	+8.9%
Minority interests	2	2	n.s.
Net income	260	283	+9.0%
Cost-income ratio	38.0%	33.4%	
ROEE ⁽³⁾	27.2%	31.6%	
Allocated equity (end of period)	966	904	

(1) Pro forma for full year 2003.

(2) Economic Equity Allocated.

(3) Return on Economic Equity.