22A Management's discussion and analysis
67A Consolidated financial statements
103A Supplementary information

CANADIAN GAAP

FINANCIAL REVIEW

Caution regarding forward-looking statements
From time to time, we make written and oral forward-looking statements within the meaning of certain securities laws, included in this Annual Report, in other filings with Canadian regulators or the U.S. Securities and Exchange Commission, in reports to shareholders and in other communications. These forward-looking statements include, among others, statements with respect to our objectives for 2004, and the medium and long terms, and strategies to achieve those objectives, as well as statements with respect to our beliefs, plans, expectations, anticipations, estimates and intentions. The words "may," "could," "should," "would," "suspect," "outlook," "believe," "anticipate," "estimate," "expect," "intend," "plan," and words and expressions of similar import are intended to identify forward-looking statements.

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks exist that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers not to place undue reliance on these statements as a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements. These factors include, but are not limited to, the strength of the Canadian economy in general and the strength of the local economies within Canada in which we conduct operations; the strength of the United States economy and the economies of other nations in which we conduct significant operations; the effects of changes in monetary and fiscal policy, including changes in interest rate policies of the Bank of Canada and the Board of Governors of the Federal Reserve System in the United States; the effects of competition in the markets in which we operate; inflation; judicial decisions; capital market and currency market fluctuations; the timely development and introduction of new products and services in receptive markets; the impact of changes in the laws and regulations regulating financial services (including banking, insurance and securities); changes in tax laws; technological changes; our ability to complete strategic acquisitions and to integrate acquisitions; judicial or regulatory proceedings; changes in consumer spending and saving habits; the possible impact on our businesses of international conflicts and other developments including those relating to the war on terrorism; and our anticipation of and success in managing the risks implicated by the foregoing.

We caution that the foregoing list of important factors is not exhaustive. When relying on our forward-looking statements to make decisions, investors and others should carefully consider the foregoing factors and other uncertainties and potential events. We do not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by us or on our behalf.

This portion of the Annual Report provides a discussion and analysis of our financial condition and results of operations so as to enable a reader to assess material changes in financial condition and results of operations for the 12 months ended October 31, 2003, compared to those of the 12 months ended October 31, 2002. The consolidated financial statements prepared in accordance with Canadian generally accepted accounting principles (GAAP) are on pages 67A to 102A.

In the fourth quarter of 2003, we changed the presentation of revenues and expenses of RBC Insurance and Royal Bank of Canada, without any effect on net income, to provide additional disclosures, which, we believe, make our disclosure more consistent with disclosure practices in the insurance industry. All comparative information has been appropriately reclassified. Total insurance revenues are now reported in non-interest income as insurance premiums, investment and fee income. Previously they had been reported in net interest income and in several lines of non-interest income, the largest of which was insurance revenues. The costs associated with generating these revenues are now captured in insurance policyholder benefits, claims and acquisition expense, whereas previously they were netted against the insurance revenues line in non-interest income. The administrative costs of RBC Insurance continue to be reported in non-interest expense. The table on page 30A provides a further breakout of these lines, and the accounting policies related to our insurance operations are contained in Note 1 to the consolidated financial statements on page 75A.

Our fiscal year-end is October 31. All dollar amounts in management's discussion and analysis are in Canadian dollars, unless otherwise specified.

Overview

TABLE 1 Net income and diluted earnings per share (EPS)

(C$ millions, except per share and percentage amounts)	% change	2003	2002
Net income	9%	$ 3,005	$ 2,762
EPS	12%	$ 4.39	$ 3.93

As shown in the table above, net income in 2003 increased $243 million or 9% over 2002 despite a $60 million decline in net income due to the strengthening of the Canadian dollar relative to the U.S. dollar, which resulted in a lower translated value of U.S. dollar-denominated earnings. The Canadian dollar appreciated 9% relative to the U.S. dollar, averaging US$.697 in 2003 compared to US$.637 in 2002. The movement of the Canadian dollar compared to currencies other than the U.S. dollar had a minimal impact on the change in our earnings compared to a year ago.

The higher net income in 2003 predominantly reflected a reduction in the provision for credit losses of approximately $220 million after-tax.

Diluted earnings per share were $4.39, up $.46 or 12% from a year ago, with approximately $.04 of the increase due to a reduction in the number of common shares outstanding, primarily as a result of the repurchase of common shares, which is discussed on page 59A. The stronger Canadian dollar reduced diluted earnings per share by $.09 in 2003.

As shown in Table 2 below, our 2003 revenues continue to be diversified, with revenues from outside Canada totalling $6.9 billion or 39% of revenues, including U.S. revenues of $4.8 billion or 28% of total revenues.

Canadian net income declined by $32 million or 2%, reflecting lower earnings from the domestic capital markets operations. U.S. net income increased by $238 million or 155%, largely due to stronger performance from RBC Dain Rauscher's full-service brokerage and fixed income businesses and a $45 million after-tax decline in retention compensation costs, as well as a significantly lower provision for credit losses related to our business and government loan portfolio. Other international net income was up $37 million or 7% from 2002, reflecting higher earnings from the international reinsurance business.

TABLE 2 Earnings by geographic segment

	2003				2002			
(C$ millions)	Canada	United States	Other International	Total	Canada	United States	Other International	Total
Net interest income	$ 5,186	$ 1,188	$ 268	$ 6,642	$ 5,472	$ 1,106	$ 357	$ 6,935
Non-interest income	5,382	3,618	1,776	10,776	4,969	3,682	1,669	10,320
Total revenues	10,568	4,806	2,044	17,418	10,441	4,788	2,026	17,255
Provision for credit losses	527	106	88	721	529	440	96	1,065
Insurance policyholder benefits, claims and acquisition expense	679	580	437	1,696	498	502	535	1,535
Non-interest expense	5,992	3,511	906	10,409	5,920	3,676	824	10,420
Income taxes (1)	1,316	217	54	1,587	1,408	16	49	1,473
Net income	$ 2,054	$ 392	$ 559	$ 3,005	$ 2,086	$ 154	$ 522	$ 2,762

(1) Includes non-controlling interest in net income of subsidiaries.

Outlook

We are targeting growth in diluted earnings per share of 10–15% and a return on common equity of 17–19% in fiscal 2004 based on the expectations that our cost management and revenue enhancement efforts will allow expenses to grow at a lower rate than revenues and that business and capital market conditions will continue to improve in 2004.

Financial priorities

Revenue growth and diversification

In 2003, total revenues were up $163 million or 1% from a year ago, despite a $510 million decline in the translated value of U.S. dollar-denominated revenues due to the significant appreciation of the Canadian dollar relative to the U.S. dollar. The increase in revenues largely reflects higher insurance premiums, investment and fee income, and higher trading revenues in 2003. A detailed discussion follows on pages 38A to 41A.

Cost control

Non-interest expense was $11 million lower in 2003. While the stronger Canadian dollar relative to the U.S. dollar reduced the translated value of non-interest expense by $340 million, there were increases in pension and other postretirement benefit costs, costs related to further automating our retail banking technology infrastructure and expanding our retail sales force, and costs related to companies we acquired during the year. A full discussion is provided on pages 42A to 44A.

Strong credit quality

Provisions for credit losses declined by $344 million or 32% and gross impaired loans by $543 million or 24% this year due to a significant improvement in the quality of our corporate loan portfolio. Detailed discussion and tables can be found on pages 45A to 52A.

Balance sheet and capital management

Total assets were $403.0 billion at October 31, 2003, up $26.1 billion or 7% from October 31, 2002. At October 31, 2003, using Superintendent of Financial Institutions Canada (OSFI) guidelines and Canadian GAAP financial information, our Tier 1 capital ratio was 9.7% versus 9.3% at October 31, 2002, while the Total capital ratio was 12.8% versus 12.7%. Both ratios were above our medium-term (three- to five-year) capital goals of 8–8.5% for Tier 1 capital and 11–12% for Total capital. More details are provided on pages 58A to 60A.

Factors that may affect future results

There are numerous factors, many beyond our control, that could cause results to differ significantly from our expectations. Some of these factors are described below. Other factors, including credit, market, liquidity, insurance, operational and other risks are described in the Risk management section beginning on page 53A.

By their very nature, and as noted in the "Caution regarding forward-looking statements" on page 21A, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks that predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers not to place undue reliance on such statements in this management's discussion and analysis as a number of important factors could cause actual results to differ materially from the plans, objectives, goals, targets, expectations, estimates and intentions expressed in such forward-looking statements.

Industry and non-company factors

As an integrated financial services company conducting business in Canada, the United States and other countries, our revenues and earnings are affected by the health of the economic, business and capital markets environments specific to the geographic regions in which we conduct business.

Factors such as interest rates, inflation, exchange rates, consumer spending, business investment, government spending, the health of the capital markets, and terrorism impact the business and economic environment and, ultimately, the amount of business we conduct in a specific geographic region. For example, in an economic downturn characterized by higher unemployment, lower family income, lower corporate earnings, lower business investment and consumer spending, the demand for our loan and other products would be adversely affected and the provision for credit losses would likely increase, resulting in lower earnings. Similarly, a downturn in the equity markets could cause a reduction in new issue and investor trading activity, assets under management (AUM) and assets under administration (AUA), resulting in lower fee, commission and other revenues.

Our earnings are affected by the monetary policies of the Bank of Canada and the Board of Governors of the Federal Reserve System in the United States.

Bond and money market expectations about inflation and central bank monetary policy decisions have an impact on the level of interest rates, which can have an impact on earnings. Our policy for the non-trading balance sheet is to manage the interest rate risk to a target level. We have defined this target level as a risk neutral balance sheet where the interest rate exposures of most assets and liabilities are matched, with the residual assets representing a notional investment of equity spread evenly across a term of 60 months. As a result, our interest rate risk profile has slightly faster repricing of assets than liabilities. Consequently, a decline in interest rates would tend to reduce the net interest income earned on our non-trading portfolio as shorter-term assets reprice and to increase the value of our longer-term assets. Conversely, an increase in interest rates would result in an increase in the net interest income and a decrease in the value of our longer-term assets. For a more complete discussion of interest rate risk and its potential impact on our non-trading portfolio, please refer to the discussion of asset/liability management activities in our non-trading portfolio on page 61A. For a more complete discussion of interest rate risk and its potential impact on our trading business, please refer to the discussion of trading activities on page 55A.

Our performance can be influenced by the degree of competition in the markets in which we operate.

The competition for clients among financial services companies in the consumer and business markets in which we operate is intense. Customer loyalty and retention can be influenced by a number of factors, including relative service levels, the prices and attributes of products or services, and actions taken by competitors. Non-financial companies can provide consumers with the option to pay bills and transfer funds without involving banks. Such disintermediation could reduce fee revenues.

Changes in the statutes, regulations and regulatory policies that govern activities in our various business lines could impact our results.
Regulations are in place to protect the financial and other interests of our clients. Changes to statutes, regulations or regulatory policies, including changes in the interpretation or implementation of statutes, regulations or regulatory policies, could affect us by increasing the ability of competitors to compete with the products and services we provide. In addition, our failure to comply with applicable statutes, regulations or regulatory policies could result in sanctions and financial penalties by regulatory agencies that could adversely impact our reputation and earnings.

Although we take what we believe to be reasonable measures designed to ensure compliance with governing statutes, laws, regulations and regulatory policies in the jurisdictions in which we conduct business, there is no assurance that we will always be in compliance or deemed to be in compliance. Accordingly, it is possible that we could receive a judicial or regulatory judgment or decision that results in fines, damages and other costs that would have a negative impact on our earnings.

Failure to obtain accurate and complete information from or on behalf of customers and counterparties could adversely impact our results.
When deciding to extend credit or enter into other transactions with customers and counterparties, we may rely on information provided to us by or on behalf of customers and counterparties, including audited financial statements and other financial information. We also may rely on representations of customers and counterparties as to the completeness and accuracy of that information. Our financial condition could be adversely impacted if the financial statements on which we rely do not comply with generally accepted accounting principles (GAAP) or are materially misleading, and if customers or counterparties default on amounts owing to us.

Company specific factors

Our financial performance will be influenced by our ability to execute our U.S. expansion and integration strategy.
The first phase of our U.S. expansion strategy entailed putting together the original building blocks by acquiring businesses largely in the personal and commercial banking, insurance, and wealth management areas. The second phase entails adding to these original building blocks through additional strategic acquisitions, branch openings, greater market penetration, new product and service offerings, heightened marketing and sales initiatives, and more client referrals between the companies operating in our different business lines. It also entails achieving cost synergies through the integration of the back-office and head office functions of our business units. Although we regularly explore opportunities for strategic acquisitions of companies in our lines of business, there is no assurance that we will be able to continue to complete acquisitions on terms and conditions that satisfy our investment criteria. While results to date have generally met our targets, there is no assurance we will continue to achieve anticipated cost synergies from the integration of acquired companies. Our performance is contingent on retaining the clients and key employees of acquired companies, and there can be no assurance that we will always succeed in doing so.

The accounting policies and methods we utilize determine how we report our financial condition and results of operations, and they may require management to make estimates or rely on assumptions about matters that are inherently uncertain.
Our financial condition and results of operations are reported using accounting policies and methods prescribed by GAAP. In certain cases, GAAP allows accounting policies and methods to be selected from two or more alternatives, any of which might be reasonable, yet result in our reporting materially different amounts.

Management exercises judgment in selecting and applying our accounting policies and methods to ensure that, while GAAP compliant, they reflect our best judgment of the most appropriate manner in which to record and report our financial condition and results of operations. Significant accounting policies to the consolidated financial statements are described on pages 72A to 76A.

As detailed on pages 25A to 26A, two accounting policies have been identified as being "critical" to the presentation of our financial condition and results of operations as they (1) require management to make particularly subjective and/or complex judgments about matters that are inherently uncertain and (2) carry the likelihood that materially different amounts could be reported under different conditions or using different assumptions and estimates. These critical accounting policies relate to adequacy of our allowance for credit losses and the determination of the fair value of certain of our financial instruments.

Other factors

Other factors that may affect future results include changes in trade policy, the timely development and introduction of new products and services in receptive markets, changes in tax laws, technological changes, unexpected changes in consumer spending and saving habits, and our anticipation of and success in managing the associated risks.

We caution that the foregoing discussion of factors that may affect future results is not exhaustive. When relying on forward-looking statements to make decisions with respect to Royal Bank of Canada, investors and others should carefully consider the foregoing factors, other uncertainties and potential events, and other external and company specific factors that may adversely affect future results and the market valuation placed on our common shares. We do not undertake to update any forward-looking statement, whether written or oral, that may be made from time to time by us, or on our behalf.

Critical accounting policies

Application of critical accounting policies

Our significant accounting policies are contained in Note 1 to the consolidated financial statements on pages 72A to 76A. Certain of these policies are recognized as critical accounting policies because they require us to make particularly subjective or complex judgments about matters that are inherently uncertain and because of the likelihood that materially different amounts could be reported under different conditions or using different assumptions. Our critical accounting policies relate to the allowance for credit losses and the fair value of certain financial instruments. They have been reviewed and approved by our Audit Committee, in consultation with management, as part of their review and approval of our significant accounting policies.

Allowance for credit losses

The allowance for credit losses of $2,164 million reflects management's estimate of probable losses in our loan and off-balance sheet portfolios at October 31, 2003. This comprises a specific allowance of $757 million and a general allowance of $1,407 million as outlined in Note 6 on page 82A. Provisions for credit losses, which are charged to the income statement, increase the allowance, while write-offs net of any recoveries reduce the allowance. We determine and maintain the allowance based on a comprehensive and systematic review of our lending and off-balance sheet portfolios. As outlined in Note 1 on page 73A, the allowance is determined based on management's identification and evaluation of problem accounts and estimation of probable losses that may exist in the remaining portfolio.

Specific allowance – This is maintained to absorb losses relating to both specifically identified borrowers and pools of homogeneous loans that include loans that have been recognized as impaired. The losses relating to identified large business and government debtors are estimated on an account-by-account basis based on the present value of expected cash flows. Management's judgment is required when forecasting the amount and timing of future cash flows, determining the fair value of any underlying security, estimating the costs of realization, assessing observable market prices, and determining expectations about future prospects of the borrower and any guarantors on loans specifically identified as impaired. The losses relating to other portfolio-type products, excluding credit cards, which are directly written off after 180 days in arrears, are estimated based on the historical net write-off experience. This amount represents the average percentage lost on impaired balances and is based on past history and management's judgment.

General allocated allowance – The general allocated allowance, which is reviewed on a quarterly basis, represents our best estimate of probable loan losses that have been incurred within the portfolio on loans not yet specifically identified as impaired. The size of this allowance is dependent largely on the quality of the portfolio and economic conditions.

The methodology we employ to determine the general allocated allowance for business and government loans is supported by several parameters, such as the expected default frequencies associated with each borrower's risk rating, loss in the event of default and exposure at default. These parameters, which allow us to generate a range of probable credit losses within the portfolio, are based on historical experience and are supported by external data. Management judgment and other supporting factors are then applied to determine the general allocated allowance within the range of probable credit losses. An adverse change in any of the above parameters would affect the range of probable credit losses derived and may have a similarly adverse impact on our general allocated allowance, while a favourable change may have a similarly corresponding impact. For more homogeneous loans, probable losses are estimated based upon historical migration and write-off rates we have experienced on each portfolio. Management uses this information in conjunction with its assessment of portfolio credit quality and economic and business conditions to determine the level of the general allocated allowance.

General unallocated allowance – The general unallocated allowance, also reviewed on a quarterly basis, reflects the subjective and judgmental elements involved in our determination of credit risk and the resulting loss estimates, and is an estimate of probable credit losses that have not been captured as part of the specific and general allocated allowance. In determining the general unallocated allowance, management considers regulatory requirements, recent loan loss experience and trends in credit quality and concentration as well as any inherent model imprecision.

Fair value of financial instruments

In accordance with Canadian GAAP, certain financial instruments are carried on our balance sheet at their fair value. These financial instruments comprise assets held in our trading portfolio, obligations related to securities sold short and derivative financial instruments (excluding non-trading derivatives subject to hedge accounting). At October 31, 2003, approximately $117 billion of our financial assets and $61 billion of our financial liabilities were carried at fair value. Fair value is defined as the amount at which an instrument could be bought or sold in a current transaction between willing parties, other than in a forced or liquidation sale.

The fair value of the majority of the financial instruments in our portfolios is determined based on their quoted market price as it provides the best evidence of value, and best reflects the price between two willing parties attempting to transact in an open market. Note 23 on pages 98A to 99A provides disclosure of the estimated fair value of all our financial instruments at October 31, 2003.

If a quoted market price is not available, we use internal or external financial valuation models to estimate the fair value. Where we believe the potential exists that the amount realized on sale will be less than the estimated fair value due to insufficient liquidity over a short period of time, a provision is made. We also maintain a provision for model risk, which may occur when the estimated value does not reflect the true value under certain stress market conditions. These provisions reflect varying levels of management judgment based on quantitative research and analysis, and industry practice.

The majority of our trading portfolio and obligations related to securities sold short comprise or relate to actively traded debt and equity securities which are carried at fair value based on available quoted market prices. Where quoted market prices are not available for a particular security, the quoted market price of a security with similar characteristics and risk profile is used to estimate the fair value of the unquoted security.

For derivative financial instruments, we determine fair value using various methodologies, including quoted market prices, prevailing market values for similar instruments, net present value of future cash flows and other internal or external pricing models. As few over-the-counter (OTC) derivative financial instruments are actively quoted, we rely primarily on internally developed pricing models and established industry standard pricing models, such as Black-Scholes, to determine fair value. For further information on our derivative instruments, refer to Note 21 on pages 95A to 97A.

In determining the assumptions to be used in our pricing models, we look primarily to external readily observable market inputs including factors such as interest rate yield curves, currency rates and price and rate volatilities as applicable. However, certain derivative financial instruments are valued using significant unobservable market inputs such as default correlations, among others. These inputs are subject to significantly more quantitative analysis and management judgment.

The following table summarizes our significant financial assets and liabilities by valuation methodology at October 31, 2003:

Assets and liabilities carried at fair value by valuation methodology

	Financial assets		Financial liabilities	
(C$ millions, except percentage amounts)	Trading securities	Derivatives	Obligations related to securities sold short	Derivatives
Fair Value	$ 81,827	$ 35,668	$ 22,855	$ 37,655
Based on				
Quoted market prices	87%	–%	95%	–%
Pricing models with significant observable market parameters	13	99	5	100
Pricing models with significant unobservable market parameters	–	1	–	–
Total	100%	100%	100%	100%

The use of methodologies, models and assumptions in pricing and valuing these financial assets and liabilities is subjective and requires varying degrees of judgment by management. The use of different methodologies, models and assumptions may result in significantly different fair values and financial results. To mitigate this risk, all significant financial valuation models are vetted by our risk management function, which is not involved in trading the assets and liabilities and is mandated to provide an independent perspective. Our internal financial valuation models for accounting are strictly controlled and regularly recalibrated, and require the approval of our risk management function. In addition, OSFI reviews our models selectively based on the risk profile of the business to ensure appropriateness of the models and validity of the assumptions used by management.

As outlined in Note 1 on page 72A, changes in the fair value of trading securities and obligations related to securities sold short are recognized as trading revenues in non-interest income.

Changes in the fair value of our trading and non-trading derivatives that do not qualify for hedge accounting are recognized in non-interest income. Refer to Note 1 on page 73A for further details.

Line of business results

Overview

Table 3 below shows our results by business segment in 2003. GAAP does not prescribe a method for allocating equity to business segments. For management and reporting purposes, we attribute common equity to our business segments (including the Other segment) based on methodologies designed to measure the equity capital necessary to underpin the risks of the businesses in each segment, as discussed in the Economic Capital section on page 54A. The difference between our total common equity and the common equity attributed to our business segments is allocated to the Other segment. The capital attribution methodologies involve judgment by management, are revised from time to time with changes applied prospectively and affect measures such as business segment return on equity (ROE).

Furthermore, the attribution of common equity is a dynamic process and is affected by current business activity, volumes and environmental factors. Average common equity attributed to our business segments, except RBC Insurance and RBC Global Services, is lower than a year ago partially as a result of the decline in the value of U.S. dollar-denominated assets due to the appreciation of the Canadian dollar relative to the U.S. dollar. The decreases in RBC Banking and RBC Capital Markets are also the result of lower credit risk. Average common equity attributed to RBC Insurance is higher largely due to the acquisition of Business Men's Assurance Company of America (BMA) on May 1, 2003.

In addition, effective the first quarter of this year, we reduced the equity capital attributed to goodwill and intangibles risk, consistent with our capital attribution for other risk categories and to reflect the benefits of having diversified businesses and risks. This resulted in reductions in average common equity attributed to the RBC Banking, RBC Investments and RBC Capital Markets segments.

We generated 52% of our net income from RBC Banking, which had an ROE of 21.0%. Net income increased $30 million from 2002, as discussed on page 28A. Net income from U.S. operations was $154 million, $41 million lower than in 2002. This decrease largely reflected the effect of the lower translated value of U.S. dollar-denominated earnings due to the strengthening of the Canadian dollar relative to the U.S. dollar, as well as to higher costs associated with both RBC Mortgage (a subsidiary of RBC Centura) and with acquisitions completed during the year.

Net income from RBC Insurance was 7% of total net income, and its ROE was 25.0%. Net income was $99 million or 85% higher than in 2002, as discussed on page 30A. Total U.S. net income was $25 million, up from a loss of $6 million in 2002, due to a substantial improvement in earnings from the U.S. life operations.

RBC Investments generated 14% of our net income, and had an ROE of 15.0%. Net income rose $67 million or 20% from last year, as discussed on page 32A. Net income from the U.S. increased to $87 million from a loss of $2 million in 2002, primarily as a result of improved earnings from RBC Dain Rauscher's full-service brokerage and fixed income businesses, and a $25 million after-tax reduction in retention compensation costs.

Net income from RBC Capital Markets was 17% of total net income, and its ROE was 13.0%. Net income increased $91 million or 22% compared to the previous year, as discussed on page 34A. U.S. net income was $120 million, up from a loss of $40 million in 2002, as there was a significant decline in the provision for credit losses related to the U.S. corporate loan portfolio.

RBC Global Services contributed 6% of our net income and recorded an ROE of 27.5%. This segment's net income improved $6 million or 4% from 2002, as discussed on page 36A.

The Other segment, which mainly comprises Corporate Treasury, Corporate Resources, Systems & Technology and Real Estate Operations, generated 4% of our net income in 2003, and produced an ROE of 5.6%. Its 2002 results are shown in Note 3 on page 78A. Net income was $133 million, down $50 million from 2002, due largely to refinements in the methodology for attributing net interest income to our business segments.

TABLE 3 Results by business segment

(C$ millions, except per share and percentage amounts)	2003 RBC Banking	RBC Insurance	RBC Investments	RBC Capital Markets	RBC Global Services	Other (1)	Total	2002 Total
Net interest income	$ 5,546	$ –	$ 419	$ 409	$ 166	$ 102	$ 6,642	$ 6,935
Non-interest income	2,127	2,356	3,110	2,247	824	112	10,776	10,320
Total revenues	7,673	2,356	3,529	2,656	990	214	17,418	17,255
Provision for credit losses	554	–	(2)	195	2	(28)	721	1,065
Insurance policyholder benefits, claims and acquisition expense	–	1,696	–	–	–	–	1,696	1,535
Non-interest expense	4,650	460	2,912	1,671	714	2	10,409	10,420
Income taxes	900	(16)	209	278	97	(8)	1,460	1,365
Non-controlling interest	8	–	–	4	–	115	127	108
Net income	$ 1,561	$ 216	$ 410	$ 508	$ 177	$ 133	$ 3,005	$ 2,762
U.S. net income	154	25	87	120	8	(2)	392	154
Net income								
As a % of total	52%	7%	14%	17%	6%	4%	100%	100%
% growth over prior year	2%	85%	20%	22%	4%	(27)%	9%	15%
Return on common equity	21.0%	25.0%	15.0%	13.0%	27.5%	5.6%	16.7%	15.8%
Average common equity (2)	$ 7,350	$ 850	$ 2,650	$ 3,800	$ 650	$ 2,250	$17,550	$16,800
Diluted EPS							$ 4.39	$ 3.93

(1) Represents other activities, which mainly comprise Corporate Treasury, Corporate Resources, Systems & Technology and Real Estate Operations.
(2) Calculated using methods intended to approximate the average of the daily balances for the period. Attributed to the segments as discussed above.

RBC Banking

Business profile
RBC Banking serves 11.5 million individual, small and medium-sized business, and mid-market commercial clients in Canada, the U.S., the Caribbean and the Bahamas. Our multiple distribution capabilities include a network of branches, business banking centres and other sales units, accredited financial planners, mobile sales representatives, automated banking machines, and telephone and Internet banking channels. Drawing on our extensive distribution network and working together with other RBC businesses, we offer our clients tailored solutions and financial planning and advice based on life events through a diverse range of financial products and services including deposit accounts, investments and mutual funds, credit and debit cards, business and personal loans, and residential and commercial mortgages.

Industry profile
In Canada, personal and commercial banking is a mature industry dominated by the five largest Canadian banks, although competition is fierce and niche players increasingly operate in select businesses such as credit cards. The U.S. market is more fragmented, and many regional markets are highly competitive. Many banks have expanded their focus to offer investment products and financial advice and planning to targeted clients. Critical success factors, in our opinion, include providing a superior client experience, strong revenue focused sales processes, and maintaining rigorous credit and operational risk management practices and expense control.

Our strengths
- Established Canadian retail banking brand
- Strong capabilities in Customer Relationship Management (CRM) and client segmentation and sub-segmentation, and specialized sales forces
- Comprehensive product, sales, service and national distribution capabilities compared to niche players
- Highest client household penetration ratio in personal segments, and lead market share in business deposits and financing among Canadian banks
- Growing U.S. presence in retail banking in the fast-growing Southeast, and in mortgage origination and builder finance nationally

Our strategy
Our strategy is to grow profitable relationships with each one of our business and personal clients in North America by delivering a superior and tailored client experience, reducing costs, and effectively managing risk and capital.

We are focused on achieving the following strategic priorities:

Superior client experience
- Deliver a superior and tailored client experience to each one of our business and personal clients, with extraordinary focus placed on our high value clients

Strong fundamentals
- Ensure strong revenue growth in Canada, deepening client relationships and our "share of wallet," drawing on our financial planning and advice capabilities, and delivering tailored value propositions to targeted segments
- Reinforce our risk mitigation and cost management focus, rigorously managing credit, operational, and compliance risk, and building low-cost delivery capabilities that significantly reduce the risk of errors

North American expansion
- Accelerate U.S. revenue and earnings growth, significantly growing our business with current and prospective clients of RBC Centura and its RBC Mortgage subsidiary and RBC Builder Finance division, while selectively expanding our network in the Southeast and in targeted national markets

Cross-enterprise leverage
- Create a seamless cross-enterprise and north-south experience for our clients, making it easy to do business across RBC Financial Group

Outlook for 2004
Our business is influenced by the interest rate environment, consumer and business loan demand and credit quality trends. Based on our forecast of slightly higher interest rates in Canada in 2004, we anticipate that deposit spread compression could ease. This, combined with reasonable economic and accompanying loan growth, should have positive revenue growth implications in our Canadian business. In the U.S., we anticipate that branch openings, combined with recent acquisitions in Florida and in our mortgage operations, will have a positive revenue impact. We also expect that cost synergies from the acquisitions and other cost management initiatives will contribute to U.S. net income growth.

Financial performance
Net income was up $30 million or 2% from 2002, as higher earnings in Canada more than offset a $41 million decline in U.S. earnings due to the strengthening of the Canadian dollar relative to the U.S. dollar (which accounted for $18 million of the earnings decline) and higher costs associated with RBC Mortgage operations and with acquisitions completed during the year.

Total revenues were up $43 million in 2003 despite a stronger Canadian dollar, which reduced the translated value of U.S. dollar-denominated revenues by $121 million. This reflected strong loan and deposit volume growth in Canada, which more than offset deposit spread compression, as well as the contribution of U.S. acquisitions completed in 2003 and higher revenues at RBC Mortgage.

Non-interest expense increased $122 million or 3%. Higher non-interest expense in Canada reflected higher pension and postretirement benefit costs, investments made to enhance automated service delivery capabilities and the hiring of additional salespeople in the branch network. In the U.S., expense growth reflected the acquisitions of Admiralty Bancorp, Inc. in January 2003, the mortgage unit of Bank One in August 2003 and Sterling Capital Mortgage Company in October 2003, as well as higher staffing and operational costs at RBC Mortgage due to increased origination and refinancing activity earlier in the year. The efficiency ratio increased 130 basis points as non-interest expense grew at a rate higher than revenues.

The provision for credit losses decreased by $72 million or 12% with significant improvement in the quality of the business loan portfolio, as well as lower provisions taken in the personal loan portfolio.

ROE rose to 21.0% in 2003, largely as a result of a $500 million decline in average common equity attributed to this segment, as discussed on page 27A.

Results

(C$ millions, except percentage amounts)	% change	2003	2002
Net interest income	–%	**$ 5,546**	$ 5,557
Non-interest income	3	**2,127**	2,073
Total revenues	1	**7,673**	7,630
Provision for credit losses			
Specific	(12)	**554**	626
Total	(12)	**554**	626
Non-interest expense	3	**4,650**	4,528
Net income before income taxes	–	**2,469**	2,476
Income taxes	(4)	**900**	937
Non-controlling interest	–	**8**	8
Net income	2%	**$ 1,561**	$ 1,531
U.S. net income	(21)	**$ 154**	$ 195
Net income as a % of total group net income	(300)bp	**52%**	55%
ROE	190 bp	**21.0%**	19.1%
Net interest margin (average assets)	(13)bp	**3.42%**	3.55%
Net interest margin (average earning assets)	(17)bp	**3.62%**	3.79%
Efficiency ratio (1)	130 bp	**60.6%**	59.3%
Average assets (2)	4%	**$ 162,400**	$ 156,500
Average loans and acceptances (2)	4	**147,900**	142,800
Average deposits (2)	5	**129,000**	122,900
Average common equity (2), (3)	(6)	**7,350**	7,850
Credit information			
Net impaired loans	(9)	**$ 609**	$ 668
Net write-offs	(13)	**648**	744
Net write-offs as a % of average loans and acceptances	(8)bp	**.44%**	.52%
Number of employees (full-time equivalent)	7%	**37,475**	35,014

(1) Efficiency ratio is defined in the Glossary on page 109.
(2) Calculated using methods intended to approximate the average of the daily balances for the period.
(3) Attributed to the segment as discussed on page 27A.

Strategy by division

Financial highlights by division

Canada

Operating in Canada under the RBC Royal Bank brand, we serve individuals, small and medium-sized businesses, and commercial clients in all provinces and territories. We offer our clients extensive physical and alternative distribution choices, providing them with 24/7 access. We continue to strengthen our channel distribution capabilities, including significant reinvestment in our branch network and staff, and in our electronic banking capabilities.

We offer a wide range of financial services and advice, as detailed in our business profile on page 28A, and products and expertise in specialized areas such as foreign exchange, asset-based finance, leasing and automotive finance. We also provide individual and business clients with a full choice of Visa credit card products including our increasingly popular Avion Platinum card, debit cards and other smart card applications. We provide merchants with credit and debit card acceptance services, point-of-sale capabilities and Internet-secure electronic transaction solutions through Moneris Solutions, a joint venture in which we participate equally with Bank of Montreal, managed through RBC Global Services.

Our goal is to grow profitable relationships with each one of our business and personal clients, using our expertise in CRM, client segmentation and sub-segmentation, and sales management, which includes specialized Investment Retirement Planner, Financial Planning, Mortgage, Knowledge-Based Industry and Agriculture sales forces, among others. We plan to drive revenue growth by delivering a superior and tailored client experience which includes strong capabilities in financial planning and advice, leveraging the full RBC Financial Group.

We will continue to reinforce our cost management focus by leveraging e-enabled technology and cross-enterprise economies of scale. We will continue to rigorously focus on the management of credit, operational and compliance risk, including fraud management initiatives and strengthened credit-scoring capabilities.

Total revenues were $59 million or 1% higher than in 2002 as volume growth in personal lending and deposit products, increased loan portfolio spread and higher card fees offset lower net interest margin from deposit spread compression. Card balances increased 11%, reflecting the success of the Avion card campaign, while continued strength in the housing market drove mortgage balances 6% higher. Approximately 40% of the increase in the number of employees represented the expansion of the sales force in the branch network in 2003.

Results (1)

(C$ millions)	% change	2003	2002
Total revenues	1%	**$ 6,165**	$ 6,106
Average residential mortgages	6	**72,600**	68,200
Average personal loans	3	**24,200**	23,600
Average personal deposits	8	**80,100**	74,400
Average business loans and acceptances	(2)	**32,000**	32,700
Average business deposits	–	**30,600**	30,500
Average card balances	11	**6,900**	6,200
Card spending volumes	13	**30,200**	26,700
Number of:			
Employees (full-time equivalent)	4	**30,865**	29,716
Automated banking machines	(2)	**4,062**	4,151
Branches	(1)	**1,104**	1,117
Online clients	10	**2,552,966**	2,311,915

(1) Averages are calculated using methods intended to approximate the average of the daily balances for the period.

United States

RBC Centura serves as the focal point of our personal and commercial banking businesses in the U.S. Headquartered in Rocky Mount, North Carolina, RBC Centura serves individual and business clients in the Southeastern U.S. RBC Centura also includes RBC Mortgage, a Chicago-based national retail mortgage originator, and RBC Builder Finance, a Houston-based financing division for home builders and developers. RBC Centura's footprint recently expanded with the acquisition on November 21, 2003, of the 13 Florida branches of Provident Financial Group Inc., bringing RBC Centura's Florida network to 24 branches. RBC Mortgage expanded through the acquisition of Houston-based Sterling Capital Mortgage Company, becoming one of the top 10 mortgage originators in the U.S.

Our U.S. priorities include:

- Expanding our retail banking business base in the Southeast, significantly growing our business with current and prospective clients of RBC Centura, as well as through targeted acquisitions and new branch expansion
- Strengthening our residential mortgage and builder finance national niche lines of business
- Building our private banking capabilities, working closely with RBC Investments
- Rapidly building a scalable platform to support growth
- Realizing north-south synergies and strengthening our client segmentation, sales and marketing capabilities
- Leveraging cross-selling opportunities across RBC Financial Group, including our new *RBC Snowbird Package*

Total revenues were $4 million higher than last year, despite the strengthening of the Canadian dollar relative to the U.S. dollar (which reduced the translated value of revenues by $107 million). In U.S. dollars, total revenues increased 10% to US$894 million due largely to acquisitions completed during the year and the contribution of RBC Mortgage. The growth in average mortgage balances was due primarily to higher levels of loans held for sale at RBC Mortgage, as well as the impact of the acquisition of Eagle Bancshares, Inc. (in July 2002) and the success of a new adjustable rate mortgage product. Although total mortgage originations were up $8.9 billion or 26% from 2002, origination volumes declined significantly in the fourth quarter of 2003, reflecting lower refinancing activity due to the upward movement in interest rates.

Results (1)

(C$ millions)	% change	2003	2002
Total revenues	–%	**$ 1,285**	$ 1,281
Average residential mortgages	45	**4,200**	2,900
Average personal loans	–	**3,300**	3,300
Average personal deposits	(7)	**8,000**	8,600
Average business loans and acceptances	(3)	**8,300**	8,600
Average business deposits	7	**5,800**	5,400
Average card balances	–	**100**	100
Card spending volumes	–	**400**	400
Mortgage originations ($ billions)	26	**42.6**	33.7
Number of:			
Employees (full-time equivalent)	30	**5,444**	4,181
Automated banking machines	1	**279**	275
Branches (2)	(1)	**242**	245
Online clients	17	**104,473**	89,434

(1) Averages are calculated using methods intended to approximate the average of the daily balances for the period.
(2) Excludes RBC Mortgage and RBC Builder Finance sales offices of 274 in 2003 and 252 in 2002.

Caribbean and the Bahamas

Operating under the brand name RBC Royal Bank of Canada, we provide a broad range of personal and commercial banking products and services to individual and business clients in the Bahamas, Barbados, the Cayman Islands, and the Eastern Caribbean countries of Antigua, Dominica, Montserrat, St. Kitts, and St. Lucia through a network of branches, business centres and automated banking machines.

Total revenues fell $20 million or 8% from last year, due largely to the strengthening of the Canadian dollar relative to the U.S. dollar and certain Caribbean currencies.

Results

(C$ millions)	% change	2003	2002
Total revenues	(8)%	**$ 223**	$ 243
Number of:			
Employees (full-time equivalent)	4	**1,166**	1,117
Automated banking machines	–	**60**	60
Branches	–	**43**	43

RBC Insurance

Business profile

Operating as RBC Insurance, we provide a wide range of creditor, life, health, travel, home, auto and reinsurance products and services to more than five million clients in Canada, the U.S. and internationally. These products and services are offered through a wide variety of distribution channels, including the telephone, independent brokers, travel agents, a proprietary sales force and the Internet.

Industry profile

The Canadian insurance industry comprises more than 100 life insurance companies and more than 200 property and casualty insurers and generates almost $60 billion in premiums annually. The U.S. life insurance industry, in which our U.S. business is focused, is both competitive and fragmented and includes almost 1,200 national and regional companies. The U.S. travel insurance industry, which is a new market for RBC Insurance, is estimated to be worth more than US$500 million in premiums and is served by a small number of companies. The international reinsurance industry continues to be dominated by several global players but also includes a number of niche companies.

Key industry trends that continue to affect the insurance sector include ongoing consolidation and increased government regulation and oversight. In addition, consumer product preferences are shifting to reflect demographic changes and renewed concerns over health and travel safety. Distribution is also evolving, with the Internet becoming a more important sales and support tool.

Our strengths

- An integrated North American insurance operation, focused on leveraging synergies across the organization
- A diverse set of products designed to meet a wide range of consumer needs
- Multiple distribution channels, which are supported by strong infrastructure and sales expertise
- A strong brand. As part of RBC Financial Group, we have access to a broad range of financial services, distribution channels and client bases
- Market leadership in a number of Canadian insurance markets, including travel and individual life insurance

Our strategy

We are focused on growing our insurance organization by offering a wide range of products and services through multiple distribution channels in Canada, as well as in select U.S. and international markets. To accomplish this we are seeking to:

- Focus on generating above-average revenue growth in conjunction with strong profitability through significant expansion across all of our businesses by adding distribution channels and entering into new markets
- Further integrate our operational areas on a North American basis to maximize efficiencies and economies of scale and scope, while also further leveraging the strengths of being part of RBC Financial Group
- Adopt a leadership position in seeking change in bank insurance regulation to ensure the greatest opportunities for providing integrated bank insurance products and services to our clients
- Focus on financial management to continue to build our expertise in managing capital, investment and taxes within an international bank insurance context

Outlook for 2004

Performance in our business is influenced by our policyholder claims experience, the general economic and interest rate environment, and by credit risk considerations related to our investment portfolios. Our outlook is for strong revenue growth, driven by demographic trends, reasonable economic growth in Canada and the U.S., and expansion into new products and markets with a particular focus on wealth management and living benefits solutions. We will also focus on opportunities for efficiencies from further integrating our Canadian and U.S. operations and expect that performance from our U.S. life insurance operations will improve as we integrate the acquisition of BMA and realize cost and revenue synergies.

Financial performance

Net income increased $99 million or 85% from 2002. This increase reflected strong profitability in the reinsurance business, and improvements in the Canadian and U.S. life businesses, which benefited from stronger equity markets and a more stable interest rate environment compared to 2002. Earnings from the U.S. were $25 million compared to a loss of $6 million a year ago, largely due to the improvement in the life business noted above.

While RBC Liberty Insurance reported 13 months of activity in 2002 as a result of a change in its reporting period from September 30 to October 31 to be consistent with our fiscal year, the Canadian operations reported 13 months of results in 2003 for the same reason. The extra month of results in 2003 largely offset the extra month of results reported last year.

Insurance premiums, investment and fee income were up $313 million or 15% in 2003. The increase was largely due to higher earned premiums and investment income from the acquisition of BMA in the middle of 2003 and growth in earned premiums from the home and auto business. In addition, improvements in the equity markets increased both investment income and policyholder benefits associated with customer holdings of Universal Life products by $83 million.

Insurance policyholder benefits, claims and acquisition expense was higher, primarily reflecting volume growth in the home and auto business and the increase in policyholder benefits related to Universal Life products mentioned above, which was partly offset by lower reinsurance claims.

The $23 million or 5% increase in non-interest expense was related to business volume growth as well as costs associated with the acquisition of BMA, which were partially offset by cost savings in other areas.

ROE increased to 25.0% as higher net income more than offset the additional $150 million in average common equity attributed to this segment, as discussed on page 27A.

Results

(C$ millions, except percentage amounts)	% change	2003	2002
Non-interest income			
Net earned premiums (1)	11%	$ 1,965	$ 1,767
Investment income	78	298	167
Fee income	(15)	93	109
Insurance premiums, investment and fee income	15	2,356	2,043
Insurance policyholder benefits, claims and acquisition expense	10	1,696	1,535
Non-interest expense	5	460	437
Net income before income taxes	182	200	71
Income taxes	n.m.	(16)	(46)
Net income	85%	$ 216	$ 117
U.S. net income	n.m.	$ 25	$ (6)
Net income as a % of total group net income	300 bp	7%	4%
ROE	930 bp	25.0%	15.7%
Premiums and deposits	9%	$ 2,214	$ 2,023
Average assets (2)	20	6,700	5,600
Average common equity (2), (3)	21	850	700
Number of employees (full-time equivalent)	9%	2,883	2,641

(1) Net of reinsurance premiums.
(2) Calculated using methods intended to approximate the average of the daily balances for the period.
(3) Attributed to the segment as discussed on page 27A.
n.m. not meaningful

Strategy by division

Financial highlights by division

Life

Our life business provides a wide range of individual and group life and health insurance solutions to individual and business clients as well as life retrocession to businesses in Canada, the U.S. and around the world.

In Canada, life and health insurance products are distributed through more than 7,000 independent brokers affiliated with producer groups, financial planning firms and stock brokerage firms, as well as through direct sales and a network of career sales representatives. In the U.S., we provide life and health insurance products through independent broker-dealers and a proprietary sales force. We also offer select products through direct channels.

Over the next year, our focus will be on further integrating our life insurance operations, increasing growth in premiums through enhancing our products and services and further developing our distribution network.

Higher insurance premiums, investment and fee income reflected a substantial increase in investment income associated with Universal Life products and higher earned premiums from the BMA acquisition and the Canadian life business, which more than offset lower earned premiums from the reinsurance business and from RBC Liberty Insurance due to policy surrenders. In 2003, an extra month of revenues of $37 million was reported for the Canadian life operation as it changed its reporting period to be consistent with our fiscal year, and in 2002, an extra month of revenues of $45 million was reported for the U.S. operations for the same reason. The increase in average assets was primarily due to the acquisition of BMA in May 2003.

Results

(C$ millions)	% change	2003	2002
Insurance premiums, investment and fee income	19%	$ **1,625**	$ 1,363
Average assets (1)	23	**5,400**	4,400
Number of:			
Life and health policies in force and certificates in Canada (thousands)	29	**3,850**	2,985
Life policies in force in the U.S. (thousands)	(6)	**2,185**	2,325
Sales agents (U.S. and Canada)	2	**1,268**	1,244

(1) Calculated using methods intended to approximate the average of the daily balances for the period.

Non-life

Our non-life business includes home, auto and travel insurance for individual and business clients and property reinsurance for businesses in Canada and select international markets.

We provide Canadians with a wide range of home and auto insurance products, offering them to individual clients and employee and affinity groups through direct sales. Travel insurance products, which are sold through travel agents and the Internet in Canada and the U.S., as well as through bank channels in Canada, include trip cancellation and interruption insurance, out-of-country medical and baggage insurance.

We participate in the property reinsurance business by accepting a share of the risk on property policies issued by other insurance companies. The majority of our current business is generated from insurance companies in the U.S. and Europe.

Our goal is to grow our non-life business by continuing to expand our home and auto, and travel insurance operations and effectively managing our property reinsurance portfolio.

The home and auto business drove insurance premiums, investment and fee income $64 million higher in 2003 due to increased sales of new policies. The number of home and auto policies in force increased 42% from last year. In addition, the Canadian home and auto, and travel businesses reported an extra month of revenues of $27 million in 2003 as these businesses changed their reporting period to be consistent with our fiscal year.

Results

(C$ millions)	% change	2003	2002
Insurance premiums, investment and fee income	17%	$ **436**	$ 372
Average assets (1)	29	**900**	700
Number of:			
Home and auto – personal lines policies in force (thousands)	42	**132**	93
Travel – coverages (thousands)	2	**2,388**	2,339

(1) Calculated using methods intended to approximate the average of the daily balances for the period.

Fee businesses

We are involved in a number of other key insurance and related activities that generate fee income, including travel assistance services, structured reinsurance, the administration of bank creditor insurance programs, insurance software and outsourcing and administration solutions services.

Our travel and emergency assistance services include co-ordinating the delivery of emergency health, evacuation and transportation services when clients have a travel emergency, while our structured reinsurance business provides solutions to help corporations better manage financial risk. We also oversee the creditor insurance products and services for individual and business clients of RBC Financial Group. This includes life and disability insurance for mortgages, loans and Visa cards.

In the U.S., our fee businesses include outsourcing services and administration and software systems. Our Business Process Outsourcing division provides services such as underwriting, billing and collection, and claims processing, while our Software Solutions division develops Web-enabled software for life, health, annuity and reinsurance administration. Together, these divisions have more than 200 client sites and serve domestic, international and multinational insurers worldwide.

Our goal is to continue to build on our existing infrastructure and technology to enhance our product and service offering and grow our fee businesses.

Insurance premiums, investment and fee income fell $13 million in 2003 as a result of lower outsourcing revenues from the U.S. businesses, which was related to the decline in the number of policies under administration. In addition, an extra month of results was reported in 2002, accounting for $7 million of the decrease, to align the reporting period of the U.S. operations with our fiscal year.

Results

(C$ millions)	% change	2003	2002
Insurance premiums, investment and fee income	(4)%	$ **295**	$ 308
Average assets (1)	(20)	**400**	500
Number of:			
Assistance services – calls (thousands)	(2)	**670**	681
Policies under administration in the U.S. (thousands)	(4)	**3,925**	4,100

(1) Calculated using methods intended to approximate the average of the daily balances for the period.

RBC Investments

Business profile

RBC Investments provides wealth management services including full-service and self-directed brokerage, financial planning, investment counselling, personal trust, private banking and investment management products and services to clients in Canada, the U.S. and internationally. Products and services are delivered through the RBC Royal Bank branch network across Canada, RBC Investments offices, RBC Dain Rauscher branches in the U.S., private banking offices and other locations worldwide. Services are also delivered via the Internet and telephone.

Industry profile

Wealth management remains a highly competitive business with numerous large and boutique firms serving the market. Volatile markets and the rising costs of managing the regulatory and compliance requirements of the business continue to encourage consolidation. Consolidation in the mutual fund industry has not significantly altered the competitive landscape as distribution channels continue to be expanded by all players.

Our strengths

- Relationship management capabilities from experienced people and technology applications
- Ability to deliver the breadth of products and services clients need to meet their financial goals
- Multiple distribution channels for client convenience
- Ability to access the client base and draw on the capabilities of RBC
- Solutions designed for specific investment strategies and client risk tolerance

Our strategy

Our goal is to be our clients' first choice for wealth management. We plan to do so by developing broader and deeper relationships with our clients throughout their lives.

Employee engagement, service excellence and client commitment underlie our pursuit of exceptional business performance and shareholder value creation. In order to broaden and deepen relationships with our clients, we are using segmentation strategies to develop targeted solutions for specific client groups. In addition, we are transforming our distribution models to ensure that our financial consultants and advisors have more time to focus on their clients. We are also focusing on improving our operational infrastructure and processes to efficiently support growth.

Outlook for 2004

Based on our expectation that investor confidence and capital markets performance will continue to improve modestly, we expect moderate revenue growth in 2004. Cost-containment efforts should keep the rate of expense growth below that of revenue growth. Retention compensation costs relating to U.S. acquisitions are forecast to be approximately $20 million lower in 2004 than in 2003, further contributing to net income growth.

Financial performance

Net income increased $67 million or 20% in 2003, driven primarily by improved earnings in the U.S. and ongoing cost-containment initiatives, as well as higher earnings from the Canadian self-directed brokerage and asset management businesses. U.S. net income was up $89 million from a year ago, with significantly improved performance in the full-service brokerage business, strong fixed income results and declining retention compensation costs.

Total revenues fell $116 million or 3%, largely reflecting the strengthening of the Canadian dollar relative to the U.S. dollar, which reduced the translated value of U.S. dollar-denominated revenues by $175 million. This decline more than offset higher revenues from RBC Dain Rauscher's fixed income and full-service brokerage businesses. Total revenues from the wealth management businesses in Canada were negatively affected by weak capital market conditions in the first half of the year.

The $234 million or 7% decline in non-interest expense included a $150 million reduction due to the stronger Canadian dollar, and reflected savings from cost-containment initiatives and a $41 million decline in retention compensation costs at RBC Dain Rauscher.

ROE improved 400 basis points to 15.0%, reflecting higher earnings in 2003, as well as a $350 million reduction in average common equity attributed to this segment, as discussed on page 27A.

Results

(C$ millions, except percentage amounts)	% change	2003	2002
Net interest income	13%	$ **419**	$ 371
Non-interest income	(5)	**3,110**	3,274
Total revenues	(3)	**3,529**	3,645
Provision for credit losses			
Specific	100	**(2)**	(1)
Total	100	**(2)**	(1)
Non-interest expense	(7)	**2,912**	3,146
Net income before income taxes	24	**619**	500
Income taxes	33	**209**	157
Net income	20%	$ **410**	$ 343
U.S. net income (loss)	n.m.	$ **87**	$ (2)
Net income as a % of total group net income	200 bp	**14%**	12%
ROE	400 bp	**15.0%**	11.0%
Average common equity (1)	(12)%	**2,650**	3,000
Number of employees (full-time equivalent)	(13)%	**10,464**	12,001

(1) Calculated using methods intended to approximate the average of the daily balances for the period. Attributed to the segment as discussed on page 27A.
n.m. not meaningful

Strategy by division

Canada

Wealth Management Canada

This group includes Dominion Securities (full-service brokerage) and Action Direct (self-directed brokerage), which serve both investors requiring advisor-based comprehensive financial solutions and self-managed investors. Services are provided by over 1,320 investment advisors and 115 investment representatives, as well as via telephone and the Internet. Additionally, within this group our Private Counsel, Trust Services and Private Banking businesses serve high net worth clients across Canada, offering a relationship management approach for clients in need of sophisticated financial solutions. In Canada, there are 43 investment counsellors, 67 trust officers and 51 private bankers in locations across the country. RBC Investments Financial Planning is a business operated jointly with RBC Banking. This team serves domestic branch-based clients with more than $50,000 in investable assets of which a portion must include mutual funds or managed products. There are 1,030 relationship financial planners and 530 commission-based investment and retirement planners who are also financial planners and licensed mutual funds salespeople. RBC Investments reports financial results from its share of this jointly operated business within Wealth Management Canada. Our goal is to grow our market position in Canada by continuing to build and enhance existing client relationships.

Global Asset Management

This unit includes RBC Asset Management, which became Canada's largest mutual fund company in 2003. We directly manage more than $43 billion of assets in mutual and pooled funds as well as other client assets. We provide proprietary and externally managed investment management products and advisory services through RBC Royal Bank, RBC Investments' distribution businesses and external distributors to private and institutional clients in Canada and worldwide. Our family of mutual funds and other pooled products encompasses a broad range of investment solutions including money market, fixed income, balanced and Canadian, U.S. and global equity funds, as well as alternative investments. RBC Asset Management has enjoyed strong success in asset retention, resulting from strong relative investment performance, improved client retention by RBC Royal Bank and RBC Investments Financial Planning, and support for RBC Funds in the advisory (broker and independent financial planner) channel, which contributed to a continued gain in market share. Beginning in 2004, Global Asset Management will also include Voyageur Asset Management (in 2003, included within RBC Dain Rauscher), our U.S.-based asset management company, which manages US$21 billion in mutual funds and institutional mandates. In 2004, our goal is to maximize growth opportunities by leveraging RBC partnerships in Canada and the U.S.

United States

RBC Dain Rauscher

Minneapolis-based RBC Dain Rauscher is ranked as the eighth-largest full-service securities firm in the U.S., based on number of financial consultants. We have nearly 1,750 financial consultants serving individual clients from coast to coast and a fixed income business with 327 investment bankers, sales representatives and traders serving institutional and retail clients nationwide. RBC Dain Rauscher plans to grow through broadening and deepening relationships with existing clients by understanding their needs and the potential profitability of the client relationship. We also plan to grow by focusing on opportunities that generate greater market share and scale within our existing markets.

International

Global Private Banking

Operating under the brand name Royal Bank of Canada Global Private Banking, this unit provides private banking, trust and investment counselling, and investment advisory solutions to high net worth clients in more than 100 countries from 23 offices around the world. In 2004, this group will include the International Advisory Group (in 2003, included within Wealth Management Canada) to better align this business directly with its international clients. This team has both Canadian and internationally-based employees. Our goal is to provide specialized global services to high net worth clients with assets of more than $1 million. In 2004, we will continue to grow revenues by exploring acquisition opportunities in the Americas and Europe, by building distribution alliances with financial institutions that are strong in their local market but lack an international wealth management capability, and with an increasingly aggressive outreach sales and marketing program. The addition of non-proprietary money management capabilities will expand our value proposition to clients.

Financial highlights by division

Lower transaction-based and asset value-based fee revenues drove the $67 million or 5% decline in revenues from the wealth management businesses in Canada, reflecting an extremely weak Canadian RRSP season in 2003, which more than offset strong performance from the self-directed brokerage business. Global Private Banking revenues fell $15 million, also due to lower fee-based revenues and reduced net interest income as a result of low interest rates. The decline in revenues from RBC Dain Rauscher is entirely attributable to the strengthening of the Canadian dollar relative to the U.S. dollar, as both its full-service brokerage and fixed income businesses performed well. Global Asset Management revenues remained virtually unchanged.

Total revenues

(C$ millions)	% change	2003	2002
Wealth Management Canada	(5)%	**$ 1,212**	$ 1,279
RBC Dain Rauscher	(2)	**1,666**	1,702
Global Private Banking	(4)	**368**	383
Global Asset Management	–	**287**	286
Other	n.m.	**(4)**	(5)
	(3)%	**$ 3,529**	$ 3,645

n.m. not meaningful

The AUA of the wealth management businesses in Canada was virtually unchanged despite higher year-end equity values compared to 2002, as $14 billion in custody-related AUA was transferred to RBC Global Services. RBC Dain Rauscher's AUA balance fell 4% in 2003 due to the strengthening of the Canadian dollar relative to the U.S. dollar, which reduced the translated value of U.S. dollar-denominated assets. In U.S. dollars, RBC Dain Rauscher's AUA increased US$11.8 billion. Global Private Banking's personal AUA was also affected by the stronger Canadian dollar which negatively affected the translated value of both Pound-Sterling and U.S. dollar-denominated assets. Institutional AUA grew 11% as additional business was acquired from existing clients.

Assets under administration (AUA)

(C$ millions)	% change	2003	2002
Personal			
Wealth Management Canada	–%	**$ 142,750**	$ 142,160
RBC Dain Rauscher	(4)	**128,150**	132,930
Global Private Banking	(15)	**43,750**	51,570
	(4)	**314,650**	326,660
Institutional – Global Private Banking	11	**77,520**	69,730
	(1)%	**$ 392,170**	$ 396,390

Personal AUM decreased $4 billion due to the effect of the stronger Canadian dollar on foreign currency-denominated assets in 2003. Much of the 7% increase in institutional AUM was related to the accumulation of new assets despite the foreign exchange impact mentioned above, while the higher mutual fund balances primarily reflected higher asset values at the end of 2003 compared to last year.

Assets under management (AUM)

(C$ millions)	% change	2003	2002
Personal	(12)%	**$ 31,300**	$ 35,660
Institutional	7	**19,690**	18,410
Mutual funds	7	**36,730**	34,230
	(1)%	**$ 87,720**	$ 88,300

RBC Capital Markets

Business profile

RBC Capital Markets provides wholesale financial services to large corporate, government and institutional clients in North America and in specialized product and industry sectors globally. Headquartered in Toronto, RBC Capital Markets has key centres of expertise in New York and London, and offices in 28 other cities.

Industry profile

The Canadian wholesale financial services market is mature and, as a result, many Canadian firms are seeking growth opportunities outside of their domestic market, primarily in the U.S. The U.S. capital markets are dominated by several large global investment banks whose principal focus is on the top tier of companies forming the S&P 500 Index. However, we believe significant opportunities exist for specialized players targeting the lower end of the S&P 500 as well as companies that have the potential to move into this category. To succeed in the North American context requires the ability to provide clients with innovative, value-added solutions that reflect a keen understanding of both the company and industry sector. We believe that increasingly, new business opportunities will accrue to those firms with a reputation for adhering to high ethical standards.

Our strengths

- Top-tier market shares in virtually all lines of business in Canada
- Established reputation as a premier Canadian investment dealer as evidenced by our market share leadership
- Superior origination and distribution capability in Canada as measured by our standings in underwriting league tables
- Expertise and market knowledge in a broad array of industries

Our strategy

Our goals are to be recognized as the leading corporate and investment bank in Canada based on external rankings and to build a successful integrated North American business, while continuing to expand our specialized global businesses.

Key strategies for RBC Capital Markets include the following:

- In Canada, to maintain our position as a leading full-service provider in all of our markets by continuing to leverage the breadth of our long-standing client relationships, the depth of our trading, research and sales capabilities, and the strength of our brand and reputation in the Canadian market
- In the U.S., to provide value-added solutions by offering our targeted clients a broad product portfolio delivered through specialized industry teams, with the goal of building an integrated North American franchise. We will leverage the depth of our research and advisory capabilities in targeted North American industry sectors, specifically energy, technology, communications, health care, consumer products and mid-sized financial institutions
- Continue to expand our global specialized businesses by providing clients with customized, value-added solutions in the areas of bonds, money markets, foreign exchange, structured finance and equity and credit derivatives

Outlook for 2004

Our total revenues and earnings are dependent on the performance of both capital and credit markets and the strength of the economic environment, which drive demand for new issue and advisory services, merger and acquisition activities and trading volumes. Although economic and market conditions remain uncertain, our expectation is that capital markets performance will improve modestly in 2004, resulting in moderate revenue growth. We also expect to maintain our discipline with respect to costs and credit risk.

Financial performance

Net income increased $91 million or 22% in 2003, as a significant reduction in the provision for credit losses related to the U.S. corporate loan portfolio more than offset higher non-interest expense.

Total revenues increased $12 million despite a $115 million reduction in the translated value of U.S. dollar-denominated revenues due to the stronger Canadian dollar and lower net interest income reflecting the intentional reduction in the size of the corporate loan portfolio. The increase was largely due to extremely strong performance from the fixed income businesses. The fixed income businesses benefited from highly active debt markets and the favourable interest rate environment in 2003.

Non-interest expense was up $44 million or 3% compared to last year, primarily due to higher variable compensation costs during the second half of the year related to the improvement in capital market activity, and costs associated with new growth initiatives and with restructuring the U.S. investment banking and institutional equities businesses. These increases more than offset the $69 million reduction in the translated value of U.S. dollar-denominated expenses due to the stronger Canadian dollar.

The $270 million decline in the provision for credit losses, the $342 million decline in net impaired loans and the $326 million decline in net write-offs reflected the improvement in the quality of the corporate loan portfolio compared to 2002. Exposures to higher risk sectors, such as telecommunication and energy, continue to be reduced.

ROE improved to 13.0% in 2003, due to higher net income as well as a $150 million reduction in average common equity attributed to this segment, as discussed on page 27A.

Results

(C$ millions, except percentage amounts)	% change	2003	2002
Net interest income	(23)%	**$ 409**	$ 532
Non-interest income	6	**2,247**	2,112
Total revenues	–	**2,656**	2,644
Provision for credit losses			
Specific	(58)	**195**	465
Total	(58)	**195**	465
Non-interest expense	3	**1,671**	1,627
Net income before income taxes	43	**790**	552
Income taxes	106	**278**	135
Non-controlling interest	n.m.	**4**	–
Net income	22%	**$ 508**	$ 417
U.S. net income (loss)	n.m.	**$ 120**	$ (40)
Net income as a % of total group net income	200 bp	**17%**	15%
ROE	300 bp	**13.0%**	10.0%
Average assets (1)	11%	**198,500**	178,200
Average loans, acceptances and reverse repurchase agreements (1)	2	**62,700**	61,400
Average deposits (1)	–	**79,500**	79,200
Average common equity (1), (2)	(4)	**3,800**	3,950
Credit information			
Net impaired loans	(48)	**$ 373**	$ 715
Net write-offs	(64)	**184**	510
Net write-offs as a % of average loans, acceptances and reverse repurchase agreements	(54)bp	**.29%**	.83%
Number of employees (full-time equivalent)	(1)%	**2,912**	2,938

(1) Calculated using methods intended to approximate the average of the daily balances for the period.
(2) Attributed to the segment as discussed on page 27A.
n.m. not meaningful

Strategy by division

Global Investment Banking
In February 2003, the Capital Markets Services division was split into its two component parts – Global Investment Banking and Global Equity – primarily to address the changes in the regulatory and governance environments that require the separation of research and investment banking activities.

The Global Investment Banking division houses the corporate and investment banking businesses. We offer a full range of credit and corporate finance products, including debt and equity underwriting, mergers and acquisitions advice and execution and financial sponsorship coverage.

In Canada, we intend to continue to be a full-service provider to all industries, building on the breadth and longevity of our client relationships and a long-standing reputation as a top-ranked investment bank. In the U.S., we plan to be industry-focused – specifically on technology, telecommunication, health care, energy, consumer products and mid-sized financial institutions. We expect to differentiate ourselves on our ability to provide superior market-based solutions for our target clients.

Global Equity
Global Equity provides expertise in the research and trading of North American and select international securities.

We intend to leverage our broad knowledge of Canadian markets, the strength of our research capabilities and the breadth and depth of our institutional client relationships to serve our clients better. In the U.S., our goal is to combine our traditional capital markets focus with our research capabilities to build a franchise in select segments of the U.S. middle market – specifically, the technology, health care, energy, communications, consumer products, financial institutions and real estate sectors. We plan to continue to develop our electronic trading capabilities to keep pace with the increasing demand from clients for electronic execution services.

Global Financial Products
This division brings together the business activities involving the origination, syndication, securitization, trading and distribution of debt products globally. These products include loans, bonds and derivatives at both the investment grade and sub-investment grade levels. As well, Global Financial Products is the centre of expertise for the proprietary trading activities of RBC Capital Markets. The combination of these businesses provides the ability to maximize internal expertise and deliver a broad array of value-added ideas and solutions to clients.

We intend to continue to focus on identifying opportunities where we can build from our existing strengths to provide solutions-based approaches to structuring transactions for our clients.

Global Treasury Services
Global Treasury Services combines our money markets and foreign exchange businesses and provides global clients with foreign exchange, commodities, derivatives and interest rate products, as well as prime brokerage, currency risk management and advisory services. These products and services are delivered through our extensive global sales and trading network, operating from centres that include Toronto, London, New York and Sydney. Recognized as a market leader in foreign exchange e-commerce solutions, we also deliver services through our Internet trading platform, FX Direct, and are a member of the multi-bank global trading platform, FXall. We plan to continue to invest in innovative electronic delivery channels that offer sophisticated and flexible products and services.

Global Credit
Global Credit provides centralized management of all credit exposure associated with our loan portfolio. While wholesale lending is fundamental to the attraction and expansion of high-margin client businesses, lending must be strategic in order to maximize the returns to shareholders. Our portfolio and transaction management specialists use sophisticated risk management and analytical tools designed to ensure that the pricing on loans is commensurate with the associated risk and reflects the value of all products and services a client has with RBC Financial Group.

Our transaction specialists use appropriate structures to provide clients with value-added, as opposed to commoditized, credit solutions. We work closely with our distribution teams to manage the size and credit quality of our corporate lending base.

Alternative Investments
Alternative Investments was formed in June 2002 with a mandate to expand our wholesale asset management capabilities, which today include operations in structuring hedge fund transactions and in private debt and equity. The alternative asset business provides non-traditional investment opportunities to high net worth individuals, corporations and institutional clients. These investment options include private equity and hedge funds, and can extend to other vehicles such as leveraged buyouts and Collateralized Debt Obligations. We are uniquely positioned to leverage our existing infrastructure and our superior product knowledge across other businesses within RBC Financial Group that have strong relationships with our target client base.

Financial highlights by division

Total revenues were negatively affected by the appreciation of the Canadian dollar relative to the U.S. dollar, which reduced the translated value of U.S. dollar-denominated revenues by $115 million. Revenues from Global Financial Products were up $117 million or 13%, as the favourable interest rate environment, higher market volumes and new initiatives helped to fuel revenue growth in many of our fixed income businesses. Notably strong results were experienced in bond businesses in both domestic and international markets, as well as structured products and securitization. Revenues from our proprietary trading activities in Global Financial Products were lower than last year, largely due to the appreciation of the Canadian dollar relative to the U.S. dollar. Poor capital market conditions during the first half of 2003 dampened revenues from Global Investment Banking and Global Equity. In addition, 2002 revenues from Global Investment Banking included credit derivative gains related to accounts classified as impaired last year. Global Treasury Services revenues were up $10 million on higher contributions from the foreign exchange and money market sales and trading businesses. Revenues from Global Credit were up $58 million despite lower net interest income due to the intentional reduction in the size of the corporate loan book, as this year's results included net gains on credit derivatives, while last year's results included net losses. Revenues from Alternative Investments increased $10 million, largely due to strong growth in the hedge fund business. The Alternative Investments business also recorded $39 million of losses on private equity investments related largely to the four years ended October 31, 2003. These losses were recognized as a result of our determination that certain private equity investments should be accounted for using the equity method of accounting rather than the previously applied cost method of accounting.

Total revenues

(C$ millions)	% change	2003	2002
Global Investment Banking	(24)%	$ 543	$ 714
Global Equity	(4)	292	304
Global Financial Products	13	1,004	887
Global Treasury Services	2	555	545
Global Credit	56	161	103
Alternative Investments	11	101	91
	–%	$ 2,656	$ 2,644

The decline in average assets in the Global Investment Banking and Global Credit businesses reflected the continued and intentional reduction in the size of the non-core corporate loan portfolio compared to a year ago. The increase in average assets in Global Financial Products related to the growth in fixed income and global equity derivatives businesses, and in Alternative Investments reflected the growth in the hedge fund business. Global Treasury Services also recorded a growth in average assets, due to positive mark-to-market adjustments relating to foreign exchange derivatives, and increased assets in support of our money market sales and trading and liquidity management activities.

Average assets (1)

(C$ millions)	% change	2003	2002
Global Investment Banking	(52)%	$ 5,100	$ 10,600
Global Equity	–	600	600
Global Financial Products	29	93,000	71,900
Global Treasury Services	10	84,700	77,200
Global Credit	(51)	4,900	10,100
Alternative Investments	31	10,200	7,800
	11%	$ 198,500	$ 178,200

(1) Calculated using methods intended to approximate the average of the daily balances for the period.

RBC Global Services

Business profile

RBC Global Services offers specialized transaction processing services to business, commercial, corporate and institutional clients in Canada and select international markets, principally the U.K. and Australia. Key businesses include global custody, investment administration, correspondent banking, cash management, payments and trade finance. Our 50% interest in the Moneris Solutions joint venture with Bank of Montreal for merchant card processing is reported in RBC Global Services.

Industry profile

The transaction processing services industry is highly competitive and relatively mature in the Canadian market. Monoline specialists and new market entrants compete against traditional financial institutions. Scale continues to be important to support the significant investment in technology required to introduce new products and services, accommodate industry-driven infrastructure changes and enhance operational efficiencies. The quality of client service and strength of client relationships are also key differentiating factors in these businesses. Market consolidation continued in 2003, particularly in businesses such as global custody and merchant card processing, which require global capability or significant scale.

Our strengths

- We have a leadership position in Canada in these businesses as measured by assets under administration (AUA) and number of client relationships
- We have strong client relationships as demonstrated by our high rate of client retention and new business generated from existing clients
- We are recognized for quality of service as evidenced in third-party client surveys, such as *Global Custodian* magazine's annual Agent Bank review, which has assigned us "Top Rated" status for 15 consecutive years; and our recognition by Stewart Associates as Canada's highest-rated service provider of cash management services for the past five years
- We continue to develop and deploy new technology and client service solutions
- We are able to leverage our market position by aligning the resources within RBC Global Services with the expertise of other platforms within RBC Financial Group to offer a superior integrated service

Our strategy

Our goal is to maintain and enhance our leadership position in Canada while continuing to develop a competitive international presence. To meet our goal, we will:

- Leverage our Canadian product and service strengths to profitably grow our business in North America and select international markets
- Expand the business through key alliances, acquisitions and partnerships and continue to leverage the Moneris Solutions joint venture
- Enhance our processing and systems platforms to deliver new capabilities, improve efficiencies and achieve economies of scale
- Differentiate our service offering by taking a client-centric approach that incorporates the diversified strengths and products of RBC Financial Group

Outlook for 2004

While our transaction processing revenue is primarily derived from stable, fee-based sources, interest earned on deposits and cash balances, and fees earned on client assets are variable sources of revenue that influence the overall revenue of this segment. Key risks to this income stream come from lower interest rates and poor capital markets performance. We expect interest rates to remain low in historical terms, which will continue to have an unfavourable impact on our revenue growth in 2004. Higher asset values resulting from a modest improvement in capital markets during 2004 should have a favourable impact on fee revenues, which should offset the unfavourable impact of the low interest rate environment.

Financial performance

Net income was up $6 million or 4% from 2002 as higher revenues, a lower provision for credit losses and lower income taxes offset higher non-interest expense.

Total revenues increased $33 million or 3%, reflecting growth in fee income from the cash management and custody businesses. However, lower capital markets transaction volumes and securities values earlier in 2003, as well as the low interest rate environment throughout the year, restrained the pace of revenue growth.

Non-interest expense was $46 million or 7% higher in 2003, due to increased business activity during the year, continued investments in technology and higher pension and severance costs.

The provision for credit losses decreased $8 million, as exposures to higher risk countries were closely monitored.

ROE fell 90 basis points in 2003 to 27.5%, primarily reflecting $50 million in additional average common equity attributed to the segment, as discussed on page 27A.

Results

(C$ millions, except percentage amounts)	% change	**2003**	2002
Net interest income	21%	**$ 166**	$ 137
Non-interest income	–	**824**	820
Total revenues	3	**990**	957
Provision for credit losses			
Specific	(80)	**2**	10
Total	(80)	**2**	10
Non-interest expense	7	**714**	668
Net income before income taxes	(2)	**274**	279
Income taxes	(10)	**97**	108
Net income	4%	**$ 177**	$ 171
U.S. net income	(20)	**$ 8**	$ 10
Net income as a % of total group net income	–	**6%**	6%
ROE	(90)bp	**27.5%**	28.4%
Average common equity (1)	8%	**650**	600
Credit information			
Net impaired loans	(55)	**$ 5**	$ 11
Net write-offs	n.m.	**5**	(1)
Net write-offs as a % of average loans and acceptances	41 bp	**.36%**	(.05)%
Number of employees (full-time equivalent)	(1)%	**2,550**	2,571

(1) Calculated using methods intended to approximate the average of the daily balances for the period. Attributed to the segment as discussed on page 27A.
n.m. not meaningful

Strategy by division

Financial highlights by division

Institutional & Investor Services

Institutional & Investor Services is Canada's largest custodian as measured by AUA, and a provider of investment administration services to corporate and institutional investors worldwide. We operate from 12 locations throughout the world, with a global custody network spanning 80 markets.

Our plan is to continue to leverage our leadership position in the Canadian market to expand internationally, with a focus on serving fund managers, financial institutions and private banks.

We expect to achieve growth in our fee-based revenue streams by:

- Selling newly developed products and services to existing clients
- Expanding our client offerings in Europe and Asia-Pacific
- Further exploring alliance and acquisition opportunities

Total revenues increased $16 million or 4%. Higher fee income was partially offset by lower foreign exchange revenue and weaker capital markets earlier in the year. Although the higher AUA balance in 2003 reflects the positive impact of new business, the majority of the increase was due to higher equity values at the end of the year.

Results

(C$ millions)	% change	2003	2002
Total revenues	4%	**$ 417**	$ 401
Assets under administration	16	**1,122,000**	963,200

Financial Institutions

A comprehensive range of correspondent banking services is provided to banks globally and to broker-dealers within Canada, including cash management, payments, clearing, trade, foreign exchange, derivatives lending, securities lending, custody and settlement, and structured financing.

Our goal is to leverage our leadership position in the Canadian dollar clearing market and our strong client relationships by:

- Creating differentiated value-added solutions that address the unique needs of the various market segments
- Adding new revenue streams by introducing service offerings that integrate our new products with those of other business platforms

We will continue to monitor and manage our exposure to higher risk markets.

Total revenues decreased $2 million or 2% primarily due to lower interest rates. Average asset and deposit balances have changed little from last year, although the mix has changed as we continue to manage our exposure to higher risk markets.

Results

(C$ millions)	% change	2003	2002
Total revenues	(2)%	**$ 96**	$ 98
Average assets (1)	(18)	**1,400**	1,700
Average deposits (1)	19	**2,020**	1,700

(1) Calculated using methods intended to approximate the average of the daily balances for the period.

Treasury Management & Trade

Treasury Management & Trade provides cash management, payment and trade services to business and public sector markets in Canada. Our Trade team provides importers and exporters with a variety of trade products, services and counsel. Our cash management group provides a full range of solutions to clients including disbursement, receivable and information products. Through Moneris Solutions, we provide merchants with credit and debit card transaction processing services.

Our goal is to continue to be the leading provider in Canada by retaining profitable client relationships and growing market share in strategic markets by:

- Enhancing our market segmentation approach that accommodates the diverse needs of business and public sector markets
- Expanding the functionality of our Web-based delivery channel for both cash management and trade services
- Introducing new trade products and services as well as expanding trade alliances to meet clients' international trade requirements, while effectively managing risk
- Leveraging our cash management sales and service leadership position

Total revenues increased $19 million or 4% primarily due to growth in non-interest income from cash management products and services. Net interest income also increased as deposit growth more than offset lower interest rates.

Results

(C$ millions, volumes in thousands)	% change	2003	2002
Total revenues	4%	**$ 477**	$ 458
Average deposits (1)	6	**6,740**	6,350
Payment volumes	3	**7,634**	7,440
Payment errors (per 100,000 payments)	(12)	**2.9**	3.3

(1) Calculated using methods intended to approximate the average of the daily balances for the period.

Financial priority: Revenue growth and diversification

Highlights

- Total revenues up 1%
- Net interest income down 4%
- Net interest margin of 1.68%, down 21 basis points
- Non-interest income up 4%
- Non-interest income 62% of total revenues

TABLE 4 **Total revenues**

(C$ millions)	2003	2002	2003 vs 2002 Increase (decrease)	
Net interest income	$ 6,642	$ 6,935	$ (293)	(4)%
Non-interest income	10,776	10,320	456	4
Total revenues	$ 17,418	$ 17,255	$ 163	1%

Total revenues were up $163 million or 1% from a year ago, despite a $510 million decline in the translated value of U.S. dollar-denominated revenues due to a significant appreciation of the Canadian dollar relative to the U.S. dollar. Excluding the effect of the appreciation of the Canadian dollar, revenues were up $673 million or 4%. The increase in revenues largely reflects higher insurance premiums, investment and fee income, and higher trading revenues.

Outlook

We are targeting revenue growth of 5–8% in fiscal 2004 based on, among other things, our expectations that capital markets activity will continue to improve, interest rates in Canada will rise moderately and the Canadian and U.S. economies will grow somewhat faster than in 2003.

Net interest income

Net interest income was $6.6 billion, down $293 million or 4% from 2002, with $120 million of the decrease attributable to a decline in the translated value of U.S. dollar-denominated net interest income due to the strengthening of the Canadian dollar relative to the U.S. dollar. As shown in Table 6 on page 39A, while higher asset volumes (including residential mortgages, personal and credit card loans) added $249 million to net interest income in 2003, changes in the rates received on assets and paid on liabilities reduced net interest income by $542 million, primarily reflecting price competition in retail banking and low interest rates, which led to margin compression.

TABLE 5 **Net interest income and margin**

(C$ millions, except percentage amounts)	2003	2002	2001
Average assets (1)	$ 396,400	$ 367,300	$ 327,100
Net interest income	6,642	6,935	6,311
Net interest margin (2)	1.68%	1.89%	1.93%

(1) Calculated using methods intended to approximate the average of the daily balances for the period.
(2) Net interest income, as a percentage of average assets.

Net interest margin

As shown in Table 5 above, the net interest margin decreased by 21 basis points from a year ago to 1.68%. This reflected significant growth in low-interest-yielding assets such as securities, higher amounts of non-interest-yielding assets such as derivative-related amounts (included in other assets) and spread compression resulting from price competition in retail banking and low interest rates.

As shown in Table 7 on page 40A, while the average rate paid on total liabilities decreased by 19 basis points, the average rate received on total assets decreased by 38 basis points, leading to a 21 basis point reduction in the net interest margin. The average rate received on securities dropped 47 basis points while volumes of securities were up $11.9 billion on average or 13%. Similarly, other assets, which do not earn interest, were up $8.5 billion on average.

TABLE 6 Change in net interest income

(C$ millions)	2003 vs 2002 Increase (decrease) due to changes in average volume (1)	average rate (1)	Net change	2002 vs 2001 Increase (decrease) due to changes in average volume (1)	average rate (1)	Net change
Assets						
Deposits with banks						
Canada	$ 1	$ 1	$ 2	$ (3)	$ (8)	$ (11)
United States	23	(65)	(42)	(21)	(171)	(192)
Other International	29	(96)	(67)	(17)	(128)	(145)
Securities						
Trading account	162	(199)	(37)	502	(700)	(198)
Investment account	191	(256)	(65)	156	(182)	(26)
Loan substitute	(3)	(7)	(10)	(3)	4	1
Assets purchased under reverse repurchase agreements	115	21	136	197	(709)	(512)
Loans						
Canada						
Residential mortgage	230	(237)	(7)	218	(402)	(184)
Personal	38	65	103	(116)	(475)	(591)
Credit card	100	(4)	96	(28)	(9)	(37)
Business and government	(116)	667	551	(156)	166	10
United States	(92)	(311)	(403)	655	(563)	92
Other International	55	(708)	(653)	(183)	(676)	(859)
Total interest income	$ 733	$ (1,129)	$ (396)	$ 1,201	$ (3,853)	$ (2,652)
Liabilities						
Deposits						
Canada	$ 265	$ 82	$ 347	$ 70	$ (1,818)	$ (1,748)
United States	2	(225)	(223)	399	(1,027)	(628)
Other International	(8)	(373)	(381)	322	(949)	(627)
Obligations related to securities sold short	113	(71)	42	136	7	143
Obligations related to assets sold under repurchase agreements	66	72	138	(12)	(468)	(480)
Subordinated debentures	(20)	(10)	(30)	–	(4)	(4)
Other interest-bearing liabilities	66	(62)	4	87	(19)	68
Total interest expense	484	(587)	(103)	1,002	(4,278)	(3,276)
Net interest income	$ 249	$ (542)	$ (293)	$ 199	$ 425	$ 624

(1) Volume/rate variance is allocated on the percentage relationship of changes in balances and changes in rates to the total net change in net interest income.

TABLE 7 Net interest income on average assets and liabilities

	Average balances (1)			Interest (2)			Average rate		
(C$ millions, except percentage amounts)	**2003**	2002	2001	**2003**	2002	2001	**2003**	2002	2001
Assets									
Deposits with banks									
Canada	**$ 428**	$ 367	$ 449	**$ 9**	$ 7	$ 18	**2.10%**	1.91%	4.01%
United States	**6,688**	5,631	6,035	**101**	143	335	**1.51**	2.54	5.55
Other International	**10,675**	9,751	10,119	**266**	333	478	**2.49**	3.42	4.72
	17,791	15,749	16,603	**376**	483	831	**2.11**	3.07	5.01
Securities									
Trading account	**71,148**	65,422	51,429	**1,908**	1,945	2,143	**2.68**	2.97	4.17
Investment account	**31,441**	25,171	21,154	**815**	880	906	**2.59**	3.50	4.28
Loan substitute	**354**	407	463	**17**	27	26	**4.80**	6.63	5.62
	102,943	91,000	73,046	**2,740**	2,852	3,075	**2.66**	3.13	4.21
Assets purchased under reverse repurchase agreements	**41,565**	35,463	29,591	**787**	651	1,163	**1.89**	1.84	3.93
Loans (3)									
Canada									
Residential mortgage	**69,911**	65,901	62,448	**3,896**	3,903	4,087	**5.57**	5.92	6.54
Personal	**27,201**	26,631	28,089	**1,837**	1,734	2,325	**6.75**	6.51	8.28
Credit card	**5,197**	4,354	4,586	**615**	519	556	**11.83**	11.92	12.12
Business and government	**26,259**	28,650	32,347	**1,842**	1,291	1,281	**7.01**	4.51	3.96
	128,568	125,536	127,470	**8,190**	7,447	8,249	**6.37**	5.93	6.47
United States	**28,189**	29,784	20,295	**1,388**	1,791	1,699	**4.92**	6.01	8.37
Other International	**11,884**	11,348	12,541	**572**	1,225	2,084	**4.81**	10.79	16.62
	168,641	166,668	160,306	**10,150**	10,463	12,032	**6.02**	6.28	7.51
Total interest-earning assets	**330,940**	308,880	279,546	**14,053**	14,449	17,101	**4.25**	4.68	6.12
Non-interest-bearing deposits with banks	**1,947**	1,753	1,188						
Customers' liability under acceptances	**6,838**	8,515	9,890						
Other assets	**56,675**	48,152	36,476						
Total assets	**$ 396,400**	$ 367,300	$ 327,100	**$ 14,053**	$ 14,449	$ 17,101	**3.55%**	3.93%	5.23%
Liabilities and shareholders' equity									
Deposits (4)									
Canada	**$ 121,690**	$ 111,880	$ 110,228	**$ 3,311**	$ 2,964	$ 4,712	**2.72%**	2.65%	4.27%
United States	**40,131**	40,036	29,354	**564**	787	1,415	**1.41**	1.97	4.82
Other International	**68,316**	68,584	60,275	**1,577**	1,958	2,585	**2.31**	2.85	4.29
	230,137	220,500	199,857	**5,452**	5,709	8,712	**2.37**	2.59	4.36
Obligations related to securities sold short	**22,898**	19,912	16,509	**839**	797	654	**3.66**	4.00	3.96
Obligations related to assets sold under repurchase agreements	**22,522**	19,630	19,892	**552**	414	894	**2.45**	2.11	4.49
Subordinated debentures	**6,455**	6,804	6,805	**376**	406	410	**5.82**	5.97	6.02
Other interest-bearing liabilities	**7,889**	5,546	3,042	**192**	188	120	**2.43**	3.39	3.94
Total interest-bearing liabilities	**289,901**	272,392	246,105	**7,411**	7,514	10,790	**2.56**	2.76	4.38
Non-interest-bearing deposits	**20,640**	19,897	18,568						
Acceptances	**6,838**	8,515	9,890						
Other liabilities	**60,260**	47,974	36,621						
Total liabilities	**377,639**	348,778	311,184	**7,411**	7,514	10,790	**1.96**	2.15	3.47
Shareholders' equity									
Preferred	**1,210**	1,713	2,073						
Common	**17,551**	16,809	13,843						
Total liabilities and shareholders' equity	**$ 396,400**	$ 367,300	$ 327,100	**$ 7,411**	$ 7,514	$ 10,790	**1.87%**	2.05%	3.30%
Net interest income as a % of total average assets	**$ 396,400**	$ 367,300	$ 327,100	**$ 6,642**	$ 6,935	$ 6,311	**1.68%**	1.89%	1.93%
Net interest income as a % of total average interest-earning assets									
Canada	**$ 199,292**	$ 196,321	$ 182,904	**$ 5,186**	$ 5,472	$ 5,512	**2.60%**	2.79%	3.01%
United States	**59,368**	51,144	37,865	**1,188**	1,106	371	**2.00**	2.16	.98
Other International	**72,280**	61,415	58,777	**268**	357	428	**.37**	.58	.73
Total	**$ 330,940**	$ 308,880	$ 279,546	**$ 6,642**	$ 6,935	$ 6,311	**2.01%**	2.25%	2.26%

(1) Calculated using methods intended to approximate the average of the daily balances for the period.
(2) Interest income includes loan fees of $303 million (2002 – $321 million; 2001 – $328 million).
(3) Average balances include impaired loans and are net of allowances for credit losses.
(4) Deposits include savings deposits with average balances of $38 billion (2002 – $39 billion; 2001 – $38 billion), interest expense of $.3 billion (2002 – $.3 billion; 2001 – $.6 billion) and average rates of .78% (2002 – .69%; 2001 – 1.58%). Deposits also include term deposits with average balances of $160 billion (2002 – $155 billion; 2001 – $145 billion), interest expense of $4.1 billion (2002 – $4.4 billion; 2001 – $6.9 billion) and average rates of 2.53% (2002 – 2.85%; 2001 – 4.80%).

Non-interest income

As shown in Table 8 on page 41A, non-interest income was up $456 million, or 4%, from 2002, despite a $390 million decline in the translated value of U.S. dollar-denominated revenues, for the reasons discussed below.

Insurance premiums, investment and fee income were up $313 million or 15%, largely due to a $228 million increase associated with the acquisition of Business Men's Assurance Company of America on May 1, 2003, an $83 million increase in investment income associated with customer holdings of Universal Life products and a $66 million increase in home & auto insurance revenues. Trading revenues were up $243 million or 14%, largely in fixed income and money market trading, reflecting the impact of the favourable interest rate environment on trading revenues. Gain (loss) on sale of investment account securities was up $142 million, largely due to $111 million of net losses on sale of investment account securities in 2002 that did not recur this year. Deposit and payment service charges were up $37 million or 4% due to higher automated banking machine revenues and payment processing volumes. Underwriting and other advisory fees were up $28 million, or 4%, reflecting an improvement in capital markets activity in the last six months of

TABLE 8 Non-interest income

(C$ millions, except percentage amounts)	2003	2002	2001	2003 vs 2002 Increase (decrease)	
Insurance premiums, investment and fee income	**$ 2,356**	$ 2,043	$ 1,824	**$ 313**	**15%**
Trading revenues	**2,009**	1,766	1,820	**243**	**14**
Investment management and custodial fees	**1,143**	1,177	1,094	**(34)**	**(3)**
Securities brokerage commissions	**1,108**	1,223	1,045	**(115)**	**(9)**
Deposit and payment service charges	**1,078**	1,041	887	**37**	**4**
Mutual fund revenues	**673**	723	692	**(50)**	**(7)**
Underwriting and other advisory fees	**671**	643	478	**28**	**4**
Card service revenues	**518**	496	458	**22**	**4**
Foreign exchange revenues, other than trading	**279**	276	303	**3**	**1**
Credit fees	**227**	223	237	**4**	**2**
Mortgage banking revenues	**198**	222	206	**(24)**	**(11)**
Securitization revenues	**165**	174	123	**(9)**	**(5)**
Gain (loss) on sale of investment account securities	**31**	(111)	(130)	**142**	**n.m.**
Gain from divestitures (1)	**–**	–	445	**–**	**–**
Other	**320**	424	283	**(104)**	**(25)**
Total	**$ 10,776**	$ 10,320	$ 9,765	**$ 456**	**4%**

(1) Gain on divestitures in 2001 included $89 million on formation of Moneris Solutions joint venture, $43 million on sale of Group Retirement Services and $313 million on sale of RT Capital Management.
n.m. not meaningful

the fiscal year, and card service revenues were up $22 million or 4% due to higher retail transaction volumes. However, investment management and custodial fees were down $34 million, or 3%, and mutual fund revenues were $50 million, or 7% lower, reflecting weak equity markets in the first six months of the year. Mortgage banking revenues (which relate to mortgages originated in the U.S. by RBC Centura and its subsidiary RBC Mortgage) were down $24 million or 11%, reflecting additional hedging and other costs in the fourth quarter of 2003. Securities brokerage commissions were down $115 million or 9%, reflecting weak equities markets and the resultant lower client trading volumes during the first half of the year. Other non-interest income declined by $104 million or 25%, mainly due to a $60 million charge for equity losses on private equity investments. The losses on private equity investments related largely to the four years ended October 31, 2003. These losses were recognized as a result of our determination that certain private equity investments should be accounted for using the equity method of accounting rather than the previously applied cost method of accounting.

Non-interest income accounted for 62% of total revenues, up from 60% in 2002.

TABLE 9 Trading revenues

(C$ millions)	2003	2002	2001
Net interest income (1)	**$ 73**	$ 127	$ (68)
Non-interest income (2)	**2,009**	1,766	1,820
Total	**$ 2,082**	$ 1,893	$ 1,752
By product			
Equity	**$ 614**	$ 753	$ 684
Fixed income and money markets (3)	**1,167**	876	726
Foreign exchange contracts (4)	**301**	264	342
Total	**$ 2,082**	$ 1,893	$ 1,752

(1) Includes interest earned on trading securities and other cash instruments held in the trading portfolios less funding costs associated with trading-related derivative and security positions.
(2) Primarily includes realized and unrealized gains and losses on trading securities, derivative instruments and foreign exchange trading activities.
(3) Includes government securities and corporate debt instruments, swaps, interest rate options, interest rate futures and forward rate agreements.
(4) Includes primarily foreign exchange spot, forward, futures and options contracts as well as commodity and precious metals.

Trading revenues

Trading revenues include gains and losses on securities and derivatives that arise from market-making, sales and principal trading activities. These securities and derivative positions are marked-to-market on a daily basis. Proprietary trading activities are strictly managed in accordance with Value-At-Risk (VAR) and trading limits and we continue to conduct the majority of client-related trading in the major G7 markets and currencies. A description of trading revenues included in net interest income and non-interest income is provided in Table 9 above.

As shown in Table 9 above, total trading revenues were up $189 million or 10% in 2003. Fixed income and money market trading revenues increased by $291 million, or 33%, reflecting the impact of the favourable interest rate environment, which resulted in higher bond trading revenues in international and domestic markets. Structured products, including credit derivatives, also experienced better results as a result of growth in client volumes and favourable trading returns. Foreign exchange contract trading revenues increased by $37 million, or 14%, due to higher volumes in both spot and derivative markets as global currency volatility increased. Increased sales and marketing efforts have enhanced foreign exchange trading volumes with institutional and corporate clients, while prudent risk taking and analytics contributed to higher trading revenues. Equity trading revenues decreased by $139 million, or 18%. Institutional equity trading volumes in listed and OTC markets declined during the year.

Financial priority: Cost control

Highlight

- Non-interest expense was unchanged from 2002

Non-interest expense was unchanged from 2002. While the stronger Canadian dollar relative to the U.S. dollar reduced translated value of non-interest expense by $340 million, this reduction was offset by increases in pension and other postretirement benefit costs, costs related to further automating our retail banking technology infrastructure and expanding our retail banking sales force in Canada and costs relating to companies we acquired during the year.

As shown in Table 10 on page 43A, human resources costs increased by $133 million or 2% in 2003, reflecting a $142 million or 18% increase in benefits expense. The increase in benefits expense was principally due to a $56 million increase in pension benefit expense (largely due to the amortization of prior year actuarial losses resulting from lower asset returns and a lower discount rate used to value pension liabilities in 2003). Other postretirement benefit expense increased by $69 million, primarily due to the amortization of actuarial losses resulting from higher claims experiences and a lower discount rate used to value other postretirement benefit liabilities in 2003 (see Note 17 on page 90A). Salaries increased by $58 million or 2%, largely due to the additional salaries associated with expanding our retail banking sales force in Canada and salaries associated with acquisitions that closed in 2003 (Admiralty Bancorp, Business Men's Assurance Company of America and Sterling Capital Mortgage Company). Stock compensation costs were up $18 million, reflecting the issuance of deferred shares. Acquisition retention compensation costs declined by $74 million to $84 million. We expect retention compensation costs relating to pre-2004 acquisitions to fall to approximately $45 million in 2004 and to $20 million in 2005.

Professional fees were up $47 million or 11% due to an increase in fees paid to external service providers to deal with increased volumes at RBC Mortgage and also an increase in systems upgrade and conversion costs at RBC Centura. Equipment costs were up $14 million or 2%. However, outsourced item processing costs were down $14 million or 5%, occupancy costs were down $21 million or 3%, communications costs were down $44 million or 5% and other costs were down $125 million or 14%.

Continuing our focus on cost control

The cost control initiatives undertaken in 2003 and in prior years are continuing to yield favourable results. Despite higher costs associated with growing our business, enhancing the client experience, and investing in new sales positions and technology, non-interest expense was essentially unchanged from 2002, aided by a stronger Canadian dollar, which reduced the translated value of U.S. dollar-denominated expenses.

RBC Banking continued its monitoring and containment of controllable expenses and focused on a number of initiatives. Discretionary expenses in Canada, which include stationery, professional fees and travel, were reduced by 9% from a year ago, select internal reports were eliminated, and we discontinued mailing cancelled cheques with interim statements to business clients, generating $30 million of savings in total. In the U.S., RBC Centura continued to integrate functions into RBC Royal Bank to take advantage of our Canadian operations' scale and expertise and to reduce costs. In 2002, RBC Centura's mainframe computer processing was relocated into the main processing centre in Ontario, generating cost savings in 2003, in addition to increasing scale and performance.

Moving into 2004, we expect savings from a new service platform for tellers, which we expect to begin using in January 2004 and which will simplify and streamline transaction processing and should also enhance client service levels. We also expect to realize savings from a new real-time image based tracing system, which replaces the current manual process used to resolve client issues and further enhances our fraud detection and prevention capability. However, we will continue to invest in providing standardized and flexible solutions across client segments, channels and products. These investments are expected to result in a superior client experience and net cost savings commencing in 2007 but expense outlays that exceed revenue benefits and cost savings prior to that time. In 2004, RBC Centura will continue to focus on reducing costs and improving efficiency. All in all, we are aiming to grow RBC Banking expenses by at least 2 percentage points less than revenues in each of the next three years.

RBC Insurance realized cost savings in 2003 through the introduction of a number of initiatives geared to reducing costs and enhancing efficiency. For example, the insurance operation consolidated a number of business locations, both in Canada and the U.S., to leverage existing capacity and improve service levels. In addition, RBC Insurance consolidated its technology services into a single group in order to build an integrated North American technology organization for the business. RBC Insurance also integrated recently acquired BMA into its existing operations, including moving the administration of a fixed block of business to its Greenville, South Carolina, operations in less than 30 days following the close, achieving cost reductions in excess of 30% of the pre-acquisition cost base.

At RBC Investments, the cost-cutting program, initiated in 2001 to offset the effects of market weakness, continued into 2003 and is expected to further progress in 2004. In 2003, cost savings were achieved by reducing overhead costs through integration of select branch offices and support facilities of the Canadian full-service brokerage business, restructuring the U.S. and Caribbean private banking units and right-sizing the U.S. brokerage business in response to the weak market environment during the first six months of the fiscal year. RBC Dain Rauscher achieved cost savings through the realization of the full year benefit of the prior year's integration of Tucker Anthony Sutro, which was acquired on October 31, 2001, by realizing the remaining US$30 million of the originally targeted US$60 million of annual integration cost savings.

RBC Capital Markets achieved expense reductions in 2003 through a number of initiatives. It continued to integrate the Investment Banking and Global Equity operations in the U.S. During the year, primary Nasdaq trading functions were moved from Minneapolis to New York to increase operational efficiency, while sales and trading positions that covered East coast accounts were relocated from Minneapolis to New York to better align them with the markets they serve. Also, trading operations groups in London and Toronto were integrated to eliminate duplicate and inefficient processes and generate cost savings. In addition, we are continuing to reduce loan portfolio management costs (including those relating to the structured lending portfolio). A lending process review, undertaken in 2003, has resulted in ongoing process changes that are expected to provide savings into 2004 and beyond. RBC Capital Markets will continue its focus on cost control in 2004.

TABLE 10 Non-interest expense

(C$ millions, except percentage amounts)	2003	2002	2001	2003 vs 2002 Increase (decrease)	
Human resources					
Salaries (1)	$ 3,282	$ 3,224	$ 2,770	$ 58	2%
Variable compensation	2,084	2,095	2,056	(11)	(1)
Acquisition-related retention compensation	84	158	176	(74)	(47)
Benefits	925	783	698	142	18
Stock compensation (2)	73	55	23	18	33
	6,448	6,315	5,723	133	2
Occupancy					
Net premises rent	579	595	561	(16)	(3)
Premises repairs and maintenance	72	70	55	2	3
Depreciation	95	103	91	(8)	(8)
Property taxes	11	11	6	–	–
Energy	18	17	11	1	6
	775	796	724	(21)	(3)
Equipment					
Office and computer rental and maintenance (1)	531	516	473	15	3
Depreciation	303	304	298	(1)	–
	834	820	771	14	2
Communications					
Telecommunication	328	361	290	(33)	(9)
Marketing and public relations	212	211	180	1	–
Postage and courier	113	121	108	(8)	(7)
Stationery and printing	104	108	108	(4)	(4)
	757	801	686	(44)	(5)
Professional fees (1)	466	419	412	47	11
Outsourced item processing	292	306	303	(14)	(5)
Amortization of goodwill	–	–	248	–	–
Amortization of other intangibles	71	72	36	(1)	(1)
Other					
Business and capital taxes	144	129	171	15	12
Travel and relocation	140	144	121	(4)	(3)
Employee training	39	46	43	(7)	(15)
Donations	38	41	35	(3)	(7)
Other (1)	405	531	482	(126)	(24)
	766	891	852	(125)	(14)
Total	$ 10,409	$ 10,420	$ 9,755	$ (11)	–

(1) Includes, in 2001, a U.S. retail banking restructuring charge comprising salaries of $22 million, office and computer rental and maintenance of $42 million, professional fees of $21 million and other of $6 million.
(2) Includes the cost of stock options, stock appreciation rights and performance deferred shares.

RBC Global Services realized cost savings in 2003 through a number of initiatives. Institutional & Investor Services undertook a review of common processes across the various business units to enhance efficiency and reduce costs, which resulted in a number of initiatives including the creation of a global account reconciliation services unit to perform account reconciliation activities for all domestic and global operations and the centralization of securities trade processing in Canada into one specialized unit. Treasury Management & Trade realized cost savings through a number of process improvement and technology initiatives, including the migration of regional electronic business banking support functions into its national client service centre and the introduction of a streamlined technology-based client enrollment process in its cash management business. These initiatives are expected to deliver cost savings in excess of $5 million annually.

In addition to each platform undertaking its own cost-containment initiatives, we have an E^2 (efficiency and effectiveness) effort underway throughout the group. In this regard, throughout 2003, we continued to review infrastructure and functional costs on an enterprise-wide basis, with the objective of eliminating duplication across businesses and functions and creating shared services to leverage centres of expertise. In 2004, we will review several larger initiatives to develop common systems and operational processes, enabling us to build a strong infrastructure to support our business expansion plans. This should also free up resources that can be redirected to enhancing client service and growing revenue.

TABLE 11 Taxes

(C$ millions, except percentage amounts)	2003	2002	2001
Income taxes	**$ 1,460**	$ 1,365	$ 1,340
Other taxes			
Goods and services and sales taxes	**220**	224	221
Payroll taxes	**267**	245	237
Capital taxes	**124**	107	146
Property taxes (1)	**11**	11	6
Business taxes	**20**	22	25
Insurance premium taxes	**26**	22	21
	668	631	656
Total	**$ 2,128**	$ 1,996	$ 1,996
Effective income tax rate (2)	**31.8%**	32.2%	34.7%
Effective total tax rate (3)	**40.5%**	41.0%	44.2%

(1) Includes amounts netted against non-interest income regarding investment properties.
(2) Income taxes, as a percentage of net income before income taxes.
(3) Total income and other taxes as a percentage of net income before income and other taxes.

Income and other taxes

Our operations are subject to a variety of taxes, including taxes on income and capital assessed by Canadian federal and provincial governments and the governments of foreign jurisdictions where we operate. Taxes are also assessed on expenditures or supplies consumed in support of our operations.

Income and other taxes shown in Table 11 above were $2,128 million in 2003, comprising income taxes of $1,460 million and other taxes of $668 million. Income taxes increased by $95 million from 2002, largely due to higher net income before tax. Other taxes increased by $37 million, largely due to an increase in the amount of payroll and capital taxes paid.

As shown above, the effective income tax rate decreased from 32.2% in 2002 to 31.8% in 2003, reflecting a reduction in federal and provincial tax rates in Canada. In addition to the income and other taxes reported in the consolidated statement of income, we recorded income taxes of $1,065 million in 2003 ($125 million in 2002) in shareholders' equity as shown in Note 15 on page 88A.

Financial priority: Strong credit quality

Highlights

- Business and government loans and acceptances decreased from 32% of total loans, acceptances and reverse repurchase agreements in 2002 to 28% at October 31, 2003
- Gross impaired loans down 24% to lowest level since 2000
- Net impaired loans to total loans, acceptances and reverse repurchase agreements down from .65% to .46%
- Provision for credit losses down 32% to $.7 billion, lowest level since 2000
- Specific provision ratio of .33%, down from .51%
- Net write-offs ratio of .37%, down from .60%
- Allowance for credit losses down slightly from $2.3 billion to $2.2 billion

Loan portfolio

During 2003, our loan portfolio performed well, reflecting changes in our credit practices adopted over the past few years. Three significant items affected the portfolio during 2003. The first item relates to our continued efforts to move towards a lower-risk portfolio mix, which includes more residential mortgage loans and fewer corporate loans, which entail higher risk and capital underpinning. As shown in the charts below, business and government loans and acceptances decreased to 28% of total loans, acceptances and reverse repurchase agreements in 2003 from 38% in 1999. A significant portion of this change occurred in 2003. The second item relates to our efforts to reduce exposure to the more sensitive and capital intensive sectors. The third item relates to further acquisitions in connection with our U.S. expansion strategy.

The portion of our business and government credit exposure rated investment grade remained relatively flat, moving from 70% in 2002 to 69% in 2003. Business and government loans include our small business portfolio of $9.7 billion, which is generally rated lower than our exposures to larger businesses.

Table 12 on page 47A and Table 17 on page 52A provide a detailed breakdown of loans, acceptances and reverse repurchase agreements. Our loan portfolio continues to be well diversified. Business and government loans and acceptances declined in 2003 due to our strategy of exiting non-core client relationships in RBC Capital Markets, the implementation of new single-name limits and an overall decline in demand for credit as corporate balance sheets have strengthened.

Our efforts to reduce business and government loans are reflected by decreases in various sectors. Decreases in the energy sector occurred in Canada ($1.2 billion), the United States ($1.5 billion) and other international ($.4 billion). The energy sector has been affected by two items in particular. Loans to the oil and gas (exploration and production) sub-sector have declined as a result of consolidation in the industry and our efforts to reduce single-name concentrations. The other factor has been a concerted effort to reduce exposure to the sensitive power generation and distribution sub-sector where loan outstandings have declined by 41% from 2002 to $1.2 billion.

Transportation and environment loans exposure decreased by $1.1 billion in total. Decreases occurred in both Canada ($.3 billion) and international ($.8 billion). Airlines and aerospace loans have been identified as a sensitive sub-sector and targeted for reduction. Over the year loans outstanding were down $.4 billion or 35% to $.7 billion. The decrease in international includes a reduction in loan outstandings ($.5 billion) to a particular counterparty in the United Kingdom.

Loans to telecommunications companies are also being actively managed down. Loan outstandings have decreased by 69% from $1.7 billion at year-end 2002 to only $.5 billion at the end of 2003. The decreases are spread out over Canada, United States and other international.

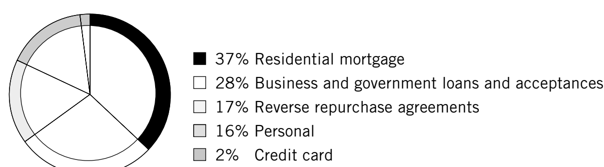
Loans to hotels, restaurants and entertainment companies have decreased $.3 billion or 10% to $2.8 billion. Approximately 38% of these loans are reported in the small business sector with the remainder in the Other sector.

Although the overall business and government portfolio decreased, there were some increases in certain areas related to our U.S. expansion strategy. During 2003 we acquired Admiralty Bancorp, Inc. (Admiralty) and Business Men's Assurance Company of America (BMA). The loans in BMA back the actuarial liabilities of the company. The increase in commercial real estate of $.9 billion in the U.S. reflects an increase of $1.5 billion resulting from the acquisitions of Admiralty and BMA which has been partially offset by other reductions.

From a risk management perspective, the sectors that utilize the most Economic Capital (EC) are commercial real estate, energy and telecommunications. For a discussion of EC see page 54A. As noted above, our real estate exposure has increased as a result of our U.S. expansion strategy but we are committed to managing this exposure. Although EC related to the energy and telecommunication sectors remains high, significant progress has been made in reducing outstandings.

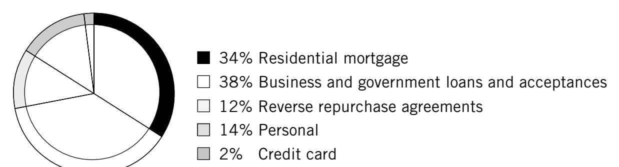
Breakdown of loans, acceptances and reverse repurchase agreements portfolio (2003)

Significant change...



Breakdown of loans, acceptances and reverse repurchase agreements portfolio (1999)

...in portfolio mix



Impaired loans
Loans are generally classified as impaired (meaning interest is no longer being accrued) under conditions described in Note 1 on page 72A.

As indicated in Table 13 on page 48A, gross impaired loans decreased by $543 million or 24% during the year to $1,745 million. Although write-offs decreased from $1,457 million in 2002 to $982 million in 2003, the significant decrease in net additions from $1,280 million in 2002 to $439 million in 2003 resulted in an overall decrease in gross impaired loans. Gross impaired loans declined in both the consumer and the business and government loan portfolios and are at their lowest level since 2000.

Gross impaired loans in the consumer portfolio declined by $71 million to $366 million, with Canada accounting for $54 million of the reduction. New additions declined, resulting from continued improvements in the portfolio due to benefits realized from the prior implementation of advanced risk modeling technology designed to optimize risk-reward and enhance credit policies and procedures.

Business and government gross impaired loans fell $472 million to $1,379 million, with reductions of $154 million in Canada, $205 million in the U.S. and $113 million in other international. In Canada, the reductions were spread over various sectors including small business ($36 million), forest products ($30 million) and transportation and environment ($20 million). The level of small business impaired loans continues to decline as a result of enhanced underwriting, monitoring and collection processes. The decrease in forest products largely relates to one particular counterparty. The reduction in transportation and environment results from the resolution of a significant land transportation account partially offset by the impairment of a Canadian transportation account. In the United States, at the end of 2003, there were no impaired telecommunications loans compared to a gross impaired amount of $77 million in 2002. This reduction largely resulted from the write-off, repayment and sale of impaired loans from 2002. The other decreases were spread over various industries. In other international, gross impaired loans in the mining and metals sector decreased by $71 million. This was largely due to one loan recovery. During the second half of the year, new impaired loan formations declined.

At the end of 2003, approximately 70% of the original impaired loan amount (amount when a loan was originally classified as impaired) in RBC Capital Markets has been written-off or specifically provided for.

Net impaired loans as a percentage of related loans, acceptances and reverse repurchase agreements decreased to .46% from .65% in 2002, reflecting improvements in both the Canadian and international ratios, as shown in Table 18 on page 52A.

Provision for credit losses
The provision for credit losses is charged to income by an amount necessary to bring the allowance for credit losses to a level determined appropriate by management, as discussed in the Allowance for credit losses section below.

The provision for credit losses was $721 million in 2003, down $344 million from 2002, as shown in Table 14 on page 49A. This was the lowest level since 2000.

In the consumer portfolio, the specific provision for credit losses decreased by $13 million, resulting from a decline of $18 million in Canada, partially offset by small increases in the United States and other international. The decline in Canada reflected a reduction in personal partially offset by an increase in credit card. Although the specific provisions for credit cards increased, the ratio to average balances decreased from 3.10% in 2002 to 2.92% in 2003, as shown in Table 18 on page 52A. This indicated that credit quality of the cards portfolio is being maintained as volume grows.

The specific provision on business and government loans decreased by $331 million or 52% to $304 million in 2003. The largest decrease related to telecommunications loans ($256 million) as this sector was provisioned for in prior years and only a small amount ($5 million) was required during the current year.

We acquire credit protection on portions of our portfolio by entering into credit derivative contracts. This year's provision for credit losses included an amount related to a European energy account that was classified as impaired. The provision for credit losses was partially offset by a gain of $29 million on a related credit derivative, recorded in non-interest income. Management believes an analysis that nets credit derivative gains on accounts in default against the related provision for credit losses is useful since it reflects the full loss associated with such accounts and management considers such information when evaluating our credit exposures. Management also believes that investors may find this information useful in their assessment of our credit quality and risk management.

As shown in Table 18 on page 52A, the specific provision for credit losses amounted to .33% of average loans, acceptances and reverse repurchase agreements (.32% net of the effect of credit derivatives), down from .51% in 2002 (.49% net of the effect of credit derivatives) and well below our 2003 objective of .45–.55%.

Outlook

In 2004, we expect an allocated specific provision for credit losses ratio in the range of .35–.45%, consistent with our medium-term goal.

Allowance for credit losses
The allowance for credit losses is maintained at a level that management believes is sufficient to absorb probable losses in the loan and off-balance sheet portfolios. The individual elements as well as the overall allowance are evaluated on a quarterly basis based on our assessment of problem accounts on an ongoing basis, recent loss experience and changes in other factors, including the composition and quality of the portfolio, economic conditions and regulatory requirements. The allowance is increased by the provision for credit losses, which is charged to income, and decreased by the amount of write-offs net of recoveries.

The determination of the allowance for credit losses is based upon estimates derived from historical analyses, which are adjusted to take into account management's assessment of underlying assumptions in relation to the current environment. As a result, the allowance for credit losses will not likely equal the actual losses incurred in the future. To minimize these differences, management undertakes an assessment of the methodology utilized and its underlying assumptions on a regular basis.

As described in Note 1 on page 73A, the allowance for credit losses comprises three components – specific, general allocated and general unallocated.

As shown in Table 15 on page 50A, the allowance for credit losses decreased by $150 million or 6% from 2002 to $2,164 million, consistent with the reduction in impaired loans over the same period. During the year, write-offs, net of recoveries, declined to $812 million or .37% of average loans, acceptances and reverse repurchase agreements, from $1,259 million or .60% a year ago as write-offs taken in 2002 in certain sectors such as telecommunications were not required in 2003.

Credit risk concentrations
Concentration risk exists if a number of clients are engaged in similar activities, are located in the same geographic region or have comparable economic characteristics such that their ability to meet contractual obligations would be similarly affected by changes in economic, political or other conditions. The strategies we use to minimize concentration risk are discussed further under risk mitigation in the Risk management section on page 55A.

As shown in Table 12 on page 47A, the largest Canadian exposure is in Ontario, which has 38% of total loans, acceptances and reverse repurchase agreements. Internationally, the largest concentration is in the U.S., where we have 14% of our total loans, acceptances and reverse repurchase agreements.

The largest sector concentrations, excluding small business, are in financial services, commercial real estate and agriculture with 4%, 4% and 2% of loans, acceptances and reverse repurchase agreements, respectively.

Table 16 on page 51A shows contractual amounts with clients outside of Canada. Of the total international contractual amounts, $72 billion or 18% of total assets are in the United States and $51 billion or 12% of total assets are outside Canada and the U.S.

TABLE 12 Loans, acceptances and reverse repurchase agreements (1)

(C$ millions, except percentage amounts)	2003	2002	2001	2000	1999	Percentage of total 2003	Percentage of total 1999
Canada							
Atlantic provinces (2)	**$ 10,021**	$ 9,770	$ 9,654	$ 9,690	$ 8,840	**4.7%**	5.1%
Quebec	**15,930**	15,190	13,863	16,191	14,936	**7.4**	8.6
Ontario	**80,831**	82,689	92,966	73,124	67,120	**37.6**	38.5
Prairie provinces (3)	**27,162**	26,989	25,192	29,402	25,521	**12.7**	14.6
British Columbia	**23,807**	23,367	22,696	25,118	23,141	**11.1**	13.2
Total Canada	**157,751**	158,005	164,371	153,525	139,558	**73.5**	80.0
Consumer							
Residential mortgage	**73,978**	67,700	64,066	61,444	58,524	**34.5**	33.5
Personal	**28,262**	25,918	27,202	27,207	24,353	**13.1**	14.0
Credit card	**4,663**	4,740	4,110	4,666	2,666	**2.2**	1.5
	106,903	98,358	95,378	93,317	85,543	**49.8**	49.0
Business and government loans and acceptances							
Small business (4)	**9,705**	9,470	9,788	11,701	10,334	**4.5**	5.9
Agriculture	**4,546**	4,427	4,758	4,931	4,217	**2.1**	2.4
Commercial mortgages	**2,616**	2,468	2,635	2,961	2,635	**1.2**	1.5
Consumer goods	**2,183**	2,238	2,447	2,874	2,086	**1.0**	1.2
Commercial real estate	**2,091**	2,393	2,325	2,594	2,400	**1.0**	1.4
Energy	**1,703**	2,911	4,293	3,754	3,350	**.8**	1.9
Government	**1,629**	1,039	1,597	1,385	2,105	**.8**	1.2
Automotive (5)	**1,472**	1,370	864	673	611	**.7**	.3
Industrial products	**1,372**	1,569	2,174	2,470	2,301	**.6**	1.3
Transportation and environment (5)	**1,112**	1,450	2,138	1,519	1,562	**.5**	.9
Forest products	**956**	954	1,275	1,362	1,151	**.4**	.7
Financial services	**856**	3,015	3,010	2,218	1,567	**.4**	.9
Media and cable (6)	**839**	994	1,510	1,120	897	**.4**	.7
Mining and metals	**333**	361	636	897	845	**.2**	.5
Telecommunication	**169**	487	677	1,008	525	**.1**	.3
Information technology	**114**	191	203	210	191	**.1**	.1
Other	**4,156**	5,194	5,803	6,437	4,650	**1.9**	2.7
	35,852	40,531	46,133	48,114	41,665	**16.7**	23.9
Reverse repurchase agreements	**14,996**	19,116	22,860	12,094	12,350	**7.0**	7.1
Total Canada	**157,751**	158,005	164,371	153,525	139,558	**73.5**	80.0
International							
United States	**30,861**	32,442	29,879	15,939	17,247	**14.4**	9.9
Europe, Middle East and Africa	**21,949**	19,006	16,860	9,782	9,642	**10.2**	5.5
Caribbean	**1,941**	2,018	1,856	2,059	1,502	**.9**	.9
Latin America	**646**	1,400	1,680	1,842	2,309	**.3**	1.3
Asia	**729**	1,004	1,328	1,781	2,417	**.3**	1.4
Australia and New Zealand	**804**	1,468	1,207	1,218	1,693	**.4**	1.0
Total international	**56,930**	57,338	52,810	32,621	34,810	**26.5**	20.0
Consumer							
Residential mortgage	**4,839**	5,140	3,376	1,540	718	**2.2**	.4
Personal	**5,741**	6,038	5,309	812	902	**2.7**	.5
Credit card	**153**	174	173	–	–	**.1**	–
	10,733	11,352	8,858	2,352	1,620	**5.0**	.9
Business and government loans and acceptances							
Consumer goods	**983**	1,383	1,699	1,111	1,411	**.4**	.8
Commercial real estate	**5,984**	5,124	4,082	271	464	**2.8**	.3
Energy	**1,872**	3,731	2,994	3,051	3,887	**.9**	2.2
Government	**126**	130	128	167	773	**.1**	.4
Automotive	**323**	411	527	513	878	**.1**	.5
Industrial products	**532**	1,199	2,116	1,749	1,325	**.2**	.8
Transportation and environment	**1,676**	2,442	1,571	1,487	1,975	**.8**	1.1
Forest products	**193**	417	385	468	549	**.1**	.3
Financial services	**7,445**	6,542	9,347	7,912	6,937	**3.5**	4.0
Media and cable (6)	**949**	1,321	1,380	2,033	1,909	**.4**	1.1
Mining and metals	**565**	1,192	1,071	901	881	**.3**	.5
Telecommunication	**371**	1,246	1,558	2,244	1,206	**.2**	.7
Information technology	**81**	180	396	433	709	**–**	.4
Other	**3,804**	3,953	3,688	1,720	2,364	**1.8**	1.5
	24,904	29,271	30,942	24,060	25,268	**11.6**	14.6
Reverse repurchase agreements	**21,293**	16,715	13,010	6,209	7,922	**9.9**	4.5
Total international	**56,930**	57,338	52,810	32,621	34,810	**26.5**	20.0
Total loans, acceptances and reverse repurchase agreements	**214,681**	215,343	217,181	186,146	174,368	**100%**	100%
Allowance for loan losses	**(2,055)**	(2,203)	(2,278)	(1,871)	(1,884)		
Total	**$ 212,626**	$ 213,140	$ 214,903	$ 184,275	$ 172,484		

(1) Based on residence of borrower.
(2) Comprises Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.
(3) Comprises Manitoba, Saskatchewan and Alberta.
(4) Comprises the following industries in 2003: commercial real estate of $1,777 million (2002 – $1,737 million; 2001 – $1,788 million), consumer goods of $1,777 million (2002 – $1,583 million; 2001 – $1,665 million), industrial products of $952 million (2002 – $887 million; 2001 – $916 million), transportation and environment of $503 million (2002 – $552 million; 2001 – $605 million), automotive of $462 million (2002 – $377 million; 2001 – $434 million), forest products of $298 million (2002 – $278 million; 2001 – $296 million), energy of $137 million (2002 – $125 million; 2001 – $157 million), information technology of $113 million (2002 – $93 million; 2001 – $133 million), mining and metals of $65 million (2002 – $69 million; 2001 – n.a.), financial services of $136 million (2002 – $132 million; 2001 – $96 million), media and cable of $81 million (2002 – $77 million; 2001 – $84 million), telecommunications of $48 million (2002 – $34 million; 2001 – $45 million), and other of $3,356 million (2002 – $3,526 million; 2001 – $3,569 million).
(5) Commencing in 2002, certain amounts were reclassified from the transportation and environment sector grouping to the automotive group.
(6) Includes cable loans of $236 million in Canada in 2003 (2002 – $267 million; 2001 – $330 million; 2000 – $262 million; 1999 – $169 million) and $432 million internationally in 2003 (2002 – $634 million; 2001 – $625 million; 2000 – $1,321 million; 1999 – $850 million).

TABLE 13 Impaired loans

(C$ millions, except percentage amounts)	2003		2002		2001	2000	1999
	Gross	**Net** (1)	Gross	Net (1)	Net (1)	Net (1)	Net (1)
Canada							
Atlantic provinces (2)	**$ 81**	**$ 44**	$ 107	$ 55	$ 67	$ 65	$ 37
Quebec	**155**	**85**	90	60	204	121	158
Ontario	**348**	**199**	471	261	330	287	190
Prairie provinces (3)	**140**	**79**	177	98	71	57	109
British Columbia	**340**	**219**	427	292	335	266	287
Total Canada	**1,064**	**626**	1,272	766	1,007	796	781
Consumer							
Residential mortgage	**110**	**98**	102	87	118	157	131
Personal	**213**	**84**	275	112	129	51	66
	323	**182**	377	199	247	208	197
Business and government							
Small business (4)	**169**	**80**	205	104	132	141	134
Agriculture (4)	**127**	**90**	141	97	86	39	49
Commercial mortgages	**24**	**18**	17	8	5	–	7
Consumer goods	**32**	**17**	47	26	5	23	19
Commercial real estate	**8**	**4**	23	11	44	41	109
Energy	**1**	**1**	1	1	9	–	32
Automotive	**–**	**–**	10	3	5	4	–
Industrial products	**18**	**5**	23	12	26	18	6
Transportation and environment	**118**	**62**	138	108	222	120	12
Forest products	**169**	**115**	199	156	184	180	197
Financial services	**3**	**3**	–	(1)	2	7	1
Media and cable	**15**	**13**	18	6	15	17	30
Mining and metals	**–**	**–**	–	–	1	(1)	(1)
Telecommunication	**8**	**3**	20	6	–	–	–
Information technology	**17**	**13**	6	2	7	(2)	2
Other	**32**	**20**	47	28	17	1	(13)
	741	**444**	895	567	760	588	584
Total Canada	**1,064**	**626**	1,272	766	1,007	796	781
International							
United States	**361**	**219**	584	355	375	69	25
Europe, Middle East and Africa	**116**	**21**	115	50	35	7	12
Caribbean	**66**	**47**	71	52	39	26	28
Latin America	**109**	**57**	217	154	5	3	3
Asia	**1**	**1**	3	–	3	2	35
Australia and New Zealand	**28**	**17**	26	17	19	–	–
Total international	**681**	**362**	1,016	628	476	107	103
Consumer							
Residential mortgage	**21**	**20**	29	26	35	5	6
Personal	**22**	**12**	31	17	8	–	–
	43	**32**	60	43	43	5	6
Business and government							
Consumer goods	**16**	**12**	10	7	7	–	2
Commercial real estate	**65**	**53**	75	62	49	1	4
Energy	**239**	**96**	242	139	–	(2)	3
Automotive	**7**	**6**	29	22	25	–	(3)
Industrial products	**7**	**2**	30	13	(2)	38	15
Transportation and environment	**18**	**7**	68	39	58	25	–
Financial services	**42**	**11**	77	46	24	(2)	22
Media and cable (5)	**71**	**57**	56	56	–	–	–
Mining and metals	**57**	**25**	128	90	29	6	2
Telecommunication	**–**	**–**	77	35	122	–	–
Information technology	**11**	**1**	48	17	70	–	–
Other	**105**	**60**	116	59	51	36	52
	638	**330**	956	585	433	102	97
Total international	**681**	**362**	1,016	628	476	107	103
Total (6), (7)	**$ 1,745**	**$ 988**	$ 2,288	$ 1,394	$ 1,483	$ 903	$ 884

(1) Net of specific allowance.
(2) Comprises Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.
(3) Comprises Manitoba, Saskatchewan and Alberta.
(4) Includes government guaranteed portions of impaired loans of $39 million in small business in 2003 (2002 – $64 million; 2001 – $95 million; 2000 – $101 million; 1999 – $79 million) and $9 million in agriculture (2002 – $10 million; 2001 – $6 million; 2000 – $6 million; 1999 – $5 million).
(5) Consists entirely of cable loans.
(6) Includes foreclosed assets of $34 million in 2003 (2002 – $32 million; 2001 – $37 million; 2000 – $16 million; 1999 – $26 million).
(7) Past due loans greater than 90 days not included in impaired loans was $222 million in 2003 (2002 – $217 million; 2001 – $245 million).

TABLE 14 Provision for credit losses

(C$ millions, except percentage amounts)	2003	2002	2001	2000	1999
Canada					
Atlantic provinces (1)	**$ 46**	$ 59	$ 63	$ 58	$ 32
Quebec	**77**	(5)	43	22	71
Ontario	**309**	330	398	342	52
Prairie provinces (2)	**55**	86	81	64	95
British Columbia	**40**	59	104	40	192
Total Canada	**527**	529	689	526	442
Consumer					
Residential mortgage	**4**	3	8	–	4
Personal	**230**	266	265	301	172
Credit card	**152**	135	125	102	55
	386	404	398	403	231
Business and government					
Small business	**77**	110	164	105	113
Agriculture	**(2)**	22	20	4	2
Commercial mortgages	**(3)**	(5)	7	2	8
Consumer goods	**2**	19	2	7	11
Commercial real estate	**(14)**	(15)	15	(17)	9
Energy	**–**	4	17	(8)	12
Automotive	**–**	–	17	–	–
Industrial products	**2**	(7)	14	2	(10)
Transportation and environment	**69**	(19)	13	56	7
Forest products	**13**	4	7	(36)	81
Financial services	**(4)**	(27)	(9)	–	5
Media and cable	**1**	(7)	13	12	8
Mining and metals	**1**	(1)	–	(1)	1
Telecommunication	**5**	59	–	(1)	(32)
Information technology	**2**	3	3	8	8
Other	**(8)**	(15)	8	(10)	(12)
	141	125	291	123	211
Total Canada	**527**	529	689	526	442
International					
United States	**108**	440	377	99	45
Europe, Middle East and Africa	**64**	38	(1)	(9)	21
Caribbean	**8**	6	(6)	3	–
Latin America	**15**	57	5	2	2
Asia	**(1)**	(10)	(19)	(50)	20
Australia and New Zealand	**–**	5	4	–	–
Total international	**194**	536	360	45	88
Consumer					
Residential mortgage	**4**	7	–	–	1
Personal	**24**	15	5	–	–
Credit card	**3**	4	2	–	–
	31	26	7	–	1
Business and government					
Consumer goods	**8**	(2)	–	(7)	(10)
Commercial real estate	**5**	4	65	1	2
Energy	**78**	141	(8)	(2)	–
Automotive	**(1)**	1	7	(8)	(2)
Industrial products	**(1)**	5	3	34	31
Transportation and environment	**8**	21	8	42	–
Financial services	**3**	21	(3)	(21)	2
Media and cable	**26**	–	3	–	–
Mining and metals	**4**	28	–	2	15
Telecommunication	**–**	202	272	–	–
Information technology	**(4)**	41	7	–	3
Other	**37**	48	(1)	4	46
	163	510	353	45	87
Total international	**194**	536	360	45	88
Total specific provision	**721**	1,065	1,049	571	530
General allocated (3)	**6**	(22)	205	73	n.a.
General unallocated (3)	**(6)**	22	(135)	47	n.a.
Total general provision (3)	**–**	–	70	120	230
Total	**$ 721**	$ 1,065	$ 1,119	$ 691	$ 760

(1) Comprises Newfoundland and Labrador, Prince Edward Island, Nova Scotia and New Brunswick.
(2) Comprises Manitoba, Saskatchewan and Alberta.
(3) The general allocated provision and the general unallocated provision together totalled $230 million in 1999. This was not separated into the general allocated and general unallocated components.

TABLE 15 Allowance for credit losses

(C$ millions, except percentage amounts)	2003	2002	2001	2000	1999
Allowance at beginning of year	**$ 2,314**	$ 2,392	$ 1,975	$ 1,900	$ 2,066
Provision for credit losses	**721**	1,065	1,119	691	760
Write-offs					
Canada					
Residential mortgage	**(6)**	(11)	(15)	(11)	(14)
Personal	**(345)**	(381)	(394)	(372)	(236)
Credit card	**(188)**	(172)	(169)	(150)	(65)
Business and government	**(224)**	(330)	(296)	(225)	(524)
	(763)	(894)	(874)	(758)	(839)
International					
Residential mortgage	**(4)**	(1)	(9)	–	–
Personal	**(28)**	(17)	(7)	–	–
Credit card	**(4)**	(6)	(2)	–	–
Business and government	**(183)**	(506)	(233)	(81)	(229)
LDC exposures	**–**	(33)	–	–	(4)
	(219)	(563)	(251)	(81)	(233)
	(982)	(1,457)	(1,125)	(839)	(1,072)
Recoveries					
Canada					
Residential mortgage	**–**	–	–	–	2
Personal	**66**	68	66	44	31
Credit card	**36**	37	44	48	10
Business and government	**53**	72	58	48	66
	155	177	168	140	109
International					
Personal	**2**	2	1	–	–
Credit card	**1**	1	–	–	–
Business and government	**12**	18	16	22	5
	15	21	17	22	5
	170	198	185	162	114
Net write-offs	**(812)**	(1,259)	(940)	(677)	(958)
Acquisition of Admiralty Bancorp, Inc.	**8**	–	–	–	–
Acquisition of Eagle Bancshares, Inc.	**–**	18	–	–	–
Acquisition of Centura Banks	**–**	–	157	–	–
Adjustments	**(67)**	98	81	61	32
Allowance at end of year	**$ 2,164**	$ 2,314	$ 2,392	$ 1,975	$ 1,900
Allocation of allowance (1)					
Canada					
Residential mortgage	**$ 33**	$ 35	$ 45	$ 46	$ 53
Personal	**395**	429	447	403	344
Credit card	**147**	147	147	88	60
Business and government	**682**	711	791	664	748
	1,257	1,322	1,430	1,201	1,205
International					
Residential mortgage	**4**	6	4	11	9
Personal	**42**	36	33	–	–
Credit card	**4**	5	5	–	–
Business and government	**510**	583	581	322	380
	560	630	623	333	389
Allocated allowance for loan losses	**1,817**	1,952	2,053	1,534	1,594
General unallocated allowance for loan losses	**238**	251	225	337	290
Total allowance for loan losses	**2,055**	2,203	2,278	1,871	1,884
Allowance for off-balance sheet and other items (2)	**109**	109	109	98	–
Allowance for loan substitute securities	**–**	2	5	6	16
Total allowance for credit losses	**$ 2,164**	$ 2,314	$ 2,392	$ 1,975	$ 1,900

(1) The allowance for loan losses includes an amount for the general allocated allowance, which has been allocated to loan categories. These amounts total $1,060 million (2002 – $1,060 million; 2001 – $1,076 million; 2000 – $765 million; 1999 – $790 million) and have been allocated as follows: for Canada – residential mortgage $21 million (2002 – $20 million; 2001 – $21 million; 2000 – $18 million; 1999 – $11 million), personal $266 million (2002 – $266 million; 2001 – $266 million; 2000 – $207 million; 1999 – $174 million), credit card $147 million (2002 – $147 million; 2001 – $147 million; 2000 – $88 million; 1999 – $60 million), business and government $385 million (2002 – $386 million; 2001 – $385 million; 2000 – $321 million; 1999 – $370 million), and for International – residential mortgage $2 million (2002 – $3 million; 2001 – $2 million; 2000 and 1999 – nil), personal $33 million (2002 – $22 million; 2001 – $26 million; 2000 and 1999 – nil), credit card $4 million (2002 – $5 million; 2001 – $5 million; 2000 and 1999 – nil), and business and government $202 million (2002 – $211 million; 2001 – $224 million; 2000 – $131 million; 1999 – $175 million).

(2) Commencing in 2000, the allowance for off-balance sheet and other items was separated and reported under other liabilities. Previously, the amount was included in the allowance for loan losses.

TABLE 16 Foreign outstandings (1)

(C$ millions, except percentage amounts)	2003	2003 % of total assets	2002	2002 % of total assets	2001	2001 % of total assets
United States – Banks	**$ 7,204**		$ 5,838		$ 7,186	
Government	**7,970**		3,257		3,834	
Other	**57,086**		62,210		49,172	
	72,260	**17.93%**	71,305	18.92%	60,192	16.75%
Western Europe						
United Kingdom – Banks	**8,600**		7,179		6,275	
Government	**512**		295		153	
Other	**9,141**		5,719		5,256	
	18,253	**4.53**	13,193	3.50	11,684	3.25
France – Banks	**4,073**		2,061		2,378	
Government	**166**		86		68	
Other	**678**		831		1,176	
	4,917	**1.22**	2,978	.79	3,622	1.01
Germany – Banks	**5,974**		5,344		5,952	
Government	**1,309**		318		173	
Other	**385**		381		559	
	7,668	**1.90**	6,043	1.60	6,684	1.86
Netherlands	**2,458**	**.61**	2,271	.60	2,218	.62
Switzerland	**763**	**.19**	1,714	.45	1,362	.38
Other	**5,223**	**1.30**	5,658	1.51	5,244	1.46
	39,282	**9.75**	31,857	8.45	30,814	8.58
Central/Eastern Europe, Middle East and Africa	**198**	**.05**	247	.07	469	.13
Latin America						
Argentina	**87**	**.02**	146	.04	193	.06
Brazil	**33**	**.01**	38	.01	71	.02
Chile	**385**	**.09**	800	.21	836	.23
Mexico	**318**	**.08**	493	.13	696	.19
Other	**42**	**.01**	42	.01	174	.05
	865	**.21**	1,519	.40	1,970	.55
Caribbean						
Bahamas	**1,255**	**.31**	1,453	.38	1,520	.42
Other	**1,437**	**.36**	485	.13	1,902	.53
	2,692	**.67**	1,938	.51	3,422	.95
Asia						
Japan – Banks	**428**		321		53	
Government	**4,263**		2,426		1,663	
Other	**92**		64		988	
	4,783	**1.19**	2,811	.75	2,704	.75
Singapore	**289**	**.07**	229	.06	217	.06
South Korea	**389**	**.10**	405	.11	449	.13
Other	**330**	**.08**	38	.01	145	.04
	5,791	**1.44**	3,483	.93	3,515	.98
Australia and New Zealand	**2,425**	**.60**	2,842	.75	2,335	.65
Allowance for loan losses (2)	**(678)**	**(.17)**	(760)	(.20)	(728)	(.20)
Total	**$ 122,835**	**30.48%**	$ 112,431	29.83%	$ 101,989	28.39%

(1) Includes contractual amounts with clients in a foreign country related to: loans, accrued interest, acceptances, interest-bearing deposits with banks, securities, other interest-earning investments and other monetary assets including net revaluation gains on foreign exchange and derivative products. Local currency outstandings, whether or not hedged or funded by local currency borrowings, are included in country exposure outstandings. Foreign outstandings are reported based on location of ultimate risk.

(2) Includes the international component of the specific, general allocated and general unallocated allowance. For years prior to 2002, the allowance for loan losses also includes the country risk allowance.

TABLE 17 U.S. loans, acceptances and reverse repurchase agreements and loan quality information (1)

	Loan balances				Gross impaired loans				Net impaired loans				Provision for credit losses			
(C$ millions)	**2003**	2002	2001	2000	**2003**	2002	2001	2000	**2003**	2002	2001	2000	**2003**	2002	2001	2000
Consumer																
Residential mortgage	**$ 4,094**	$ 4,351	$ 2,664	$ 845	**$ 7**	$ 16	$ 24	$ –	**$ 6**	$ 13	$ 22	$ –	**$ 3**	$ 7	$ 8	$ –
Personal	**5,015**	5,269	4,621	78	**22**	31	15	–	**12**	17	8	–	**24**	15	5	–
Credit card	**107**	125	128	–	**–**	–	–	–	**–**	–	–	–	**3**	4	2	–
	9,216	9,745	7,413	923	**29**	47	39	–	**18**	30	30	–	**30**	26	15	–
Business and government loans and acceptances																
Consumer goods	**816**	958	1,172	435	**16**	10	9	–	**12**	7	7	–	**8**	4	2	–
Commercial real estate	**5,480**	4,531	3,773	44	**65**	75	81	4	**53**	62	49	1	**5**	5	66	2
Energy	**1,200**	2,680	1,613	1,582	**114**	95	–	–	**49**	29	–	–	**16**	107	–	–
Government	**100**	19	23	–	**–**	–	–	–	**–**	–	–	–	**–**	–	–	–
Automotive	**318**	409	408	221	**7**	29	33	–	**6**	22	25	–	**(1)**	1	6	–
Industrial products	**449**	974	1,513	1,107	**5**	30	8	68	**2**	13	(1)	34	**(1)**	8	3	40
Transportation and environment	**350**	484	788	469	**9**	36	48	56	**2**	28	26	25	**7**	5	(4)	42
Forest products	**123**	223	98	181	**–**	–	–	–	**–**	–	–	–	**–**	–	–	–
Financial services	**3,011**	3,770	4,104	4,521	**9**	46	30	–	**6**	35	23	–	**–**	11	7	–
Media and cable (2)	**854**	1,107	1,038	1,782	**44**	56	–	–	**44**	56	–	–	**12**	–	3	–
Mining and metals	**91**	70	45	104	**–**	–	–	–	**–**	–	–	–	**–**	–	–	–
Telecommunication	**315**	689	835	1,131	**–**	77	272	–	**–**	35	122	–	**–**	202	272	–
Information technology	**81**	177	299	374	**11**	48	76	–	**1**	17	70	–	**(4)**	41	7	–
Other	**2,736**	3,348	3,089	541	**52**	35	30	17	**26**	21	24	9	**36**	30	–	15
	15,924	19,439	18,798	12,492	**332**	537	587	145	**201**	325	345	69	**78**	414	362	99
Reverse repurchase agreements	**5,721**	3,258	3,668	2,524	**–**	–	–	–	**–**	–	–	–	**–**	–	–	–
	$30,861	$32,442	$29,879	$15,939	**$ 361**	$ 584	$ 626	$ 145	**$ 219**	$ 355	$ 375	$ 69	**$ 108**	$ 440	$ 377	$ 99

(1) Based on residence of the borrower.
(2) Includes cable loans of $357 million in 2003 (2002 – $522 million; 2001 – $455 million; 2000 – $1,162 million) and gross and net impaired cable loans of $44 million in 2003 (2002 – $56 million).

TABLE 18 Risk profile

(C$ millions, except percentage amounts)	**2003**	2002	2001	2000	1999
Percentage of loans to total loans (1)					
Canada (2)					
Residential mortgage	**35%**	32%	30%	33%	34%
Personal	**13**	12	12	15	14
Credit card	**2**	2	2	2	1
Business and government	**22**	26	30	32	32
	72	72	74	82	81
International	**28**	28	26	18	19
Total	**100%**	100%	100%	100%	100%
Gross impaired loans					
Beginning of year	**$ 2,288**	$ 2,465	$ 1,678	$ 1,704	$ 2,001
Net additions	**439**	1,280	1,912	813	743
Write-offs and adjustments	**(982)**	(1,457)	(1,125)	(839)	(1,040)
End of year	**$ 1,745**	$ 2,288	$ 2,465	$ 1,678	$ 1,704
Net impaired loans as a % of related loans, acceptances and reverse repurchase agreements					
Canada (2)					
Residential mortgage	**.13%**	.13%	.18%	.26%	.22%
Personal	**.30**	.43	.48	.19	.27
Business and government	**.94**	1.00	1.17	.99	1.05
	.41	.49	.63	.52	.55
International	**.61**	1.05	.85	.33	.32
Total	**.46%**	.65%	.69%	.49%	.51%
Allowance for credit losses					
Specific	**$ 757**	$ 894	$ 951	$ 747	$ 786
Country risk	**–**	–	31	28	34
General allowance					
General allocated (4)	**1,169**	1,169	1,185	863	790
General unallocated	**238**	251	225	337	290
Total general allowance	**1,407**	1,420	1,410	1,200	1,080
Total	**$ 2,164**	$ 2,314	$ 2,392	$ 1,975	$ 1,900
As a % of loans, acceptances and reverse repurchase agreements	**1.0%**	1.0%	1.1%	1.0%	1.1%
As a % of impaired loans (coverage ratio), excluding LDCs	**118%**	96%	93%	112%	112%
Provision for credit losses					
Specific	**$ 721**	$ 1,065	$ 1,049	$ 571	$ 530
General provision (3)					
General allocated	**6**	(22)	205	73	n.a.
General unallocated	**(6)**	22	(135)	47	n.a.
Total general provision	**–**	–	70	120	230
Total	**$ 721**	$ 1,065	$ 1,119	$ 691	$ 760
Credit derivative gains	**(29)**	(102)	–	–	–
Credit derivative losses	**–**	69	–	–	–
Total provision net of credit derivative gains/losses	**$ 692**	$ 1,032	$ 1,119	$ 691	$ 760
Specific provision net of credit derivative gains/losses as a % of average loans, acceptance and reverse repurchase agreements	**.32%**	.49%	–%	–%	–%
As a % of related average loans, acceptances and reverse repurchase agreements					
Canada					
Residential mortgage	**.01%**	–%	.01%	–%	.01%
Personal	**.85**	1.00	.94	1.12	.71
Credit card	**2.92**	3.10	2.73	2.87	2.39
Business and government	**.26**	.21	.52	.22	.40
	.34	.34	.45	.36	.32
International	**.32**	.98	.74	.13	.23
Total specific provision	**.33%**	.51%	.53%	.32%	.30%
Total provision for credit losses	**.33**	.51	.56	.38	.43
Net write-offs (excluding LDCs) as a % of average loans, acceptances and reverse repurchase agreements	**.37%**	.58%	.47%	.38%	.54%
Net write-offs as a % of average loans, acceptances and reverse repurchase agreements	**.37%**	.60%	.47%	.38%	.55%

(1) Loans include acceptances and reverse repurchase agreements.
(2) Loans in Canada include all loans booked in Canada, regardless of the currency or residence of the borrower.
(3) The general allocated provision and the general unallocated provision totalled $230 million in 1999. These were not separated into the general allocated and general unallocated components.
(4) Includes the allowance for off-balance sheet and other items.

Risk management

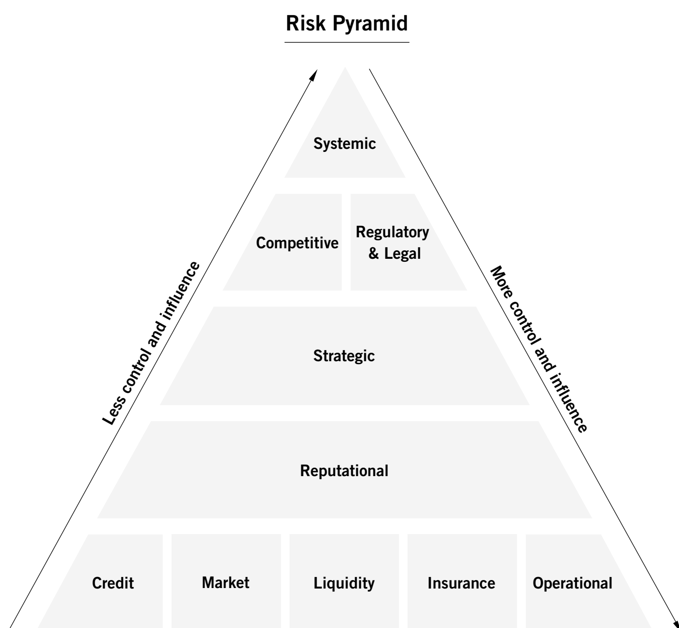
Overview

The mission of the risk management function is to build shareholder value through leadership in the strategic management of risk. Strategic priorities are to:

- Ensure alignment of risk appetite and business strategies
- Attract, develop and retain high-performing risk management professionals
- Enhance communication on risk and risk appetite throughout the organization
- Invest in capabilities to better measure, understand and manage risk
- Strengthen the efficiency, accessibility and responsiveness of key risk processes and practices

Our business activities expose us to the risks outlined in the risk pyramid below. We use the risk pyramid as a tool to identify and assess risk across the organization. Risks are shown within the pyramid according to the level of control and influence that we can exert to mitigate or manage each specific risk type.

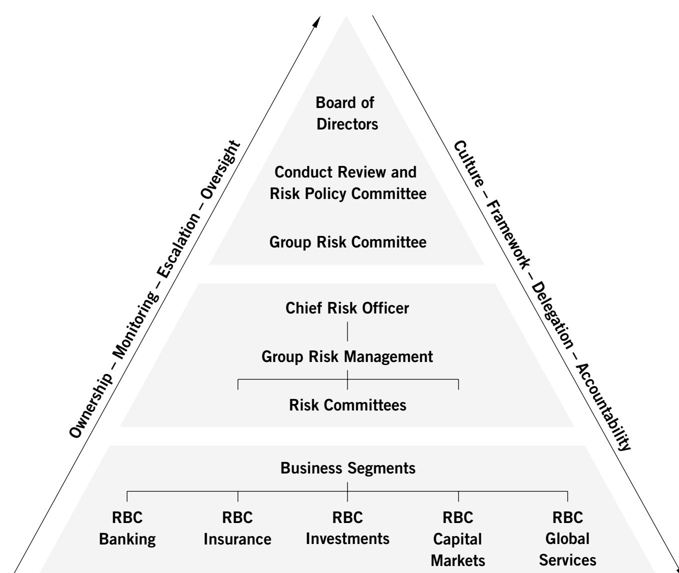
Risk Pyramid



Controllable risks

- **Credit risk** is the risk of loss due to a counterparty's inability to fulfill its payment obligations. It also refers to a loss in market value due to the deterioration of a counterparty's financial position. A counterparty may be an issuer, debtor, borrower, policyholder, reinsurer or guarantor.
- **Market risk** is the risk of loss that results from changes in interest rates, foreign exchange rates, equity prices and commodity prices.
- **Liquidity risk** is the risk that we are unable to generate or obtain sufficient cash or equivalents on a cost-effective basis to meet our commitments as they fall due.
- **Insurance risk** relative to our insurance platform, is the risk inherent in the development, issuance and administration of insurance policies, and includes product design and pricing risk, claims administration risk, underwriting risk and liability risk.
- **Operational risk** is the risk of direct or indirect loss resulting from inadequate or failed processes, technology, human performance or external events. The impact of operational risk can be financial loss, loss of reputation, loss of competitive position, poor client service and resulting legal or regulatory proceedings.

The Risk Pyramid: An organizational perspective



An organizational perspective

The cornerstone of effective risk management is a strong risk management culture, supported by numerous strategy and policy development processes, run jointly by risk management professionals and the business segments. This partnership is designed to ensure strategic alignment of business, risk and resource issues.

Risk management professionals work in partnership with the business segment and functional units to identify risks, which are then measured, monitored and managed. In line with our group-wide portfolio management approach, portfolio analysis techniques are employed in an effort to optimize the risk-reward profile and ensure the efficient and appropriate attribution of capital.

A structure of management and board committees provides oversight of the risk management process.

The Board of Directors and Group Risk Committee
The top level of the organizational perspective risk pyramid on page 53A comprises the Board of Directors, the Conduct Review and Risk Policy Committee and Group Risk Committee.

Key responsibilities are to:
- Shape, influence and communicate the organization's risk culture
- Determine and communicate the organization's risk appetite
- Define the organizational structure for Group Risk Management
- Review and approve policies for controlling risk
- Review and monitor the major risks being assumed by, or facing, the organization and provide direction as required
- Ensure there are sufficient and appropriate risk management resources across the organization to protect against the risks being taken

Risk management
The middle level of the organizational perspective risk pyramid comprises the Chief Risk Officer, Group Risk Management and the various Risk Committees. The Risk Committees include the Asset/Liability Committee, U.S. Corporate Governance Committee, Ethics and Compliance Committee, Risk Management Committee and other committees responsible for areas such as interest rate risk and trading risk. To address the increasing complexity of products in the marketplace, New Business Committees were established in 2003 in London, New York and Toronto to provide risk oversight of all new business initiatives in RBC Capital Markets.

Key responsibilities of the Chief Risk Officer, Group Risk Management and the various Risk Committees are to:
- Implement and maintain an integrated enterprise-wide risk measurement, management and reporting framework
- Establish a comprehensive risk assessment and approval process including enterprise-wide policies and procedures
- Establish guidelines and risk limits to ensure appropriate risk diversification and optimization of risk-return on both a portfolio and transactional basis
- Advise the board and executive management of major risks being assumed by, or facing, the organization
- Partner with the business segments to identify, understand, measure, mitigate and monitor the risks being taken

Economic Capital

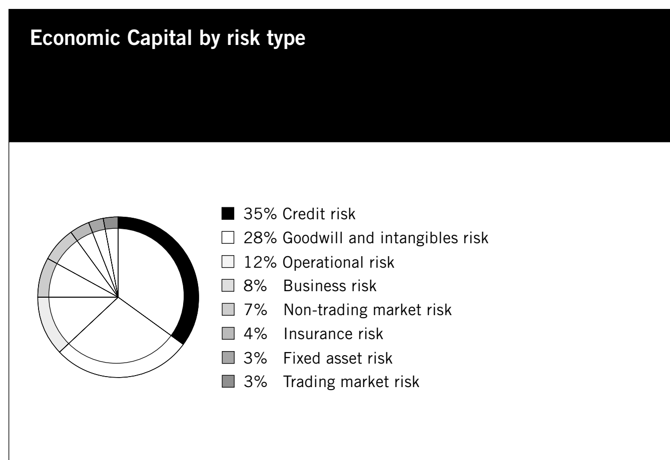
Economic Capital (EC) is an estimate of the amount of common equity required to underpin risks. It is calculated by estimating the level of capital that is necessary to cover risks consistent with our desired solvency standard and AA debt rating. EC analysis is intended to represent the shareholder's perspective and drives the optimization of shareholder returns. Calculation of EC involves a number of assumptions and judgments, and changes to them may result in materially different amounts of EC being computed. Capital attribution methodologies are continually monitored to ensure risks are being consistently quantified utilizing all available information. Periodically, enhancements are made to these methodologies with the changes applied prospectively.

EC is attributed to our business segments to provide directly comparable performance measurements for each of our business activities and to assist senior management in strategic planning, resource allocation and performance measurement.

EC is calculated for eight distinct risk types. Credit, market, insurance and operational risk are detailed in the following sections. Business risk is the risk of loss due to variances in volumes, prices and costs caused by competitive forces, regulatory changes, and reputational and strategic risks. Goodwill and intangibles, and fixed asset risks are defined as the risk that the value of these assets will be less than their net book value at a future date.

The total required economic capital takes into account the diversification benefits between and within risk categories and lines of business. These diversification benefits are passed on to our businesses and are reflected in the EC levels used in their ROE calculations.

The following chart represents the proportionate EC levels by risk type for fiscal 2003. Over the past three years there has been a shift of economic capital from credit risk to goodwill and intangibles risk, which is consistent with our strategies of reducing non-core lending exposures, and our expansion in the U.S.



The following sections discuss how we manage the major controllable risks, which include credit, market, liquidity, insurance and operational risk.

Credit risk

Our approach to credit risk management preserves the independence and integrity of risk assessment while being integrated into the portfolio management processes. Policies and procedures, which are communicated throughout the organization, guide the day-to-day management of credit risk exposure and are an essential part of our business culture. The goal of credit risk management is to evaluate and manage credit risk in order to further enhance our strong credit culture.

We manage credit risk directly through key control processes, risk measurements used by management to monitor performance and through the use of certain risk mitigation strategies.

Key control processes
Credit scoring models are used for underwriting and ongoing monitoring of consumer and certain small business credit. Applicant scoring is used for underwriting purposes and utilizes established statistical methods of analyzing applicant characteristics and past performance to determine the probability of the risk for future credit performance. Behavioural scoring is used for ongoing management of booked accounts and utilizes statistical techniques that capture past performance to predict future behaviour of existing accounts. Both applicant and behavioural scores use customer centric scoring models which consider the strength of the entire client relationship, utilizing certain variables, to predict future behaviour.

For commercial and corporate clients, we assign an internal risk rating based on a detailed review of the borrower. This examination considers industry sector trends, market competitiveness, overall company strategy, financial strength, access to funds, financial management and any other risks facing the organization. Our rating system is based on a 22-point scale. The internal risk ratings are assessed and updated on a regular basis.

In addition to control processes for credit granting and ongoing monitoring, we have established risk limits in place to ensure that we do not become over-exposed to any one borrower or family of related borrowers, industry sector or geographic area.

Risk measurements
Credit risk is monitored on an ongoing basis with formal monthly and quarterly reporting to ensure our senior management is aware of shifts in loan quality and portfolio performance. The three critical components of this reporting framework are a dashboard for consumer and small business lending, and classification reporting and expected loss monitoring on the commercial and corporate lending portfolios.

The dashboard is a monthly reporting mechanism in place for all consumer and small business loan portfolios. The performance of each portfolio is assessed against various risk/reward measures and assigned one of the following ratings – concern, monitor or good. At year-end, portfolios representing approximately 3% of consumer and small business loans outstanding at October 31, 2003, were rated as concern. To monitor any shifts in portfolio quality, further assessment criteria are applied to each portfolio to generate one of the following portfolio quality trend indicators – declining, stable or improving. At year-end, most portfolios reflected a stable or improving portfolio quality trend, including the portfolios classified as concern from a risk-reward perspective.

Classification reporting is an ongoing process in place to ensure that Account and Risk Managers are effective in early problem recognition on commercial and corporate lending. Once any sign of weakness is identified or concern is raised, the exposure is classified as Especially Mentioned, Substandard, Doubtful or Loss. Total classified outstanding loans decreased by $2.2 billion from a year ago to $3.9 billion at October 31, 2003.

In addition, current one-year expected losses on our commercial and corporate loan portfolio provides a good indicator of asset quality trends. Expected loss is compared to long-term or through-the-cycle expected losses to assess where we are in the credit cycle.

Risk mitigation
To respond proactively to credit deterioration and to mitigate risk, a problem loan workout group with specialized expertise handles the management and collection of impaired loans and certain performing loans.

Portfolio diversification remains the cornerstone of our risk mitigation activities, and as a result, our credit policies and limits are structured to ensure we are not overexposed to any given client, industry sector or geographic area.

To avoid excessive losses resulting from a particular counterparty being unable to fulfill its payment obligations, single-name limits are in place, with the limit set based on the applicable risk rating. In certain cases loans are syndicated in order to reduce overall exposure to a single name.

Limits are also in place to manage exposure to any particular country or sector. Each country and sector is assigned a risk rating. This risk rating considers factors common to all entities in a given country or sector yet outside the control of any individual entity. Limits are determined based on the risk rating along with our overall risk appetite and business strategy.

To mitigate risk on portions of our portfolio, we enter into credit derivative contracts. As at October 31, 2003, credit mitigation was in place to cover $.7 billion in corporate credit exposure, down from $1 billion as at October 31, 2002, reflecting overall improvements in asset quality which resulted in a lower need for protection.

Loan sales are also used to manage risk. We seek to identify and sell loans we have made to borrowers whose risk/reward profiles and borrower ratings no longer satisfy our requirements. Loan sales totalled approximately $.5 billion in 2003.

Market risk

Market risk is the risk of loss that results from changes in interest rates, foreign exchange rates, equity prices and commodity prices. The level of market risk to which we are exposed varies depending on market conditions, expectations of future price and market movements and the composition of our trading portfolio. We establish risk management policies and limits for our trading and asset/liability management activities that allow us to monitor and control our exposure to market risk resulting from these activities.

We conduct trading activities over-the-counter and on exchanges in the spot, forward, futures and options markets, and we also participate in structured derivative transactions. Market risks associated with trading activities are a result of market-making, positioning and sales and arbitrage activities in the interest rate, foreign exchange, equity, commodities and credit markets. Our trading operation primarily acts as a market maker, executing transactions that meet the financial requirements of our clients and transferring the market risks to the broad financial market. We also act as principal and take proprietary market risk positions within the authorizations granted by the Board of Directors.

The trading book consists of positions that are held for short-term resale, taken on with the intent of benefiting in the short term from actual and/or expected differences between their buying and selling prices or to lock in arbitrage profits.

Interest rate risk
Interest rate risk is the potential adverse impact on our earnings and economic value due to changes in interest rates. Most of our holdings in financial instruments result in exposure to interest rate risk.

Credit spread risk and debt specific risk
Credit spread and debt specific risk are the potential adverse impact on our earnings and economic value due to changes in the creditworthiness and credit rating of issuers of bonds and money market instruments, or the names underlying credit derivatives. We are exposed to credit spread risk and debt specific risk through our positions in bonds, money market instruments and credit derivatives.

Foreign exchange rate risk
Foreign exchange rate risk is the potential adverse impact on our earnings and economic value due to currency rate movements and volatilities. In our proprietary positions, we hold risk in both the spot and forward foreign exchange markets and in the derivatives market.

Equity risk
Equity risk is the potential adverse impact on our earnings due to movements in individual equity prices or general movements in the level of the stock market. We are exposed to equity risk from the buying and selling of equities as a principal in our investment banking activities. Equity risk also results from our trading activities, including the offering of tailored equity derivative products to clients, arbitrage trading and proprietary trading.

Monitoring market risk
A comprehensive risk policy framework governs trading-related risks and activities and provides guidance to trading management, middle office/ compliance functions and operation areas. We employ an extensive set of principles, rules, controls and limits, which we believe conform to industry best practice. This market risk management framework is designed to ensure that an appropriate diversification of risks is adopted on a global basis. Group Risk Management (GRM) – Market Risk is a corporate function that is independent of the trading operations and it is responsible for the daily monitoring of global trading risk exposures via risk measures such as VAR, sensitivity analysis and stress testing. GRM uses these risk measures to assess global risk-return trends and to alert senior management of adverse trends or positions. These risk measures are reported on a daily basis to senior management. The senior management of RBC Capital Markets and senior executives within GRM review trends in market risk on a weekly basis. Trends in market risk are reported to the Group Risk Committee and the Conduct Review and Risk Policy Committee on a quarterly basis.

TABLE 19 Market risk measures – Trading activities (1)

(C$ millions)	2003 Year-end	2003 High	2003 Average	2003 Low	2002 Year-end	2002 High	2002 Average	2002 Low
Global VAR by major risk category								
Equity	**$ 4**	**$ 12**	**$ 7**	**$ 4**	$ 7	$ 12	$ 8	$ 6
Foreign exchange and commodity	**2**	**7**	**3**	**1**	2	9	3	1
Interest rate	**8**	**13**	**9**	**6**	11	14	6	2
Global VAR (2)	**$ 8**	**$ 19**	**$ 13**	**$ 8**	$ 13	$ 18	$ 11	$ 7

(1) Amounts are presented on a pre-tax basis and represent one-day VAR at a 99% confidence level.
(2) Global VAR reflects the correlation effect from each of the risk categories through diversification.

VAR is an industry standard measure of market risk and is a determinant of minimum regulatory capital requirement. Our VAR model uses statistical models, historical market price information and credit migration statistics to estimate within a given level of confidence the maximum loss in market value that we would experience in our trading portfolios from an adverse movement in market rates, prices or issuer ratings. Our VAR measure is based on a 99% confidence level and is an estimate of the maximum potential trading loss in 99 out of every 100 days. We use a combination of historical simulation of the previous 500 trading days and Monte Carlo event generation for migration and default events to determine VAR for our trading portfolio.

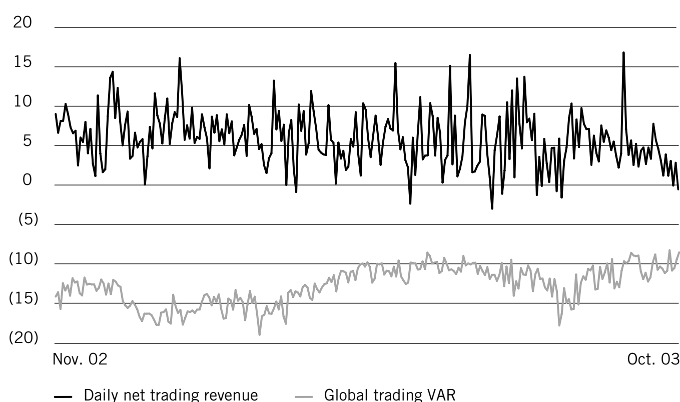
In addition to VAR, extensive sensitivity analysis and stress testing are performed, monitored and reported on a daily basis as a supplementary control on our market risk exposure. Sensitivity analysis is used to measure the impact of small changes in individual risk factors such as interest rates and foreign exchange rates and are designed to isolate and quantify exposure to the underlying risk factors that affect option prices. Stress testing measures the impact of extreme market movements and is intended to alert senior management of the exposure to potential political, economic or other disruptive events.

The year-end, high, average and low VAR by major risk category for our combined trading activities for the years ended October 31, 2003 and 2002 are shown in Table 19 above. The table also shows our global VAR, which incorporates the effects of correlation in the movements of interest rates, exchange rates, equity prices and commodity prices and the resulting benefits of diversification within our trading portfolio. As the table illustrates, the average global VAR in 2003 was $13 million, compared to $11 million in 2002. The largest contributor to VAR is the interest rate product class. The VAR associated with this product class captures the interest rate risk, credit spread risk and default risk associated with money market, fixed income, and fixed income derivatives trading. Risk in newer products not yet captured within our VAR calculation is measured by other sensitivity and stress scenarios appropriate for the products.

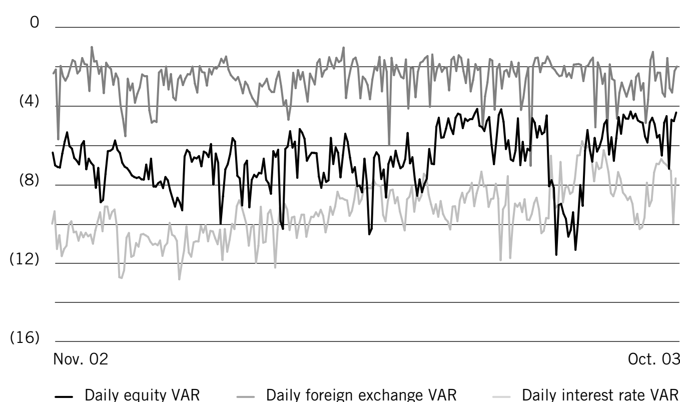
The graph on this page, top right compares the global trading VAR amounts to the relevant daily net trading revenue for the year ended October 31, 2003. During fiscal 2003, we experienced eight days of net trading losses, and net trading losses in any single day did not exceed the VAR estimate for that day. The breadth of our trading activities is designed to diversify market risk to any particular strategy, and to reduce trading revenue volatility.

Back-testing against hypothetical profit and loss is used to monitor the statistical validity of VAR models. Actual one-day changes in market rates and prices as well as actual 10-day changes in issuer ratings are used to calculate hypothetical profit and loss on a given portfolio for a particular date if the end of day portfolio was held constant during the period. Back-testing is performed daily across all trading portfolios. In fiscal 2003, there were no instances of the hypothetical net loss exceeding the VAR.

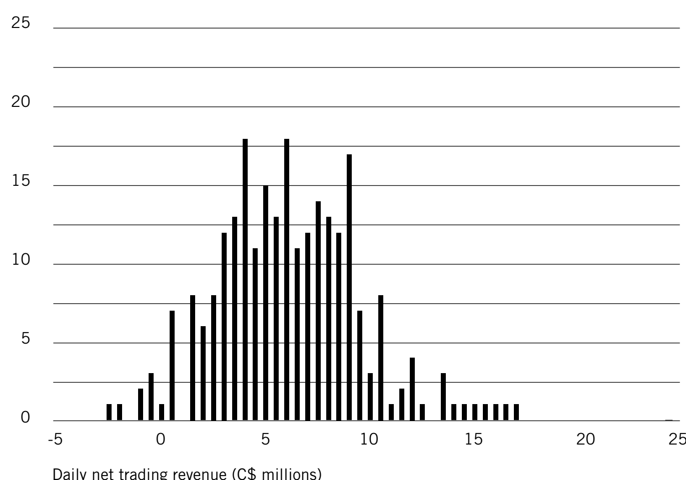
DAILY NET TRADING REVENUE VS GLOBAL TRADING VAR
(C$ millions)



GLOBAL VAR BY MAJOR RISK CATEGORY
(C$ millions)



HISTOGRAM OF DAILY NET TRADING REVENUE
(number of days)



Liquidity risk

The objective of liquidity management is to ensure we have the ability to generate or obtain sufficient cash or its equivalents on a timely and cost-effective basis to meet our commitments as they fall due. The management of liquidity risk is crucial to protecting our capital, maintaining market confidence and ensuring that we can expand into profitable business opportunities.

Liquidity risk is managed dynamically, and exposures are continually measured, monitored and mitigated. We have developed and implemented a comprehensive liquidity management framework comprising policies, procedures, methodologies and measurements.

For further information on liquidity see the Liquidity management section on page 62A.

Insurance risk

The Insurance business contains elements of credit, market and operational risk, and it also subjects us to product design and pricing risk, claims administration risk, underwriting risk and liability risk.

The process of designing and pricing products includes the estimation of many factors including future investment yields, claims experience, expenses, policy lapse rates and taxes. Product design and pricing risk is the risk that actual experience will not match the assumptions made at the time pricing was determined and, as a result, financial losses will occur.

This risk is managed through detailed experience studies to support pricing assumptions and independent verification of scenario testing by our actuaries. In addition a portion of the policy benefit liabilities held on the balance sheet provides for misestimation and deterioration of assumptions from those assumed in the pricing. Claims experience risk in relation to estimates of future mortality and morbidity can also be mitigated through reinsurance.

Claims administration risk is the exposure to higher than expected claims due to administrative practices in settling claims. Policies and procedures are in place designed to ensure that trained staff properly handle claims. There are approval limits in place to ensure that large-dollar claims are handled and reviewed by more senior staff.

Underwriting risk is the risk of exposure to financial losses resulting from the inappropriate selection and acceptance of the risks to be insured. Establishing policy retention limits that vary by market and geographic location or having property and casualty catastrophe reinsurance, mitigates exposure to large claims.

Liability risk is the risk that attributes of a specific type of risk are misunderstood and improperly quantified, resulting in the liabilities established for this type of risk being inadequate. Actuaries review the assumptions used in the calculation of policy benefit liabilities on a quarterly basis to reduce our exposure to this type of risk.

The overall insurance risks assumed are dependent on our ability to reprice the contracts. For property and casualty insurance risks (mainly travel, home & auto) and group life insurance, the price charged for coverage is guaranteed for relatively short periods (up to a year). For most individual life insurance, the price charged for coverage can be guaranteed for periods of several years and there is greater insurance risk as a result.

To measure and report on risk, each business/product line is classified as concern, monitor, or good. This classification is based on a review of solvency ratios, claim ratios, the combined (profitability) ratio and liabilities. At the end of 2003, all business/product lines were classified as monitor or good.

Operational risk

Operational risk is the risk of direct or indirect loss resulting from inadequate or failed processes, technology, human performance or from external events. We endeavour to minimize operational losses by ensuring that effective infrastructure, controls, systems and individuals are in place throughout our organization. We employ professionals who are proactive in developing and implementing new methodologies for the identification, assessment and management of operational risk.

To monitor and mitigate operational risks in the organization, we have developed and are in the process of implementing the Risk and Control Self-Assessment process and the Loss Event Database, both enterprise-wide initiatives.

Risk and Control Self-Assessment (RCSA)

RCSA is a formal process established to identify, document, assess and manage our operational risks. Each business segment and functional unit is divided into its component activities, which become entities to be assessed. Each entity completes a self-assessment, usually in a cross-functional workshop setting, to determine key risks, mitigating controls, the potential impact should a problem occur, the likelihood of a problem occurring, and the acceptability of the residual exposure. Where residual exposure is deemed unacceptable, the group will identify root causes and agree on an action plan and timeline. The findings of the various RCSAs conducted are documented, aggregated, analyzed and reported on a group-wide basis.

At October 31, 2003, RCSAs had been completed on approximately 30% of the entities deemed to be medium-to-high priority. It is expected that all risk assessments for this group will be completed by mid-2005.

Loss Event Database (LED)

The LED is a centralized database designed to capture information pertaining to operational losses, with more detailed information collected for losses exceeding $25,000. The losses tracked are mapped to the entities identified in the RCSA process. Information such as the frequency, severity and nature of operational losses is captured. This data capture allows for analysis at the business segment and enterprise level and leads to a better understanding of the root causes of operational losses and improved risk mitigation strategies. Based on data collected to date, we have determined that the most frequent losses relate to process risk where there is a failure in the transaction processes in high-volume environments.

Ongoing developments

While operational risk is not a new risk, increased focus and renewed rigour in its management are evident throughout the industry, be it with respect to capital reform or changing expectations for managing and reporting this risk. The RCSA and LED initiatives outlined above are key to our strategies for effectively managing operational risk, while research and development efforts will continue in the areas of quantification methodologies, scenario analysis and key risk indicators as we strive to stay at the forefront of operational risk management best practices.

Changing regulatory landscape

As a globally active, diversified financial services company, we fall within the purview of multiple regulatory bodies in different jurisdictions, geographic locations and business lines. There is also continued expansion in regulatory interest and expectations with respect to areas such as capital, risk management, corporate governance, reporting and disclosure. Some of the more visible of these are the capital reform efforts of the Basel Committee, the disclosure and certification requirements under the *Sarbanes-Oxley Act of 2002* in the U.S., anti–money laundering requirements, and updated standards for sound business and financial practices from the Canada Deposit Insurance Corporation. Key to addressing this changing regulatory landscape effectively are ongoing assessments of how the requirements of multiple regulators overlap, and an integrated, coordinated approach to evaluating how the practices supporting our sound and prudent management measure up against evolving regulatory requirements. Wherever possible, we base compliance on existing sound and prudent practices, and endeavour to meet multiple regulatory requirements concurrently.

Financial priority: Balance sheet and capital management

Highlights

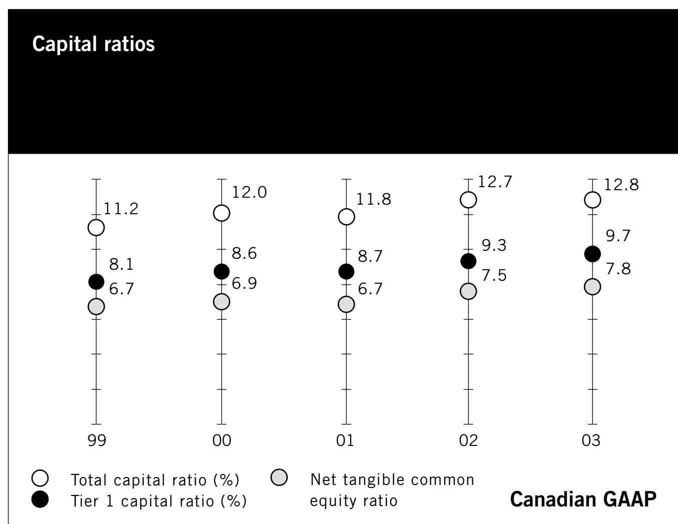
- Consumer loans up 7%
- Deposits up 6%
- Internally generated capital of $1.8 billion
- Capital ratios stronger
- Common share repurchases of $852 million
- $900 million of Innovative Tier 1 capital, Trust Capital Securities – Series 2013 issued
- First Preferred Shares Series J redeemed for $300 million
- US$ First Preferred Shares Series K redeemed for US$250 million

Total assets were $403.0 billion at October 31, 2003, up $26.1 billion or 7% from October 31, 2002.

Securities were up $23.6 billion or 25% from a year ago reflecting an increase in trading account securities of $13.5 billion due to increased trading activity, and $10.1 billion in investment account securities primarily due to redeployment of funds to higher-yielding investments.

Loans (before allowance for loan losses) were up $1.0 billion or 1%. Consumer loans (residential mortgage, personal and credit card loans) were up $7.9 billion or 7%, with residential mortgages up $6.0 billion or 8% (after $4.1 billion of securitizations during the year), personal loans up $2.0 billion or 6% and credit card balances down $.1 billion or 2% (after $1.0 billion of securitizations during the year). Business and government loans were down, reflecting our deliberate effort to reduce the size of our corporate loan portfolio and a reduction in the demand for credit.

Other assets were up $4.7 billion to $61.4 billion. This reflected a $5.4 billion increase in the fair value of our foreign exchange derivative-related amounts and a $1.9 billion increase in other – other assets (primarily due to an increase in investment in associated corporations). Other – other assets includes $425 million (US$322 million) of receivables due from Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A. (Rabobank), relating to a derivative contract that is the subject of litigation with Rabobank, as discussed in Note 20 to the financial statements on page 94A. This amount is net of a settlement we received in the fourth quarter, valued at approximately US$195 million plus interest, which was in accordance with the terms of a settlement agreement with Enron Corporation, the Enron Creditors' Committee and Rabobank. The settlement received has reduced the amount owing by Rabobank but did not otherwise affect the ongoing litigation with Rabobank.



Management expects to recover the amount owing from Rabobank in its entirety, and accordingly a provision for loss has not been recorded.

Deposits were $259.1 billion, up $15.7 billion or 6% from October 31, 2002. Interest-bearing deposits were up $13.3 billion or 6% and non-interest-bearing deposits up $2.4 billion or 10%. Personal deposits were up $4.8 billion, business and government deposits up $10.3 billion and bank deposits were up $.6 billion. Further details on deposits are provided in Note 10 on page 84A.

The fair values of loans and deposits differ from their respective book values due to changes in the level of interest rates and changes in credit status. The estimated fair value of loans due from clients exceeded book values by $1.9 billion at October 31, 2003, and $2.3 billion at October 31, 2002. The estimated fair value of deposits owed to clients exceeded book value by $1.4 billion at October 31, 2003, and $1.7 billion at October 31, 2002. The net amount of the fair value excess of loans due from clients and the fair value excess of deposits due to clients was $474 million at October 31, 2003, as shown in Note 23 on page 98A. The estimated fair values of loans and deposits were in excess of their book values largely due to a decline in interest rates.

Other liabilities increased $10.3 billion to $116.9 billion. The growth was largely due to a $5.6 billion increase in derivative-related amounts, a $3.7 billion increase in obligations related to securities sold short, and a $2.4 billion increase in insurance claims and policy benefit liabilities largely due to the acquisition of Business Men's Assurance Company of America by RBC Liberty Insurance in May 2003.

Subordinated debentures (**subordinated indebtedness**) decreased by $371 million to $6.2 billion.

Non-controlling interest in subsidiaries consists primarily of RBC Capital Trust, a closed-end trust, and RBC Capital Trust II, an open-end trust, which have $1.4 billion and $.9 billion of transferable trust units (RBC TruCS) outstanding, respectively. The RBC TruCS are included in Tier 1 capital under guidelines issued by OSFI.

Shareholders' equity was $18.4 billion at October 31, 2003, down $408 million from a year ago reflecting $645 million of preferred share redemptions.

We fund pension plans in compliance with applicable legislative and regulatory requirements, which require funding when there is a deficit on an actuarial funding basis. Different assumptions and methods are prescribed for regulatory funding purposes versus accounting purposes. This year we contributed $737 million to pension plans, fully funding them for regulatory purposes. Note 17 on page 90A describes the funding position for accounting purposes and the sensitivity of key assumptions.

Capital management

Capital management requires balancing the desire to maintain strong capital ratios and high debt ratings with the need to provide competitive returns to shareholders. In striving to achieve this balance, we consider expected levels of risk-adjusted assets and balance sheet assets, our future investment plans, and the costs and terms of current and potential capital issuances.

We are committed to maintaining strong capital ratios through internal capital generation, the issuance of capital instruments when appropriate, and controlled growth in assets. During 2003, we achieved strong levels of internal capital generation notwithstanding the weak capital markets environment during the first six months of the fiscal year. The weak market environment and planned reductions of corporate loans also contributed to slower growth in risk-adjusted assets, which enabled us to continue repurchasing shares and redeeming some of our outstanding capital instruments, replacing them partly with more cost-effective Innovative Tier 1 capital. Our debt ratings continue to favourably impact our ability to raise capital at competitive prices.

Capital management activity

In 2003, we repurchased 14.5 million common shares, of which 8.6 million shares were repurchased for $502 million under a normal course issuer bid that expired in June 2003; and 5.9 million shares were repurchased for $350 million under a normal course issuer bid that allows for the repurchase of up to 25 million common shares, representing approximately 3.8% of outstanding common shares, between June 24, 2003, and June 23, 2004. In total, during 2003, we spent $852 million to repurchase our common shares and issued 5.3 million common shares for $183 million in connection with the exercise of employee stock options.

On July 23, 2003, RBC Capital Trust II, an SPE and open-end trust we sponsored, issued $900 million of Innovative Tier 1 capital, Trust Capital Securities – Series 2013 (RBC TruCS – Series 2013).

In May 2003, we redeemed $300 million of First Preferred Shares Series J, and US$250 million of First Preferred Shares Series K, both of which were included in our Tier 1 capital.

In September 2003, we redeemed $100 million of subordinated debentures.

Regulatory capital

Capital levels for Canadian banks are regulated pursuant to guidelines issued by OSFI, based on standards issued by the Bank for International Settlements. Regulatory capital is allocated into two tiers. Tier 1 capital comprises the more permanent components of capital. The components of Tier 1 and Tier 2 capital are shown in Table 20 below.

Regulatory capital ratios are calculated by dividing Tier 1 and Total capital by risk-adjusted assets based on Canadian GAAP financial information. Risk-adjusted assets, as shown in Table 21 on page 60A, are determined by applying OSFI prescribed risk weights to balance sheet assets and off-balance sheet financial instruments according to the deemed credit risk of the counterparty. Risk-adjusted assets also include an amount for the market risk exposure associated with our trading portfolio.

TABLE 20 Capital ratios (1)

(C$ millions, except percentage amounts)	2003	2002	2001
Tier 1 capital			
Common equity	$ 17,543	$ 17,238	$ 16,141
Non-cumulative preferred shares	832	1,545	2,024
Non-controlling interest in subsidiaries			
RBC Capital Trust	1,400	1,400	1,400
RBC Capital Trust II	900	–	–
Other	27	29	28
Goodwill	(4,443)	(4,832)	(4,742)
	16,259	15,380	14,851
Tier 2 capital			
Permanent subordinated debentures	396	467	477
Other subordinated debentures (2), (3)	5,847	6,147	5,935
General allowance (4)	1,407	1,420	1,410
	7,650	8,034	7,822
Investment in insurance subsidiaries	(2,143)	(2,014)	(2,107)
Other substantial investments	(371)	(368)	(387)
First loss facility	(21)	(20)	(8)
Total capital	$ 21,374	$ 21,012	$ 20,171
Risk-adjusted assets	$ 166,911	$ 165,559	$ 171,047
Capital ratios			
Common equity to risk-adjusted assets	10.5%	10.4%	9.4%
Tier 1 capital to risk-adjusted assets	9.7%	9.3%	8.7%
Total capital to risk-adjusted assets	12.8%	12.7%	11.8%
Assets-to-capital multiple (5)	18.2	17.3	17.2
U.S. basis (6)			
Tier 1 capital to risk-adjusted assets	8.7%	8.5%	8.1%
Total capital to risk-adjusted assets	12.0%	11.9%	11.2%
Equity to assets (7)	4.9%	5.3%	5.1%

(1) Using guidelines issued by OSFI and Canadian GAAP financial information except as noted in footnote (6).
(2) Subordinated debentures that are within five years of maturity are subject to straight-line amortization to zero during their remaining term and, accordingly, are included above at their amortized value.
(3) On November 3, 2003, we issued $1 billion of subordinated debentures, which increased Total capital by the same amount.
(4) The general allowance for credit losses may be included in Tier 2 capital up to a maximum of .875% (2002–2001 – .875%) of risk-adjusted assets.
(5) Total assets and specified off-balance sheet financial instruments, as prescribed by OSFI, divided by Total capital.
(6) Using guidelines issued by the Board of Governors of the Federal Reserve System in the United States and U.S. GAAP financial information.
(7) Average total shareholders' equity divided by average total assets (including netted derivatives). Average total shareholders' equity is calculated as the average of the month-end balances for the period.

In 1999, OSFI formally established risk-based capital targets for deposit-taking institutions in Canada. These targets are a Tier 1 capital ratio of 7% and a Total capital ratio of 10%. As at October 31, 2003, our Tier 1 and Total capital ratios were 9.7% and 12.8%, respectively, compared to 9.3% and 12.7% at October 31, 2002. Throughout 2003, we maintained capital ratios that exceeded our medium-term goals of 8.0–8.5% for the Tier 1 capital ratio and 11–12% for the Total capital ratio. Our capital ratios, calculated using guidelines issued to U.S. banks by the Board of Governors of the Federal Reserve System and using U.S. GAAP financial information are shown in Table 20 on page 59A.

In addition to the Tier 1 and Total capital ratios, Canadian banks need to operate within a leverage constraint, and ensure that their assets-to-capital multiple does not exceed the level prescribed by regulators. The assets-to-capital multiple shown in Table 20 on page 59A is calculated by dividing gross adjusted assets based on Canadian GAAP by Total capital. Gross adjusted assets represent the bank's total assets including specified off-balance sheet items and are net of prescribed deductions.

Our policy is to remain well capitalized so as to provide a cushion for the risks we are exposed to in the conduct of our business.

Pending developments

Changes to the Basel II agreement for assessing capital adequacy are currently in the process of being finalized. The implementation is not expected prior to fiscal 2007.

Several changes in accounting principles have either been introduced or are being proposed in the U.S. and in Canada in the areas of consolidation of Variable Interest Entities (as described in Note 1 to the consolidated financial statements on pages 75A and 76A) and classification of certain financial instruments as either equity or liabilities. These changes could significantly affect the reporting of assets and capital instruments. The lack of definitive guidance by accounting boards and uncertainties regarding the response of regulators to the accounting changes have increased capital management challenges. We continue to closely monitor changes in the accounting framework and their potential impact on our capitalization levels through ongoing dialogue with our external auditors, other financial institutions, the Canadian Bankers Association and OSFI.

TABLE 21 Risk-adjusted assets (1)

(C$ millions, except percentage amounts)			Balance sheet amount	Weighted average of risk weights (2)	Risk-adjusted balance 2003	2002
Balance sheet assets						
Cash resources			$ 17,554	12%	**$ 2,026**	$ 2,054
Securities						
Issued or guaranteed by Canadian or other OECD governments			37,692	0%	**28**	36
Other			79,698	6%	**4,557**	4,929
Residential mortgages (3)						
Insured			36,308	1%	**377**	379
Conventional			42,472	52%	**21,951**	20,168
Other loans and acceptances (3)						
Issued or guaranteed by Canadian or other OECD governments			20,141	19%	**3,778**	3,098
Other			113,705	72%	**82,169**	89,836
Other assets			55,463	13%	**6,996**	5,692
			$ 403,033		**$ 121,882**	$ 126,192
	Contract amount	Credit conversion factor	Credit equivalent amount			
Off-balance sheet financial instruments						
Credit instruments						
Guarantees and standby letters of credit						
Financial	$ 14,504	100%	$ 14,504	91%	**$ 13,201**	$ 8,560
Non-financial	3,038	50%	1,519	100%	**1,519**	1,609
Documentary and commercial letters of credit	2,014	20%	403	99%	**399**	150
Securities lending	17,520	100%	17,520	6%	**1,087**	646
Commitments to extend credit						
Original term to maturity of 1 year or less	40,432	0%	–		**–**	–
Original term to maturity of more than 1 year	28,182	50%	14,091	95%	**13,357**	15,638
Uncommitted amounts	59,801	0%	–	–	**–**	–
Note issuance/revolving underwriting facilities	24	50%	12	100%	**12**	12
	$ 165,515		$ 48,049		**$ 29,575**	$ 26,615
Derivatives	2,137,758		26,652	24%	**6,320**	6,469
Total off-balance sheet financial instruments	$ 2,303,273		$ 74,701		**$ 35,895**	$ 33,084
Total specific and general market risk					**9,134**	6,283
Total risk-adjusted assets					**$ 166,911**	$ 165,559

(1) Using guidelines issued by the Superintendent of Financial Institutions Canada and Canadian GAAP financial information.
(2) Represents the weighted average of counterparty risk weights within a particular category.
(3) Amounts are shown net of allowance for loan losses.

Asset/liability management

Overview

Asset/liability management comprises the evaluation, monitoring and management of our non-trading portfolio, liquidity management and funding. It is important to note that liquidity and capital resources are likely to be affected by many of the same factors that are detailed in this section of Management's discussion and analysis, the factors discussion on pages 23A to 24A and the Risk management discussion on pages 53A to 57A. Additionally, off-balance sheet financing arrangements are often integral to both liquidity and capital resources, and are discussed in detail on pages 63A to 65A of this section.

Non-trading portfolio

Traditional non-trading banking activities, such as deposit taking and lending, expose us to market risk, of which interest rate risk, as described on page 55A, is the largest component.

We actively manage the interest rate risk for the North American non-trading balance sheet and oversee all other non-trading units that have been assigned interest rate risk limits. We endeavour to adopt the industry's best practices and carry out the following functions:

Policy

The Conduct Review and Risk Policy Committee of the Board of Directors approves the global policies governing interest rate risk management. The policies define the acceptable limits within which risks to net interest income over a 12-month horizon, and the economic value of equity, are to be contained. These ranges are based on immediate and sustained ± 200 basis points parallel shifts of the yield curve. The limit for net interest income risk is 6% of projected net interest income, and for economic value of equity risk is 12% of projected common equity. The economic value of equity is equal to the present value of assets less the present value of liabilities, plus or minus the market value of off-balance sheet instruments.

Interest rate funds transfer pricing

We use a funds transfer pricing mechanism to centralize interest rate risk within Corporate Treasury and to ensure an equitable allocation of interest income to the various business units. Funds transfer pricing at the transactional level ensures that interest rate risk is appropriately transferred to Corporate Treasury for management. The funds transfer pricing rates are market-based and are aligned with interest rate risk management principles. They are supported by empirical research into client behaviour and are an integral input to the retail business pricing decisions.

Applied research

We investigate best practices in instrument valuation, econometric modeling and new hedging techniques on an ongoing basis. Our investigations range from the evaluation of traditional asset/liability management processes to pro forma application of recent developments in quantitative methods to our processes.

We also focus on developing retail product valuation models that incorporate consumer behaviour. These valuation models are typically derived through econometric estimation of consumer exercise of options embedded in retail products. The most significant embedded options are mortgage rate commitments and prepayment options. On the liability side of the balance sheet, we tend to focus on modeling administered rates and the sensitivity of liability balances to interest rate changes.

Risk measurement

We measure our risk position on a daily, weekly or monthly basis with the frequency employed commensurate with the size and complexity of the portfolio. Measurement of risk is based on client rates as well as funds transfer pricing rates. We continue to make investments in new technology to facilitate measurement and timely management of our interest rate risk position. In 2003, Key Rate Analysis was introduced as the primary measure of our risk position. Key Rate Analysis provides us with an assessment of the sensitivity of the exposure of our economic value of equity to instantaneous changes in individual points on the yield curve.

We supplement our assessment by measuring interest rate risk for a range of dynamic and static market scenarios. Dynamic scenarios simulate our interest income in response to various combinations of business and market factors. Business factors include assumptions about future pricing strategies and volume and mix of new business, whereas market factors include assumed changes in interest rate levels and changes in the shape of the yield curve. Static scenarios supplement dynamic scenarios and are also employed for assessing both value of equity risk and net interest income risk.

Interest rate risk management

Our goal is to manage interest rate risk of the non-trading balance sheet to a targeted level, on an ongoing basis. We modify the risk profile of the balance sheet through proactive hedging activity to achieve our targeted level.

The interest rate risk can be disaggregated into linear risk and nonlinear risk based on the varying responses of the balance sheet to different interest rate movements. The linear risk is primarily managed through interest rate swaps. The non-linear risk arises primarily from embedded options in our products that allow clients to modify the maturities of their loans or deposits. Examples are a client prepaying a personal loan or a prospective client getting a committed rate on a new mortgage before the mortgage loan takes effect. Embedded options are modeled using assumptions based on empirical research and the risks are managed by either purchasing options or by a dynamic hedging strategy.

The performance of the interest rate risk management function within Corporate Treasury is benchmarked on a total return basis. A by-product of this benchmarking exercise is a methodology that controls model risk by continuously back-testing model assumptions against actual client behaviour.

Table 22 below shows the potential impacts of 100 and 200 basis point increases and decreases in interest rates on economic value of equity and net interest income of our non-trading portfolio. These measures are as of October 31, 2003, and are based on assumptions made by management and validated by empirical research. The methodology assumes that no further hedging is undertaken. We have defined a risk neutral balance sheet as one where net residual assets representing equity are notionally invested evenly over a five-year horizon. As a result of this decision, our interest rate risk profile has slightly faster repricing of assets than of liabilities with the duration of equity at about 2.5 years.

All interest rate measures in this section are based upon our interest rate exposures at a specific time. The exposures change continually as a result of day-to-day business activities and our risk management initiatives.

TABLE 22 Market risk measures – Non-trading activities (1)

	2003		2002	
(C$ millions)	**Economic value of equity risk**	**Net interest income risk**	Economic value of equity risk	Net interest income risk
100bp increase	**$ (423)**	**$ 115**	$ (309)	$ 104
100bp decrease	**261**	**(126)**	145	(151)
200bp increase	**$ (869)**	**$ 207**	$ (662)	$ 190
200bp decrease	**545**	**(294)**	345	(327)

(1) Amounts are presented on a pre-tax basis as at October 31.

Liquidity management

Our liquidity management framework is designed to ensure that reliable and cost-effective sources of cash are available to satisfy current and prospective commitments, both on- and off-balance sheet. The primary goals of this framework are the preservation of a large base of core customer deposits, ongoing access to diversified sources of wholesale funding and the maintenance of a dedicated pool of unencumbered marketable securities that provide ready access to cash. The discussion that follows reflects our consolidated liquidity management practices and processes.

The Corporate Treasury function has global responsibility for the development of liquidity management policies, strategies and contingency plans and for recommending and monitoring limits within this framework. Our principal regional trading and funding platforms provide transactional support for liquidity management policies and strategies. The Group Risk Committee and the Asset/Liability Committee share management oversight responsibility for liquidity management and liquidity policies and receive regular reports detailing compliance with limits and guidelines. Committees of the Board of Directors approve our liquidity management framework and significant related policies, and the Board of Directors is informed on a periodic basis about our current and prospective liquidity condition. Additionally, we have a liquidity contingency plan in place, which is maintained and administered by the Liquidity Crisis Team.

Since most of the funding of our subsidiaries is provided by the parent organization, managing our liquidity position on a consolidated basis is the most pragmatic and relevant approach. When managing the flow of liquidity between different legal entities within the consolidated group, we take into account the tax and regulatory considerations associated with each jurisdiction. While such tax and regulatory considerations add a degree of complexity to internal fund flows, given intra-group funding arrangements, our consolidated liquidity management approach already takes into account the maximum funding demands associated with intra-group requirements. Subsidiaries responsible for managing their own liquidity do so in compliance with policies and practices established by Corporate Treasury and with governing regulatory requirements.

We measure and monitor our liquidity condition from structural, tactical and contingent perspectives. The assessment of our liquidity position based on these measures reflects management estimates and judgments pertaining to the behaviour of our customers and future market conditions. We monitor industry practices and regulatory developments and, as appropriate, upgrade our liquidity management framework to reflect relevant developments. We consider our liquidity profile to be sound and there are no known trends, demands, commitments, events or uncertainties that are presently viewed as likely to materially change our current liquidity position.

Structural liquidity risk management

Existing balance sheet composition can create liquidity exposure due to mismatches in effective maturities between assets and liabilities. Structural liquidity risk management addresses this type of exposure, which is measured and monitored through ongoing analysis of our balance sheet.

We use the cash capital model to assist in the evaluation of balance sheet liquidity and in the determination of the appropriate term structure of our debt financing. This methodology provides a comprehensive, formula-based approach to assess our ability to continue as a going concern during a prolonged liquidity event, such as an unexpected withdrawal of short-term funding. In the context of a sustainable business model, the cash capital methodology allows us to measure and monitor the relationship between illiquid assets and core funding. This reconstruction of our balance sheet enables us to more accurately estimate our exposure to, and make appropriate contingency plans for, a protracted loss of unsecured funding as well as to quantify our longer-term financing requirements.

Tactical liquidity risk management

Tactical liquidity risk management addresses our normal day-to-day funding requirements and is managed by imposing limits on net fund outflows for specified periods, particularly for key short-term time horizons. Scenario analysis is performed periodically on the assumed behaviour of cash flows under varying conditions to assess funding requirements and, as required, to update assumptions and limits. Detailed reports on our principal short-term asset/liability mismatches are monitored on a daily basis to ensure compliance with the prudential limits established for overall group exposure and by major currency and geographic location. Corporate Treasury issues procedural directives to the individual units engaged in executing policy to ensure consistent application of cash flow management principles across the entire organization.

Contingent liquidity risk management

The liquidity contingency plan identifies comprehensive action plans that would be implemented in the event of general market disruptions or adverse economic developments that could jeopardize our ability to meet commitments. Four different market scenarios, of varying duration and severity, are addressed in the liquidity contingency plan to highlight potential liquidity exposures and requisite responses. The Liquidity Crisis Team, comprising senior individuals from business and functional units, meets regularly to review, test and update implementation plans and to consider the need for activation in view of developments in Canada and globally.

To address potential liquidity exposures identified by our scenario analyses, we maintain a pool of segregated and unencumbered marketable securities. These high-quality assets can be readily sold or pledged for secured borrowing and represent a dedicated and reliable source of emergency funding. Based on our scenario analyses, our holdings of segregated liquid assets are considered to be sufficient to meet all on- and off-balance sheet obligations if access to funding is temporarily impaired. In addition, we maintain a separate portfolio of eligible assets to support our participation in Canadian payment and settlement systems. All pledging activities are subject to review or approval by the Asset/Liability Committee and are managed and monitored against defined limits. Assets that are encumbered are not accorded any liquidity value in our tactical and contingent liquidity calculations.

Liquid assets and assets purchased under reverse repurchase agreements (before pledging as detailed below) totalled $178 billion or 44% of total assets at October 31, 2003, as compared to $154 billion or 41% at October 31, 2002. Liquid assets are primarily diversified and highly rated marketable securities. As at October 31, 2003, $14 billion of assets had been pledged as collateral, up from $10 billion at October 31, 2002. We have another $46 billion in obligations related to assets sold under repurchase agreements and securities sold short at October 31, 2003, compared to $40 billion at October 31, 2002. For further details, see Note 20 to the consolidated financial statements on page 93A.

Funding strategy

Diversification of funding sources is a crucial component of our overall liquidity management strategy since it expands funding flexibility, minimizes funding concentration and dependency and generally lowers financing costs. Core funding, comprising capital, longer-term liabilities and a diversified pool of personal and, to a lesser extent, commercial deposits, is the foundation of our strong structural liquidity position.

Credit ratings

Our ability to access unsecured funding markets and our financing costs in such markets are primarily dependent upon maintaining an acceptable credit rating, which in turn is largely determined by the quality of our earnings, the adequacy of our capital and the effectiveness of our risk management programs. While our estimates suggest that a minor downgrade would not materially influence our funding capacity or costs, we recognize the importance of avoiding such an event and are committed to actions that should reinforce existing external assessments of our financial strength. A series of downgrades could have an adverse impact on our funding capacity and on the results of our operations.

Deposit profile

The composition of our global deposit liabilities is summarized in Note 10 on page 84A. Personal deposits remain the prime source of funding for our Canadian dollar balance sheet while most foreign currency deposits originate from unsecured, "wholesale" sources, including large corporate and institutional clients and foreign commercial and central banks. Our personal deposit franchise constitutes a principal source of predictable and dependable funding. Certain commercial and institutional client groups also maintain relational balances with relatively low volatility profiles. Taken together, these depositors represent a consistently reliable component of core funding as they typically have extensive banking relationships and are less responsive to market developments than transactional lenders and investors. Behavioural characteristics, rather than contractual or repricing terms, are used to categorize core deposits. We also promote wholesale funding diversity and regularly review sources of short-term funds to ensure maintenance of wide diversification by provider, product and geographic origin. In addition, we maintain an ongoing presence in different funding markets, constantly monitoring market developments and trends in order to identify opportunities or risks and to take appropriate pre-emptive actions.

Term funding sources

Long-term funding strategy is integrated with our current and estimated structural liquidity position as reflected in our cash capital position. Liquidity objectives, as well as market conditions, interest rates, credit spreads and desired financial structure, influence annual long-term funding activities, including currency mix and market concentration. Diversification into new markets and untapped investor segments is constantly evaluated against relative issuance costs. Our long-term funding sources are managed to minimize concentration by geographic location, investor segment, and currency and maturity profile. During fiscal 2003, we continued to expand our long-term funding base by issuing, either directly or through our subsidiaries, $5.7 billion of senior deposit notes in various currencies and markets. We also established a U.S. shelf registration, to enable us to more conveniently raise senior and subordinated indebtedness in the U.S. public market. Total long-term funding outstanding on October 31, 2003, was $14.2 billion, compared to $13.2 billion on October 31, 2002.

We use asset securitization programs as an alternative source of funding and for liquidity and asset/liability management purposes. During 2003, $1.6 billion of new financing was obtained through the securitization and sale of $1.0 billion of credit card receivables funded by medium-term notes and $610 million of government guaranteed residential mortgages. In addition, we sold $131 million of commercial mortgages to a third-party securitization special purpose vehicle. As of October 31, 2003, $2.7 billion of our credit card receivables were financed through notes issued by a securitization special purpose entity. Our total outstanding mortgage-backed securities (MBS) sold at October 31, 2003, was $2.9 billion (see Note 7 on pages 82A and 83A, and off-balance sheet arrangements below for more details).

Contractual obligations

In the normal course of business, we enter into contracts that give rise to commitments of future minimum payments. Depending on the nature of these commitments, the obligation may be recorded on- or off-balance sheet. Table 23 below provides a summary of our future contractual funding commitments.

TABLE 23 **Contractual obligations**

(C$ millions)	Within 1 year	1 to 3 years	Over 3 to 5 years	Over 5 years	Total
Unsecured long-term funding	$ 3,016	$ 5,510	$ 5,573	$ 145	$ 14,244
Subordinated debentures	–	–	–	6,243	6,243
Obligations under capital leases	358	628	480	681	2,147
Obligations under operating leases	30	37	4	–	71
Purchase obligations	25	11	–	–	36
Total	$ 3,429	$ 6,186	$ 6,057	$ 7,069	$ 22,741

Off-balance sheet arrangements

In the normal course of business, we engage in a variety of financial transactions that, under GAAP, are either not recorded on our balance sheet or are recorded on our balance sheet in amounts that differ from the full contract or notional amounts. These transactions involve, among other risks, varying degrees of market, credit and liquidity risk, which are discussed in the Risk management section on pages 53A to 57A.

Off-balance sheet transactions are either proprietary or client transactions, represent an ongoing part of our business and are generally undertaken for risk management, capital management and/or funding management purposes. Off-balance sheet activities we undertake include derivative financial instruments, transactions with special purpose entities and issuance of guarantees. We do not reasonably expect any presently known trend or uncertainty to affect our ability to continue using these arrangements. Each of these types of arrangements, including their nature, business purpose, importance and significant financial impact, as applicable, is discussed below.

Derivative financial instruments

Derivatives are primarily used in sales and trading activities. Sales activities include the structuring and marketing of derivative products to clients to enable them to transfer, modify or reduce current or expected risks. Trading involves market-making, positioning and arbitrage activities. We also use derivatives to manage our exposures to interest, currency and other market risks. To the extent that one or more of the derivative financial transactions we undertake involve amounts owing from third-party counterparties, we are exposed to counterparty credit risk (credit risk is discussed in more detail on pages 54A and 55A).

All derivatives, except those for other than trading purposes that qualify for hedge accounting, are recorded at fair value on our balance sheet (fair value assumptions are discussed on page 25A). Although derivative transactions are measured in terms of their notional amounts, these amounts are not recorded on our balance sheet, as the notional amounts serve as points of reference for calculating payments, and are not the actual amounts that are exchanged.

The total notional amount of our derivatives amounted to $2,139 billion at October 31, 2003, compared to $2,081 billion at October 31, 2002. The fair value of our trading and non-trading derivative assets totalled $35.2 billion and $1.6 billion compared to $30.1 billion and $1.6 billion at October 31, 2002, respectively, while the fair value of our trading and non-trading derivative liabilities totalled $37.6 billion and $1.1 billion compared to $32.0 billion and $1.0 billion at October 31, 2002, respectively. Changes in the fair value of our trading and non-trading derivatives that do not qualify for hedge accounting are recorded in non-interest income.

Notes 1 and 21 on pages 73A and 95A to 97A, respectively, provide more detail on our accounting for, and types of, derivatives.

Special purpose entities

Special purpose entities (SPEs) are principally used to securitize financial and other assets in order to obtain access to funding, to mitigate credit risk and to manage capital. SPEs are an important part of the financial markets, providing market liquidity by facilitating investors' access to specific portfolios of assets and risks in a form that meets their investment criteria. We use SPEs to securitize certain loans. We also act as an intermediary or agent for clients who want to use SPEs to securitize their own financial assets. We provide SPE repackaging services to clients who seek access to financial assets in a form different than what is conventionally available.

SPEs are typically set up for a single, discrete purpose, have a limited life and serve to legally isolate the financial assets held by the SPE

from the selling organization. SPEs are not operating entities, usually have no employees and may be Variable Interest Entities (VIEs) as defined by Canadian Institute of Chartered Accountants (CICA) Accounting Guideline 15, *Consolidation of Variable Interest Entities* (AcG 15).

We provide services to, and/or may have variable interests in, SPEs through a number of different key arrangements as outlined below.

Variable interests represent contractual, ownership or other pecuniary interests in an unconsolidated SPE that will absorb a portion of that SPE's expected losses if they occur, or receive portions of the SPE's expected residual returns if they occur.

We manage and monitor our direct involvement with SPEs through our SPE Risk Committee, which comprises representatives from functional areas including risk management, corporate treasury, finance, subsidiary governance office, law, taxation, subsidiary banking groups and human resources. This committee's key activities include formulating policies governing SPEs, reviewing new and unusual SPE transactions and monitoring the ongoing activities of SPEs.

Securitization of our financial assets

Credit card receivables

We securitize a portion of our credit card receivables through an SPE. The SPE is funded through the issuance of senior and subordinated notes collateralized by the underlying credit card receivables. The primary economic purposes of this activity are to diversify our funding sources and to enhance our liquidity position. Although these credit card receivables are no longer on our balance sheet, we maintain the client account and retain the relationship.

The securitization of our credit card receivables is a sale from a legal perspective and qualifies for sale treatment from an accounting perspective. At the time of sale these receivables are removed from our balance sheet resulting in a gain or loss reported in non-interest income.

This SPE meets the criteria for a Qualifying SPE (QSPE) pursuant to CICA Accounting Guideline 12, *Transfers of Receivables* (AcG 12) and, accordingly, as the transferor of the credit card receivables, we are precluded from consolidating this SPE. We continue to service the credit card receivables sold to the QSPE for which we receive benefits equivalent to market-based compensation for such services. In addition, we perform an administrative role for the QSPE in which we are responsible for ensuring that the ongoing public filings of the QSPE are performed, as required, and that the investors in the QSPE's asset-backed securities receive interest and principal payments on a timely basis.

We provide first-loss protection to the QSPE in two forms. Our interest in the excess spread from the QSPE is subordinate to the QSPE's obligation to the holders of its asset-backed securities. Excess spread is the residual net interest income after all trust expenses have been paid. Therefore, our excess spread serves to absorb losses with respect to the credit card receivables before payments to the QSPE's noteholders are affected. The present value of this excess spread is reported as a retained interest within available for sale securities on our consolidated balance sheet. In addition, we provide loans to the QSPE to pay upfront expenses. These loans rank subordinate to all notes issued by the QSPE.

At October 31, 2003, total credit card receivables securitized and held off-balance sheet amounted to $2.7 billion, compared to $1.7 billion at October 31, 2002. The carrying value of our retained interests in securitized credit card receivables at October 31, 2003, was $15.5 million compared to $6.7 million in 2002, and amounts receivable under subordinated loan agreements were $8.7 million compared to $5.2 million in 2002.

Residential mortgage loans

We routinely securitize residential mortgage loans through the creation of MBS and sell a portion of these MBS to an independent SPE. Due to the high quality of the residential mortgages backing the MBS, the securitization and subsequent sale provide a cost-effective source of liquidity and help diversify our funding sources. We retain interests in the excess spread on the sold MBS and continue to service the mortgages underlying these MBS for which we receive benefits, equivalent to market-based compensation.

At October 31, 2003, total residential mortgage loans securitized and held off-balance sheet amounted to $2.9 billion, compared to $2.4 billion at October 31, 2002. The carrying value of our retained interests in securitized residential mortgage loans at October 31, 2003, was $94.8 million compared to $90.8 million in 2002.

Further details about the securitization of our financial assets during the year are shown in Note 7 on pages 82A to 83A.

Securitization of client financial assets

Within our global securitization group, our principal relationship with SPEs comes in the form of administering multi-seller asset-backed commercial paper conduit programs (multi-seller SPEs) totalling $26.8 billion as at October 31, 2003, and $22.2 billion as at October 31, 2002. We currently administer five multi-seller SPEs – three in Canada and two in the U.S. These five multi-seller SPEs have purchased financial assets from our clients totalling $22.5 billion. Under current accounting standards, the five multi-seller SPEs that we administer are not consolidated on our balance sheet.

We are involved in the multi-seller SPE markets because our clients value these transactions, they offer a growing source of revenue and they generate a favourable risk-adjusted return for us. Our clients primarily utilize multi-seller SPEs to diversify their financing sources and to reduce funding costs by leveraging the value of high-quality collateral.

The multi-seller SPEs purchase various financial assets from clients and finance the purchases by issuing highly rated asset-backed commercial paper. The multi-seller SPEs typically purchase the financial assets as part of a securitization transaction by our clients. In these situations, the sellers of the financial assets continue to service the respective assets and generally provide some amount of first-loss protection on the assets. While we do not maintain any ownership or retained interests, we do have variable interests in these multi-seller SPEs. We provide or retain certain services such as transaction structuring and administration as specified by the multi-seller SPE program documents and based on rating agency criteria for which we receive fees. In addition, we provide backstop liquidity facilities and partial credit enhancement to the multi-seller SPEs. We have no rights to, or control of, the assets owned by the multi-seller SPE.

Fee revenue for such services, which is reported as non-interest income, amounted to $34.2 million during the year compared to $32.2 million during 2002.

The table below summarizes the financial assets owned by the multi-seller SPEs at fiscal years ended October 31.

Asset class

(C$ millions)	2003	2002
Credit cards	$ 6,248	$ 4,671
Auto loans and leases	3,681	3,615
Equipment receivables	2,566	2,509
Trade receivables	3,680	2,479
Residential mortgages	1,138	2,004
Other loans	1,159	1,275
Dealer floor plan receivables	1,269	1,208
Consumer loans	1,004	1,196
Asset-backed securities	952	926
Other	754	706
	$ 22,451	$ 20,589

The commercial paper issued by each multi-seller SPE is in the multi-seller SPE's own name with recourse to the financial assets owned by the multi-seller SPE. The multi-seller SPE commercial paper is non-recourse to us except through our participation in liquidity and/or credit enhancement facilities, and non-recourse to the other multi-seller SPEs that we administer. Each multi-seller SPE is largely prohibited from issuing medium-term notes or other forms of indebtedness to finance the asset purchases. Consequently, each multi-seller SPE's commercial paper liabilities are generally equal to the assets owned by that multi-seller SPE. The small difference between each of the multi-seller SPE's asset and liability balances is mostly related to the discount or interest costs attributable to the commercial paper. As of October 31, 2003, the total face amount of commercial paper issued by the multi-seller SPEs equaled $22,494 million, generating $22,451 million of cash proceeds, with the difference between these amounts representing the commercial paper discount.

At fiscal years ended October 31, total commitments and amounts outstanding under liquidity and credit enhancement facilities, which are included in our discussion on Guarantees below, are shown in the following table:

Liquidity and credit facilities

	2003		2002	
(C$ millions)	**Committed** (1)	**Outstanding**	Committed (1)	Outstanding
Liquidity facilities	**$ 25,727**	**$ –**	$ 22,593	$ –
Credit facilities	**6,791**	**–**	7,211	–

(1) Our maximum exposure to loss under these facilities is $25.7 billion for 2003 and $22.6 billion for 2002.

The economic exposure that we assume when we provide backstop liquidity commitments and partial credit enhancement is contingent in nature. We manage these exposures within our risk management functions in the same manner that we manage other contingent and non-contingent risk exposures. Our risk management process considers the credit, liquidity and interest rate exposure related to each of the assets. The risk exposure of each of these components individually and taken as a whole is deemed to be acceptable. All transactions are reviewed by external rating agencies. The weighted average credit quality of the assets supported by our backstop liquidity and partial credit enhancement is among the highest quality rating levels based on our internal risk rating system, which is described on page 54A. The liquidity risk to us is deemed to be low based on the historical performance and high credit quality of the multi-seller SPEs' assets. Interest rate exposure is deemed to be low and is generally managed at the transaction level by passing on the funding cost variability to the securitization structures.

Corporate Treasury scrutinizes contingent balance sheet risk, in effect monitoring the risk of drawdown under any of the credit facilities.

Creation of investment products

We use repackaging SPEs, which generally transform credit derivatives into cash instruments, to distribute credit risk and to create customized credit products, to meet the needs of investors with specific requirements. As part of this process, we may acquire variable interests, by entering into trading derivative contracts with these SPEs in order to convert various risk factors such as yield, currency or credit risk of underlying assets to meet the needs of the investors. In this role as derivative counterparty to the SPE, we also assume the associated counterparty credit risk of the SPE. In order to enter into these transactions, we establish an internal risk rating for the SPE and provide ongoing risk assessment and monitoring of the SPE's credit risk. As with all counterparty credit exposures, these exposures are put in place and reviewed pursuant to our normal risk management process in order to effectively manage and monitor this credit risk profile.

These SPEs often issue notes. Those notes may be rated by external rating agencies, as well as listed on a stock exchange, and are generally traded via recognized bond clearing systems. While the majority of the notes that are created in repackagings are expected to be sold on a "buy & hold" basis, we may on occasion act as market maker. We do not, however, provide any repackaging SPE with any guarantees or other similar support commitments. There are many functions required to create a repackaged product. We fulfill some of these functions and independent third parties or specialist service providers fulfill the remainder.

Currently we act as sole arranger and swap provider for SPEs where we are involved, and in most cases, as paying and issuing agent as well.

As with all our trading derivatives, these derivative variable interests are carried at fair value in derivative-related assets and liabilities.

Asset management

We act as collateral manager for Collateralized Debt Obligation (CDO) SPEs, which invest in leveraged bank-initiated term loans, high-yield bonds and mezzanine corporate debt. As collateral manager, we are engaged by the CDO SPE, pursuant to a Collateral Management Agreement, to advise the SPE on the purchase and sale of collateral assets it holds. For these advisory services, we are paid a predetermined market-based fee, which may constitute a variable interest, based on a percentage of assets held by the SPE.

The notional amount of the CDOs we managed at the end of fiscal 2003 was US$.8 billion (2002 – US$1.6 billion). Although we have a nominal investment in the first-loss tranche of a US$300 million CDO, we provide no liquidity or credit support to these SPEs beyond this investment. The CDOs we manage may from time to time purchase collateral assets originated by us or third parties.

The program documents covering the formation and operation of the individual CDOs provide strict guidelines for the purchase of such assets. We recognize fee income from collateral management services and, where indicated, interest income from investments in individual CDOs.

For other types of off-balance sheet arrangements we enter into through VIEs, please refer to Note 1 on pages 75A and 76A.

Guarantees

We issue guarantee products, as defined by CICA Accounting Guideline 14, *Disclosure of Guarantees* (AcG 14), to our clients to help them meet their financing needs in return for fees recorded in non-interest income. Our significant types of guarantee products are backstop liquidity facilities, financial standby letters of credit, credit enhancements, stable value products, performance guarantees and certain indemnification agreements.

Our maximum potential exposure in relation to these items at October 31, 2003, amounted to $61 billion. The maximum potential exposure represents the maximum risk of loss if there were a total default by the guaranteed parties, without consideration of possible recoveries under recourse provisions, insurance policies or from collateral held or pledged.

Note 20 on pages 93A and 94A provides detailed information regarding the nature and maximum potential exposure for the types of guarantee products mentioned above.

In addition to guarantees, we also provide commercial commitments to our clients to help them meet their financing needs. On behalf of our clients we undertake written documentary and commercial letters of credit, authorizing a third party to draw drafts from us to a stipulated amount and typically having underlying shipments of goods as collateral. We make commitments to extend credit, which may represent unused portions of authorizations to extend credit in the form of loans, acceptances and letters of credit. We have uncommitted amounts, but not obligations to extend credit. Table 24 below provides a detailed summary of our off-balance sheet commercial commitments.

TABLE 24 **Commercial commitments** (1)

(C$ millions)	Within 1 year	1 to 3 years	Over 3 to 5 years	Over 5 years	Total
Documentary and commercial letters of credit	$ 1,509	$ 505	$ –	$ –	$ 2,014
Commitments to extend credit	40,278	19,123	5,212	4,001	68,614
Uncommitted amounts	59,801	–	–	–	59,801
Total	$ 101,588	$ 19,628	$ 5,212	$ 4,001	$ 130,429

(1) Based on remaining term to maturity.

2002 compared to 2001

The following discussion and analysis provides a comparison of our results of operations for the years ended October 31, 2002, and October 31, 2001. This discussion should be read in conjunction with the consolidated financial statements and related Notes on pages 67A to 102A.

Business segment results

Net income from RBC Banking increased 30% to $1,531 million in 2002 from $1,181 million in 2001, reflecting the acquisition of Centura Banks on June 5, 2001, and a lower provision for credit losses. ROE increased from 16.9% to 19.1% due to the higher earnings.

Net income from RBC Insurance was down 12% to $117 million in 2002. Earnings in 2001 were adversely affected by claims resulting from the events of September 11, 2001. ROE increased from 15.0% to 15.7% due to lower common equity attributed to this segment.

Net income from RBC Investments was down 33% from 2001 to $343 million primarily due to the gain on sale of RT Capital Management's institutional money management business in 2001. ROE declined from 27.2% to 11.0% due to lower earnings and higher common equity attributed to this segment.

Net income from RBC Capital Markets increased by 24% to $417 million, as expenses fell far more than revenues. ROE was 10.0%, up from 9.3% in 2001 due to higher earnings.

Net income from RBC Global Services was down 35% to $171 million due to higher loan losses pertaining to Argentine loans, and lower net interest income and foreign exchange revenues. ROE declined from 48.9% to 28.4%, due to lower earnings and higher common equity attributed to this segment.

The Other segment's net income improved to $183 million from $(15) million in 2001. ROE increased from (2.8)% to 24.4% due to higher earnings.

Net interest income

Net interest income increased 10% to $6.9 billion in 2002 from $6.3 billion in 2001, largely due to increased net interest income associated with U.S. acquisitions.

Non-interest income

Non-interest income increased 6% to $10.3 billion in 2002 and accounted for 60% of total revenues.

Non-interest expense

Non-interest expense increased 7% to $10.4 billion, largely due to higher human resources costs, reflecting an increase in salaries expense and benefits expense.

Taxes

Income taxes were $1.4 billion in 2002, up from $1.3 billion in 2001, while the effective income tax rate was 32.2% compared to 34.7% in 2001.

Provision for credit losses

The provision for credit losses decreased 5% to $1,065 million in 2002 from $1,119 million in 2001. The total allowance for loan losses was $2.2 billion, or 1.0% of total loans, acceptances, and reverse purchase agreements down from $2.3 billion or 1.1% in 2001.

Quarterly financial information

Selected financial information for the eight most recently completed quarters is shown on page 108A.

Table of contents

	Page
Management's responsibility for financial reporting & Auditors' report	67A
Consolidated balance sheet	68A
Consolidated statement of income	69A
Consolidated statement of changes in shareholders' equity	70A
Consolidated statement of cash flows	71A
Note 1 Significant accounting policies	72A
Note 2 Significant acquisitions	77A
Note 3 Results by business and geographic segment	78A
Note 4 Goodwill and Other intangibles	79A
Note 5 Securities	80A
Note 6 Loans	81A
Note 7 Securitizations	82A
Note 8 Premises and equipment	84A
Note 9 Other assets	84A
Note 10 Deposits	84A
Note 11 Other liabilities	84A
Note 12 Subordinated debentures	85A
Note 13 Non-controlling interest in subsidiaries	85A
Note 14 Capital stock	86A
Note 15 Income taxes	88A
Note 16 Insurance operations	89A
Note 17 Pensions and other postretirement benefits	90A
Note 18 Stock-based compensation	91A
Note 19 Earnings per share	93A
Note 20 Guarantees, commitments and contingencies	93A
Note 21 Derivative financial instruments	95A
Note 22 Concentrations of credit risk	97A
Note 23 Estimated fair value of financial instruments	98A
Note 24 Subsequent events	99A
Note 25 Contractual repricing and maturity schedule	100A
Note 26 Reconciliation of Canadian and United States generally accepted accounting principles	101A