

M Banco Modal



(A translation of the original report in Portuguese, containing financial statements and consolidated financial statements (economic-financial consolidation) prepared in accordance with accounting practices derived from the Brazilian Corporation Law and rules of the Central Bank of Brazil)

Financial Statements at December 31, 2003 and 2002 and Independent Auditor's Report

Financial Statements

Independent Auditor's Report

The Directors and Shareholders
Banco Modal S.A.
Rio de Janeiro - RJ

We have examined the balance sheets of Banco Modal S.A. and the consolidated balance sheets of Banco Modal S.A. (economic-financial consolidation) as of December 31, 2003 and 2002 and the related statements of income, changes in shareholders' equity and changes in financial position for the years then ended, which were prepared under the responsibility of its management. The consolidated financial statements (economic-financial consolidation) were prepared to comply with the rules and procedures determined by the Central Bank of Brazil and are not required by the accounting practices derived from the Brazilian Corporation Law. Our responsibility is to express an opinion on these financial statements.

Our examinations were conducted in accordance with auditing standards generally accepted in Brazil and included: (a) planning of the audit work, considering the materiality of the balances, the volume of transactions and the accounting systems and internal accounting controls of the Bank; (b) verification, on a test basis, of the evidence and records which support the amounts and accounting information disclosed; and (c) evaluation of the most significant accounting policies and estimates adopted by the Bank's management, as well as the presentation of the financial statement taken as a whole.

In our opinion, the aforementioned financial statements present fairly, in all material respects, the financial position of Banco Modal S.A. and the consolidated financial position of Banco Modal S.A. (economic-financial consolidation) as of December 31, 2003 and 2002, and the results of its operations, changes in its shareholders' equity and changes in its financial position for the years then ended, in conformity with accounting practices adopted in Brazil, and for the consolidated financial statements, in accordance with rules of the Central Bank of Brazil, as disclosed in Note 3.

January 16, 2004

KPMG Auditores Independentes
CRC-SP-14.428-"S"-RJ

José M. Matos Nicolau
Accountant CRC-RJ-42.216/O-7

Financial Statements

Balance Sheets

Years ended December 31, 2003 and 2002

(In thousand of reais)

	Banco Modal S.A.		Economic-Financial Consolidation	
	2003	2002	2003	2002
Assets				
Current assets	519,410	168,385	519,462	168,443
Cash and cash equivalents	438	389	438	395
Cash	48	27	48	27
Bank deposits	-	-	-	6
Banking reserves	390	362	390	362
Short-term interbank investments	11,008	50,540	11,008	50,540
Money market	11,008	50,540	11,008	50,540
Securities and derivative financial instruments	401,700	19,967	401,700	19,967
Own portfolio	59,404	6,019	59,404	6,019
Subject to repurchase agreements	241,389	-	241,389	-
Pledged as collateral	82,774	4,628	82,774	4,628
Deposited with the Central Bank of Brazil	9,198	2,562	9,198	2,562
Derivative financial instruments	8,935	6,758	8,935	6,758
Interbank accounts	534	362	534	362
Restricted credits - deposits with the Central Bank of Brazil	334	358	334	358
Correspondents	200	4	200	4
Loan operations - private sector	97,167	94,775	97,167	94,775
Loans and discounted notes - private sector	72,859	38,981	72,859	38,981
FINAME/BNDES repasses	24,448	55,795	24,448	55,795
(-) Allowance for doubtful debts	(140)	(1)	(140)	(1)
Other receivables	8,460	2,313	8,512	2,365
Income receivable	61	120	61	9
Securities clearing accounts	3,108	7	3,108	7
Miscellaneous	5,291	2,186	5,343	2,349
Other assets	103	39	103	39
Prepaid expenses	103	39	103	39
Long-term assets	78,055	20,780	78,055	20,780
Securities and derivative financial instruments	1,226	-	1,226	-
Derivative financial instruments	1,226	-	1,226	-
Loan operations - private sector	75,767	20,758	75,767	20,758
FINAME/BNDES repasses	75,767	20,758	75,767	20,758
Other credits	1,062	22	1,062	22
Others	1,062	22	1,062	22
Permanent assets	3,743	3,381	1,922	1,747
Investments	2,371	2,174	550	540
Fixed assets for own use	1,152	1,012	1,152	1,012
Deferred charges	220	195	220	195
Total	601,208	192,546	599,439	190,970

See accompanying notes to financial statements.

Financial Statements

Balance Sheets

Years ended December 31, 2003 and 2002

(In thousand of reais)

	Banco Modal S.A.		Economic-Financial Consolidation	
	2003	2002	2003	2002
Liabilities				
Current liabilities	453,289	116,615	451,520	115,039
Deposits	112,263	50,823	110,406	49,108
Demand deposits	288	23	287	22
Interbank deposits	28,555	-	28,555	-
Time deposits	83,420	50,800	81,564	49,086
Money market repurchase commitments	233,213	-	233,213	-
Own portfolio	233,213	-	233,213	-
Funds from acceptances and issuance of securities	50,481	-	50,481	-
Obligations from securities abroad	50,481	-	50,481	-
Repasses	24,308	55,717	24,308	55,717
FINAME/BNDES	24,308	55,717	24,308	55,717
Derivative financial instruments	2,991	3,198	2,991	3,198
Derivative financial instruments	2,991	3,198	2,991	3,198
Other liabilities	30,033	6,877	30,121	7,016
Collection of taxes	26	60	26	60
Social and statutory	4,762	546	4,762	546
Taxes and social security contributions	14,583	3,363	14,671	3,485
Securities clearing accounts	9,722	2,370	9,722	2,370
Miscellaneous	940	538	940	555
Long-term liabilities	76,670	21,984	76,670	21,984
Deposits	86	1,226	86	1,226
Time deposits	86	1,226	86	1,226
Repasses	75,767	20,758	75,767	20,758
FINAME/BNDES	75,767	20,758	75,767	20,758
Derivative financial instruments	684	-	684	-
Derivative financial instruments	684	-	684	-
Other liabilities	133	-	133	-
Taxes and social security contributions	133	-	133	-
Shareholders' equity	71,249	53,947	71,249	53,947
Capital stock: Domiciled in Brazil	53,793	46,226	53,793	46,226
Capital reserve	158	148	158	148
Earnings reserve	1,015	443	1,015	443
Adjustments to fair value - securities and derivatives	844	6	844	6
Retained earnings	15,439	7,124	15,439	7,124
Total	<u>601,208</u>	<u>192,546</u>	<u>599,439</u>	<u>190,970</u>

Financial Statements

Statements of income

(In thousand of reais, except net income per share)

	Banco Modal S.A.			Economic-Financial Consolidation		
	Second semester of 2003	Years ended December 31		Second semester of 2003	Years ended December 31	
		2003	2002		2003	2002
Income from financial operations	48,474	85,357	28,492	48,474	85,357	28,502
Loans interest	18,113	35,754	26,694	18,113	35,754	26,694
Securities trading	24,887	47,294	5,890	24,887	47,294	5,900
Derivative financial instruments	5,469	2,297	(4,100)	5,469	2,297	(4,100)
Compulsory investment	5	12	8	5	12	8
Expenses on financial operations	(26,097)	(50,562)	(9,594)	(25,920)	(50,197)	(9,448)
Funding operations	(21,742)	(44,168)	(5,136)	(21,565)	(43,803)	(4,990)
Repasses	(4,486)	(6,255)	(4,457)	(4,486)	(6,255)	(4,457)
Reversal of (allowances for) doubtful debts	131	(139)	(1)	131	(139)	(1)
Gross income on financial operations	22,377	34,795	18,898	22,554	35,160	19,054
Other operating income (expenses)	(1,020)	5,557	(8,427)	(1,156)	5,279	(8,462)
Income from services rendered	7,738	9,272	1,737	7,738	9,272	1,768
Personel expenses	(3,135)	(5,554)	(4,848)	(3,135)	(5,554)	(4,848)
Other administrative expenses	(3,861)	(6,998)	(4,391)	(3,864)	(7,010)	(4,455)
Tax expenses	(1,941)	(3,414)	(1,523)	(1,956)	(3,439)	(1,567)
Equity in income of subsidiaries	119	246	307	-	-	-
Other operating income	75	12,058	310	76	12,063	659
Other operating expenses	(15)	(53)	(19)	(15)	(53)	(19)
Operating income	21,357	40,352	10,471	21,398	40,439	10,592
Non-operating expenses	72	71	(4)	72	71	(4)
Income before income tax and participations	21,429	40,423	10,467	21,470	40,510	10,588
Income and social contribution taxes	(4,767)	(10,093)	(2,438)	(4,808)	(10,180)	(2,559)
Provision for income tax	(3,738)	(8,753)	(1,613)	(3,765)	(8,810)	(1,695)
Provision for social contribution	(1,743)	(3,552)	(597)	(1,757)	(3,582)	(636)
Deferred tax assets	714	2,212	(228)	714	2,212	(228)
Profit sharing	(2,242)	(3,836)	(1,037)	(2,242)	(3,836)	(1,037)
Net income	14,420	26,494	6,992	14,420	26,494	6,992
Interest on shareholders' equity	(4,700)	(6,200)	(2,357)	(4,700)	(6,200)	(2,357)
Net income per share	469.71	863.00	227.75	469.71	863.00	227.75

See accompanying notes to financial statements.

Financial Statements

Statements of changes in shareholders' equity Years ended December 31, 2003 and 2002 (In thousand of reais)

	Capital	Increase of capital stock	Capital reserve Revaluation of securities	Earnings reserve Statutory	Adjustment to fair value - securities and derivatives	Retained earnings	Total
Year ended December 31, 2002							
Balance as of January 1	41,726	-	139	211	-	3,086	45,162
Capital reserve constitution:							
Revaluation of securities - BM&F and CETIP	-	-	9	-	-	-	9
Increase of capital stock:							
In cash	4,500	-	-	-	-	-	4,500
Prior years adjustment:							
Change in accounting practice	-	-	-	-	-	(365)	(365)
Adjustment to fair value - securities and derivatives	-	-	-	-	6	-	6
Net income for the year	-	-	-	-	-	6,992	6,992
Distributions:							
Legal reserve	-	-	-	232	-	(232)	-
Interest on shareholders' equity (R\$76.79 per share)	-	-	-	-	-	(2,357)	(2,357)
Balance as of December 31, 2002	46,226	-	148	443	6	7,124	53,947
Changes during the year	4,500	-	9	232	6	4,038	8,785
Year ended December 31, 2003							
Balance as of January 1	46,226	-	148	443	6	7,124	53,947
Capital reserve constitution:							
Revaluation of securities - BM&F and CETIP	-	-	10	-	-	-	10
Increase of capital stock:							
With reserves	7,567	-	-	(443)	-	(7,124)	-
Adjustments to fair value - securities and derivatives	-	-	-	-	838	-	838
Net income for the year	-	-	-	-	-	26,494	26,494
Distributions:							
Legal reserve	-	-	-	1,015	-	(1,015)	-
Interest on shareholders' equity (R\$201.95 per share)	-	-	-	-	-	(6,200)	(6,200)
Dividends	-	-	-	-	-	(3,840)	(3,840)
Balance as of December 31, 2003	53,793	-	158	1,015	844	15,439	71,249
Changes during the year	7,567	-	10	572	838	8,315	17,302
Semester ended December 31, 2003							
Balance as of July 1	46,226	7,567	158	529	86	8,725	63,291
Increase of capital stock with reserves	7,567	(7,567)	-	-	-	-	-
Adjustment to fair value - TVM and derivatives	-	-	-	-	758	-	758
Net income for the period	-	-	-	-	-	14,420	14,420
Distributions:							
Legal reserve	-	-	-	486	-	(486)	-
Interest on shareholders' equity (R\$153.09 per share)	-	-	-	-	-	(4,700)	(4,700)
Dividends	-	-	-	-	-	(2,520)	(2,520)
Balance as of December 31, 2003	53,793	-	158	1,015	844	15,439	71,249
Changes during the semester	7,567	(7,567)	-	486	758	6,714	7,958

See accompanying notes to financial statements.

Financial Statements

Statements of changes in financial position

(In thousand of reais)

	Banco Modal S.A.			Economic-Financial consolidation		
	Second semester of 2003	Years ended December 31		Second semester of 2003	Years ended December 31	
		2003	2002		2003	2002
Source of funds	360,513	458,405	106,656	360,524	458,399	105,548
Adjusted net income	14,487	26,617	7,033	14,606	26,863	7,340
Net income	14,420	26,494	6,992	14,420	26,494	6,992
Adjustments to net income:						
Depreciation and amortization	186	369	348	186	369	348
Equity in income of subsidiaries	(119)	(246)	(307)	-	-	-
Adjustment to fair value - securities and derivatives	758	838	6	758	838	6
Funds from shareholders	-	-	4,500	-	-	4,500
Increase of capital	-	-	4,500	-	-	4,500
Funds from third parties arising from	345,268	430,950	95,117	345,160	430,698	93,702
Increase in current and long-term liabilities	318,971	391,360	95,076	318,921	391,166	93,662
Deposits	41,544	60,300	29,654	41,467	60,157	29,215
Money market repurchase commitments	233,213	233,213	-	233,213	233,213	-
Funds from acceptances and issuance of securities	-	50,481	-	-	50,481	-
Repasses	42,335	23,600	58,451	42,335	23,600	58,451
Derivative financial instruments	-	477	2,262	-	477	2,262
Other obligations	1,879	23,289	4,709	1,906	23,238	3,734
Decrease in current and long-term assets	26,239	39,532	40	26,239	39,532	40
Short-term interbank investments	25,832	39,532	-	25,832	39,532	-
Interbank accounts	407	-	40	407	-	40
Dividends received from subsidiaries	58	58	1	-	-	-
Application of funds	360,330	458,356	106,408	360,341	458,356	105,294
Prior years adjustment	-	-	365	-	-	365
Dividends and bonuses proposed	2,520	3,840	-	2,520	3,840	-
Interest on shareholders' equity	4,700	6,200	2,357	4,700	6,200	2,357
Acquisition of	341	413	638	341	413	638
Investments	-	-	263	-	-	263
Fixed assets for own use	341	413	375	341	413	375
Increase in deferred charges	93	120	52	93	120	52
Increase in current and long-term assets	334,407	447,783	101,796	334,418	447,783	100,682
Short-term interbank investments	-	-	31,216	-	-	31,216
Securities and derivative financial instruments	296,447	382,959	6,355	296,447	382,959	6,355
Interbank accounts	-	172	-	-	172	-
Loan operations	32,358	57,401	62,883	32,358	57,401	62,883
Other receivables	5,554	7,187	1,334	5,565	7,187	220
Other assets	48	64	8	48	64	8
Decrease in current and long-term liabilities	18,269	-	1,200	18,269	-	1,200
Money market repurchase commitments	-	-	1,200	-	-	1,200
Funds from acceptances and issuance of securities	17,279	-	-	17,279	-	-
Interbank accounts	383	-	-	383	-	-
Derivative financial instruments	607	-	-	607	-	-
Increase in cash and cash equivalents	183	49	248	183	43	254
Changes in financial position						
Cash and cash equivalents						
At the beginning of the semester/year	255	389	141	255	395	141
At the end of the semester/year	438	438	389	438	438	395
Increase in cash and cash equivalents	183	49	248	183	43	254

See accompanying notes to financial statements..

Financial Statements

Notes to the financial statements Years ended December 31, 2003 and 2002 (In thousand of reais)

1 Operations

The main activity of Banco Modal S.A., a joint-stock company, is to perform banking operations and render such services as multiservice banks with commercial and investment portfolios are authorized to offer, and to hold share interests in other companies.

2 Presentation of the financial statements

The financial statements were prepared in accordance with the accounting practices derived from the Brazilian Corporation Law and the rules established by the Central Bank of Brazil (BACEN), and are presented in conformity with the Accounting Chart for Institutions of the National Financing System - COSIF.

3 Consolidated financial statements (Economic-Financial Consolidation - CONEF)

The consolidated financial statements were prepared in accordance with the consolidation principles determined by the Central Bank of Brazil - BACEN. The consolidated financial statements comprise the following institutions:

- Banco Modal S.A.;
- Modal Trading S.A. **(a)**; and
- Modal Energy S.A. **(b)**.

(a) Banco Modal S.A. holds 100% share interests in Modal Trading S.A., which was formed on November 5, 1999. On December 31, 2003, its shareholders' equity was R\$1,689 (2002 R\$1,510) and the annual net income was R\$234 (2002 R\$303).

(b) Banco Modal S.A. holds 100% share interests in Modal Energy, which was formed on July 12, 2000. On December 31, 2003, its shareholders' equity was R\$133 (2002 R\$124) and the annual net income was R\$13 (2002 R\$4).

The Economic-Financial Consolidation of the equity accounts and income statement accounts corresponds to the aggregate of the balances of the assets, liabilities, income, and expense accounts, according to their nature, together with the elimination of interests in capital, retained earnings and investments and the balances of current accounts and other asset and/or liability accounts maintained by the institutions and companies whose balance sheets were consolidated.

Financial Statements

Notes to the financial statements Years ended December 31, 2003 and 2002 (In thousand of reais)

4 Significant accounting practices

a. Income recognition

Revenues and expenses are recognized on an accrual basis.

b. Securities

Fixed income securities were recorded at cost plus accrued interest and equity securities were recorded at cost, both being adjusted to market value. Securities are classified in three categories, as follows:

I - Securities for trading: acquired for the purpose of being frequently and actively traded;

II - Securities held to maturity: acquired with the intention of holding them to maturity; and

III - Securities available for sale: the securities that are not classified in categories I e II.

Securities classified in categories I and III are adjusted to their market value, with the portfolio adjustments recorded as balancing items in income and in a specific shareholders' equity account, net of taxes, respectively, and those classified in category II are adjusted according to their respective acquisition cost, with the accrued interest recorded in an income account.

c. Loans, interbank and time deposits and other receivables and liabilities

Fixed interest transactions were recorded at redemption value, adjusted to present value in deferred income/expense.

Transactions subject to contractual indexation were recorded at present value, adjusted pro-rata to the balance sheet date.

d. Allowance for doubtful debts

The allowance for doubtful debts is estimated based on an analysis of outstanding loans carried out by management in order to determine their value and takes into consideration the economic scenario, past experience, and the specific and overall risks of the portfolio as well as the rules and instructions established by BACEN.

e. Permanent assets

Stated at acquisition cost, together with the following aspects:

Investments: Investments in subsidiaries are accounted for by the equity method, and other investments are valued at cost. The shares of the commodities on the futures exchange (BM&F) and the local clearance house (CETIP) were revalued based on equity value and the result of these revaluations was recorded in capital reserves - revaluation of securities.

Fixed assets: Depreciation was calculated on the straight-line method based on the estimated useful lives of the corresponding assets.

Deferred charges: Amortization of deferred charges, basically improvements to leasehold properties, on a straight-line basis, in accordance with the term of the lease.

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Notes to the financial statements Years ended December 31, 2003 and 2002 (In thousand of reais)

f. Current and long-term liabilities

Stated at known or estimated amounts, plus, when applicable, the corresponding charges, and monetary and exchange variations incurred on a daily "pro-rata die" basis.

g. Income tax and social contribution

Provision for income tax was calculated at the rate of 15% on taxable profits and, when applicable, plus an additional rate of 10% on taxable profits in excess of R\$240. Provision for social contribution tax was calculated at the rate of 9% on profits before income tax, adjusted in accordance with current legislation.

h. Derivatives

Transactions with derivatives are recorded as follows:

Options: The face value of call option contracts on stocks, financial assets and commodities, both issued and outstanding, are recorded in memorandum accounts. Premiums received and/or paid when the operations are realized are recorded in equity accounts.

Futures: Contracts for transactions of financial assets and commodities in the futures market are recorded in memorandum accounts. These contracts are adjusted daily according to the type of asset and its maturity, and recognized monthly in the income.

Swap: Swap contracts are recorded in memorandum accounts at the nominal amounts. The differences payable or receivable are recorded in equity accounts.

Derivatives are valued at market value, recording the valuation and/or devaluation in accordance with the respective classifications:

- I - Not destined for hedge: in income for the period;
- II - Destined for market risk hedge: recorded as balancing items in income or expenses, in income for the period; and
- III - Destined for cash flow hedge: the valuation and the devaluation of the effective portion of the hedge are recorded as balancing items in a specific shareholders' equity account.

i. Adjustment to market value

Adjustments to market value of securities and derivatives are based on quotations of prices and market agents and on pricing models usually adopted by the financial institutions and their representative associations.

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Notes to the financial statements Years ended December 31, 2003 and 2002

(In thousand of reais)

5 Securities and derivative financial instruments (Bank and Economic-Financial Consolidation)

a. Securities

	2003		2002	
	Cost value	Fair value	Cost value	Fair value
Own portfolio:				
Securities for trading				
Shares of publicly traded companies	590	615	2,227	2,269
Securities available for sale				
Debentures	-	-	1,775	1,774
Financial Treasury Bills	-	-	1,975	1,976
National Treasury Bills	58,787	58,789	-	-
	<u>59,377</u>	<u>59,404</u>	<u>5,977</u>	<u>6,019</u>
Subject to repurchase agreements:				
Securities available for sale				
National Treasury Notes	132,086	133,370	-	-
National Treasury Bills	108,049	108,019	-	-
	<u>240,135</u>	<u>241,389</u>	<u>-</u>	<u>-</u>
Pledged as collateral:				
Securities for trading				
Shares of publicly traded companies	8,164	12,530	788	822
Securities available for sale				
Financial Treasury Bills	-	-	3,797	3,806
National Treasury Bills	70,299	70,244	-	-
	<u>78,463</u>	<u>82,774</u>	<u>4,585</u>	<u>4,628</u>
Deposit with the Central Bank of Brazil:				
Securities available for sale				
Financial Treasury Bills	-	-	2,561	2,562
National Treasury Bills	9,120	9,198	-	-
	<u>9,120</u>	<u>9,198</u>	<u>2,561</u>	<u>2,562</u>

Except for shares, on December 31, 2003 securities had the following maturities: R\$264,037 (2002 - R\$8,344) up to 360 days and R\$115,584 (2002 - R\$1,744) up to 720 days.

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Notes to the financial statements Years ended December 31, 2003 and 2002 (In thousand of reais)

b. *Derivative financial instruments*

	Cost value	2003 Market value	Cost value	2002 Market value
Asset position				
Premiums on stock options	4,257	2,756	15	22
Receivable differentials on swap transactions	10,388	7,405	5,604	6,736
	<u>14,645</u>	<u>10,161</u>	<u>5,619</u>	<u>6,758</u>
Liability position				
Premiums on written options	5,528	2,816	-	-
Forward contracts obligation	-	-	(130)	54
Payable differentials on swap transactions	237	859	5,104	3,144
	<u>5,765</u>	<u>3,675</u>	<u>4,974</u>	<u>3,198</u>

Banco Modal S.A. engages in transactions with financial instruments aimed at meeting its own and clients' needs, to reduce exposure to market, currency, and interest rate risks. These risks are managed using policies that define the strategy of the operation, monitoring controls and position limits.

The operations with these instruments are duly registered in the Futures and Commodities Exchange (BM&F), in the Clearing House for the Custody and Financial Settlement of Securities (GETIP) and/or in the Brazilian Center for Settlement and Custody (CBLIC). For the operations maintained with these institutions at December 31, 2003, margins in guarantee were required in the amount of R\$82,774 (2002 - R\$8,628), which are represented by public securities and guarantees.

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Notes to the financial statements Years ended December 31, 2003 and 2002

(In thousand of reais)

Commitments derived from operations with derivatives recorded in memorandum accounts on December 31, 2003 and 2002 may be presented as follows:

b.1 By type

	Place of trading	Asset position	2003 Liability position	Asset position	2002 Liability position
Options market:					
Shares	CBLC	6,800	156,121	392	-
Financial assets:					
Call options	BM&F	350,250	1,538,460	-	-
Put options	BM&F	571,352	-	-	-
Futures market:					
Interest rates	BM&F	843,551	283,066	15,673	6,488
Currency	BM&F	59,229	69,133	-	-
Price indexes	BM&F	-	-	2,407	-
Forward market:					
Currency	CETIP	-	-	-	54
Swap:					
Interest rate	CETIP	179,028	1,417	38,148	15,120
Currency	CETIP	1,396	168,721	-	38,195
Price indexes	CETIP	-	-	12,641	-
Interest rate	BM&F	21,072	24,527	63,045	102,403
Currency	BM&F	-	204	46,501	323
Price indexes	BM&F	24,312	20,787	14,551	18,344

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Notes to the financial statements Years ended December 31, 2003 and 2002 (In thousand of reais)

b.2 By maturity

	Up to 30 days	From 31 to 90 days	From 91 to 180 days	From 181 to 360 days	More than 360 days	2003	Total 2002
Options:							
Shares:							
Purchase contracts	6,800	-	-	-	-	6,800	392
Sales contracts	156,121	-	-	-	-	156,121	-
Financial assets:							
Purchase contracts	418,352	-	130,000	373,250	-	921,602	-
Sales contracts	152,500	-	1,075,850	310,110	-	1,538,460	-
Futures market:							
Purchase contracts	59,229	18,609	514,533	123,692	186,717	902,780	18,080
Sales contracts	146,187	83,643	-	44,739	77,630	352,199	6,499
Forward market:							
Sales contracts	-	-	-	-	-	-	54
Swap:							
Asset position	177	671	4,831	500	1,226	7,405	6,736
Liability position	112	-	-	63	684	859	3,144

6 Risk management

The management of risk in the operations is performed through control and limit policies defined by a Risk Committee, formed by senior management, the economic department and the risk area, which is totally independent from the Bank's business areas.

a. Market risk

Market stress testing and historical crisis simulations are used on a routine basis for decision-making. Before the market opens, reports are released which include a value-at-risk analysis, Monte Carlo simulation and tests to validate the calculation methodology (back testing), detailing all asset and liability positions.

b. Liquidity risks

Liquidity risk is managed by adopting controls that assure the allocation of funds to assets of high quality and liquidity, based on equity and/or capital obtained from counterparties of good reputation at rates in line with the market. This control also includes the analysis of possible mismatches in time between assets and liabilities and the resulting adjustments needed.

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(In thousand of reais)

c. Credit risk

The Institution has a policy for granting credit whereby procedures for assessment of clients and counterparties are established. An assessment of each client or counterparty is made prior to realizing operations and includes objective analyses of financial data, comparative ratios, cash flow, working capital, coverage of interest rates and quality of the guarantees provided, as well as subjective analyses including data on the economic sector, regulatory environment and market share. The limits are approved by the Credit Committee and are regularly reviewed together with the sufficiency of the guarantees provided.

7 Loan operations (Bank and Economic-Financial Consolidation)

Loan operations are rated according to nine risk levels and the provision for doubtful debts is made based on the client's rating under the risk levels defined by the National Monetary Council (Conselho Monetário Nacional - CMN). This rating considers, among others, a cyclical analysis of the operation, overdue payments, the client's history, and guarantees provided, when applicable.

The classification of loan operations is as follows:

a. By type of client, economic activity and risk level

Type of credit	Type of client	Economic activity	Risk level	2003		2002	
				Balance	Provision for losses	Balance	Provision for losses
Loans and discounted notes:							
	Corporate	Industry	AA	24,966	-	23,932	-
	Corporate	Commerce	AA	27,021	-	1,510	-
	Corporate	Service	AA	20,187	-	13,526	-
	Corporate	Commerce	C	371	11	-	-
	Corporate	Service	C	1	-	-	-
	Corporate	Industry	D	199	20	13	1
	Corporate	Industry	G	16	11	-	-
	Corporate	Industry	H	98	98	-	-
FINAME/BNDES:							
	Corporate	Industry	AA	88,947	-	35,221	-
	Corporate	Commerce	AA	6,145	-	18,671	-
	Corporate	Service	AA	-	-	22,661	-
	Individual	-	AA	5,123	-	-	-
				<u>173,074</u>	<u>140</u>	<u>115,534</u>	<u>1</u>

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Notes to the financial statements Years ended December 31, 2003 and 2002

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b. By maturity

Type of credit	Overdue up to 180 days		Falling due up to 180 days		Falling due from 181 to 360 days		Falling due after 360 days		Total	
	2003	2003	2002	2003	2002	2003	2002	2003	2002	
Loans and discounted notes:	257	72,160	38,981	442	-	-	-	72,859	38,981	
FINAME/BNDES:	-	5,574	50,596	18,874	5,199	75,767	20,758	100,215	76,553	
	<u>257</u>	<u>77,734</u>	<u>89,577</u>	<u>19,316</u>	<u>5,199</u>	<u>75,767</u>	<u>20,758</u>	<u>173,074</u>	<u>115,534</u>	

c. Cession of credits

Banco Modal S.A. carried out cession of credits, without co-obligations, in accordance with Resolution nr. 2,836 of May 30, 2001 of the Central Bank of Brazil - BACEN. The values of these negotiations are presented as follows:

	2003	2002
Book value of cession of credits	27,475	10,022
Traded value of cession of credits	<u>27,915</u>	<u>10,812</u>
Gain on cession of credits	<u>440</u>	<u>790</u>

At the year ended December 31, 2003, Banco Modal S.A. recorded a provision for receivables in arrears in the amount of R\$140. During this year, there was no recovery or write-off of overdue receivables.

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8 Repasses (Bank and Economic-Financial Consolidated)

	2003	2002
Represented by loans from the National Bank for Economic and Social Development - BNDES and the Government Agency for Machinery and Equipment Financing - FINAME, subject to:		
- Interest rates from 1.0% to 5.0% per annum plus Long-term Interest Rate - TJLP, with maturities up to September 2010.	92,854	32,524
- Interest rate up to 2.5% per annum plus LIBOR plus variation of the US dollar commercial exchange rate, with maturities up to March 2003.	-	39,585
- Interest rates from 1.0% to 3.0% per annum and updated with BNDES currency mix with maturities up to April 2009.	<u>7,221</u>	<u>4,366</u>
	100,075	76,475
Current	<u>(24,308)</u>	<u>(55,717)</u>
Long-term	<u>75,767</u>	<u>20,758</u>

9 Obligations for securities abroad (Bank and Economic-Financial Consolidated)

In March, 2003, Banco Modal S.A. raised funds with banks abroad under a US\$50,000,000 Eurobonus Program. The funds were raised in two issues, being one in the amount of US\$6,000,000 bearing interest of 8.75% per annum and with payment of the principal and interest in September 2003 and the second in the amount of US\$17,000,000 bearing interest of 10% per annum and with payment of interest in September 2003 and final maturity in March 2004.

These obligations, which are subject to exchange variation, were duly hedged through derivative financial instruments. During the first semester of 2003, due to the Real appreciation against the US dollar, revenue from exchange variation in the amount of R\$11,585 was recorded under the caption "Other operating income" and the hedging expenses were recorded under the caption "Derivative financial instruments" in the amount of R\$12,658.

10 Other liabilities

	2003	2002
Securities clearing accounts:		
Creditors - outstanding accounts	621	5
Obligations for share loans	<u>9,101</u>	<u>2,365</u>
	<u>9,722</u>	<u>2,370</u>

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Notes to the financial statements Years ended December 31, 2003 and 2002 (In thousand of reais)

11 Income tax and social contribution

The reconciliation between the amounts calculated according to the nominal rates and the amount recorded in the income statement can be summarized as follows:

	2003		2002	
	Income tax	Social contribution	Income tax	Social contribution
Income before taxes on income after profit sharing and interest on shareholders' equity	<u>30,387</u>	<u>30,387</u>	<u>7,073</u>	<u>7,073</u>
Income tax and social contribution at nominal rates	7,573	2,735	1,744	636
Addition of adjustments to market value of securities and derivatives	138	50	(738)	(265)
Non-deductible provisions	35	12	-	-
Other permanent additions (exclusions)	(184)	(66)	(58)	(21)
Fiscal incentives	<u>(44)</u>	<u>-</u>	<u>(20)</u>	<u>-</u>
Current income tax and social contribution	7,518	2,731	928	350
Deferred tax liability on temporary differences related to the adjustment to market value of securities and derivatives	<u>1,235</u>	<u>821</u>	<u>685</u>	<u>247</u>
	8,753	3,552	1,613	597
Reversal (constitution) of tax credits on temporary differences related to the adjustment to market value of securities and derivatives	<u>(1,626)</u>	<u>(586)</u>	<u>168</u>	<u>60</u>
Income tax and social contribution - total	<u>7,127</u>	<u>2,966</u>	<u>1,781</u>	<u>657</u>

The tax credits and deferred tax liability arising from the valuation to market of securities and derivatives were calculated and recorded in accordance with the rules established by Circular nr. 3,171 of December 30, 2002, considering the prevailing rates for income tax and social contribution. The balances of these tax credits and liabilities are recorded at present values and are presented as follows:

	2003	2002
Other receivables - miscellaneous		
Deferred tax assets realizable in up to five years	<u>2,495</u>	<u>228</u>
Other liabilities - taxes and social security contributions		
Deferred tax liability	<u>3,744</u>	<u>1,202</u>

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12 Shareholders' equity

a. *Capital*

Capital stock comprises 15,350 common shares (2002 - 15,350) and 15,350 nominative preferred shares (2002 - 15,350), with no par value.

In an Extraordinary Shareholders' Meeting held on May 23, 2003, the shareholders approved the capital increase of Banco Modal S.A. of R\$7,567, through the statutory reserve of R\$443 and retained earnings of R\$7,124, without issuance of new shares.

b. *Rights of shares*

Shareholders of Banco Modal S.A. are assured a minimum dividend of 6% of capital, not less than 25% of net income adjusted in accordance with Law nr. 6404/76.

Preferred shares, with no voting rights, have priority in the return of capital, in the case of Bank liquidation without the payment of a premium, and the right to a minimum dividend of R\$0.01 per share.

In Extraordinary Shareholders' Meetings held on June 30, 2003 and December 31, 2003, dividends were proposed in the amount of R\$1,320 and R\$2,520, respectively.

c. *Interest on shareholders' equity*

During the year ended on December 31, 2003, using the rights established in Law nr. 9,249/95, the Bank to its shareholders interest on equity in the amount of R\$6,200 (2002 - R\$2,357).

For financial statement presentation purposes, in accordance with BACEN Circular nº 2739/97, this interest is presented in the changes in retained earnings. Tax effect on net income for the year was R\$2,108 (2002 - R\$802).

d. *Statutory reserve*

This reserve is composed of the equivalent of 5% of net income in each financial year, up to the limits established by Brazilian Corporation Law.

13 Operational limits (Basle Committee)

Financial institutions have to maintain minimum shareholders' equity equivalent to 11% of their consolidated assets weighted by risk factors, increased by percentages of the credit risk on swap operations, the exposures in gold and on assets and liabilities linked to variations in foreign exchange and interest rates in accordance with rules and instructions from BACEN.

Banco Modal S.A. is in compliance with this operational limit, with a Basle Committee ratio of 43.07% (2002 - 32.87%) as of December 31, 2003.

14 Other information (Bank and Economic-Financial Consolidation)

a. Income from services rendered refers basically to commissions received for performing structured operations for clients as well as income arising from the management and performance of investment funds managed by Banco Modal S.A., the net equity of which at December 31, 2003 totaled R\$14,274 (2002 - R\$232,587).

b. On December 31, 2003, the Bank had co-obligations from guarantees rendered in the amount of R\$19,059 (2002 - R\$28,826).

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