

# chairman's letter to the shareholders

*"Building sustainable value involves decisively embracing a dynamic where unrelenting growth is the driver."*



*Dear Shareholders,*

It is an honour for me to report to you for the first time as Chairman of Banco de Chile. In a favorable environment, both globally and domestically, our Bank met numerous of its objectives during 2005. With growth in national product of over 6%, the highest in the last eight years, increasing investment and solid institutions, Chile enjoys prestige and responsibility in its financial and commercial behaviour, enabling it to reach agreements of mutual benefit with important regions of the world which pledge us to more and better achievements.

In the light of this global, but also individual, commitment, the year 2005 has been a milestone in the performance of our organization. This has positioned us, for the second consecutive year, as the most profitable bank in the Chilean financial system, achieving a return on capital of 30%, far above the average for the system.

With a real growth of 14% over the net income produced in 2004, Banco de Chile increased its share in the overall results of the financial system, contributing more than 23% of the banking industry's net income. This performance, which is not only extraordinary compared with its peer group but also from the perspective of its own history, has the additional merit of having simultaneously combined with other undertakings that most surely will constitute fundamental pieces in the future development of our Corporation.

The successful replacement in the market of 2.5% of the Bank's shares, previously acquired in April 2004, certainly marked a high point for the year. With the shares oversubscribed several times, the sale of the 1,702 million shares at a price of Ch\$ 34.50 per share was completed in August. Through a public offering process, whereby an order book was auctioned on the Santiago Stock Exchange, Banco de Chile openly and transparently allocated the demand, assigning the shares offered to more than 3,000 shareholders and receiving a total of over Ch\$ 58 billion, equivalent at the time to approximately US\$ 105 million.

The whole process of buying and later replacing its own shares not only had the merit of permitting the Bank to optimize its equity base, thus promoting the return for its shareholders, but also experiencing and confirming the Corporation's ability to increase its capital base when it needs to, counting with the support of the investor community and with a clear and proven mechanism for this purpose.

During its 112 years of history, our Corporation has not only shown an outstanding position in financial management but, perhaps even more important, it has exercised firm leadership in matters that, throughout our history, have laid the foundations for the development of our society.

Transparency and correctness in our daily tasks, firm support for the institutions, social responsibility, commitment to equality of opportunities and the pursuit of healthy lives at the individual and collective levels are some of the values that sustain the development of our business and which have enabled Banco de Chile to occupy an important place in the commercial preferences of the individuals and companies of Chile.

The Board which I preside is conscious that effectiveness in corporate governance goes further than faithfully complying with legal obligations and even best practices. It also involves an active contribution to the organization's performance by reinforcing values, persevering in them and advising management in the search for greater long-term profit for our shareholders. It is in this context that we perceive most positively the substantial progress made in matters of compliance and control. We have strongly and pro-actively responded to the requirements set down, in particular by the regulators of our branches in New York and Miami, in matters like the reporting of sensitive transactions and the prevention of asset laundering, to name just two aspects.

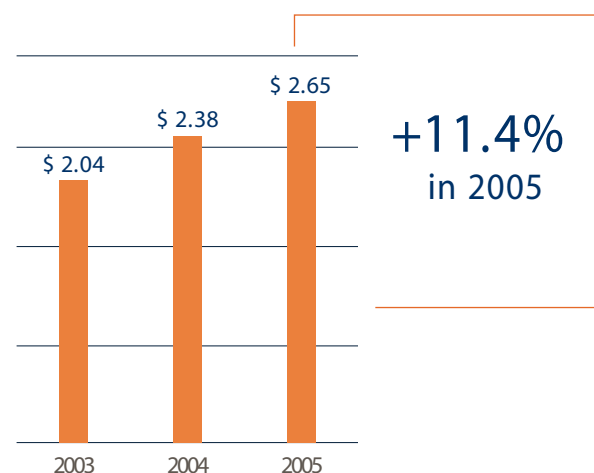
The creation of a new Global Compliance Division, reporting directly to this Board through its Directors' and Audit Committee, the action plan prepared by the United States regulators and its complete step-by-step implementation, and the large investment in operative and information systems that provide the intelligence necessary for a correct business management, are all actions that enable us to be confident that the delicate situations lived, for the first and only time in the history of the branches of Banco de Chile in the United States, will have served as an opportunity to revise, reinforce and persevere with our commitment to excellence in all its aspects.

In recent years, the financial industry has experienced a large number of different incentives. The growing demand by customers for better and more convenient financial options has led to significant changes in the sector. We expect further consolidation among banks and also the greater incorporation of new participants. It is also possible to imagine new alliances between financial corporations and leading companies in other industries like, for example, the retail business, insurance, pension management and telecommunications.

These growing dynamics will not only open up a range of new businesses for financial providers but also the entry of a wide spectrum of new users to the universe of individuals and companies currently served by banks. Potential customers, beginning with determination- and a greater capacity for discrimination- in the use of financial products, micro-businessmen seeking support for their enterprises and benefiting from an auspicious environment, will be added to the traditional segments of individuals and companies that today show reasonable equity levels, capable of sustaining interesting growth rates in their operations. In all, an extensive and intensive broadening of the possible banking areas.

## Earnings per share

(CH\$ at December 31, 2005)



Number of shares year 2003 and 2005: 68,080 million.  
Number of shares year 2004: 66,378 million.

In this scenario, building sustainable value involves decisively embracing a dynamic where unrelenting growth is the driver. The commercial strategy, designed some years ago now and which has permitted the focusing of commercial efforts on those most profitable market segments having also the greatest growth potential, was significantly strengthened during 2005. A new organizational structure that responds to these strategies with greater agility was implemented. More emphasis on the retail segments, both individuals and small and middle-sized companies, a greater integration of the products of subsidiaries into the Bank's network, strengthening the distribution network and, in particular, the remote channels, are the pillars for obtaining the best portfolio composition that will allow us to continue increasing our volumes while retaining interesting profitability levels.

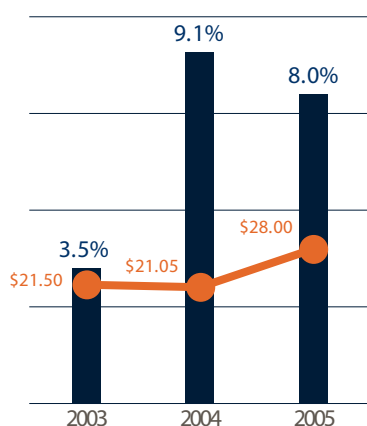
The challenges we will have to face in this area are various. On the one hand, the Board I preside will have to balance justly and wisely, but also farsightedly, the capital equation that will enable us to support the desired growth.

# chairman's letter

Capital needs will be the consequence not only of larger business volumes but of the new regulations arising from the Basle agreements, known as Basle II. With a view to strengthening financial systems at the global level, higher capital requirements have in practice been put in place for equal business volumes. We should therefore provide the management with the capital structure needed for sustaining our projects, whether by discreet increases in the capital base or through the partial capitalization of earnings.

The high returns that Banco de Chile has managed to generate in recent years make it reasonable to consider compensation policies for our shareholders that combine the distribution of dividends with the issue and distribution of new shares. This formula not only allows our investors to preserve a high dividend yield but to increase their effective participation in our company, at the same time satisfying the objective of providing a larger capital base to support the substantial levels of projected growth.

## Dividend yield



The dividend yield ■ for the year, takes into account the next income and the ex-dividend share price ● of the previous year, both in constant pesos.

It is in this context that the Board has resolved to propose to the shareholders' meeting the distribution of the net income for 2005 by paying a cash dividend for the equivalent of 70% of net income and the remaining 30% through the distribution to shareholders, and further capitalization, of its equivalent in shares. These shares will be valued at the weighted average price of the share over the 60-day period prior to the year-end, after deducting earnings per share for the year.

It is my conviction that, whichever the route chosen, the variable that finally permits us to maintain the support of our investors is the organization's capacity to provide adequate returns on investment. To this avail, operating efficiency will keep up being one great challenge. While the performance of Banco de Chile, with its non-consolidated efficiency ratio of 50% for 2005, was better than the financial system as a whole, we are conscious that we still have space for improvement when comparing ourselves with international standards. Despite the numerous, and successful efforts made in the control and reduction of costs, the principal driver to greater efficiency is an increase in revenues under equal productive capacity.

And that is the direction to which our business model and its corresponding organizational structure are pointed. The possibility of adding large business volumes without sacrificing the service quality to which we are committed, and with efficiency levels that make us profitable, require the intensive use of technology. Since its origination, as a result of identifying customers' potential and needs; to the processing of large homogenous volumes of transactions, maintaining the capacity to identify specific situations; passing through the sales stage with tariffs in line with the cost of the service provided, the challenge has to rest on intelligent information systems that add value to our relationship with the customer. Overall, we have to be capable of providing our customers with what it is they need, on a timely basis and on competitive terms. This is the purpose of our project of technological change, which we have called Neos and which has been gradually introduced since 2004. With a total investment of close to 50 million dollars, the plan will enable us to expand our business base while optimizing the cost structure.

These important undertakings at the level of our organization are no more than additional to a series of matters that are being discussed at the industry level and lead us to expect that 2006 will be particularly challenging. This is the case of the initiatives contemplated in the bill for the Reform of Capital Markets II and which is designed

# The Chile we all want

to modernize and make corporate governance rules more efficient, like: greater safeguards for the interests of minority shareholders in situations of conflicts of interest, redefinition of the concept of privileged or confidential information in the securities market and greater demands for quality in the information provided by corporations, among other proposals. In the business area, the bill puts forward interesting matters like those relating to the better development of the risk capital industry and the introduction of new pension saving options and incentives.

We have ended 2005, a year of great achievements and efforts, receiving also important compensations. Among other recognitions, our Bank was named, for the second consecutive year, as The Bank of the Year by "The Banker" magazine, a member of the Financial Times Group, which awards prizes to institutions that have been outstanding in their performance, technological innovation and business strategy. On behalf of the Board which I preside, I should like to thank all our staff for these achievements which are not just a reflection of their quality of work but of their identification with our principles and values.

Our Corporation also recognizes its role in the community and its efforts in this area are focused on producing a social benefit that is sustainable over time. We feel satisfied to be able to provide concrete support for social, cultural and educational activities. We have participated actively since late 2004 in the San José de Lampa College educational project which seeks to provide an education of excellence to the country's lower-income sectors. This effort is in addition to the known support that Banco de Chile, and its thousands of employees, voluntarily provide for the Teletón project and, more recently, to the Fondo Esperanza program. This last initiative has captured our enthusiasm as a seed in the financial business area where we hope it to be the origin of numerous enterprises based on the individual projects of those with fewer resources.

We firmly believe that work well done, jointly with these and other projects will contribute to building the Chile we dream of.

Together with management, directly responsible for our achievements, we shall continue to persevere with these values and common objectives that have made it possible to give shape to the largest and oldest domestic bank in the Chilean financial system.

Finally, a special thanks to you, our shareholders. With your support, Banco de Chile will continue to grow and prosper. We will work to return your trust and we will continue to make every effort to strengthen a long-term, fructiferous and mutually beneficial relationship.



**Fernando Cañas**  
Chairman of the Board