

REPORT OF THE DIRECTORS

The directors are pleased to present their report together with the audited consolidated accounts of the Company and its subsidiaries for the year ended 31 December 2003.

Principal Activities

The principal activities of the Group are the provision of banking and related financial services. An analysis of the Group's performance for the year by business segments is set out in Note 40 to the accounts.

Results and Appropriations

The results of the Group for the year are set out in the consolidated profit and loss account on page 71.

The Board has recommended a final dividend of HK\$0.320 per ordinary share, amounting to approximately HK\$3,383 million, subject to the approval of shareholders at the forthcoming Annual General Meeting to be held on Friday, 21 May 2004. If approved, the final dividend will be paid on Tuesday, 25 May 2004 to shareholders whose names appear on the Register of Members of the Company on Wednesday, 19 May 2004. Together with the interim dividend of HK\$0.195 per share declared in September 2003, the total dividend payout for 2003 would be HK\$0.515 per share.

Closure of Register of Members

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to the final dividend, from Wednesday, 12 May 2004 to Wednesday, 19 May 2004 (both days inclusive), during which period no transfer of shares will be registered. In order to rank for the final dividend, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong, not later than 4:00 p.m. on Tuesday, 11 May 2004.

Reserves

Details of the reserves of the Group are set out in Note 33 to the accounts.

Donations

Charitable and other donations made by the Group during the year amounted to HK\$4,678,000.

Fixed Assets

Details of the movements in fixed assets of the Group are set out in Note 26 to the accounts.

Distributable Reserves

Distributable reserves of the Company at 31 December 2003, calculated under section 79B of the Hong Kong Companies Ordinance, amounted to approximately HK\$4,058 million.

Five-Year Financial Summary

A summary of results, assets and liabilities of the Group for the last five years is set out on page 2.

Purchase, Sale or Redemption of the Company's Shares

During the year, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares.

Share Options

Pursuant to written resolutions of all the Company's shareholders passed on 10 July 2002, the Company has approved and adopted two share option schemes, namely, the Share

Option Scheme and the Sharesave Plan. In connection with its listing on the Stock Exchange, the Company has undertaken to the Stock Exchange that for a period of six months from its listing i.e. until 25 January 2003, the Company shall not, among other things, grant or offer or agree to grant options over any shares without the prior consent of the Stock Exchange. No options have been granted by the Company pursuant to the Share Option Scheme or the Sharesave Plan during the year.

The following is a summary of the Share Option Scheme and the Sharesave Plan disclosed in accordance with the Listing Rules:

	Share Option Scheme	Sharesave Plan
Purpose of the scheme	To provide the participants with the opportunity to acquire proprietary interests in the Company, to attract and retain the best available personnel, to encourage and motivate the participants to work towards enhancing the value of the Company and its shares, to allow the participants to participate in the growth of the Company and to align the interests of the shareholders and the participants.	To encourage broad-based employee ownership of the Company's shares, to increase employee awareness and participation in the Company's share price performance, to provide employees with an additional vehicle for asset accumulation and to align the interests of all employees with those of the Company's shareholders.
Participants of the scheme	Subject to compliance with applicable laws, full-time or part-time employee, executive or officer of the Group, executive or non-executive director of the Group, or full-time or part-time employee, executive, officer or director of BOC or any of its subsidiaries serving as a member of any committee of the Group.	Employee, executive, officer or director of the Group, having such qualifying period of service (if any) as the Board may determine from time to time and not having been granted any options under the Share Option Scheme.
Total number of shares available for issue under the scheme and percentage of issued share capital as at 31 December 2003	The maximum number of shares in respect of which options may be granted under the Share Option Scheme, the Sharesave Plan and any other share option schemes and savings-based share option plans of any company in the Group (the "Other Schemes and Plans") shall not in aggregate exceed 10% of the shares in issue on 10 July 2002, that is, 1,057,278,026 shares.	Same as Share Option Scheme.
Maximum entitlement of each participant under the scheme	The total number of shares issued and to be issued upon the exercise of the options granted and to be granted to any one participant under the Share Option Scheme and the Other Schemes and Plans (including exercised, cancelled and outstanding options) in any twelve-month period up to and including the date of grant shall not exceed 1% of the shares in issue from time to time.	The maximum number of shares (rounded down to the next whole number) which can be paid for at the exercise price with monies equal to the aggregate of the savings contributions the participant has undertaken to make by the Maturity Date (defined as below) and interest which may be accrued thereon. Provided that the total number of shares issued and to be issued upon the exercise of the options granted and to be granted to any one participant under the Sharesave Plan and the Other Schemes and Plans (including exercised, cancelled and outstanding options) in any twelve-month period up to and including the date of grant shall not exceed 1% of the shares in issue from time to time. The amount of the monthly contribution to be made by a participant shall not be less than 1% and not more than 10% of the participant's monthly salary or such other maximum or minimum amounts, as permitted by the Board.
The period within which the shares must be taken up under an option	Such period as shall be prescribed by the directors and specified in the letter of offer.	The thirty day period (excluding the anniversary days) immediately after the first and second anniversary days from the date of grant or such other date as determined by the Board, or the thirty day period immediately after the third anniversary of the date of grant or such other date as determined by the Board (the "Maturity Date"), or such other period(s) as may be determined by the Board.
The minimum period for which an option must be held before it can be exercised	Such minimum period as shall be prescribed by the directors and specified in the letter of offer.	One year.
(a) The amount payable on acceptance of the option	(a) HK\$1.00	(a) HK\$1.00
(b) The period within which payments or calls must or may be made	(b) Payment or an undertaking to make payment on demand of the Company must be received by the Company within the period open for acceptance as set out in the letter of offer which shall not be less than 7 days after the offer date.	(b) Payment or an undertaking to make payment on demand of the Company must be received by the Company not later than the date specified in the letter of invitation as the directors may determine.
(c) The period within which loans for such purposes must be repaid	(c) Not applicable.	(c) Not applicable.
The basis of determining the exercise price	The exercise price is determined on the date of grant by the directors and shall not be less than the highest of: (a) the nominal value of the Company's shares; (b) the closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheet on the date of grant, which must be a business day; and (c) the average closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheets for the five business days immediately preceding the date of grant.	Same as Share Option Scheme.
The remaining life of the scheme	The Share Option Scheme shall remain in force for a period of ten years commencing on the first day of dealings in the Company's shares on the Stock Exchange which was 25 July 2002.	The Sharesave Plan shall remain in force for a period of ten years after the date of approval and adoption of the Sharesave Plan by the Company's shareholders which was 10 July 2002.

Please refer to the section “Directors’ Rights to Acquire Shares” for details of the options granted by BOC (BVI) over shares of the Company pursuant to the Pre-Listing Share Option Scheme.

Directors

The present directors of the Company are set out on page 37.

On 28 May 2003, Mr. Xiao Gang replaced Mr. Liu Mingkang as Chairman of the Company and Mr. He Guangbei replaced Mr. Liu Jinbao as Vice Chairman, Executive Director and Chief Executive of the Company. Further, on 11 July 2003, Mr. Chia Pei-yuan resigned as Independent Non-executive Director of the Company and on 12 November 2003, Ambassador Yang Linda Tsao was appointed as Independent Non-executive Director of the Company. On 2 February 2004, Mr. Ping Yue resigned as Non-executive Director of the Company.

Article 103 of the Company’s Articles of Association provides that any director appointed by the Board shall hold office only until the next annual general meeting of the Company, but shall be eligible for re-election at such meeting. Accordingly, Ambassador Yang Linda Tsao, being director so appointed, shall retire at the forthcoming annual general meeting and, being eligible, offer herself for re-election.

Further, in accordance with Article 98 of the Company’s Articles of Association, one-third of the directors or the nearest number to but not exceeding one-third of the directors shall retire from office and be eligible for re-election. However, Chairman, Vice Chairman and Chief Executive are not subject to retirement by rotation. Accordingly, Messrs. Zhou Zaiqun and Tung Chee Chen shall retire by rotation at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

The term of office for each Non-executive Director is three years from the date of his/her appointment.

Biographical Details of Directors and Senior Management

Biographical details of the directors and senior management are set out on pages 39 to 44 of this Annual Report.

Directors’ Service Contracts

No director offering for re-election at the forthcoming Annual General Meeting has a service contract with the Company or any of its subsidiaries, which is not determinable by the employing company within one year without payment of compensation other than the normal statutory compensation.

Directors’ Interests in Contracts of Significance

No contracts of significance, in relation to the Group’s business to which the Company, its holding companies or any of its subsidiaries or fellow subsidiaries was a party and in which a director had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

Directors’ Rights to Acquire Shares

On 5 July 2002, the following directors were granted options by BOC (BVI), the immediate holding company of the Company, pursuant to a Pre-Listing Share Option Scheme to purchase

from BOC (BVI) an aggregate of 13,737,000 existing issued shares of the Company at a price of HK\$8.50 per share. The option shares represent approximately 0.13% of the Company's issued share capital as at the date of grant and as at 31 December 2003. None of these options may be exercised within one year from 25 July 2002. These options have a vesting period of four years from 25 July 2002 with a valid exercise period of ten years. 25% of the number of shares subject to such options will vest at the end of each year. No offer to grant any options under the Pre-Listing Share Option Scheme may be made on or after 25 July 2002, the date on which dealings in the Company's shares commenced on the Stock Exchange.

Particulars of the options granted to the directors under the Pre-Listing Share Option Scheme are set out below:

	Date of grant	Exercise price (HK\$)	Exercisable Period	Number of share options					
				Granted on 5 July 2002	Balances as at 1 January 2003	Exercised during the year	Surrendered during the year	Lapsed during the year	Balances as at 31 December 2003
SUN Changji	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,590,600	1,590,600	-	-	-	1,590,600
HE Guangbei	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,446,000	1,446,000	-	-	-	1,446,000
HUA Qingshan	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,446,000	1,446,000	-	-	-	1,446,000
LI Zaohang	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,446,000	1,446,000	-	-	-	1,446,000
ZHOU Zaiqun	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,446,000	1,446,000	-	-	-	1,446,000
ZHANG Yanling	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,446,000	1,446,000	-	-	-	1,446,000
LIU Mingkang *	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,735,200	1,735,200	-	1,735,200	-	-
LIU Jinbao *	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,735,200	1,735,200	-	-	-	1,735,200
PING Yue **	5 July 2002	8.50	25 July 2003 to 4 July 2012	1,446,000	1,446,000	-	-	-	1,446,000
Total:				13,737,000	13,737,000	-	1,735,200	-	12,001,800

* Resigned with effect from 28 May 2003.

** Resigned with effect from 2 February 2004.

Save as disclosed above, at no time during the year was the Company or its holding companies, or any of its subsidiaries or fellow subsidiaries a party to any arrangements to enable the directors to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

Directors' and Chief Executive's Interests in Shares, Underlying Shares and Debentures

Save as disclosed above, as at 31 December 2003, none of the directors or chief executive of the Company had any interests or short positions in the shares, underlying shares or debentures of the Company or any associated corporation (within the meaning of Part XV of the SFO) as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies.

Directors' Interests in Competing Business

Save and except the Independent Non-executive Directors, all other directors are also directors of BOC, the ultimate holding company of the Company, at the same time. BOC is a state-owned commercial bank in the Mainland of China and provides a full range of commercial banking and other financial services through its associates throughout the world. Certain of the Group's operations overlap with and/or are complementary to those of BOC and its associates. To the extent that BOC or its associates compete with the Group, the directors believe that the Group's interests are adequately protected by adhering to good corporate governance practices and the involvement of the Independent Non-executive Directors.

Save as disclosed above, none of the directors is interested in any business apart from the Group's business, which competes or is likely to compete, either directly or indirectly, with the Group's business.

Substantial Interests in Share Capital

The register maintained by the Company pursuant to section 336 of the SFO recorded that, as at 31 December 2003, the following corporations had the following interests (as defined in the SFO) in the Company:

	Name of Corporation		
	BOC	BOCHKG	BOC (BVI)
Aggregate long position in shares and underlying shares	7,004,340,277	6,961,755,277	6,961,755,277
% of total issued shares of the Company	66.25%	65.85%	65.85%
Capacity in which such interests are held	Through controlled corporation (Notes 1, 2 and 3)	Through controlled corporation (Note 1)	Held 6,959,753,556 shares as beneficial owner Held 2,001,721 shares through controlled corporation (Note 4)
Nature of such interests			
1. Interests in shares	6,986,155,277	6,961,755,277	6,961,755,277
2. Interests under equity derivatives			
• Cash settled	10,000,000	–	–
• Physically settled	8,185,000	–	–

Notes:

1. BOC holds the entire issued share capital of BOCHKG which in turn holds the entire issued share capital of BOC (BVI). Accordingly, BOC and BOCHKG are deemed to have the same interests in the Company as BOC (BVI) for the purpose of the SFO.
2. BOC holds the entire issued share capital of BOC Investment which in turn holds 94.5% of the issued share capital of BOC Insurance which in turn holds the entire issued share capital of BOC Life. Accordingly, for the purpose of the SFO, BOC is deemed to have the same interests in the Company as BOC Insurance and BOC Life, each of which had an interest in 5,700,000 shares of the Company.
3. BOC holds the entire issued share capital of BOCI which in turn holds the entire issued share capital of BOCI Financial Products Limited. Accordingly, BOC is deemed to have the same interests in the Company as BOCI Financial Products Limited which had an interest in 13,000,000 shares of the Company and an interest in 18,185,000 shares under equity derivatives of which an interest in 10,000,000 shares is cash settled and an interest in 8,185,000 shares is physically settled.
4. BOC (BVI) holds 93.64% of the issued share capital of Hua Chiao which is in members' voluntary winding-up and Hua Chiao had an interest in 2,001,721 shares of the Company.

All the interests stated above represented long positions. Save as disclosed above, as at 31 December 2003, no other interests or short positions were recorded in the register maintained by the Company under section 336 of the SFO.

Pursuant to a placing agreement dated 15 December 2003, BOC (BVI) sold 1,070,000,000 shares of the Company (approximately 10.12% of the Company's issued share capital) to independent investors at a price of HK\$13.70 per share. Upon completion of the placing, BOC's shareholding in the Company was reduced to 66.25% and the Company's public shareholding was increased to 33.75%. The placing was completed on 18 December 2003.

Management Contracts

No contracts concerning the management or administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

Major Customers

During the year, the five largest customers of the Group accounted for less than 30% of the total of interest income and other operating income of the Group.

Connected Transactions

The Independent Non-executive Directors have reviewed the transactions for which the Stock Exchange has granted a waiver and confirmed that these transactions were:

- (i) entered into in the ordinary and usual course of business of the Group;
- (ii) conducted either on normal commercial terms or, if there were not sufficient comparable transactions to judge whether they were on normal commercial terms, were on terms that were fair and reasonable so far as the Company's shareholders are concerned;
- (iii) entered into either in accordance with the terms of the agreements governing such transactions or (where there were no such agreements) on terms no less favourable than those available to or from independent third parties, as applicable; and
- (iv) in each case where an annual cap had been agreed with the Stock Exchange, such caps were not exceeded.

Audit Committee and Compliance Committee

The Audit Committee consists of five Non-executive Directors, four of whom, including the chairman, are Independent Non-executive Directors. The members of the Audit Committee are: Mr. Shan Weijian (Chairman), Dr. Fung Victor Kwok King, Mr. Tung Chee Chen, Ambassador Yang Linda Tsao and Mr. Zhou Zaiqun. In addition to assisting the Board in fulfilling its oversight responsibilities, the functions of the Audit Committee also include reviewing significant accounting policies and supervising the Company's financial reporting process; monitoring the performance of both the internal and external auditors; reviewing and examining the effectiveness of the Company's financial reporting procedures and internal controls; ensuring compliance with applicable statutory accounting and reporting requirements, legal and regulatory requirements, and internal rules and procedures approved by the Board. The Head of the Audit Department reports directly to the Board and to the Audit Committee.

The Audit Committee has set up the Compliance Committee, which consists of six members, all of whom are experienced professionals in the legal or accounting fields. The members of

the Committee are: Ms. Wang Qi (Chairman), Mr. Yeung Jason Chi Wai (Vice Chairman), Ms. Liu Yanfen, Mr. Chen Xiaoxin, Mr. Chiu Ming Wah and Mr. Wang Andrew Wei Hung. The Compliance Committee is responsible for monitoring the Company's legal and compliance matters and reporting to the Audit Committee in this respect.

Budgetary Discipline and Reporting

The annual budget of the Group is reviewed and approved by the Board of Directors prior to its implementation by the Management. Financial and business targets are allocated to departments and subsidiaries. There are defined procedures for the appraisal, review and approval of major capital and recurrent expenditures. Proposed significant expenditures outside the approved budget will be referred to the Board or the relevant Board committee for decision. Results of operations against budget will be reported quarterly to the Board and the Audit Committee. If there are significant changes in relation to the operations, a revised budget will be submitted to the Board for review in a timely manner.

Compliance with the Guideline on “Financial Disclosure by Locally Incorporated Authorized Institutions”

The accounts for the year ended 31 December 2003 fully comply with the requirements set out in the guideline on “Financial Disclosure by Locally Incorporated Authorized Institutions” under the Supervisory Policy Manual issued by the HKMA.

Compliance with the Code of Best Practice of the Listing Rules

The directors confirm that the Company has complied with the Code of Best Practice as set out in Appendix 14 of the Listing Rules throughout the year.

Auditors

The accounts have been audited by PricewaterhouseCoopers. A resolution for their re-appointment as auditors for the ensuing year will be proposed at the forthcoming Annual General Meeting.

On behalf of the Board



XIAO Gang
Chairman
Hong Kong, 22 March 2004



WELL- PREPARED

Seismograph 候風地動儀

Originating in China, the first instrument in the world to accurately detect and predict earthquakes