*The following is the text of a report, prepared for the purpose of incorporation in this prospectus, received from our reporting accountants, PricewaterhouseCoopers, Certified Public Accountants, Hong Kong:*

PRICEWATERHOUSECOOPERS

羅兵咸永道會計師事務所

**PricewaterhouseCoopers**
22nd Floor
Prince's Building
Central, Hong Kong

13 June 2005

The Board of Directors
Bank of Communications Co., Ltd.

Goldman Sachs (Asia) L.L.C.
The Hongkong and Shanghai Banking Corporation Limited

Dear Sirs,

We set out below our report on the financial information relating to Bank of Communications Co., Ltd. (the "Bank") and its subsidiaries (the "Group") for each of the years ended 31 December 2002, 2003 and 2004 (the "Relevant Periods") for inclusion in the prospectus of the Bank dated 13 June 2005 (the "Prospectus") in connection with the initial listing of the shares of the Bank on the Main Board of the Stock Exchange of Hong Kong Limited.

The Bank was reorganised in the People's Republic of China ("PRC") on 1 April 1987 as a joint stock national commercial bank, with approval from the State Council of the PRC and the People's Bank of China (the "PBOC").

Details of the Bank's direct and indirect interests in its subsidiaries at the date of this report are set out in Note 36 of section VI below. All companies comprising the Group have adopted 31 December as their financial year end date, except for Amiwell Co., Ltd., City Wisdom Limited, Eastern Sky Limited, Right Master Investment Limited and Unique Profit Limited which have adopted 31 March as their financial year end date. The financial statements of the Bank for the years ended 31 December 2002 and 2003 prepared in accordance with Accounting Standards for Business Enterprises and Accounting System for Financial Institutions (1993 version) and for the year ended 31 December 2004 prepared in accordance with Accounting System for Financial Institutions (2001 version) in the People's Republic of China ("PRC GAAP Accounts") were audited by Pan China CPA Ltd. 天健會計師事務所. The Directors of the Bank have also prepared the financial statements of the Bank under International Financial Reporting Standards ("IFRS") for the year ended 31 December 2002, and the financial statements of the Group under IFRS for the years ended 31 December 2003 and 2004 (collectively the "IFRS Statements") based on PRC GAAP Accounts, the audited financial statements and unaudited management accounts of the Bank's subsidiaries, after making certain adjustments as appropriate to comply with IFRS. IFRS Statements for the years ended 31 December 2002 and 2003 were audited by PricewaterhouseCoopers Zhong Tian CPA Company Limited 普華永道中天會計師事務所有限公司. The financial statements of the subsidiaries of the Bank for the year ended 31 December 2002 were audited by independent auditors as set out in Note 36. We have carried out an independent audit on IFRS Statements for the year ended 31 December 2004. The Directors of the Bank and the Directors of the respective companies comprising the Group, at the Relevant Periods, are responsible for preparing the financial statements which give a true and fair view. In preparing these financial statements, it is fundamental that appropriate accounting policies are selected and applied consistently.

The financial information as set out in sections I to VII below ("Financial Information") has been prepared based on IFRS Statements, after making certain reclassification adjustments to conform to the current presentation. We have examined IFRS Statements and have carried out such additional procedures as are necessary in accordance with the Auditing Guideline "Prospectuses and the Reporting Accountants" issued by the Hong Kong Institute of Certified Public Accountants.

The Directors of the Bank are responsible for the Financial Information. It is our responsibility to form an independent opinion, based on our examination, on the Financial Information and to report our opinion.

In our opinion, the Financial Information, for the purpose of this report, gives a true and fair view of the state of affairs of the Group and the Bank as at 31 December 2002, 2003 and 2004, and of the Group's results and cash flows for each of the three years ended 31 December 2002, 2003 and 2004.

**BANK OF COMMUNICATIONS CO., LTD.**

**SECTION I: CONSOLIDATED PROFIT AND LOSS ACCOUNTS**
(All amounts expressed in millions of RMB unless otherwise stated.)

| | Note | For the year ended 31 December 2002 | 2003 | 2004 |
|---|---|---|---|---|
| Interest income | | 25,878 | 29,979 | 38,352 |
| Interest expense | | (9,270) | (10,305) | (13,160) |
| **Net interest income** | 4 | 16,608 | 19,674 | 25,192 |
| Fee and commission income | | 1,067 | 1,418 | 1,996 |
| Fee and commission expense | | (254) | (261) | (321) |
| **Net fee and commission income** | | 813 | 1,157 | 1,675 |
| Dividend income | 5 | 93 | 82 | 55 |
| Gains less losses arising from trading activities | 6 | 364 | 502 | 325 |
| Gains less losses arising from investment securities | 19 | 8 | (2) | 77 |
| Other operating income | 7 | 286 | 527 | 633 |
| Impairment losses on loans and advances | 8 | (947) | (5,115) | (3,215) |
| Other operating expenses | 9 | (10,735) | (12,690) | (16,992) |
| **Operating profit before tax** | | 6,490 | 4,135 | 7,750 |
| Income tax | 12 | (2,061) | 241 | (6,146) |
| **Net profit for the year** | | 4,429 | 4,376 | 1,604 |
| **Basic and diluted earnings per share (in RMB)** | 13 | 0.26 | 0.26 | 0.06 |

**BANK OF COMMUNICATIONS CO., LTD.**

**SECTION II: CONSOLIDATED BALANCE SHEETS**
(All amounts expressed in millions of RMB unless otherwise stated.)

*Group*

| | Note | As at 31 December 2002 | 2003 | 2004 |
|---|---|---|---|---|
| **ASSETS** | | | | |
| Cash and balances with central banks | 14 | 83,310 | 113,072 | 128,501 |
| Due from other banks and financial institutions | 15 | 97,293 | 99,935 | 88,923 |
| Trading assets | 16 | 141 | 3,106 | 1,533 |
| Loans and advances to customers | 18 | 395,153 | 516,675 | 631,612 |
| Investment securities – originated loans | 19 | 94,057 | 104,670 | 159,826 |
| Investment securities – available-for-sale | 19 | 14,639 | 36,687 | 90,028 |
| Investment securities – held-to-maturity | 19 | 7,942 | 6,721 | — |
| Property and equipment | 20 | 14,672 | 19,981 | 23,863 |
| Deferred tax assets | 26 | 11,304 | 11,712 | 5,025 |
| Other assets | 21 | 13,492 | 13,361 | 16,144 |
| **Total assets** | | 732,003 | 925,920 | 1,145,455 |
| **LIABILITIES** | | | | |
| Due to other banks and financial institutions | 22 | 24,682 | 21,150 | 31,711 |
| Trading liabilities | 23 | 180 | 3,463 | 5,086 |
| Due to customers | 24 | 689,153 | 874,159 | 1,029,941 |
| Other liabilities | 25 | 8,144 | 8,584 | 12,457 |
| Current taxes | | 410 | 421 | 39 |
| Deferred tax liabilities | 26 | — | 62 | 393 |
| Subordinated term debt | 28 | — | — | 12,275 |
| **Total liabilities** | | 722,569 | 907,839 | 1,091,902 |
| **SHAREHOLDERS' EQUITY** | | | | |
| Share capital | 29 | 17,033 | 17,108 | 39,070 |
| Capital surplus | 29 | 6,579 | 11,035 | 10,872 |
| Other reserves | 30 | 10,753 | 10,973 | — |
| Revaluation reserves | | 347 | 723 | 3,757 |
| Accumulated losses | 30 | (25,278) | (21,758) | (146) |
| **Total shareholders' equity** | | 9,434 | 18,081 | 53,553 |
| **Total equity and liabilities** | | 732,003 | 925,920 | 1,145,455 |

**BANK OF COMMUNICATIONS CO., LTD.**

**SECTION III: BALANCE SHEETS**
(All amounts expressed in millions of RMB unless otherwise stated.)

***Bank***

| | Note | As at 31 December 2002 | 2003 | 2004 |
|---|---|---|---|---|
| **ASSETS** | | | | |
| Cash and balances with central banks | 14 | 83,310 | 112,653 | 128,376 |
| Due from other banks and financial institutions | 15 | 97,293 | 99,935 | 88,923 |
| Trading assets | 16 | 141 | 3,106 | 1,533 |
| Loans and advances to customers | 18 | 395,153 | 516,675 | 631,612 |
| Investment securities – originated loans | 19 | 94,057 | 104,670 | 159,826 |
| Investment securities – available-for-sale | 19 | 14,193 | 36,363 | 89,937 |
| Investment securities – held-to-maturity | 19 | 7,942 | 6,721 | — |
| Investments in and due from subsidiaries | 36 | 2,398 | 2,202 | 1,276 |
| Property and equipment | 20 | 12,795 | 17,940 | 22,322 |
| Deferred tax assets | 26 | 11,304 | 11,712 | 5,025 |
| Other assets | 21 | 13,182 | 13,197 | 15,315 |
| **Total assets** | | 731,768 | 925,174 | 1,144,145 |
| **LIABILITIES** | | | | |
| Due to other banks and financial institutions | 22 | 24,682 | 21,150 | 31,711 |
| Trading liabilities | 23 | 180 | 3,463 | 5,086 |
| Due to customers | 24 | 689,153 | 874,159 | 1,029,941 |
| Other liabilities | 25 | 7,909 | 8,046 | 10,525 |
| Current taxes | | 410 | 421 | 39 |
| Deferred tax liabilities | 26 | — | 62 | 286 |
| Subordinated term debt | 28 | — | — | 12,275 |
| **Total liabilities** | | 722,334 | 907,301 | 1,089,863 |
| **SHAREHOLDERS' EQUITY** | | | | |
| Share capital | 29 | 17,033 | 17,108 | 39,070 |
| Capital surplus | 29 | 6,579 | 11,035 | 11,764 |
| Other reserves | 30 | 10,753 | 10,973 | — |
| Revaluation reserves | | 347 | 723 | 3,448 |
| Accumulated losses | 30 | (25,278) | (21,966) | — |
| **Total shareholders' equity** | | 9,434 | 17,873 | 54,282 |
| **Total equity and liabilities** | | 731,768 | 925,174 | 1,144,145 |

**BANK OF COMMUNICATIONS CO., LTD.**

## SECTION IV: CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(All amounts expressed in millions of RMB unless otherwise stated.)

| | Share capital Note 29 | Capital surplus Note 29 | Statutory reserve Note 30 | Discretionary reserve Note 30 | Statutory welfare reserve Note 30 | Revaluation reserve for AFS securities | Revaluation reserve for properties | Accumulated losses Note 30 | Total |
|---|---|---|---|---|---|---|---|---|---|
| **Balance at 1 January 2002** | 15,910 | 5,455 | 4,476 | 4,833 | 850 | 109 | — | (26,102) | 5,531 |
| Donation received | — | 1 | — | — | — | — | — | — | 1 |
| Gains from changes in fair value of AFS securities, net of tax | — | — | — | — | — | 238 | — | — | 238 |
| Net profit | — | — | — | — | — | — | — | 4,429 | 4,429 |
| Dividends | — | — | — | — | — | — | — | (3,011) | (3,011) |
| Transfer to reserves | — | — | 122 | 350 | 122 | — | — | (594) | — |
| Issue of share capital | 120 | 120 | — | — | — | — | — | — | 240 |
| Capitalization of dividends payable | 1,003 | 1,003 | — | — | — | — | — | — | 2,006 |
| **Balance at 31 December 2002/1 January 2003** | 17,033 | 6,579 | 4,598 | 5,183 | 972 | 347 | — | (25,278) | 9,434 |
| Losses from changes in fair value of AFS securities, net of tax | — | — | — | — | — | (105) | — | — | (105) |
| Net profit | — | — | — | — | — | — | — | 4,376 | 4,376 |
| Dividends | — | — | — | — | — | — | — | (636) | (636) |
| Transfer to reserves | — | — | — | 220 | — | — | — | (220) | — |
| Revaluation of property and equipment | — | — | — | — | — | — | 4,862 | — | 4,862 |
| Capitalization of revaluation surplus | — | 4,381 | — | — | — | — | (4,381) | — | — |
| Capitalization of dividends payable | 75 | 75 | — | — | — | — | — | — | 150 |
| **Balance at 31 December 2003/1 January 2004** | 17,108 | 11,035 | 4,598 | 5,403 | 972 | 242 | 481 | (21,758) | 18,081 |
| Restructuring transactions with government (Note 1) | 13,556 | 1,681 | — | — | — | — | — | — | 15,237 |
| Reserves offset against accumulated losses | — | (9,035) | (4,598) | (5,403) | (972) | — | — | 20,008 | — |
| Restructuring transactions with third parties (Note 1) | 8,406 | 7,191 | — | — | — | — | — | — | 15,597 |
| Losses from changes in fair value of AFS securities, net of tax | — | — | — | — | — | (64) | — | — | (64) |
| Revaluation of property and equipment | — | — | — | — | — | — | 3,098 | — | 3,098 |
| Net profit | — | — | — | — | — | — | — | 1,604 | 1,604 |
| **Balance at 31 December 2004** | 39,070 | 10,872 | — | — | — | 178 | 3,579 | (146) | 53,553 |

**BANK OF COMMUNICATIONS CO., LTD.**

**SECTION V: CONSOLIDATED STATEMENTS OF CASH FLOWS**
(All amounts expressed in millions of RMB unless otherwise stated.)

| | For the year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Cash flows from operating activities:** | | | |
| Net profit before taxation: | 6,490 | 4,135 | 7,750 |
| Adjustments for: | | | |
| Impairment of loans and advances to customers | 815 | 4,788 | 3,041 |
| Impairment of other receivables | 290 | 308 | 394 |
| Impairment of due from banks and financial institutions | 178 | 458 | 324 |
| Write-down of foreclosed assets | 349 | 60 | 730 |
| Depreciation of property and equipment | 1,674 | 1,646 | 2,471 |
| Revaluation deficit of property and equipment | — | 448 | 389 |
| Amortization of prepaid staff subsidies | 92 | 114 | 84 |
| Amortization of prepaid rental expenses | 207 | 188 | 198 |
| Amortization of land use rights | 24 | 21 | 75 |
| Amortization of computer software | 19 | 3 | 77 |
| Net losses/ (gains) on investment securities | (8) | 2 | (77) |
| Gains on disposal of fixed assets | (5) | (40) | (214) |
| Decrease/(Increase) in the fair value of investment property | — | (138) | 32 |
| Interest expense for subordinated loan | — | — | 275 |
| Net (increase) in due from central banks | (7,367) | (15,890) | (11,424) |
| Net (increase)/decrease in due from other banks and financial institutions | (33,674) | 7,147 | 5,440 |
| Net (increase)/decrease in trading assets | 586 | (2,965) | 1,573 |
| Net (increase) in loans and advances to customers | (66,650) | (126,310) | (120,058) |
| Net (increase) in other assets | (2,176) | (335) | (3,600) |
| Net (decrease)/increase in due to other banks | (4,991) | (3,532) | 10,561 |
| Net increase/(decrease) in trading liabilities | (567) | 3,283 | 1,623 |
| Net increase in due to customers | 106,250 | 185,006 | 155,782 |
| Net increase in other liabilities | 3,010 | 483 | 3,641 |
| Net increase/(decrease) in business tax payable | (107) | 194 | 242 |
| Income tax paid | (824) | (180) | (603) |
| **Net cash from operating activities** | 3,615 | 58,894 | 58,726 |
| **Cash flows from investing activities:** | | | |
| Purchase of investment securities | (57,363) | (84,594) | (203,919) |
| Disposal or redemption of investment securities | 34,311 | 53,031 | 101,105 |
| Prepaid rental expenses | (194) | (184) | (167) |
| Purchase of land use rights | (15) | (6) | (337) |
| Disposal of land use rights | 47 | — | — |
| Purchase of computer software | (16) | (114) | (114) |
| Purchase of property and equipment | (2,721) | (2,414) | (2,828) |
| Disposal of property and equipment | 238 | 228 | 414 |
| **Net cash used in investing activities** | (25,713) | (34,053) | (105,846) |
| **Cash flows from financing activities:** | | | |
| Issue of shares | 240 | — | 33,597 |
| Issue of subordinated term debt | — | — | 12,000 |
| Dividends paid | (758) | (723) | (8) |
| **Net cash from/(used in) financing activities** | (518) | (723) | 45,589 |
| **Net increase/(decrease) in cash and cash equivalents** | (22,616) | 24,118 | (1,531) |
| **Cash and cash equivalents at the beginning of the year** | 75,786 | 53,170 | 77,288 |
| **Cash and cash equivalents at the end of the year (Note 35)** | 53,170 | 77,288 | 75,757 |
| **Major non-cash transactions** | | | |
| Capitalization of dividends payable | 2,006 | 150 | — |
| Transfer from other assets to fixed assets | 805 | 213 | 261 |
| Transfer from fixed assets to other assets | — | — | 703 |
| **Supplementary Information** | | | |
| Interest received | 26,509 | 30,260 | 37,527 |
| Interest paid | (9,662) | (9,303) | (12,227) |

**BANK OF COMMUNICATIONS CO., LTD.**

**SECTION VI: NOTES TO THE FINANCIAL INFORMATION**
(All amounts expressed in millions of RMB unless otherwise stated.)

## 1 GENERAL

Bank of Communications Co., Ltd. (the "Bank") is a commercial and retail bank providing banking services mainly in the PRC. The Bank was reorganised as a joint stock national commercial bank on 1 April 1987, in accordance with the approval notice (Guo Fa (1986) No. 81) issued by the State Council of the PRC and the approval notice (Yin Fa (1987) No. 40) issued by the PBOC. Headquartered in Shanghai, the Bank operates about 92 branches in the PRC. In addition, the Bank has branches in Hong Kong, New York, Tokyo and Singapore.

### Financial Restructuring and Recapitalization

On June 24 2004, the PBOC, with the approval of the State Council, issued Yin Fu [2004] "Approval on the Packaged Capital Restructuring Program of Bank of Communications Co., Ltd. by the PBOC" (the "Restructuring Package"), approving a series of financial restructuring transactions (each, individually, a "Restructuring Transaction") intended to increase the Bank's capital and resolve certain impaired loans. The aggregate effect achieved through the Restructuring Package was to increase outstanding shares and capital surplus by 21,962 million shares and RMB8,872 million, respectively.

The following Restructuring Transactions were conducted with entities wholly-owned or controlled by the PRC Government (the "Government Restructuring Transactions"). Together, these resulted in increases to outstanding shares and capital surplus of 13,556 million shares and RMB1,681 million, respectively.

- On 25 June 2004, the National Council For Social Security Fund subscribed 5,556 million shares at RMB1.8 per share with a total consideration of RMB10,000 million. The excess over par value of RMB4,444 million was included in capital surplus.
- On 27 June 2004, the Bank transferred impaired loans (the "Transferred Loans") with an aggregate original principal balance of RMB53,020 million to Cinda Asset Management Company on a non-recourse basis in exchange for RMB20,700 million in a bill issued by the PBOC (the "Bills"). The Bills are non-transferable, with a fixed annual rate of 1.89%, and will mature on 29 June 2009 with an early redemption right attached to the issuer. RMB2,763 million of carrying value of the Transferred Loans in excess of the fair value of the Bills of RMB20,017 million, net of tax, was offset against capital surplus (Note 39). The Bills are included in the balance of originated loans as of 31 December 2004.
- On 30 June 2004, under the authority of Cai Jin [2004] No. 58 issued by the Ministry of Finance (the "MOF"), the MOF subscribed 5,000 million shares at par with a total consideration of RMB5,000 million.
- On 30 June 2004, China SAFE Investment Limited subscribed 3,000 million shares at par with a total consideration of RMB3,000 million.

The following Restructuring Transactions were conducted with unrelated third parties (the "Third Party Restructuring Transactions"). Together, these resulted in increases to outstanding shares and capital surplus of 8,406 million shares and RMB7,191 million, respectively.

- On 19 July 2004, a total of 631 million shares were subscribed by various third parties at a price of RMB1.8 per share with a total consideration of RMB1,136 million. The excess over par of RMB505 million was included in capital surplus.

- On 18 August 2004, according to the investment agreement between the Bank and the Hongkong and Shanghai Banking Corporation Limited ("HSBC"), HSBC subscribed 7,775 million shares of the Bank at an issue price of RMB1.86 per share with a total consideration of RMB14,461 million. The excess over par value of RMB6,686 million was included in capital surplus.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of the consolidated financial information are set out below. These policies have been consistently applied to all the periods presented unless otherwise stated.

### *A Basis of presentation*

The consolidated financial information of the Group has been prepared in accordance with IFRS. The consolidated financial information has been prepared under the historical cost convention as modified by the revaluation of investment securities classified as available for sale, financial assets and financial liabilities held for trading, property and equipment, investment properties and all derivative contracts.

The preparation of financial information in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies.

The Group has early adopted the following revised International Accounting Standards ("IAS") which are effective for accounting periods commencing on or after 1 January 2005, when the Group changed its accounting policies on property and equipment, and investment property from an amortised cost basis to a valuation basis on 31 December 2003.

IAS 8 (revised 2003) Accounting Policies, Changes in Accounting Estimates and Errors
IAS 16 (revised 2003) Property, Plant and Equipment
IAS 17 (revised 2003) Leases
IAS 40 (revised 2003) Investment Property

The early adoption is mainly related to the accounting for land use rights attached to buildings for both own use and investment purposes. Land in the PRC is state-owned and will not be transferred to any entities. Upon the payment of a premium, an entity is allowed to have the rights to use the land for a specific period of time. Land use rights so derived by the entity should be accounted for as operating leases under IFRS. Whilst the previous version of IAS 17 prescribes the lease accounting for land use rights, it does not provide guidance on how to derive the lease amount when the rights are acquired together with a building erected thereon through a finance lease or an outright purchase. IAS 17 (revised 2003) however provides explicit guidance on the allocation of lease payments between land use rights and buildings erected thereon. It provides that if the lease payments cannot be allocated reliably between these two elements, the entire lease is classified as a finance lease, unless it is clear that both elements are operating leases, in which case the entire lease is classified as an operating lease. This guidance is considered extremely relevant to the Group when the property market in the PRC does not really distinguish a payment for the land use rights and a payment for the buildings erected thereon.

The Group believes that the change in accounting policy enables the Group to reflect its financial position more accurately in the financial statements. The change in accounting policy is allowed under both old and revised IAS. Compared to the previous version of IAS 16 and IAS 40, the two revised IAS were considered more advanced. IAS 16 (revised 2003) sets a new basis for the valuation model by prescribing that an entity may carry all items of property and equipment at revaluation when the fair value can be measured reliably. Under the previous version of IAS 16, use of revalued amounts did not depend on whether fair values were reliably measured. IAS 40 (revised 2003) does not change the fundamental approach to the accounting for investment properties contained in the previous version of IAS 40 but it does expand the scope of the standard by permitting a property interest held by a lessee under an operating lease to qualify as investment properties under specified conditions.

In light of the foregoing, the Group decided to early adopt IAS 16, 17 and 40 (all revised 2003) which are extremely relevant to the Group's circumstances. Also, when changing the accounting policy on measuring its property and equipment and investment properties at 31 December 2003, the Group chose to early adopt IAS 8 (revised 2003) as it has also been revised.

The financial information of the Group for the previous years has been adjusted when required in accordance with the transition provisions in the respective standards, unless the effects on the financial information is considered immaterial.

Except for above early adopted IAS, the IAS board has also issued the following IFRS which are effective for accounting periods commencing on or after 1 January 2005:

IAS 1 (revised 2003) Presentation of Financial Statements
IAS 10 (revised 2003) Events after the Balance Sheet Date
IAS 21 (revised 2003) The Effects of Changes in Foreign Exchange Rates
IAS 24 (revised 2003) Related Party Disclosures
IAS 27 (revised 2003) Consolidated and Separate Financial Statements
IAS 28 (revised 2003) Investments in Associates
IAS 32 (revised 2003) Financial Instruments: Disclosure and Presentation
IAS 33 (revised 2003) Earnings per Share
IAS 39 (revised 2003) Financial Instruments: Recognition and Measurement
IFRS 2 (issued 2004) Share-based Payment
IFRS 4 (issued 2004) Insurance Contract
IFRS 5 (issued 2004) Non-current Assets Held for Sale and Discontinued Operations

The Group has not early adopted these new IAS or IFRS in the consolidated financial statements. However, the Group has assessed the impact of those IAS and IFRS effective 1 January 2005 other than those already early adopted, and concluded that the most significant impact to the Group would be the reclassification of most of the originated loans to available-for-sale securities in accordance with IAS 39 (revised 2003) and its financial impact. Certain originated loans that are not quoted in an active market would be reclassified as "investment securities – loans and receivables", which are measured at amortised cost using the effective interest method. The remaining originated loans would be re-classified as trading securities, which are measured at fair value on quoted bid prices. The impact of the reclassifications and their impact on the opening financial position of the Group at 1 January 2005 are set out below:

| | **RMB million** |
|---|---|
| Increase in available-for-sale securities | 125,495 |
| Decrease in originated loans | 159,826 |
| Decrease in revaluation reserve, net of tax | 1,450 |
| Increase in deferred tax assets | 714 |
| Increase in investment securities – loans and receivables | 31,205 |
| Increase in trading securities | 962 |

Except for the impact of IAS 39 (revised 2003), the Group considers that there would be no significant impact on opening shareholders' equity at 1 January 2005 from the adoption of other revised IAS or new IFRS. Also, the Group considers that other revised IAS or new IFRS would not result in substantial changes to the Group's accounting policies. In summary:

– IAS 1 (revised 2003) would affect only the presentation of minority interest and other disclosures.

– IAS 10, 21, 27, 28, 32, 33 (all revised 2003), and IFRS 2, 4 and 5 (all issued 2004) would have no material effect on the Group's policies.

– IAS 24 (revised 2003) only affects disclosures. It would have no financial impact and would not result in a change in Group's accounting policy. The revised IAS 24 requires the disclosure of the compensation of key management personnel. Also, it requires the Group to disclose related party transactions with other state-controlled entities because those profit-oriented state-controlled entities are no longer exempted from disclosing transactions with other state-controlled entities.

IFRS 2 (issued 2004) requires an entity to recognise share-based payment transactions in its financial statements, including transactions with employees or other parties to be settled in cash, other assets, or equity instruments of the entity. However, the Group's Board of Directors has indicated that the Group will not effect any kind of share-based payment in the year of 2005. Therefore, IFRS 2 is not relevant to the Group for the year ending 31 December 2005.

*B Subsidiary undertakings*

Subsidiaries, which are those companies and other entities (including Special Purpose Entities) in which the Group, directly or indirectly, has control, are consolidated.

The Group controls another entity when the Group has the power to govern the financial and operating policies of the entity. The existence and effect of potential voting rights that are presently exercisable or presently convertible are also considered when assessing whether the Group controls the entity.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. The purchase method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured at the fair value of the assets given up, shares issued or liabilities undertaken at the date of acquisition, plus costs directly attributable to the acquisition. The excess of the cost of acquisition over the fair value of the net assets of the subsidiary acquired is recorded as goodwill. Inter-company transactions, balances and unrealized gains on transactions between group companies are eliminated; unrealized losses are also eliminated unless the loss cannot be recovered. Where necessary, accounting policies of subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

In the stand alone financial statements of the Bank, the subsidiaries are measured at cost less provision for impairment, as the fair value of these subsidiaries cannot be reliably measured. The amount of impairment loss is included in the net profit or loss for the year.

*C Derivative financial instruments*

Derivative financial instruments including foreign exchange contracts, currency and interest rate swaps, and other derivative financial instruments are initially recognised in the balance sheet at cost and subsequently re-measured at their fair value. Fair values are obtained from quoted market prices, discounted cash flow models and options pricing models as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Certain derivatives embedded in other financial instruments are treated as separate derivatives when their risks and economic characteristics are not closely related to those of the host contract and the host contract is not carried at fair value with unrealized gains and losses reported in income.

Changes in the fair value of derivatives held for trading are included in gains less losses arising from trading activities.

Certain derivative transactions, while considered as hedges under the Group's risk management policies, do not qualify for hedge accounting under the specific rules in IAS 39 and are therefore treated as derivatives held for trading with fair value gains and losses reported as gains less losses arising from trading activities.

The fair values of derivative instruments held for trading are disclosed in Note 17.

*D Interest income and expense*

Interest income and expense are recognised in the profit and loss account for interest-bearing instruments on an accruals basis using the effective interest method. Interest income includes coupons earned on fixed income investment and trading securities and accrued discount and premium on treasury bills and other discounted instruments. When loans become doubtful of collection, they are written down to their recoverable amounts and interest income is thereafter recognised based on the rate of interest that was used to discount the future cash flows for the purpose of measuring the recoverable amounts.

*E Fee and commission income*

Fees and commission are generally recognised on an accruals basis when the service has been provided. Loan origination fees for loans which are probable of being drawn down, are deferred (together with related direct costs) and recognised as an adjustment to the effective interest on the loan. Fees and commission arising from negotiating, or participating in the negotiation of a transaction for a third party, such as the acquisition of loans, shares or other securities or the purchase or sale of businesses, are recognised on completion of the underlying transaction. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts. Asset management fees related to assets held in a fiduciary capacity are recognised ratably over the period the service is provided.

*F Trading securities*

Trading securities are securities which were either acquired for generating a profit from short-term fluctuations in price or dealer's margin, or are securities included in a portfolio in which a pattern of short-term profit taking exists. Trading securities are initially recognised at cost (which includes transaction costs) and subsequently re-measured at fair value based on quoted bid prices. All related realized and unrealized gains and losses are included in gains less losses arising from trading activities. Interest earned whilst holding trading securities is reported as interest income. Dividends received are included in dividend income.

All purchases and sales of trading securities that require delivery within the time frame established by regulation or market convention ('regular way' purchases and sales) are recognised at trade date, which is the date that the Group commits to purchase or sell the asset. Otherwise such transactions are treated as derivatives until settlement occurs.

*G Sale/purchase and repurchase/resale agreements*

Securities sold subject to a linked repurchase agreements ('repos') with banks and other financial institutions are retained in the financial statements as trading or investment securities, as the Group still retains controls of the contractual rights over these securities. The counterparty liability is included in amounts due to other banks and financial institutions.

Securities purchased under agreements to resell ('reverse repos') are recorded as due from other banks and financial institutions. The difference between sale and repurchase price (purchase and resale price) is treated as interest expense (income) and accrued over the life of repos (reverse repos) using the effective interest method.

*H Investment securities*

The Group classifies its investment securities into the following three categories: originated loans, held-to-maturity and available-for-sale securities. Investment securities are initially recognised at cost (which includes transaction costs), and subsequently they are measured as follows:

1) Investment securities – originated loans

   Debt securities that are purchased at original issuance without the intent to sell immediately or in the short term are classified as originated loans. After initial recognition, the originated loans are carried at amortised cost using the effective interest method, less any provision for impairment.

2) Investment securities – held-to-maturity

   Investment securities with fixed maturity where management has both the intent and the ability to hold to maturity are classified as held to maturity. After initial recognition, the held-to-maturity securities are carried at amortised cost using the effective interest method, less any provision for impairment.

3) Investment securities – available–for-sale

   Investment securities intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices are classified as available for sale. After initial recognition, the available-for-sale financial assets are subsequently re-measured at fair value. The fair value is determined by the following hierarchy:

- the published quoted price is the best evidence of fair value when the financial instrument is quoted in an active market.
- the price used in recent transactions of similar financial instruments with adjustment when the market conditions have changed.
- valuation techniques, including: cash flow models etc.
- if fair value cannot be measured reliably, equity security investments are recognised at cost less impairment.

   Gains and losses arising from changes in the fair value of available-for-sale securities are recognised as they arise in equity as revaluation reserve. When the securities are disposed of or impaired, the related accumulated fair value adjustments are included in the profit and loss account as gains and losses arising from investment securities.

An investment security is impaired if its carrying amount is greater than its estimated recoverable amount. The amount of the impairment loss for assets carried at amortised cost is calculated as the difference between the asset's carrying amount and the present value of expected future cash flows discounted at the financial instrument's original effective interest rate. By comparison, the recoverable amount of an instrument measured at fair value is the present value of expected future cash flows discounted at the current market rate of interest for a similar financial asset.

Interest earned whilst holding investment securities is reported as interest income. Dividends receivable are included separately in dividend income when a dividend is declared.

All regular way purchases and sales of investment securities are recognised at settlement date, which is the date that an asset is delivered to or by the Group. Any change in the fair value of the asset during the period between the trade date and the settlement date is accounted for in the same way as the Group accounts for the acquired asset. In other words, the change in value is not recognised for assets carried at cost or amortised cost; it is recognised in equity for assets classified as available for sale.

*I Originated loans and allowance for loan impairment*

Loans originated by the Group by providing money directly to the borrower or to a sub-participation agent at drawdown are categorized as loans originated by the Group and are carried at amortised cost. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction.

All loans and advances are recognised when cash is advanced to borrowers. An allowance for loan impairment is established if there is objective evidence that the Group will not be able to collect all amounts due according to the original contractual terms of loans. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, including amounts recoverable from guarantees and collateral, discounted at the original effective interest rate of loans. The loan loss provision also covers losses where there is objective evidence that losses are present in components of the loan portfolio at the balance sheet date though not individually identified. These have been estimated based upon historical patterns of losses in each component, the credit ratings allocated to the borrowers and reflecting the current economic climate in which the borrowers operate.

When a loan is uncollectible, it is written off against the related allowance for impairment; subsequent recoveries are credited to the impairment losses on loans and advances in the profit and loss account. If the amount of the impairment subsequently decreases due to an event occurring after the write-down, the release of the allowance is credited as a reduction of the impairment losses on loans and advances.

*J Property and equipment*

Prior to 31 December 2003, property and equipment were measured at cost, less accumulated depreciation and impairment losses. On 31 December 2003, the Group adopted alternative treatment on measurement subsequent to initial recognition allowed by IAS 16 (2003) to carry all classes of property and equipment except for leasehold improvements at revaluation, being their fair value at the date of the revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Leasehold improvements continue to be stated at cost less accumulated impairment losses and depreciation. The effect of the change of accounting policy is stated in Note 20.

Increases in the carrying amount arising on revaluation of property and equipment are credited to revaluation reserves in shareholders' equity. Decreases that offset previous increases of the same asset are charged against revaluation reserves; all other decreases are charged to the profit and loss account.

Depreciation is calculated on the straight-line method to write off the cost or revalued amount of each asset to their residual values over their estimated useful lives as follows:

| | |
|---|---|
| Buildings . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 25-50 years |
| Leasehold improvements . . . . . . . . . . . . . . . . . . . | 3-10 years |
| Equipment and motor vehicles . . . . . . . . . . . . . . | 3-8 years |

No depreciation is provided against construction in progress.

At each balance sheet date, both internal and external sources of information are considered to assess whether there is any indication that the Group's property and equipment are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment losses are recognised in the profit and loss account except where the asset is carried at valuation and the impairment loss does not exceed the revaluation surplus for that same asset, in which case it is treated as a revaluation decrease.

The gain or loss on disposal of a property or an equipment is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the profit and loss account. Any revaluation reserve balance remaining attributable to the relevant asset is transferred to retained earnings and is shown as a movement in reserves.

Repairs and maintenance are charged to the profit and loss account during the financial period in which they are incurred.

*K Foreclosed assets*

Foreclosed assets are initially recognised at market value on a portfolio basis based on both internal and external sources of information. All related revaluation gains and losses are recognised in the profit and loss account.

*L Land use rights*

Land use rights are recognised initially at 'cost', being the consideration paid for the rights to use and occupy the land. Land use rights are amortised using the straight-line method to write off the cost over their estimated useful lives of 30 to 70 years.

Land use rights are not separately presented from building, when they are acquired together with the building at inception and the costs attributable to the land use rights cannot be reasonably measured and separated from that of the building.

*M Computer software*

Costs associated with maintaining computer software programmes are recognised as an expenses as incurred. However, expenditure that enhances or extends the performance of computer software programmes beyond their original specifications is recognised as a capital improvement and added to the original cost of the software. Computer software development costs recognised as assets are amortised using the straight-line method over their estimated useful lives which are usually between 3 to 5 years.

*N Investment property*

Property held to earn rentals which is not occupied by the Group is classified as investment property.

Investment property comprises land and buildings. Prior to 31 December 2003, investment properties were measured at cost, less accumulated depreciation and impairment losses. On 31 December 2003, the Group changed its accounting policy on investment property from the cost model to the fair value model and early adopted IAS 17 (2003) and IAS 40 (2003). Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. In case this information is not available, the Group uses alternative valuation methods such as discounted cash flow projections or recent prices on less active markets. These valuations are reviewed annually by an independent valuer. Changes in fair values are recorded in the profit and loss account.

As a result of the abovementioned change in accounting policy, investment property was stated at a market value of RMB172 million at 31 December 2003, and the change in fair value of the investment property amounting to RMB138 million was recognized in the profit and loss account for the year. No adjustment to the opening balance of the Group's retained earnings for the year ended 31 December 2003 as the Group considers that the effect of this change in accounting policy on the financial statements is not material.

*O Leases*

The leases entered into by the Group as lessee or lessor are operating leases. The lease payments/receipts made under operating leases are charged to/recognised in the profit and loss account on a straight-line basis over the period of the lease.

*P Cash and cash equivalents*

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than 90 days maturity from the date of acquisition including: cash and balances with central banks (after deduction of mandatory reserve deposits), amounts due from other banks and financial institutions and trading securities used for the purpose of meeting short-term cash commitments.

*Q Provisions*

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

*R Deferred income taxes*

Deferred income tax is provided, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements.

The principal temporary differences arise from depreciation of property and equipment, impairment of loans and advances, receivables and other assets, and revaluation of certain financial assets and liabilities. The rates enacted or substantively enacted at the balance sheet date are used to determine deferred income tax.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences, unused tax losses and unused tax credits can be utilized. Deferred tax liabilities are the amounts of income tax payable in respect of taxable temporary differences, which are measured at the amount expected to be paid to the tax authorities in the future.

Income tax payable on profits, based on the applicable tax law in each jurisdiction is recognised as an expense in the period in which profits arise. The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

Deferred tax related to fair value re-measurement of available-for-sale investments, which are charged or credited directly to equity, is also credited or charged directly to equity and is subsequently recognised in the profit and loss account together with the deferred gain or loss.

*S Borrowings*

Borrowings are recognised initially at 'cost', being their issue proceeds (fair value of consideration received) net of transaction costs incurred. Borrowings are subsequently stated at amortised cost and any difference between net proceeds and the redemption value is recognised in the profit and loss account over the period of the borrowings using the effective interest method.

*T Share capital*

(1) Share issue costs

External costs directly attributable to the issue of new shares, other than on a business combination, are deducted from equity net of any related income taxes.

(2) Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity in the financial period in which they are declared and approved.

*U Acceptances*

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers. Acceptances are accounted for as off-balance-sheet transactions and are disclosed as contingent liabilities and commitments.

*V Staff benefit and retirement benefit obligations*

The Group participates in various defined contribution retirement plans principally organised by municipal and provincial governments. The Group's contributions to these pension plans are charged to the profit and loss account in the financial period to which they relate.

*W Foreign currency translation*

(1) Measurement and reporting currency

The Group's reporting currency is Renminbi ("RMB"), the legal currency of China. Items included in the financial statements of the entity of the Group are measured using the currency that best reflects the economic substance of the underlying events and circumstances relevant to that entity ("the measurement currency"). The consolidated financial statements are presented in Renminbi which is the measurement currency of the parent.

(2) Transactions and balances

Foreign currency transactions are translated into the measurement currency at the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the profit and loss account. Profit and loss accounts and cash flows of foreign entities are translated into the Group's reporting currency at average exchange rates for the financial period and their balance sheets are translated at the exchange rates ruling at the balance sheet date. Exchange differences arising from the translation of net investment in foreign subsidiaries are taken directly to reserves.

Translation differences on debt securities and other monetary financial assets measured at fair value are included in foreign exchange gains and losses. Translation differences on non-monetary items such as equities held for trading are reported as part of the fair value gain or loss. Thus, underlying translation differences on available-for-sale equities are included in the revaluation reserve in equity.

(3) Group Companies

Exchange differences arising from the translation of the net investment in foreign entities and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign entity is sold, such exchange differences are recognised in the profit and loss account as part of the gain or loss on sale.

*X Contingent liabilities and contingencies*

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that an outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the financial statements. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

*Y Financial guarantee contracts*

The Group has the following types of financial guarantee contracts: letters of credit and letters of guarantees issued. These contracts provide for specified payments to be made to reimburse the holder for a loss it incurs when a guaranteed party defaults under the original or modified terms of a debt instrument.

The Group initially recognises all financial guarantee contracts at proceeds received in the balance sheet, which is amortised into profit and loss accounts ratably over the guarantee period. Subsequently, they are carried at the higher of amortised carrying value and any provision related to the Group's guarantee obligation. The changes in carrying value are recorded in the profit and loss account as fee and commission income.

The contractual amounts of financial guarantee contracts are disclosed as off-balance sheet items in Note 32.

*Z Fiduciary activities*

Assets and income arising thereon together with related undertakings to return such assets to customers are excluded from the financial statements where the Group acts in a fiduciary capacity such as nominee, trustee or agent.

The Group grants entrusted loans on behalf of third-party lenders. The Group grants loans to borrowers, as agent, at the direction of the third-party lenders, who fund these loans. The Group has been contracted by these third-party lenders to manage the administration and collection of these loans on their behalf. The third-party lenders determine both the underwriting criteria for and all terms of the entrusted loans including their purposes, amounts, interest rates, and repayment schedule. The Group charges a commission related to its activities in connection with the entrusted loans which is recognised ratably over the period the service is provided. The risk of loss is borne by the third-party lenders.

*AA Segment reporting*

A geographical segment is engaged in providing products or services within a particular economic environment, which are subject to risks and returns that are different from those of segments operating in other economic environments. A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. In accordance with the Group's internal financial reporting format, the Group has determined that geographical segments be presented as the primary reporting format. The geographical segment reporting format is based upon location of assets, as the local branches mainly serve local customers with only a few customers from other regions. Business segments are presented as secondary segment reporting format, which is divided into corporate, retail, treasury and others.

*AB De-recognition of financial assets and liabilities*

Financial assets are derecognised only when the control of the contractual rights that comprise the financial assets is lost due to the realization of the rights to benefits specified in the contract, or the rights expired and surrendered, and where the Group has transferred substantially all risks and rewards of ownership.

Financial liabilities are derecognised only when the obligation specified in the contract is discharged, cancelled, or expires.

*AC Offset financial assets and liabilities*

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legal enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the assets and settle the liability simultaneously.

## 3 USE OF FINANCIAL INSTRUMENTS

*A Strategy in using financial instruments*

By its nature, the Group is engaged in the extensive use of financial instruments including derivatives. The Group accepts deposits from customers at both fixed and floating rates and for various periods and seeks to earn above average interest margins by investing these funds in high quality assets. The Group seeks to increase these margins by consolidating short-term funds and lending for longer periods at higher rates whilst maintaining sufficient liquidity to meet all claims that might fall due. The Group predominantly operates its business in mainland China under interest rate scheme regulated by the PBOC.

The Group also seeks to raise its interest margins by obtaining above average margins, net of provisions, through lending to commercial and retail borrowers with a range of credit standing. Such exposures involve not just on-balance-sheet loans and advances but also guarantees and other commitments such as letters of credit and performance, and other bonds.

*B Credit risk*

The Group takes on exposure to credit risk which is the risk that a counterparty will be unable to pay amounts in full when due. Credit risk is increased when counterparties are concentrated in the same industries or geographical regions. The majority of the Group's operation is located within China; however different areas in China have their own unique characteristics in economic development. Therefore, each area in China could present different credit risks.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower. Such risks are monitored on a regular basis and subject to an annual review.

Exposure to credit risk is managed through regular analysis of the ability of borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

The Group also maintains strict control limits on net open derivative positions, i.e. the difference between purchase and sale contracts, by both amount and term.

The Group further restricts its exposure to credit losses by entering into master netting arrangements for its interest rate swap transactions with counterparties with which it undertakes a significant volume of transactions. Master netting arrangements do not generally result in an offset of balance sheet assets and liabilities as transactions are usually settled on a gross basis. However, the credit risk associated with favorable contracts is reduced by a master netting arrangement to the extent that if an event of default occurs, all amounts with the counterparty are terminated and settled on a net basis. The Group's overall exposure to credit risk on derivative instruments subject to master netting arrangements can change substantially within a short period since it is affected by each transaction subject to the arrangement.

The Group has issued credit related commitments including guarantees and letters of credit. The primary purpose of these instruments is to ensure that funds are available to customers as required. These instruments represent irrevocable assurances that the Group will make payments in the events that a customer cannot meet its obligations to third parties. These instruments carry the same credit risk as loans.

Geographical concentrations of assets, liabilities and off balance sheet items

***Group***

| | Total assets | Total liabilities | Off balance sheet and credit commitments |
|---|---|---|---|
| **As at 31 December 2002** | | | |
| Mainland China | 665,857 | 657,529 | 68,509 |
| Hong Kong | 54,505 | 53,214 | 13,449 |
| Others | 11,641 | 11,826 | 1,910 |
| Total | 732,003 | 722,569 | 83,868 |
| **As at 31 December 2003** | | | |
| Mainland China | 825,269 | 808,905 | 110,365 |
| Hong Kong | 88,903 | 87,022 | 8,614 |
| Others | 11,748 | 11,912 | 2,580 |
| Total | 925,920 | 907,839 | 121,559 |
| **As at 31 December 2004** | | | |
| Mainland China | 1,039,494 | 988,055 | 152,330 |
| Hong Kong | 92,180 | 89,900 | 12,532 |
| Others | 13,781 | 13,947 | 2,773 |
| Total | 1,145,455 | 1,091,902 | 167,635 |

*Bank*

| | Total assets | Total liabilities | Off balance sheet and credit commitments |
|---|---|---|---|
| **As at 31 December 2002** | | | |
| Mainland China | 665,856 | 657,528 | 68,509 |
| Hong Kong | 54,271 | 52,980 | 13,449 |
| Others | 11,641 | 11,826 | 1,910 |
| Total | 731,768 | 722,334 | 83,868 |
| **As at 31 December 2003** | | | |
| Mainland China | 825,269 | 808,906 | 110,365 |
| Hong Kong | 88,157 | 86,483 | 8,614 |
| Others | 11,748 | 11,912 | 2,580 |
| Total | 925,174 | 907,301 | 121,559 |
| **As at 31 December 2004** | | | |
| Mainland China | 1,038,995 | 986,572 | 152,330 |
| Hong Kong | 91,369 | 89,344 | 12,532 |
| Others | 13,781 | 13,947 | 2,773 |
| Total | 1,144,145 | 1,089,863 | 167,635 |

Total assets, total liabilities and off balance sheet and credit commitments are based on the country/region in which the branch or the group entity is located.

Geographic sector risk concentration for loans and advances to customers (gross):

*Group and Bank*

| | 31 December 2002 | | 31 December 2003 | | 31 December 2004 | |
|---|---|---|---|---|---|---|
| | | % | | % | | % |
| Domestic regions | | | | | | |
| – Jiangsu | 51,176 | 12 | 66,027 | 12 | 80,331 | 13 |
| – Shanghai | 45,828 | 11 | 63,511 | 12 | 68,611 | 11 |
| – Beijing | 30,325 | 7 | 46,362 | 8 | 71,565 | 11 |
| – Guangdong | 33,704 | 8 | 44,333 | 8 | 53,294 | 8 |
| – Zhejiang | 25,274 | 6 | 36,418 | 7 | 45,964 | 7 |
| – Liaoning | 26,038 | 6 | 31,587 | 6 | 25,153 | 4 |
| – Shandong | 22,759 | 5 | 28,352 | 5 | 36,071 | 6 |
| – Henan | 21,003 | 5 | 25,741 | 5 | 28,579 | 4 |
| – Others | 140,948 | 33 | 174,459 | 31 | 192,764 | 30 |
| Domestic regions total | 397,055 | 93 | 516,790 | 94 | 602,332 | 94 |
| Hong Kong and overseas countries | 28,480 | 7 | 31,969 | 6 | 36,452 | 6 |
| Interest receivables | 1,228 | — | 1,184 | — | 1,274 | — |
| Gross amount of loans and advances before allowance for impairment | 426,763 | 100 | 549,943 | 100 | 640,058 | 100 |

A geographical region is reported where it contributes more than 4% of the relevant disclosure item.

The above tables show the geographic sector risk concentration relating to loans and advances to customers, the most significant type of on-balance-sheet assets. The Group's off-balance-sheet exposures mainly comprise acceptances and credit related commitments.

The economic sector risk concentration analysis for loans and advances to customers (gross):

***Group and Bank***

| | 31 December 2002 | % | 31 December 2003 | % | 31 December 2004 | % |
|---|---|---|---|---|---|---|
| Corporate loans | | | | | | |
| Manufacturing | | | | | | |
| – Steel | 14,261 | 3 | 15,378 | 3 | 19,267 | 3 |
| – Machinery | 18,662 | 4 | 17,412 | 3 | 18,711 | 3 |
| – Electronics | 12,111 | 3 | 21,847 | 4 | 24,001 | 4 |
| – Petroleum and chemical | 17,105 | 4 | 22,240 | 4 | 27,929 | 5 |
| – Textile | 12,441 | 3 | 16,659 | 3 | 18,850 | 3 |
| – Other manufacturing | 47,286 | 11 | 64,099 | 12 | 71,263 | 11 |
| Trading | 57,942 | 14 | 69,947 | 13 | 67,846 | 11 |
| Real estate | 47,368 | 11 | 53,970 | 10 | 63,321 | 10 |
| Transportation | 23,760 | 6 | 32,806 | 6 | 43,436 | 7 |
| Services | 18,777 | 4 | 28,530 | 5 | 33,978 | 5 |
| Post and telecommunications | 13,082 | 3 | 14,470 | 3 | 15,114 | 2 |
| Construction | 12,140 | 3 | 17,124 | 3 | 20,916 | 3 |
| Utilities | 15,975 | 4 | 24,723 | 5 | 36,125 | 6 |
| Educations and scientific research | 12,127 | 3 | 19,825 | 4 | 26,367 | 4 |
| Agriculture | 2,684 | 1 | 4,630 | 1 | 2,082 | — |
| Non-banking financial institutions | 5,892 | 1 | 2,193 | — | 8,063 | 1 |
| Others | 41,299 | 10 | 38,681 | 7 | 11,742 | 2 |
| Corporate loans total | 372,912 | 88 | 464,534 | 86 | 509,011 | 80 |
| Mortgage loans | 26,306 | 6 | 42,596 | 8 | 63,978 | 10 |
| Car loans | 4,120 | 1 | 6,156 | 1 | 5,113 | 1 |
| Short-term working capital loans | 1,325 | — | 2,614 | — | 3,718 | — |
| Medium-term and long-term working capital loans | 3,168 | 1 | 7,263 | 1 | 10,821 | 2 |
| Credit card advances | 36 | — | 43 | — | 107 | — |
| Others | 1,343 | — | 1,515 | — | 2,040 | — |
| Individual loans total | 36,298 | 8 | 60,187 | 10 | 85,777 | 13 |
| Discounted bills | 16,325 | 4 | 24,038 | 4 | 43,996 | 7 |
| Interest receivables | 1,228 | — | 1,184 | — | 1,274 | — |
| Gross amount of loans and advances before allowance for impairment | 426,763 | 100 | 549,943 | 100 | 640,058 | 100 |

The economic sector risk concentration analysis for loans and advances to customers is based on the Group's internal classification system.

Loans and advances to customers analysed by customer type (gross):

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Domestic** | | | |
| Corporate entities | | | |
| State owned entities | 157,691 | 184,455 | 178,533 |
| Collective owned entities | 20,090 | 20,964 | 11,484 |
| Private unlimited companies | 9,954 | 19,740 | 26,429 |
| Private limited companies | 67,054 | 100,326 | 132,148 |
| Joint stock companies | 38,933 | 48,793 | 56,894 |
| Foreign invested enterprises | 45,579 | 56,790 | 66,677 |
| Other domestic entities | 15,981 | 12,967 | 13,252 |
| | 355,282 | 444,035 | 485,417 |
| Individuals | 25,591 | 48,988 | 73,406 |
| | 380,873 | 493,023 | 558,823 |
| **Hong Kong and Overseas** | | | |
| Corporate entities | 17,630 | 20,499 | 23,594 |
| Individuals | 10,707 | 11,199 | 12,371 |
| | 28,337 | 31,698 | 35,965 |
| Discounted bills | 16,325 | 24,038 | 43,996 |
| Interest receivables | 1,228 | 1,184 | 1,274 |
| Gross amount of loans and advances before allowance for impairment | 426,763 | 549,943 | 640,058 |

*C Market risk*

Market risks arise from open positions in interest rate and currency products, which are exposed to general and specific market movements. The Group principally operates in the PRC, in which the interest rate is set by the PBOC, and hence the Group has little exposure to interest rate risk. Further, the exchange rates between RMB and other major foreign currencies are relatively stable. The market risk to the Group is considered low.

*D Currency risk*

The Group conducts the majority of its businesses in RMB, with certain foreign transactions in Hong Kong dollars and US dollars. The exchange rates between RMB and US dollars, RMB and Hong Kong dollars, are set by the PBOC, which had minimum movements during the reporting periods. The Directors set limits on the level of exposure by currency, which are monitored regularly. The tables below summarize the Group's and the Bank's exposure to foreign currency exchange rate risk at the end of each year. The tables show the Group's and the Bank's assets and liabilities at carrying amounts in RMB, categorized by the original currency.

*Group*

| | RMB | US Dollars | HK Dollars | Others | Total |
|---|---|---|---|---|---|
| **As at 31 December 2002** | | | | | |
| **Assets** | | | | | |
| Cash and balances with central banks | 80,215 | 1,762 | 588 | 745 | 83,310 |
| Due from other banks and financial institutions | 49,431 | 31,721 | 5,239 | 10,902 | 97,293 |
| Trading assets | — | 4 | 136 | 1 | 141 |
| Loans and advances to customers | 352,321 | 18,610 | 21,586 | 2,636 | 395,153 |
| Investment securities | | | | | |
| – originated loans | 86,739 | 2,921 | 4,222 | 175 | 94,057 |
| – available-for-sale | 513 | 3,930 | 6,534 | 3,662 | 14,639 |
| – held-to-maturity | 1,096 | 4,839 | — | 2,007 | 7,942 |
| Other assets, including deferred tax assets | 34,113 | 1,607 | 3,538 | 210 | 39,468 |
| **Total assets** | 604,428 | 65,394 | 41,843 | 20,338 | 732,003 |
| **Liabilities** | | | | | |
| Due to other banks and financial institutions | (14,532) | (5,676) | (1,274) | (3,200) | (24,682) |
| Trading liabilities | — | (43) | (136) | (1) | (180) |
| Due to customers | (588,547) | (51,521) | (38,034) | (11,051) | (689,153) |
| Other liabilities, including deferred tax liabilities | (1,162) | (3,779) | (1,609) | (2,004) | (8,554) |
| **Total liabilities** | (604,241) | (61,019) | (41,053) | (16,256) | (722,569) |
| **Net on balance sheet position** | 187 | 4,375 | 790 | 4,082 | 9,434 |
| **Off balance sheet and credit commitments** | 48,012 | 18,922 | 13,608 | 3,326 | 83,868 |

***Bank***

| | RMB | US Dollars | HK Dollars | Others | Total |
|---|---|---|---|---|---|
| **As at 31 December 2002** | | | | | |
| **Assets** | | | | | |
| Cash and balances with central banks | 80,215 | 1,762 | 588 | 745 | 83,310 |
| Due from other banks and financial institutions | 49,431 | 31,721 | 5,239 | 10,902 | 97,293 |
| Trading assets | — | 4 | 136 | 1 | 141 |
| Loans and advances to customers | 352,321 | 18,610 | 21,586 | 2,636 | 395,153 |
| Investment securities | | | | | |
| – originated loans | 86,739 | 2,921 | 4,222 | 175 | 94,057 |
| – available-for-sale | 68 | 3,930 | 6,533 | 3,662 | 14,193 |
| – held-to-maturity | 1,096 | 4,839 | — | 2,007 | 7,942 |
| Investments in and due from subsidiaries | 636 | — | 1,762 | — | 2,398 |
| Other assets, including deferred tax assets | 33,922 | 1,607 | 1,542 | 210 | 37,281 |
| **Total assets** | 604,428 | 65,394 | 41,608 | 20,338 | 731,768 |
| **Liabilities** | | | | | |
| Due to other banks and financial institutions | (14,532) | (5,676) | (1,274) | (3,200) | (24,682) |
| Trading liabilities | — | (43) | (136) | (1) | (180) |
| Due to customers | (588,547) | (51,521) | (38,034) | (11,051) | (689,153) |
| Other liabilities, including deferred tax liabilities | (1,162) | (3,779) | (1,374) | (2,004) | (8,319) |
| **Total liabilities** | (604,241) | (61,019) | (40,818) | (16,256) | (722,334) |
| **Net on balance sheet position** | 187 | 4,375 | 790 | 4,082 | 9,434 |
| **Off balance sheet and credit commitments** | 48,012 | 18,922 | 13,608 | 3,326 | 83,868 |

*Group*

| | RMB | US Dollars | HK Dollars | Others | Total |
|---|---|---|---|---|---|
| **As at 31 December 2003** | | | | | |
| **Assets** | | | | | |
| Cash and balances with central banks | 109,203 | 1,982 | 1,072 | 815 | 113,072 |
| Due from other banks and financial institutions | 41,641 | 23,110 | 27,030 | 8,154 | 99,935 |
| Trading assets | — | 34 | 3,063 | 9 | 3,106 |
| Loans and advances to customers | 454,591 | 33,075 | 22,835 | 6,174 | 516,675 |
| Investment securities | | | | | |
| – originated loans | 100,184 | 948 | 3,251 | 287 | 104,670 |
| – available-for-sale | 18,079 | 9,161 | 5,781 | 3,666 | 36,687 |
| – held-to-maturity | 1,175 | 4,956 | 75 | 515 | 6,721 |
| Other assets, including deferred tax assets | 40,819 | 561 | 3,659 | 15 | 45,054 |
| **Total assets** | 765,692 | 73,827 | 66,766 | 19,635 | 925,920 |
| **Liabilities** | | | | | |
| Due to other banks and financial institutions | (9,255) | (9,363) | (274) | (2,258) | (21,150) |
| Trading liabilities | — | (435) | (3,020) | (8) | (3,463) |
| Due to customers | (743,665) | (56,377) | (61,652) | (12,465) | (874,159) |
| Other liabilities, including deferred tax liabilities | (6,416) | (724) | (1,518) | (409) | (9,067) |
| **Total liabilities** | (759,336) | (66,899) | (66,464) | (15,140) | (907,839) |
| **Net on balance sheet position** | 6,356 | 6,928 | 302 | 4,495 | 18,081 |
| **Off balance sheet and credit commitments** | 83,325 | 27,999 | 6,883 | 3,352 | 121,559 |

*Bank*

| | RMB | US Dollars | HK Dollars | Others | Total |
|---|---|---|---|---|---|
| **As at 31 December 2003** | | | | | |
| **Assets** | | | | | |
| Cash and balances with central banks | 109,203 | 1,982 | 653 | 815 | 112,653 |
| Due from other banks and financial institutions | 41,641 | 23,110 | 27,030 | 8,154 | 99,935 |
| Trading assets | — | 34 | 3,063 | 9 | 3,106 |
| Loans and advances to customers | 454,591 | 33,075 | 22,835 | 6,174 | 516,675 |
| Investment securities | | | | | |
| – originated loans | 100,184 | 948 | 3,251 | 287 | 104,670 |
| – available-for-sale | 17,756 | 9,161 | 5,780 | 3,666 | 36,363 |
| – held-to-maturity | 1,175 | 4,956 | 75 | 515 | 6,721 |
| Investments in and due from subsidiaries | 645 | — | 1,557 | — | 2,202 |
| Other assets, including deferred tax assets | 42,537 | (1,479) | 1,776 | 15 | 42,849 |
| **Total assets** | 767,732 | 71,787 | 66,020 | 19,635 | 925,174 |
| **Liabilities** | | | | | |
| Due to other banks and financial institutions | (9,255) | (9,363) | (274) | (2,258) | (21,150) |
| Trading liabilities | — | (435) | (3,020) | (8) | (3,463) |
| Due to customers | (743,665) | (56,377) | (61,652) | (12,465) | (874,159) |
| Other liabilities, including deferred tax liabilities | (6,416) | (724) | (980) | (409) | (8,529) |
| **Total liabilities** | (759,336) | (66,899) | (65,926) | (15,140) | (907,301) |
| **Net on balance sheet position** | 8,396 | 4,888 | 94 | 4,495 | 17,873 |
| **Off balance sheet and credit commitments** | 83,325 | 27,999 | 6,883 | 3,352 | 121,559 |

*Group*

| | RMB | US Dollars | HK Dollars | Others | Total |
|---|---|---|---|---|---|
| **As at 31 December 2004** | | | | | |
| **Assets** | | | | | |
| Cash and balances with central banks | 125,535 | 1,772 | 637 | 557 | 128,501 |
| Due from other banks and financial institutions | 37,472 | 38,145 | 5,943 | 7,363 | 88,923 |
| Trading assets | — | 168 | 1,351 | 14 | 1,533 |
| Loans and advances to customers | 563,158 | 36,544 | 25,619 | 6,291 | 631,612 |
| Investment securities | | | | | |
| – originated loans | 147,215 | 5,182 | 5,993 | 1,436 | 159,826 |
| – available-for-sale | 60,700 | 18,304 | 4,858 | 6,166 | 90,028 |
| Other assets, including deferred tax assets | 38,814 | 3,464 | 4,568 | (1,814) | 45,032 |
| Total assets | 972,894 | 103,579 | 48,969 | 20,013 | 1,145,455 |
| **Liabilities** | | | | | |
| Due to other banks and financial institutions | (18,437) | (5,623) | (2,471) | (5,180) | (31,711) |
| Trading liabilities | — | (1,944) | (2,999) | (143) | (5,086) |
| Due to customers | (900,469) | (78,131) | (39,970) | (11,371) | (1,029,941) |
| Other liabilities, including deferred tax liabilities | (14,376) | (6,586) | (3,569) | (633) | (25,164) |
| Total liabilities | (933,282) | (92,284) | (49,009) | (17,327) | (1,091,902) |
| Net on balance sheet position | 39,612 | 11,295 | (40) | 2,686 | 53,553 |
| Off balance sheet and credit commitments | 110,034 | 42,077 | 9,376 | 6,148 | 167,635 |

*Bank*

| | RMB | US Dollars | HK Dollars | Others | Total |
|---|---|---|---|---|---|
| **As at 31 December 2004** | | | | | |
| **Assets** | | | | | |
| Cash and balances with central banks | 125,535 | 1,772 | 512 | 557 | 128,376 |
| Due from other banks and financial institutions | 37,472 | 38,145 | 5,943 | 7,363 | 88,923 |
| Trading assets | — | 168 | 1,351 | 14 | 1,533 |
| Loans and advances to customers | 563,158 | 36,544 | 25,619 | 6,291 | 631,612 |
| Investment securities | | | | | |
| – originated loans | 147,215 | 5,182 | 5,993 | 1,436 | 159,826 |
| – available-for-sale | 60,609 | 18,304 | 4,858 | 6,166 | 89,937 |
| Investments in and due from subsidiaries | 219 | — | 1,057 | — | 1,276 |
| Other assets, including deferred tax assets | 38,083 | 3,464 | 2,929 | (1,814) | 42,662 |
| **Total assets** | 972,291 | 103,579 | 48,262 | 20,013 | 1,144,145 |
| **Liabilities** | | | | | |
| Due to other banks and financial institutions | (18,437) | (5,623) | (2,471) | (5,180) | (31,711) |
| Trading liabilities | — | (1,944) | (2,999) | (143) | (5,086) |
| Due to customers | (900,469) | (78,131) | (39,970) | (11,371) | (1,029,941) |
| Other liabilities, including deferred tax liabilities | (13,048) | (6,586) | (2,858) | (633) | (23,125) |
| **Total liabilities** | (931,954) | (92,284) | (48,298) | (17,327) | (1,089,863) |
| **Net on balance sheet position** | 40,337 | 11,295 | (36) | 2,686 | 54,282 |
| **Off balance sheet and credit commitments** | 110,034 | 42,077 | 9,376 | 6,148 | 167,635 |

*E Interest rate risk*

**Interest sensitivity of assets, liabilities and off balance sheet items**

The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. Currently, interest rates for loans and deposits within mainland China are set by the PBOC. The Group operates its business predominantly in mainland China under the interest rate scheme regulated by the PBOC. It is normal practice for the interest rates of both interest-bearing assets and liabilities to move in the same direction. Consequently, the Group has little exposure in terms of interest rate risk. However, there is no guarantee that the PBOC will continue this practice in future.

The Group conducts most of its domestic on-balance-sheet businesses including loans and deposits as well as the majority of off-balance-sheet businesses based upon basic interest rates. The basic interest rates for the loans and the deposits normally move in tandem. Under this regulated environment, the Group is not subject to significant interest rate risk exposure. The interest rate repricing risk for foreign currency denominated debt securities and the remaining part of off-balance-sheet businesses which are not based upon these basic interest rates is not expected to be significant.

According to the PBOC regulations, the ceiling for loan interest rates has been adjusted from 30% to 70% above the stipulated interest rates on 1 January 2004 and finally has been removed from 29 October 2004 onwards, whilst the floor is 10% below the stipulated rates.

Interest rate for discounted bills is determined by reference to the PBOC/market re-discount interest rate. However, it is generally lower than the interest rate for a loan with same term (including the above floating rate).

The tables below summarise the Group's and the Bank's exposure to interest rate risks. The tables show the Group's and the Bank's assets and liabilities at carrying amounts, categorized by the earlier of contractual repricing or maturity dates.

Expected repricing and maturity dates do not differ significantly from the contract dates, except for the maturity of "Due to customers" up to one month represent balances on current accounts considered by the Group as a relatively stable core source of funding of its operations.

*Group*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2002** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 76,384 | — | — | — | — | 6,926 | 83,310 |
| Due from other banks and financial institutions | 14,212 | 68,196 | 12,068 | 108 | — | 2,709 | 97,293 |
| Trading assets | 141 | — | — | — | — | — | 141 |
| Loans and advances to customers | 4,729 | 87,428 | 194,608 | 63,725 | 44,663 | — | 395,153 |
| Investment securities | | | | | | | |
| – originated loans | 1,591 | 1,770 | 32,744 | 43,630 | 14,322 | — | 94,057 |
| – available-for-sale | 4,213 | 1,683 | 3,924 | 4,037 | 782 | — | 14,639 |
| – held-to-maturity | 1,717 | 3,617 | 1,499 | 1,018 | 91 | — | 7,942 |
| Other assets, including deferred tax assets | — | — | — | — | — | 39,468 | 39,468 |
| **Total assets** | 102,987 | 162,694 | 244,843 | 112,518 | 59,858 | 49,103 | 732,003 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (17,407) | (5,835) | (465) | (975) | — | — | (24,682) |
| Trading liabilities | (121) | (8) | (9) | (11) | (31) | — | (180) |
| Due to customers | (402,798) | (79,652) | (126,085) | (61,576) | (89) | (18,953) | (689,153) |
| Other liabilities, including deferred tax liabilities | — | — | — | — | — | (8,554) | (8,554) |
| **Total liabilities** | (420,326) | (85,495) | (126,559) | (62,562) | (120) | (27,507) | (722,569) |
| **Total interest sensitivity gap** | (317,339) | 77,199 | 118,284 | 49,956 | 59,738 | 21,596 | 9,434 |

*Bank*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2002** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 76,384 | — | — | — | — | 6,926 | 83,310 |
| Due from other banks and financial institutions | 14,212 | 68,196 | 12,068 | 108 | — | 2,709 | 97,293 |
| Trading assets | 141 | — | — | — | — | — | 141 |
| Loans and advances to customers | 4,729 | 87,428 | 194,608 | 63,725 | 44,663 | — | 395,153 |
| Investment securities | | | | | | | |
| – originated loans | 1,591 | 1,770 | 32,744 | 43,630 | 14,322 | — | 94,057 |
| – available-for-sale | 4,213 | 1,683 | 3,924 | 3,591 | 782 | — | 14,193 |
| – held-to-maturity | 1,717 | 3,617 | 1,499 | 1,018 | 91 | — | 7,942 |
| Investments in and due from subsidiaries | — | — | — | 446 | — | 1,952 | 2,398 |
| Other assets, including deferred tax assets | — | — | — | — | — | 37,281 | 37,281 |
| **Total assets** | 102,987 | 162,694 | 244,843 | 112,518 | 59,858 | 48,868 | 731,768 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (17,407) | (5,835) | (465) | (975) | — | — | (24,682) |
| Trading liabilities | (121) | (8) | (9) | (11) | (31) | — | (180) |
| Due to customers | (402,798) | (79,652) | (126,085) | (61,576) | (89) | (18,953) | (689,153) |
| Other liabilities, including deferred tax liabilities | — | — | — | — | — | (8,319) | (8,319) |
| **Total liabilities** | (420,326) | (85,495) | (126,559) | (62,562) | (120) | (27,272) | (722,334) |
| **Total interest sensitivity gap** | (317,339) | 77,199 | 118,284 | 49,956 | 59,738 | 21,596 | 9,434 |

*Group*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2003** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 104,698 | — | — | — | — | 8,374 | 113,072 |
| Due from other banks and financial institutions | 58,403 | 25,431 | 5,411 | 750 | 84 | 9,856 | 99,935 |
| Trading assets | 3,106 | — | — | — | — | — | 3,106 |
| Loans and advances to customers | 5,583 | 136,023 | 245,916 | 72,862 | 56,291 | — | 516,675 |
| Investment securities | | | | | | | |
| – originated loans | 514 | 3,635 | 34,298 | 48,151 | 18,072 | — | 104,670 |
| – available-for-sale | 3,066 | 10,210 | 14,594 | 6,736 | 2,081 | — | 36,687 |
| – held-to-maturity | 801 | 3,781 | 789 | 1,046 | 304 | — | 6,721 |
| Other assets, including deferred tax assets | — | — | — | — | — | 45,054 | 45,054 |
| **Total assets** | 176,171 | 179,080 | 301,008 | 129,545 | 76,832 | 63,284 | 925,920 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (13,197) | (6,317) | (466) | (1,170) | — | — | (21,150) |
| Trading liabilities | (1,958) | (1,120) | (301) | (60) | (24) | — | (3,463) |
| Due to customers | (548,084) | (126,995) | (152,873) | (27,064) | (8) | (19,135) | (874,159) |
| Other liabilities, including deferred tax liabilities | — | — | — | — | — | (9,067) | (9,067) |
| **Total liabilities** | (563,239) | (134,432) | (153,640) | (28,294) | (32) | (28,202) | (907,839) |
| **Total interest sensitivity gap** | (387,068) | 44,648 | 147,368 | 101,251 | 76,800 | 35,082 | 18,081 |

*Bank*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2003** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 104,698 | — | — | — | — | 7,955 | 112,653 |
| Due from other banks and financial institutions | 58,403 | 25,431 | 5,411 | 750 | 84 | 9,856 | 99,935 |
| Trading assets | 3,106 | — | — | — | — | — | 3,106 |
| Loans and advances to customers | 5,583 | 136,023 | 245,916 | 72,862 | 56,291 | — | 516,675 |
| Investment securities | | | | | | | |
| – originated loans | 514 | 3,635 | 34,298 | 48,151 | 18,072 | — | 104,670 |
| – available-for-sale | 3,066 | 10,210 | 14,594 | 6,412 | 2,081 | — | 36,363 |
| – held-to-maturity | 801 | 3,781 | 789 | 1,046 | 304 | — | 6,721 |
| Investments in and due from subsidiaries | — | — | — | 324 | — | 1,878 | 2,202 |
| Other assets, including deferred tax assets | — | — | — | — | — | 42,849 | 42,849 |
| **Total assets** | 176,171 | 179,080 | 301,008 | 129,545 | 76,832 | 62,538 | 925,174 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (13,197) | (6,317) | (466) | (1,170) | — | — | (21,150) |
| Trading liabilities | (1,958) | (1,120) | (301) | (60) | (24) | — | (3,463) |
| Due to customers | (548,084) | (126,995) | (152,873) | (27,064) | (8) | (19,135) | (874,159) |
| Other liabilities, including deferred tax liabilities | — | — | — | — | — | (8,529) | (8,529) |
| **Total liabilities** | (563,239) | (134,432) | (153,640) | (28,294) | (32) | (27,664) | (907,301) |
| **Total interest sensitivity gap** | (387,068) | 44,648 | 147,368 | 101,251 | 76,800 | 34,874 | 17,873 |

*Group*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2004** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 119,885 | — | — | — | — | 8,616 | 128,501 |
| Due from other banks and financial institutions | 76,629 | 11,126 | 530 | 300 | — | 338 | 88,923 |
| Trading assets | 973 | 267 | 149 | 128 | 16 | — | 1,533 |
| Loans and advances to customers | 53,203 | 126,571 | 288,067 | 77,151 | 86,620 | — | 631,612 |
| Investment securities | | | | | | | |
| – originated loans | 5,094 | 9,266 | 50,641 | 68,069 | 26,756 | — | 159,826 |
| – available-for-sale | 8,594 | 26,353 | 29,446 | 20,280 | 5,331 | 24 | 90,028 |
| Other assets, including deferred tax assets | — | — | — | — | — | 45,032 | 45,032 |
| **Total assets** | 264,378 | 173,583 | 368,833 | 165,928 | 118,723 | 54,010 | 1,145,455 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (22,978) | (5,161) | (1,602) | — | (1,956) | (14) | (31,711) |
| Trading liabilities | (1,988) | (1,532) | (268) | (1,248) | (50) | — | (5,086) |
| Due to customers | (706,196) | (67,609) | (175,714) | (56,690) | (2,987) | (20,745) | (1,029,941) |
| Other liabilities, including deferred tax liabilities | — | — | (275) | (12,000) | — | (12,889) | (25,164) |
| **Total liabilities** | (731,162) | (74,302) | (177,859) | (69,938) | (4,993) | (33,648) | (1,091,902) |
| **Total interest sensitivity gap** | (466,784) | 99,281 | 190,974 | 95,990 | 113,730 | 20,362 | 53,553 |

*Bank*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Non-interest bearing | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2004** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 119,885 | — | — | — | — | 8,491 | 128,376 |
| Due from other banks and financial institutions | 76,629 | 11,126 | 530 | 300 | — | 338 | 88,923 |
| Trading assets | 973 | 267 | 149 | 128 | 16 | — | 1,533 |
| Loans and advances to customers | 53,203 | 126,571 | 288,067 | 77,151 | 86,620 | — | 631,612 |
| Investment securities | | | | | | | |
| – originated loans | 5,094 | 9,266 | 50,641 | 68,069 | 26,756 | — | 159,826 |
| – available-for-sale | 8,503 | 26,353 | 29,446 | 20,280 | 5,331 | 24 | 89,937 |
| Investments in and due from subsidiaries | — | — | 60 | 225 | — | 991 | 1,276 |
| Other assets, including deferred tax assets | — | — | — | — | — | 42,662 | 42,662 |
| **Total assets** | 264,287 | 173,583 | 368,893 | 166,153 | 118,723 | 52,506 | 1,144,145 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (22,978) | (5,161) | (1,602) | — | (1,956) | (14) | (31,711) |
| Trading liabilities | (1,988) | (1,532) | (268) | (1,248) | (50) | — | (5,086) |
| Due to customers | (706,196) | (67,609) | (175,714) | (56,690) | (2,987) | (20,745) | (1,029,941) |
| Other liabilities, including deferred tax liabilities | — | — | (275) | (12,000) | — | (10,850) | (23,125) |
| **Total liabilities** | (731,162) | (74,302) | (177,859) | (69,938) | (4,993) | (31,609) | (1,089,863) |
| **Total interest sensitivity gap** | (466,875) | 99,281 | 191,034 | 96,215 | 113,730 | 20,897 | 54,282 |

The tables below summarise the effective interest rate by major currencies for monetary financial instruments:

*Group and Bank*

| | RMB | US Dollars | HK Dollars | Others |
|---|---|---|---|---|
| **As at 31 December 2002** | | | | |
| **Assets** | | | | |
| Cash and balances with central banks | 1.87% | 0.03% | 0.19% | — |
| Due from other banks and financial institutions | 2.35% | 1.64% | 1.86% | 2.96% |
| Loans and advances to customers | 5.42% | 3.07% | 3.28% | 2.58% |
| Investment securities | | | | |
| – originated loans | 3.48% | 2.48% | 1.83% | 0.51% |
| – available-for-sale | 2.63% | 3.36% | 3.98% | 3.97% |
| – held-to-maturity | 6.31% | 2.29% | 2.20% | 0.80% |
| **Liabilities** | | | | |
| Due to other banks and financial institutions | 1.86% | 1.41% | 1.72% | 0.22% |
| Due to customers | 1.19% | 0.76% | 0.87% | 0.51% |
| **As at 31 December 2003** | | | | |
| **Assets** | | | | |
| Cash and balances with central banks | 1.83% | 0.03% | 0.12% | — |
| Due from other banks and financial institutions | 2.23% | 1.33% | 1.10% | 3.94% |
| Loans and advances to customers | 5.38% | 2.32% | 2.71% | 2.47% |
| Investment securities | | | | |
| – originated loans | 3.25% | 2.42% | 2.17% | 3.40% |
| – available-for-sale | 2.22% | 2.60% | 1.28% | 3.34% |
| – held-to-maturity | 5.87% | 1.66% | 1.38% | 0.57% |
| **Liabilities** | | | | |
| Due to other banks and financial institutions | 1.92% | 1.06% | 1.05% | 1.33% |
| Due to customers | 1.20% | 0.56% | 0.32% | 0.61% |
| **As at 31 December 2004** | | | | |
| **Assets** | | | | |
| Cash and balances with central banks | 1.82% | 0.06% | 0.00% | — |
| Due from other banks and financial institutions | 2.21% | 2.16% | 0.35% | 2.37% |
| Loans and advances to customers | 5.34% | 2.94% | 2.25% | 2.36% |
| Investment securities | | | | |
| – originated loans | 3.34% | 3.09% | 0.53% | 5.10% |
| – available-for-sale | 2.93% | 3.29% | 2.03% | 2.30% |
| **Liabilities** | | | | |
| Due to other banks and financial institutions | 1.64% | 1.75% | 0.24% | 0.49% |
| Due to customers | 1.36% | 0.92% | 0.36% | 2.58% |

The effective interest rate for the RMB denominated investment securities-held to maturity was relatively high during the Track Record Periods because the majority of these securities were issued before 2000 when the then coupon rate was higher than international bond rates and PBOC rates.

*F Liquidity risk*

The Group is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs, guarantees and from margin and other calls on cash settled derivatives. The Directors set limits on the minimum proportion of maturing funds to be made available to meet such calls and on the minimum level of interbank and other borrowing facilities that should be in place to cover different levels of unexpected withdrawals. In addition, the Group limits its loan to deposit ratio at below 75% as required by the PBOC. 7.5% of the Group's total RMB denominated deposits and 2% of the total foreign currency denominated deposits must be deposited with central banks. The tables below analyze the assets and liabilities of the Group and the Bank into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date.

**Maturities of assets and liabilities**

***Group***

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Overdue | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2002** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 83,310 | — | — | — | — | — | 83,310 |
| Due from other banks and financial institutions | 6,788 | 76,248 | 12,153 | 108 | — | 1,996 | 97,293 |
| Trading assets | 141 | — | — | — | — | — | 141 |
| Loans and advances to customers | 4,729 | 85,084 | 194,186 | 58,778 | 32,462 | 19,914 | 395,153 |
| Investment securities | | | | | | | |
| – originated loans | 627 | 1,938 | 13,455 | 49,053 | 28,984 | — | 94,057 |
| – available-for-sale | 4,120 | 1,754 | 2,666 | 5,230 | 847 | 22 | 14,639 |
| – held-to-maturity | 1,551 | 283 | 1,760 | 4,257 | 91 | — | 7,942 |
| Other assets, including deferred tax assets | 10,848 | 848 | 1,236 | 8,260 | 17,569 | 707 | 39,468 |
| **Total assets** | 112,114 | 166,155 | 225,456 | 125,686 | 79,953 | 22,639 | 732,003 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institution | (17,407) | (5,835) | (465) | (975) | — | — | (24,682) |
| Trading liabilities | (121) | (8) | (9) | (11) | (31) | — | (180) |
| Due to customers | (421,571) | (79,832) | (126,085) | (61,576) | (89) | — | (689,153) |
| Other liabilities, including deferred tax liabilities | (8,026) | (56) | (65) | (14) | (237) | (156) | (8,554) |
| **Total liabilities** | (447,125) | (85,731) | (126,624) | (62,576) | (357) | (156) | (722,569) |
| **Net liquidity gap** | (335,011) | 80,424 | 98,832 | 63,110 | 79,596 | 22,483 | 9,434 |

*Bank*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Overdue | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2002** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 83,310 | — | — | — | — | — | 83,310 |
| Due from other banks and financial institutions | 6,788 | 76,248 | 12,153 | 108 | — | 1,996 | 97,293 |
| Trading assets | 141 | — | — | — | — | — | 141 |
| Loans and advances to customers | 4,729 | 85,084 | 194,186 | 58,778 | 32,462 | 19,914 | 395,153 |
| Investment securities | | | | | | | |
| – originated loans | 627 | 1,938 | 13,455 | 49,053 | 28,984 | — | 94,057 |
| – available-for-sale | 4,120 | 1,754 | 2,666 | 4,784 | 847 | 22 | 14,193 |
| – held-to-maturity | 1,551 | 283 | 1,760 | 4,257 | 91 | — | 7,942 |
| Investments in and due from subsidiaries | — | — | — | 2,376 | 22 | — | 2,398 |
| Other assets, including deferred tax assets | 10,848 | 848 | 1,236 | 6,330 | 17,312 | 707 | 37,281 |
| **Total assets** | 112,114 | 166,155 | 225,456 | 125,686 | 79,718 | 22,639 | 731,768 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (17,407) | (5,835) | (465) | (975) | — | — | (24,682) |
| Trading liabilities | (121) | (8) | (9) | (11) | (31) | — | (180) |
| Due to customers | (421,571) | (79,832) | (126,085) | (61,576) | (89) | — | (689,153) |
| Other liabilities, including deferred tax liabilities | (8,026) | (56) | (65) | (14) | (2) | (156) | (8,319) |
| **Total liabilities** | (447,125) | (85,731) | (126,624) | (62,576) | (122) | (156) | (722,334) |
| **Net liquidity gap** | (335,011) | 80,424 | 98,832 | 63,110 | 79,596 | 22,483 | 9,434 |

*Group*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Overdue | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2003** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 113,072 | — | — | — | — | — | 113,072 |
| Due from other banks and financial institutions | 39,260 | 54,043 | 5,411 | 20 | 84 | 1,117 | 99,935 |
| Trading assets | 3,106 | — | — | — | — | — | 3,106 |
| Loans and advances to customers | 5,583 | 102,158 | 243,478 | 85,312 | 57,934 | 22,210 | 516,675 |
| Investment securities | | | | | | | |
| – originated loans | 2 | 1,919 | 9,457 | 57,824 | 35,468 | — | 104,670 |
| – available-for-sale | 1,071 | 5,743 | 13,956 | 13,718 | 2,168 | 31 | 36,687 |
| – held-to-maturity | 42 | 675 | 1,366 | 4,324 | 314 | — | 6,721 |
| Other assets, including deferred tax assets | 11,989 | 1,049 | 1,491 | 6,669 | 22,656 | 1,200 | 45,054 |
| **Total assets** | 174,125 | 165,587 | 275,159 | 167,867 | 118,624 | 24,558 | 925,920 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (13,197) | (6,317) | (466) | (1,170) | — | — | (21,150) |
| Trading liabilities | (1,958) | — | — | (1,409) | (96) | — | (3,463) |
| Due to customers | (564,964) | (128,931) | (153,192) | (27,064) | (8) | — | (874,159) |
| Other liabilities, including deferred tax liabilities | (8,726) | (153) | (95) | (68) | (25) | — | (9,067) |
| **Total liabilities** | (588,845) | (135,401) | (153,753) | (29,711) | (129) | — | (907,839) |
| **Net liquidity gap** | (414,720) | 30,186 | 121,406 | 138,156 | 118,495 | 24,558 | 18,081 |

*Bank*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Overdue | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2003** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 112,653 | — | — | — | — | — | 112,653 |
| Due from other banks and financial institutions | 39,260 | 54,043 | 5,411 | 20 | 84 | 1,117 | 99,935 |
| Trading assets | 3,106 | — | — | — | — | — | 3,106 |
| Loans and advances to customers | 5,583 | 102,158 | 243,478 | 85,312 | 57,934 | 22,210 | 516,675 |
| Investment securities | | | | | | | |
| – originated loans | 2 | 1,919 | 9,457 | 57,824 | 35,468 | — | 104,670 |
| – available-for-sale | 1,071 | 5,743 | 13,956 | 13,394 | 2,168 | 31 | 36,363 |
| – held-to-maturity | 42 | 675 | 1,366 | 4,324 | 314 | — | 6,721 |
| Investments in and due from subsidiaries | — | — | — | 493 | 1,709 | — | 2,202 |
| Other assets, including deferred tax assets | 10,283 | 1,049 | 1,491 | 6,669 | 22,157 | 1,200 | 42,849 |
| **Total assets** | 172,000 | 165,587 | 275,159 | 168,036 | 119,834 | 24,558 | 925,174 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (13,197) | (6,317) | (466) | (1,170) | — | — | (21,150) |
| Trading liabilities | (1,958) | — | — | (1,409) | (96) | — | (3,463) |
| Due to customers | (564,964) | (128,931) | (153,192) | (27,064) | (8) | — | (874,159) |
| Other liabilities, including deferred tax liabilities | (8,188) | (153) | (95) | (68) | (25) | — | (8,529) |
| **Total liabilities** | (588,307) | (135,401) | (153,753) | (29,711) | (129) | — | (907,301) |
| **Net liquidity gap** | (416,307) | 30,186 | 121,406 | 138,325 | 119,705 | 24,558 | 17,873 |

*Group*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Overdue | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2004** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 128,501 | — | — | — | — | — | 128,501 |
| Due from other banks and financial institutions | 76,503 | 11,470 | 650 | 300 | — | — | 88,923 |
| Trading assets | 973 | 254 | 146 | 143 | 17 | — | 1,533 |
| Loans and advances to customers | 43,804 | 104,553 | 285,017 | 97,181 | 87,421 | 13,636 | 631,612 |
| Investment securities | | | | | | | |
| – originated loans | 2,861 | 3,182 | 29,146 | 79,448 | 45,189 | — | 159,826 |
| – available-for-sale | 2,397 | 19,875 | 29,703 | 30,845 | 7,208 | — | 90,028 |
| Other assets, including deferred tax assets | 14,788 | 951 | 1,939 | 7,501 | 19,400 | 453 | 45,032 |
| **Total assets** | 269,827 | 140,285 | 346,601 | 215,418 | 159,235 | 14,089 | 1,145,455 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (22,992) | (5,161) | (1,602) | — | (1,956) | — | (31,711) |
| Trading liabilities | (830) | (240) | (173) | (3,534) | (309) | — | (5,086) |
| Due to customers | (724,497) | (68,546) | (175,982) | (56,552) | (4,364) | — | (1,029,941) |
| Subordinated term debt | — | — | (275) | (12,000) | — | — | (12,275) |
| Other liabilities, including deferred tax liabilities | (10,903) | (197) | (638) | — | (1,151) | — | (12,889) |
| **Total liabilities** | (759,222) | (74,144) | (178,670) | (72,086) | (7,780) | — | (1,091,902) |
| **Net liquidity gap** | (489,395) | 66,141 | 167,931 | 143,332 | 151,455 | 14,089 | 53,553 |

*Bank*

| | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Overdue | Total |
|---|---|---|---|---|---|---|---|
| **As at 31 December 2004** | | | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with central banks | 128,376 | — | — | — | — | — | 128,376 |
| Due from other banks and financial institutions | 76,503 | 11,470 | 650 | 300 | — | — | 88,923 |
| Trading assets | 973 | 254 | 146 | 143 | 17 | — | 1,533 |
| Loans and advances to customers | 43,804 | 104,553 | 285,017 | 97,181 | 87,421 | 13,636 | 631,612 |
| Investment securities | | | | | | | |
| – originated loans | 2,861 | 3,182 | 29,146 | 79,448 | 45,189 | — | 159,826 |
| – available-for-sale | 2,306 | 19,875 | 29,703 | 30,845 | 7,208 | — | 89,937 |
| Investments in and due from subsidiaries | — | — | 60 | 153 | 1,063 | — | 1,276 |
| Other assets, including deferred tax assets | 13,959 | 951 | 1,939 | 7,501 | 17,859 | 453 | 42,662 |
| **Total assets** | 268,782 | 140,285 | 346,661 | 215,571 | 158,757 | 14,089 | 1,144,145 |
| **Liabilities** | | | | | | | |
| Due to other banks and financial institutions | (22,992) | (5,161) | (1,602) | — | (1,956) | — | (31,711) |
| Trading liabilities | (830) | (240) | (173) | (3,534) | (309) | — | (5,086) |
| Due to customers | (724,497) | (68,546) | (175,982) | (56,552) | (4,364) | — | (1,029,941) |
| Subordinated term debt | — | — | (275) | (12,000) | — | — | (12,275) |
| Other liabilities, including deferred tax liabilities | (8,970) | (197) | (638) | — | (1,045) | — | (10,850) |
| **Total liabilities** | (757,289) | (74,144) | (178,670) | (72,086) | (7,674) | — | (1,089,863) |
| **Net liquidity gap** | (488,507) | 66,141 | 167,991 | 143,485 | 151,083 | 14,089 | 54,282 |

The matching and controlled mismatching of the maturities of assets and liabilities is fundamental to the management of the Group. It is unusual for banks ever to be completely matched since business transacted is often of uncertain term and of different types. An unmatched position potentially enhances profitability, but also increases risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest–bearing liabilities as they mature, are important factors in assessing the liquidity of the Group and its exposure to changes in exchange rates.

The Group provides guarantees and issues letters of credit based on a third party's creditability and deposit amount. Liquidity requirements to support calls under guarantees and letters of credit are considerably less than the amounts under commitments because the Group does not generally expect the third party to draw funds under those agreements. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

*G Fair values of financial assets and liabilities*

The following table summarizes the carrying amounts and the approximate fair values of those financial assets and liabilities not presented on the Group's and the Bank's balance sheets at their fair value. Bid prices are used to estimate fair values of assets, whereas offer prices are applied for liabilities.

*Group and Bank*

| | 31 December 2002 | | 31 December 2003 | | 31 December 2004 | |
|---|---|---|---|---|---|---|
| | Carrying Value | Fair Value | Carrying Value | Fair Value | Carrying Value | Fair Value |
| **Financial assets** | | | | | | |
| Due from other banks and financial institutions | 97,293 | 97,293 | 99,935 | 99,935 | 88,923 | 88,923 |
| Loans and advances to customers | 395,153 | 395,153 | 516,675 | 516,675 | 631,612 | 631,612 |
| Investment securities | | | | | | |
| – originated loans | 94,057 | 96,171 | 104,670 | 105,017 | 159,826 | 157,588 |
| – held-to-maturity | 7,942 | 8,021 | 6,721 | 6,741 | — | — |
| Due from subsidiaries | 886 | 886 | 776 | 776 | 66 | 66 |
| **Financial liabilities** | | | | | | |
| Due to other banks and financial institutions | 24,682 | 24,682 | 21,150 | 21,150 | 31,711 | 31,711 |
| Due to customers | 689,153 | 689,598 | 874,159 | 875,119 | 1,029,941 | 1,029,286 |

The fair values of those financial assets and liabilities such as amounts due from/to other banks, loans and advances to customers and customer deposits are approximately equal to their carrying values as the interest rates of most of these assets and liabilities are instantaneously adjusted to changes in interest rates set by the PBOC and other regulatory bodies. The Group only has an insignificant amount of fixed rate deposits due to and from banks, deposits due to customers and loans and advances due from customers.

**Due from other banks and financial institutions**

Due from other banks and financial institutions includes inter-bank placements and items in the course of collection. The fair values of floating rate placements and overnight deposits are their carrying amounts. The estimated fair value of fixed interest bearing deposits, which are normally less than one year, is based on discounted cash flows using prevailing money market interest rates for debts with similar credit risk and remaining maturities. Therefore, the fair value of due from other banks and financial institutions is approximately equal to its carrying value.

**Loans and advances to customers**

Loans and advances to customers are stated net of impairment allowance. All except a very insignificant portion of loans and advances to customers bear interest at a floating rate.

Therefore, the carrying value of loans and advances to customers is a reasonable estimate of fair value.

**Investment securities**

Investment securities include only interest-bearing assets which are originated loans and held-to-maturity, as available-for-sale securities are measured at fair value. The fair value is determined by following the hierarchy given below:

- the published quoted price is the best evidence of fair value when the financial instrument is quoted in an active market.
- the price used in recent transactions of similar financial instruments with adjustment when the market conditions have changed.
- valuation techniques, including: cash flow models etc.
- if fair value cannot be measured reliably, equity and security investments are recognised at cost less impairment.

**Due to other banks and financial institutions and customers**

The estimated fair value of liabilities due to other banks and financial institutions and customers with no stated maturity, which includes non-interest-bearing liabilities due to other banks and financial institutions and customers, is the amount repayable on demand. The fair value of floating rate liabilities due to other banks and customers is their carrying amount. The estimated fair value of fixed interest bearing liabilities due to other banks and financial institutions and customers without quoted market price, which are normally less than one year, is based on discounted cash flows using interest rates for new debts with similar remaining maturities. Therefore, the fair value of due to other banks and financial institutions and customers is approximately equal to its carrying value.

*H Fiduciary activities*

The Group provides custody and trustee services to third parties. Those assets that are held in a fiduciary capacity are not included in the financial statements.

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Investment custody accounts | 23,283 | 46,534 | 71,662 |

## 4 NET INTEREST INCOME

***Group***

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Interest income** | | | |
| Balances with central banks | 1,697 | 1,502 | 1,855 |
| Due from other banks and financial institutions | 1,783 | 2,015 | 2,231 |
| Trading securities | 4 | 9 | 6 |
| Loans and advances to customers | 18,532 | 22,174 | 28,287 |
| Investment securities | 3,843 | 4,242 | 5,885 |
| Others | 19 | 37 | 88 |
| | 25,878 | 29,979 | 38,352 |
| **Interest expense** | | | |
| Due to other banks and financial institutions | (609) | (588) | (1,129) |
| Due to customers | (8,661) | (9,717) | (12,031) |
| | (9,270) | (10,305) | (13,160) |
| **Net interest income** | 16,608 | 19,674 | 25,192 |

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Interest income accrued on individually identified loans and advances to customers with impairment | 3,181 | 2,416 | 1,431 |
| Interest income accrued on impaired amount of due from other banks and financial institutions | 40 | 36 | 12 |

## 5 DIVIDEND INCOME

***Group***

| | Year ended 31 December | | |
|---|---|---|---|
| | **2002** | **2003** | **2004** |
| Dividend income | 93 | 82 | 55 |

Dividend income was from equity investment classified as available-for-sale securities or as held for trading financial assets.

## 6 GAINS LESS LOSSES ARISING FROM TRADING ACTIVITIES

***Group***

| | Year ended 31 December | | |
|---|---|---|---|
| | **2002** | **2003** | **2004** |
| Foreign exchange | 385 | 518 | 594 |
| Interest rate instruments | (21) | (16) | (269) |
| | 364 | 502 | 325 |

Net income on foreign exchange includes gains and losses from spot and forward contracts and from the translation of foreign currency monetary assets and liabilities into Renminbi.

Net income on interest rate instruments mainly include the results of marking interest rate and currency swaps and other derivatives to market.

## 7 OTHER OPERATING INCOME

***Group***

| | Year ended 31 December | | |
|---|---|---|---|
| | **2002** | **2003** | **2004** |
| Profit on sales of land use rights and building | 5 | 40 | 214 |
| Penalty income | 16 | 24 | 19 |
| Sales of foreclosed assets and other assets | 47 | 56 | 46 |
| Write back of dormant customer deposit to income | 7 | 17 | 5 |
| Revaluation surplus of investment property | — | 138 | — |
| Other miscellaneous income | 211 | 252 | 349 |
| | 286 | 527 | 633 |

Other miscellaneous income includes income arising from miscellaneous banking services provided to the Group's customers.

## 8 IMPAIRMENT LOSSES ON LOANS AND ADVANCES

*Group*

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Due from other banks and financial institutions and securities purchased under resale agreements, net (Note 15(b)) | 178 | 458 | 324 |
| Loans and advances to customers (Note 18(b)) | 815 | 4,788 | 3,041 |
| Less: recovery of loans previously written off | (46) | (131) | (150) |
| | 947 | 5,115 | 3,215 |

## 9 OTHER OPERATING EXPENSES

*Group*

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Staff costs (Note 10) | 3,473 | 3,830 | 4,660 |
| Depreciation (Note 20) | 1,674 | 1,646 | 2,471 |
| Operating lease rentals | 793 | 775 | 747 |
| General and administrative expenses | 2,379 | 2,466 | 2,758 |
| Write-down of foreclosed assets | 349 | 60 | 730 |
| Impairment of other receivables | 290 | 308 | 394 |
| Impairment of available-for-sale securities | 4 | 99 | — |
| Revaluation deficit of property and equipment | — | 448 | 389 |
| Revaluation deficit of investment property | — | — | 32 |
| Business tax and surcharges | 1,050 | 1,260 | 1,639 |
| Regulator's supervision fee | — | — | 185 |
| Provision for outstanding litigation | — | 356 | 633 |
| Professional fees | 6 | 7 | 159 |
| Others | 717 | 1,435 | 2,195 |
| | 10,735 | 12,690 | 16,992 |
| Including: | | | |
| Auditors' remuneration | 6 | 7 | 45 |

## 10 STAFF COSTS

*Group*

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Salaries and bonus | 1,878 | 2,241 | 2,717 |
| Management performance bonus | 122 | — | — |
| Pension costs | 193 | 306 | 392 |
| Housing benefits and subsidies | 586 | 491 | 609 |
| Other social security and benefit costs | 694 | 792 | 942 |
| | 3,473 | 3,830 | 4,660 |
| Average number of employees | 57,204 | 56,601 | 55,421 |

## 11 DIRECTORS', SUPERVISORS' AND THE FIVE HIGHEST PAID INDIVIDUALS' EMOLUMENTS

a) Details of the directors' and the supervisors' emoluments are as follows:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Fees | 5 | 7 | 5 |

The numbers of directors whose emoluments fell within the following band are set out below:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Nil – RMB1,000,000 | 8 | 8 | 17 |

No directors or supervisors waived or agreed to waive any emolument during the Relevant Periods.

In 2004, RMB100,000 was paid to independent non-executive directors (2002 and 2003: nil).

b) Five Highest Paid Individuals

All the five highest paid individuals in the Group for the Relevant Periods are directors of the Bank whose emoluments are already reflected in the analysis presented above.

During the Relevant Periods, no emoluments were paid by the Group to any of the directors or supervisors as an inducement to join or upon joining the Group or as compensation for loss of office.

## 12 INCOME TAX EXPENSE

***Group***

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Current tax | | | |
| – Mainland China income tax | 541 | 89 | 141 |
| – Hong Kong profits tax | 1 | 99 | 75 |
| – Overseas taxation | 2 | 3 | 5 |
| | 544 | 191 | 221 |
| Deferred tax (Note 26) | 1,517 | (432) | 5,925 |
| | 2,061 | (241) | 6,146 |

The provision for Mainland China income tax is calculated based on the statutory rate of 33% of the assessable income of the Bank and each of the subsidiaries established in Mainland China as determined in accordance with the relevant PRC income tax rules and regulations for the Relevant Periods.

Profits earned by the Hong Kong branch or subsidiaries in Hong Kong are subject to Hong Kong profits tax at the rate of 16%, 17.5% and 17.5%, on the estimated assessable profit for the years ended 31 December 2002, 2003 and 2004 respectively. Taxation on overseas profits has been calculated on the estimated assessable profit at the rates of taxation prevailing in the countries in which the Group operates during the Relevant Periods.

The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the taxation rate of the home country of the Bank at 33%. The reconciliation is as follows:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Profit before tax | 6,490 | 4,135 | 7,750 |
| Tax calculated at a tax rate of 33% | 2,142 | 1,365 | 2,557 |
| Effect of different tax rates in other countries | (2) | 6 | 5 |
| Tax credit arising from Income not subject to tax (note 4) | (679) | (842) | (3,747) |
| Tax effect of expenses that are not deductible for tax purposes (note 5) | 681 | 1,055 | 1,248 |
| Tax effect arising from: | | | |
| (a) Recognition of deferred tax asset, not previously recognised (note 1) | (119) | (1,295) | — |
| (b) De-recognition of deferred tax liability, previously recognised (note 2) | — | (510) | — |
| (c) De-recognition of deferred tax assets in relation to loans disposed of (note 3) | — | — | 9,671 |
| (d) Recognition of deferred tax assets in relation to tax loss (note 4) | 38 | (20) | (3,588) |
| Income tax expense | 2,061 | (241) | 6,146 |

Note 1:

Prior to 1 January 2003, the Group did not recognise deferred tax asset for all temporary differences arising from loan impairment because the Group was uncertain whether the tax authorities would allow these temporary differences be utilized against future taxable profits. Upon discussions with the tax authorities in 2003, the Group has managed to claim tax deduction of and clarified the basis of tax treatment on these temporary differences. On this basis, management believes that all temporary differences in this regard can be utilized in full ultimately and hence a deferred tax asset is recognised in 2003.

Note 2:

Prior to 1 January 2003, the Group recognised deferred tax liabilities for certain property and equipment of which the tax base was zero. Upon the approval of the revised tax base by the tax authority after the Group began to carry its property and equipment at valuation at 31 December 2003, the Group derecognised deferred tax liabilities in this connection amounting to RMB510 million for the year ended 31 December 2003.

Note 3:

The Group had recognised deferred tax asset for all temporary differences arising from loan impairment amounting to RMB10,015 million before the majority of impaired loans were disposed of to an asset management company in June 2004. Following the disposal of the impaired loans, all deferred tax assets in relation thereto of RMB9,671 million (Note 26) had been derecognised accordingly.

Note 4:

The Group obtained written approvals from the MOF and the tax authority on 10 January 2005 and 25 March 2005 respectively, which confirm the Group's accumulated losses to be RMB11,002 million, and the accumulated losses can be used to offset against future taxable profit from 1 January 2005 onwards. Therefore, the Group recognised deferred tax assets up to RMB3,631 million (Note 26), being 33% of RMB11,002 million at 31 December, 2004.

Included in the amount of RMB3,747 million of income not subject to tax for the year ended 31 December 2004 is an amount of RMB2,932 million being income tax on profit of the Bank for the year ended 31 December 2004. The Group believes that this amount of profit earned will be income tax exempt in consideration of the loss incurred by the Bank on its disposal of impaired loans in June 2004.

Note 5:

Tax effect of expenses that are not deductible for tax purposes:

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Tax effect of:** | | | |
| Non-deductible staff cost & staff welfare | 482 | 564 | 756 |
| Non-deductible business entertainment | 24 | 25 | 35 |
| Non-deductible depreciation & amortization | 4 | 33 | 102 |
| Non-deductible loan loss provision/write-off | 145 | — | — |
| Unrecognized deferred tax assets related to subsidiary losses | — | — | 145 |
| IPO professional fees not charged to the profit and loss account under PRC GAAP | — | — | 52 |
| Non-deductible loss on equity investments written off | — | — | 62 |
| Provision for outstanding litigation | — | 117 | — |
| Revaluation deficit of property and equipment | — | 148 | — |
| Others | 26 | 168 | 96 |
| Total | 681 | 1,055 | 1,248 |

## 13 BASIC AND DILUTED EARNINGS PER SHARE

Basic and diluted earnings per share is calculated by dividing the net profit attributable to equity holders of the Bank by the weighted average number of ordinary shares in issue during the year.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Profit attributable to equity holders of the Group | 4,429 | 4,376 | 1,604 |
| Weighted average number of ordinary shares in issue | 16,933 | 17,045 | 26,396 |
| Basic and diluted earnings per share (expressed in RMB per share) | 0.26 | 0.26 | 0.06 |

## 14 CASH AND BALANCES WITH CENTRAL BANKS

***Group***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Cash | 6,926 | 8,374 | 8,616 |
| Balances with central banks other than mandatory reserve deposits | 42,027 | 54,452 | 58,215 |
| Included in cash and cash equivalents (Note 35) | 48,953 | 62,826 | 66,831 |
| Mandatory reserve deposits | 34,357 | 50,246 | 61,670 |
| | 83,310 | 113,072 | 128,501 |

***Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Cash | 6,926 | 7,955 | 8,491 |
| Balances with central banks other than mandatory reserve deposits | 42,027 | 54,452 | 58,215 |
| | 48,953 | 62,407 | 66,706 |
| Mandatory reserve deposits | 34,357 | 50,246 | 61,670 |
| | 83,310 | 112,653 | 128,376 |

The Group is required to place mandatory deposits with central banks. The deposits are calculated based on the amount of deposits placed with the Group by its customers.

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Mandatory reserve rate for deposits denominated in RMB | 6% | 7% | 7.5% |
| Reserve rate for deposits denominated in foreign currency | 2% | 2% | 2% |

Mandatory reserve deposits with central banks are not available for use by the Group in its day to day operations.

## 15 DUE FROM OTHER BANKS AND FINANCIAL INSTITUTIONS

*(a) Due from other banks and financial institutions*

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Placement with other banks and included in cash equivalents (Note 35) | 4,217 | 14,462 | 8,926 |
| Securities purchased under resale agreement | 42,638 | 28,667 | 27,109 |
| Less: allowance for impairment losses on securities purchased under resale agreement | (116) | (68) | (82) |
| | 42,522 | 28,599 | 27,027 |
| Loans purchased under resale agreement | — | 5,060 | 2,395 |
| Loans and advances to other banks | 45,956 | 50,475 | 49,197 |
| Loans to other financial institutions | 5,183 | 2,239 | 2,300 |
| | 51,139 | 52,714 | 51,497 |
| Less: allowance for impairment losses on amounts due from other banks and financial institutions | (585) | (900) | (922) |
| | 50,554 | 51,814 | 50,575 |
| | 97,293 | 99,935 | 88,923 |

*(b) Movements in allowance for impairment losses on amounts due from other banks and financial institutions and securities purchased under resale agreement*

***Group and Bank***

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Balance at beginning of the year** | 588 | 701 | 968 |
| Provision for impairment, net (Note 8) | 178 | 458 | 324 |
| Amounts written off/ transferred out during the year as uncollectible | (65) | (191) | (288) |
| **Balance at end of the year** | 701 | 968 | 1,004 |

*(c) Impaired amount of due from other banks and financial institutions:*

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Impaired amount of due from other banks and financial institutions | 2,697 | 2,085 | 1,004 |
| Impaired amount of due from other banks and financial institutions percentage | 2.75% | 2.07% | 1.12% |

## 16 TRADING ASSETS

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Derivative financial instruments (Note 17) | 19 | 188 | 219 |
| Government bonds-listed in Hong Kong | 15 | 107 | 1,191 |
| Other debt securities | | | |
| – Listed in Hong Kong | — | 28 | 2 |
| – Unlisted-government bonds | 107 | 2,671 | — |
| – Unlisted-corporate bonds | — | 42 | 72 |
| – Unlisted-public sector | — | 25 | 49 |
| Other equity securities-unlisted | — | 45 | — |
| | 141 | 3,106 | 1,533 |

Included in the balance above, there were treasury bills amounting to RMB122 million, RMB2,778 million and RMB1,191 million as of 31 December 2002, 2003 and 2004 respectively.

## 17 DERIVATIVE FINANCIAL INSTRUMENTS

The following derivative instruments are utilized by the Group for trading purpose:

Currency forwards represent commitments to purchase/sell foreign exchanges including undelivered spot transactions.

Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or interest rates (for example, fixed rate for floating rate) or a combination of all these (i.e. cross-currency interest rate swaps). The Group's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligation. This risk is monitored on an ongoing basis with reference to the current fair value, the notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Group assesses counterparties using the same techniques as for its lending activities.

Foreign currency and interest rate options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of a foreign currency or a financial instrument at a predetermined price. The seller receives a premium from the purchaser in consideration for the assumption of foreign exchange or interest rate risk. Options may be either exchange-traded or negotiated between the Group and a customer (OTC).

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Group's exposure to credit or price risks. The derivative instruments become favorable (assets) or unfavorable (liabilities) as a result of fluctuations in market interest rates or foreign exchange rates relative to their terms. The aggregate fair values of derivative financial assets and liabilities can fluctuate significantly from time to time. The fair values of derivative instruments held are set out in the following tables.

*Group and Bank*

| | Contract/notional Amount | Fair values | |
|---|---|---|---|
| | | Assets | Liabilities |
| **As at 31 December 2002** | | | |
| **Foreign exchange derivatives** | | | |
| Currency forwards | 25,528 | 12 | (12) |
| Currency swaps | 20,096 | 7 | (6) |
| | | 19 | (18) |
| **Interest rate derivatives** | | | |
| Interest rate swaps | 298 | — | (42) |
| **Total recognised derivative assets** | | 19 | (60) |
| **As at 31 December 2003** | | | |
| **Foreign exchange derivatives** | | | |
| Currency forwards | 3,956 | 12 | (2) |
| Currency swaps | 64,003 | 174 | (237) |
| | | 186 | (239) |
| **Interest rate derivatives** | | | |
| Interest rate swaps | 886 | 2 | (53) |
| **Total recognised derivative assets** | | 188 | (292) |
| **As at 31 December 2004** | | | |
| **Foreign exchange derivatives** | | | |
| Currency forwards | 3,818 | 28 | (13) |
| Currency swaps | 45,234 | 94 | (176) |
| OTC currency options bought and sold | 360 | 7 | — |
| | | 129 | (189) |
| **Interest rate derivatives** | | | |
| Interest rate swaps | 13,536 | 70 | (230) |
| Cross currency interest rate swaps | 3,759 | 17 | (158) |
| OTC interest rate options | 248 | 3 | — |
| **Total recognised derivative assets** | | 219 | (577) |

The tables above provide a detailed breakdown of the contractual or notional amounts and the fair values of the Group's and the Bank's derivative financial instruments outstanding at each year end. These instruments, comprising foreign exchange and interest rate derivatives allow the Group and its customers to transfer, modify or reduce their foreign exchange and interest rate risks.

The Group mostly undertakes its transactions in foreign exchange and interest rate contracts with other financial institutions. Management has established notional limits of these contracts by counterparties, industry sectors and countries. Actual credit exposures and limits are regularly monitored and controlled by management.

**Credit risk weighted amounts**

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Derivatives | | | |
| – Exchange rate contracts | 97 | 233 | 171 |
| – Interest rate contracts | 1 | 17 | 30 |
| – Other derivative contracts | — | — | 4 |
| | 98 | 250 | 205 |

The credit risk weighted amount refers to the amount as computed in accordance with the Hong Kong Banking Ordinance and depends on the status of the counterparty and the maturity characteristics.

**Replacement costs**

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Derivatives | | | |
| – Exchange rate contracts | 20 | 243 | 134 |
| – Interest rate contracts | — | — | 49 |
| – Other derivative contracts | — | — | 11 |
| | 20 | 243 | 194 |

Replacement cost is the cost of replacing all contracts which have a positive value when marked to market (should the counterparty default on its obligations) and is obtained by marking to market contracts with a positive value. Replacement cost is a close approximation of the credit risk for these contracts at the balance sheet date.

The above credit risk weighted amounts and replacement costs are calculated in accordance with the formula promulgated by the HKMA because there are no relevant standards prescribed by IFRS. There was no relevant standard prescribed by the PRC banking regulators for determining the credit risk weighted amounts of derivatives and the Group is not required to report any credit risk weighted amounts of derivatives to the banking regulators either.

The credit risk weighted amounts and replacement costs stated above have taken into account of the effects of bilateral netting arrangements.

**Notional amounts of derivative financial instruments by original currency (net position)**

***Group and Bank***

| | RMB | US Dollars | HK Dollars | Others | Total |
|---|---|---|---|---|---|
| As at 31 December 2002 | | | | | |
| Notional amount of derivative financial instruments | — | 21,194 | 24,166 | 562 | 45,922 |
| As at 31 December 2003 | | | | | |
| Notional amount of derivative financial instruments | — | 33,347 | 34,521 | 977 | 68,845 |
| As at 31 December 2004 | | | | | |
| Notional amount of derivative financial instruments | — | 57,833 | 5,294 | 3,828 | 66,955 |

## 18 LOANS AND ADVANCES TO CUSTOMERS

*(a) Loans and advances to customers*

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Loans and advances to customers | 426,763 | 549,943 | 640,058 |
| Less: allowance for impairment losses on loans and advances | (31,610) | (33,268) | (8,446) |
| | 395,153 | 516,675 | 631,612 |

*(b) Movements in allowance for losses on loans and advances:*

***Group and Bank***

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Balance at beginning of year** | 44,993 | 31,610 | 33,268 |
| Provision for loan impairment | 815 | 4,788 | 3,041 |
| Loans written off during the year as uncollectible | (14,365) | (3,192) | (928) |
| Written back on disposal of impaired loans (Note 39) | — | — | (26,935) |
| Exchange and other adjustments | 167 | 62 | — |
| **Balance at end of the year** | 31,610 | 33,268 | 8,446 |

*(c) Individually identified loans with impairment:*

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Individually identified loans with impairment | 71,106 | 65,199 | 19,193 |
| Individually identified loans with impairment to loans and advances to customers percentage | 16.66% | 11.86% | 3.00% |

## 19 INVESTMENT SECURITIES

*Group*

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Securities – originated loans** | | | |
| Debt securities – at amortised cost | | | |
| – Listed in Hong Kong | 83 | 1,661 | 1,077 |
| – Listed outside Hong Kong | 2,988 | 3,002 | 15,255 |
| – Unlisted | 90,986 | 100,007 | 143,494 |
| | 94,057 | 104,670 | 159,826 |
| **Securities – available-for-sale** | | | |
| Debt securities – at fair value | | | |
| – Listed in Hong Kong | 1,584 | 3,378 | 4,948 |
| – Listed outside Hong Kong | 3,931 | 3,970 | 20,105 |
| – Unlisted | 8,356 | 28,704 | 64,453 |
| Equity securities – at fair value | | | |
| – Listed outside Hong Kong | 2 | 2 | 2 |
| – Unlisted | 600 | 545 | 429 |
| Equity securities at cost less impairment | | | |
| – Unlisted | 166 | 88 | 91 |
| | 14,639 | 36,687 | 90,028 |
| **Securities – held-to-maturity** | | | |
| Debt securities – at amortised cost | | | |
| – Listed outside Hong Kong | 6,847 | 5,546 | — |
| – Unlisted | 1,095 | 1,175 | — |
| | 7,942 | 6,721 | — |

***Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Securities – originated loans** | | | |
| Debt securities – at amortised cost | | | |
| – Listed in Hong Kong | 83 | 1,661 | 1,077 |
| – Listed outside Hong Kong | 2,988 | 3,002 | 15,255 |
| – Unlisted | 90,986 | 100,007 | 143,494 |
| | 94,057 | 104,670 | 159,826 |
| **Securities – available-for-sale** | | | |
| Debt securities – at fair value | | | |
| – Listed in Hong Kong | 1,584 | 3,378 | 4,948 |
| – Listed outside Hong Kong | 3,931 | 3,970 | 20,105 |
| – Unlisted | 8,356 | 28,704 | 64,453 |
| Equity securities – at fair value | | | |
| – Listed outside Hong Kong | 2 | 2 | 2 |
| – Unlisted | 313 | 309 | 429 |
| Equity securities at cost less impairment | | | |
| – Unlisted | 7 | — | — |
| | 14,193 | 36,363 | 89,937 |
| **Securities – held-to-maturity** | | | |
| Debt securities – at amortised cost | | | |
| – Listed outside Hong Kong | 6,847 | 5,546 | — |
| – Unlisted | 1,095 | 1,175 | — |
| | 7,942 | 6,721 | — |

As certain unlisted equity securities held by the Group have no published quoted prices available or are not able to be benchmarked with similar financial instruments, or valuation techniques are not cost effective, the Group states such unlisted equity securities at cost less impairment. The market values of above listed securities are set out below:

| | 31 December 2002 | | 31 December 2003 | | 31 December 2004 | |
|---|---|---|---|---|---|---|
| | Carrying Value | Market Value | Carrying Value | Market Value | Carrying Value | Market Value |
| Investment securities – originated loans | | | | | | |
| – Listed in Hong Kong | 83 | 83 | 1,661 | 1,713 | 1,077 | 1,077 |
| – Listed outside Hong Kong | 2,988 | 3,033 | 3,002 | 3,061 | 15,255 | 15,150 |
| Investment securities – held-to-maturity | | | | | | |
| – Listed outside Hong Kong | 6,847 | 6,853 | 5,546 | 5,632 | — | — |

Due to the change in management's investment strategy, the Group re-designated all its investment securities originally classified as held to maturity to become available for sale during 2004. Investment securities amounting to RMB1,014 million were disposed of immediately and investment securities amounting to RMB4,378 million have been reclassified as available for sale in the Group's financial statements. After such reclassification of investment securities, the Group may not recognise any held to maturity securities in the following two financial years.

The fair values of originated loans and held-to-maturity securities of the Group are shown in Note 3(G).

Gains less losses arising from investment securities comprise:

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Gains less losses arising from de-recognition of investment securities | 8 | (2) | 77 |

The movement in investment securities may be summarized as follows:

***Group***

| | Originated loans | Available-for-sale | Held-to-maturity | Total |
|---|---|---|---|---|
| At 1 January 2002 | 75,788 | 11,093 | 6,414 | 93,295 |
| Additions | 42,754 | 4,659 | 3,221 | 50,634 |
| Disposals (sale or redemption) | (24,485) | (1,448) | (1,724) | (27,657) |
| Gains from changes in fair value | — | 287 | — | 287 |
| Exchange differences | — | 52 | 31 | 83 |
| Impairment | — | (4) | — | (4) |
| At 31 December 2002/1 January 2003 | 94,057 | 14,639 | 7,942 | 116,638 |
| Additions | 28,708 | 54,737 | 1,149 | 84,594 |
| Disposals (sale or redemption) | (18,133) | (32,760) | (2,410) | (53,303) |
| Losses from changes in fair value | — | (121) | — | (121) |
| Exchange differences | 38 | 291 | 40 | 369 |
| Impairment | — | (99) | — | (99) |
| At 31 December 2003/1 January 2004 | 104,670 | 36,687 | 6,721 | 148,078 |
| Additions | 81,419 | 120,109 | 840 | 202,368 |
| Disposals (sale or redemption) | (26,269) | (71,778) | (2,981) | (101,028) |
| Reclassification | — | 4,378 | (4,378) | — |
| Losses from changes in fair value | — | (96) | — | (96) |
| Exchange differences | 6 | 728 | (202) | 532 |
| At 31 December 2004 | 159,826 | 90,028 | — | 249,854 |

***Bank***

| | Originated loans | Available-for-sale | Held-to-maturity | Total |
|---|---|---|---|---|
| At 1 January 2002 | 75,788 | 10,566 | 6,414 | 92,768 |
| Additions | 42,754 | 4,659 | 3,221 | 50,634 |
| Disposals (sale or redemption) | (24,485) | (1,367) | (1,724) | (27,576) |
| Gains from changes in fair value | — | 287 | — | 287 |
| Exchange differences | — | 52 | 31 | 83 |
| Impairment | — | (4) | — | (4) |
| At 31 December 2002/1 January 2003 | 94,057 | 14,193 | 7,942 | 116,192 |
| Additions | 28,708 | 54,737 | 1,149 | 84,594 |
| Disposals (sale or redemption) | (18,133) | (32,638) | (2,410) | (53,181) |
| Losses from changes in fair value | — | (121) | — | (121) |
| Exchange differences | 38 | 291 | 40 | 369 |
| Impairment | — | (99) | — | (99) |
| At 31 December 2003/1 January 2004 | 104,670 | 36,363 | 6,721 | 147,754 |
| Additions | 81,419 | 120,109 | 840 | 202,368 |
| Disposals (sale or redemption) | (26,269) | (71,545) | (2,981) | (100,795) |
| Reclassification | — | 4,378 | (4,378) | — |
| Losses from changes in fair value | — | (96) | — | (96) |
| Exchange differences | 6 | 728 | (202) | 532 |
| At 31 December 2004 | 159,826 | 89,937 | — | 249,763 |

The investment securities are analysed by issuer as follows:

***Group***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Securities – originated loans** | | | |
| – Central governments and central banks | 87,188 | 97,428 | 85,449 |
| – Public sector entities | — | — | 125 |
| – Banks and other financial institutions | 6,220 | 6,569 | 74,112 |
| – Corporate entities | 649 | 673 | 140 |
| | 94,057 | 104,670 | 159,826 |
| **Securities – available-for-sale** | | | |
| – Central governments and central banks | 1,429 | 19,909 | 53,229 |
| – Public sector entities | — | — | 2,398 |
| – Banks and other financial institutions | 9,116 | 12,082 | 29,497 |
| – Corporate entities | 4,094 | 4,696 | 4,904 |
| | 14,639 | 36,687 | 90,028 |
| **Securities – held-to-maturity** | | | |
| – Central governments and central banks | 1,380 | 1,341 | — |
| – Banks and other financial institutions | 6,406 | 5,233 | — |
| – Corporate entities | 156 | 147 | — |
| | 7,942 | 6,721 | — |

Included in the balance above, there were treasury bills amounting to RMB170 million, RMB12,791 million and RMB50,383 million as of 31 December 2002, 2003 and 2004 respectively.

*Bank*

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Securities – originated loans** | | | |
| – Central governments and central banks | 87,188 | 97,428 | 85,449 |
| – Public sector entities | — | — | 125 |
| – Banks and other financial institutions | 6,220 | 6,569 | 74,112 |
| – Corporate entities | 649 | 673 | 140 |
| | 94,057 | 104,670 | 159,826 |
| **Securities – available-for-sale** | | | |
| – Central governments and central banks | 1,429 | 19,909 | 53,229 |
| – Public sector entities | — | — | 2,398 |
| – Banks and other financial institutions | 9,116 | 12,082 | 29,497 |
| – Corporate entities | 3,648 | 4,372 | 4,813 |
| | 14,193 | 36,363 | 89,937 |
| **Securities – held-to-maturity** | | | |
| – Central governments and central banks | 1,380 | 1,341 | — |
| – Banks and other financial institutions | 6,406 | 5,233 | — |
| – Corporate entities | 156 | 147 | — |
| | 7,942 | 6,721 | — |

The Certificates of deposit held included in investment securities are analysed as follows:

*Group and Bank*

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Originated loans, at amortised cost** | | | |
| – Listed in Hong Kong | — | 1,158 | — |
| – Listed outside Hong Kong | 82 | 213 | — |
| – Unlisted | 1,568 | 432 | 1,306 |
| | 1,650 | 1,803 | 1,306 |
| **Available-for-sale, at fair value** | | | |
| – Listed in Hong Kong | — | 731 | — |
| – Listed outside Hong Kong | — | — | — |
| – Unlisted | 894 | 625 | 1,915 |
| | 894 | 1,356 | 1,915 |
| | 2,544 | 3,159 | 3,221 |
| **Market value of listed certificates of deposit held** | 82 | 2,137 | — |

The maturity profile of certificates of deposit held analysed by the remaining period as at 31 December to the contractual maturity dates is as follows:

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Up to 3 months | — | — | 309 |
| 3 to 12 months | 1,051 | 1,423 | 846 |
| 1 to 5 years | 1,493 | 1,736 | 2,066 |
| | 2,544 | 3,159 | 3,221 |

## 20 PROPERTY AND EQUIPMENT

*Group*

| | Land and Buildings | Construction in Progress | Equipment | Motor Vehicles | Leasehold Improvement | Total |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| At 1 January 2002 | 9,361 | 1,326 | 5,365 | 878 | 1,935 | 18,865 |
| Additions | 161 | 1,316 | 1,139 | 60 | 45 | 2,721 |
| Disposals | (75) | — | (316) | (73) | (482) | (946) |
| Transfers | 2,675 | (2,138) | — | — | 268 | 805 |
| At 31 December 2002 | 12,122 | 504 | 6,188 | 865 | 1,766 | 21,445 |
| **Accumulated depreciation** | | | | | | |
| At 1 January 2002 | (1,145) | — | (3,040) | (543) | (1,084) | (5,812) |
| Charge for the year | (371) | — | (921) | (102) | (280) | (1,674) |
| Disposals | 6 | — | 189 | 64 | 454 | 713 |
| At 31 December 2002 | (1,510) | — | (3,772) | (581) | (910) | (6,773) |
| **Net book value** | | | | | | |
| At 31 December 2002 | 10,612 | 504 | 2,416 | 284 | 856 | 14,672 |
| **Cost or valuation** | | | | | | |
| At 1 January 2003 | 12,122 | 504 | 6,188 | 865 | 1,766 | 21,445 |
| Additions | 313 | 893 | 1,038 | 83 | 87 | 2,414 |
| Disposals | (55) | — | (301) | (87) | (135) | (578) |
| Transfers | 578 | (578) | — | — | 213 | 213 |
| Revaluation surplus / (deficit) | 1,887 | 451 | (4,145) | (512) | — | (2,319) |
| At 31 December 2003 | 14,845 | 1,270 | 2,780 | 349 | 1,931 | 21,175 |
| **Accumulated depreciation** | | | | | | |
| At 1 January 2003 | (1,510) | — | (3,772) | (581) | (910) | (6,773) |
| Charge for the year | (267) | — | (1,010) | (62) | (307) | (1,646) |
| Disposals | 4 | — | 282 | 81 | 23 | 390 |
| Revaluation | 1,773 | — | 4,500 | 562 | — | 6,835 |
| At 31 December 2003 | — | — | — | — | (1,194) | (1,194) |
| **Net book value** | | | | | | |
| At 31 December 2003 | 14,845 | 1,270 | 2,780 | 349 | 737 | 19,981 |
| **Carrying amount at 31 December 2003, if at cost** | 11,185 | 819 | 2,425 | 299 | 737 | 15,465 |
| **Cost at valuation** | | | | | | |
| At 1 January 2004 | 14,845 | 1,270 | 2,780 | 349 | 1,931 | 21,175 |
| Additions | 103 | 1,387 | 1,272 | 60 | 6 | 2,828 |
| Disposals | (113) | — | (680) | (124) | (629) | (1,546) |
| Transfers | 747 | (1,450) | — | — | 261 | (442) |
| Revaluation | 3,551 | (61) | (743) | (13) | — | 2,734 |
| At 31 December 2004 | 19,133 | 1,146 | 2,629 | 272 | 1,569 | 24,749 |
| **Accumulated depreciation at valuation** | | | | | | |
| At 1 January 2004 | — | — | — | — | (1,194) | (1,194) |
| Charge for the year | (740) | — | (1,356) | (121) | (254) | (2,471) |
| Disposals | 63 | — | 613 | 108 | 562 | 1,346 |
| Revaluation | 677 | — | 743 | 13 | — | 1,433 |
| At 31 December 2004 | — | — | — | — | (886) | (886) |
| **Net book value at valuation** | | | | | | |
| At 31 December 2004 | 19,133 | 1,146 | 2,629 | 272 | 683 | 23,863 |
| **Carrying amount at 31 December 2004, if at cost** | 11,508 | 948 | 2,409 | 256 | 683 | 15,804 |

***Bank***

| | Land and Buildings | Construction in Progress | Equipment | Motor Vehicles | Leasehold Improvement | Total |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| At 1 January 2002 | 8,385 | 893 | 5,365 | 878 | 1,935 | 17,456 |
| Additions | 161 | 800 | 1,139 | 60 | 45 | 2,205 |
| Disposals | (27) | — | (316) | (73) | (482) | (898) |
| Transfers | 1,576 | (1,039) | — | — | 268 | 805 |
| At 31 December 2002 | 10,095 | 654 | 6,188 | 865 | 1,766 | 19,568 |
| **Accumulated depreciation** | | | | | | |
| At 1 January 2002 | (1,145) | — | (3,040) | (543) | (1,084) | (5,812) |
| Charge for the year | (371) | — | (921) | (102) | (280) | (1,674) |
| Disposals | 6 | — | 189 | 64 | 454 | 713 |
| At 31 December 2002 | (1,510) | — | (3,772) | (581) | (910) | (6,773) |
| **Net book value** | | | | | | |
| At 31 December 2002 | 8,585 | 654 | 2,416 | 284 | 856 | 12,795 |
| **Cost or valuation** | | | | | | |
| At 1 January 2003 | 10,095 | 654 | 6,188 | 865 | 1,766 | 19,568 |
| Additions | 149 | 893 | 1,038 | 83 | 87 | 2,250 |
| Disposals | (55) | — | (301) | (87) | (135) | (578) |
| Transfers | 578 | (578) | — | — | 213 | 213 |
| Revaluation surplus / (deficit) | 1,887 | 451 | (4,145) | (512) | — | (2,319) |
| At 31 December 2003 | 12,654 | 1,420 | 2,780 | 349 | 1,931 | 19,134 |
| **Accumulated depreciation** | | | | | | |
| At 1 January 2003 | (1,510) | — | (3,772) | (581) | (910) | (6,773) |
| Charge for the year | (267) | — | (1,010) | (62) | (307) | (1,646) |
| Disposals | 4 | — | 282 | 81 | 23 | 390 |
| Revaluation | 1,773 | — | 4,500 | 562 | — | 6,835 |
| At 31 December 2003 | — | — | — | — | (1,194) | (1,194) |
| **Net book value** | | | | | | |
| At 31 December 2003 | 12,654 | 1,420 | 2,780 | 349 | 737 | 17,940 |
| **Carrying amount at 31 December 2003, if at cost** | 8,995 | 969 | 2,425 | 299 | 737 | 13,425 |
| **Cost or valuation** | | | | | | |
| At 1 January 2004 | 12,654 | 1,420 | 2,780 | 349 | 1,931 | 19,134 |
| Additions | 1,123 | 1,237 | 1,272 | 60 | 6 | 3,698 |
| Disposals | (113) | — | (680) | (124) | (629) | (1,546) |
| Transfers | 747 | (1,450) | — | — | 261 | (442) |
| Revaluation | 3,181 | (61) | (743) | (13) | — | 2,364 |
| At 31 December 2004 | 17,592 | 1,146 | 2,629 | 272 | 1,569 | 23,208 |
| **Accumulated depreciation at valuation** | | | | | | |
| At 1 January 2004 | — | — | — | — | (1,194) | (1,194) |
| Charge for the year | (740) | — | (1,356) | (121) | (254) | (2,471) |
| Disposals | 63 | — | 613 | 108 | 562 | 1,346 |
| Revaluation | 677 | — | 743 | 13 | — | 1,433 |
| At 31 December 2004 | — | — | — | — | (886) | (886) |
| **Net book value at valuation** | | | | | | |
| At 31 December 2004 | 17,592 | 1,146 | 2,629 | 272 | 683 | 22,322 |
| **Carrying amount at 31 December 2004, if at cost** | 10,337 | 948 | 2,409 | 256 | 683 | 14,633 |

The Group's land and buildings, construction in progress, equipment and motor vehicles were revalued by the Group's management with reference to a valuation made on an open market and existing use basis by external valuers from 31 December 2003 onwards. Beijing Pan-China Assets Appraisal Co. Ltd, a subsidiary of Pan-China Certified Public Accountants (北京天健興業資產評估有限公司, 天健會計師事務所的成員之一) and Sallmanns (Far East) Ltd. (西門(遠東)有限公司) are the external valuers appointed for valuation at 31 December 2003 and 2004 respectively. Beijing Pan-China Assets Appraisal Co. Ltd. is a qualified provider of general valuation services since 1991 and valuation services for companies seeking a public float since March 1993.

The revaluation reserve relating to revaluation of property and equipment is not distributable to shareholders. The Group has received the formal approval from the tax authority, Guo Shui Han [2005] No.143 – the Notice for the enterprise income tax treatment in relation to the assets valuation surplus of the Bank of Communications, for an exemption of the revaluation surplus or deficit in Mainland China at 31 December 2003 from income tax at the date of valuation and for deduction of the surplus or deficit for income tax purposes in the future. Accordingly, no deferred tax liabilities or assets have been accounted for by the Group in this connection for the year ended 31 December 2003.

Reconciliation between revaluation surplus/deficit of property and equipment and its corresponding changes in shareholders' equity and deferred tax is set below:

***Group***

| | Year ended 31 December | |
|---|---|---|
| | 2003 | 2004 |
| Revaluation surplus classified in equity, net of tax | 4,862 | 3,098 |
| Deferred tax liability (Note 26) | 102 | 1,458 |
| Revaluation deficit charged to profit and loss account (Note 9) | (448) | (389) |
| | 4,516 | 4,167 |

***Bank***

| | Year ended 31 December | |
|---|---|---|
| | 2003 | 2004 |
| Revaluation surplus classified in equity, net of tax | 4,862 | 2,789 |
| Deferred tax liability (Note 26) | 102 | 1,341 |
| Revaluation deficit charged to profit and loss account | (448) | (333) |
| | 4,516 | 3,797 |

All land and buildings of the Group are located outside Hong Kong, except for those of Hong Kong branch.

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Net book value of land and buildings of Hong Kong branch | 270 | 842 | 1,211 |

## 21 OTHER ASSETS

***Group***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Settlement accounts | 2,323 | 3,164 | 5,124 |
| Other receivables | 3,738 | 3,618 | 4,383 |
| Less: impairment | (1,227) | (1,535) | (2,209) |
| Foreclosed assets | 7,381 | 7,143 | 6,832 |
| Less: impairment | (995) | (1,055) | (1,785) |
| Prepaid staff housing subsidies | 378 | 336 | 252 |
| Prepaid rental expenses | 391 | 387 | 356 |
| Land use rights | 466 | 368 | 630 |
| Computer software | 108 | 219 | 256 |
| Investment property | 28 | 172 | 708 |
| Others | 901 | 544 | 1,597 |
| | 13,492 | 13,361 | 16,144 |

***Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Settlement accounts | 2,323 | 3,164 | 5,124 |
| Other receivables | 3,385 | 3,069 | 3,723 |
| Less: impairment | (1,227) | (1,535) | (2,209) |
| Foreclosed assets | 7,381 | 7,143 | 6,832 |
| Less: impairment | (995) | (1,055) | (1,785) |
| Prepaid staff housing subsidies | 378 | 336 | 252 |
| Prepaid rental expenses | 391 | 387 | 356 |
| Land use rights | 716 | 618 | 630 |
| Computer software | 108 | 219 | 256 |
| Investment property | 28 | 172 | 708 |
| Others | 694 | 679 | 1,428 |
| | 13,182 | 13,197 | 15,315 |

The Group commissioned Beijing Pan-China Assets Appraisal Co. Ltd. to value the foreclosed assets on an open market basis at each balance sheet date.

## 22 DUE TO OTHER BANKS AND FINANCIAL INSTITUTIONS

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Due to central banks | — | — | 28 |
| Deposits from other banks and financial institutions | 15,518 | 10,472 | 16,224 |
| Loans from other banks and financial institutions | 9,164 | 10,678 | 15,459 |
| | 24,682 | 21,150 | 31,711 |

## 23 TRADING LIABILITIES

*Group and Bank*

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Derivative financial instruments (Note 17) | 60 | 292 | 577 |
| Short position of trading securities | 120 | 1,958 | 1,158 |
| Debt securities in issue | — | 1,213 | 3,351 |
| | 180 | 3,463 | 5,086 |

Debt securities in issue are:

*Group and Bank*

| | As at 31 December 2003 | | As at 31 December 2004 | |
|---|---|---|---|---|
| | Amount | Interest rate per Annum (%) | Amount | Interest rate per Annum (%) |
| HKD medium term Certificate of Deposit | 172 | 4.12 | 760 | 3.23 |
| USD medium term Certificate of Deposit | 189 | 3.65 | 362 | 3.48 |
| HKD floating rate Certificate of Deposit(maturing in September 2006) | 426 | HIBOR + 0.20 | 426 | HIBOR+0.20 |
| HKD floating rate Certificate of Deposit(maturing in September 2008) | 426 | HIBOR + 0.26 | 426 | HIBOR+0.26 |
| HKD reverse Certificate of Deposit(maturing in May 2009 | — | — | 138 | 6.9%-3m HIBOR |
| USD floating rate Certificate of Deposit( maturing in January 2007) | — | LIBOR +0.20 | 1,239 | LIBOR+0.20 |
| | 1,213 | | 3,351 | |

## 24 DUE TO CUSTOMERS

*Group and Bank*

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Corporate current deposits | 264,936 | 327,109 | 385,556 |
| Corporate savings deposits | 2,517 | 16,909 | 5,011 |
| Corporate time deposits | 103,817 | 141,936 | 186,216 |
| Individual current deposits | 94,299 | 120,745 | 143,461 |
| Individual savings deposits | 8,173 | 12,543 | 14,879 |
| Individual time deposits | 170,833 | 191,886 | 210,561 |
| Pledged deposits | 22,703 | 31,520 | 53,705 |
| Promissory notes | 2,240 | 1,693 | 3,055 |
| Customer margin deposits | 644 | 1,736 | 2,075 |
| Other deposits | 14,044 | 22,133 | 18,815 |
| Interest payable | 4,947 | 5,949 | 6,607 |
| | 689,153 | 874,159 | 1,029,941 |
| Including: | | | |
| Pledged deposits held as collateral for letter of credit | 3,584 | 3,647 | 4,965 |

## 25 OTHER LIABILITIES

*Group*

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Settlement accounts | 4,798 | 4,620 | 4,971 |
| Dividends payable | 386 | 149 | 141 |
| Staff benefits payables | 1,196 | 1,327 | 1,604 |
| Tax payable | 219 | 413 | 655 |
| Provision for outstanding litigation | — | 356 | 989 |
| Others | 1,545 | 1,719 | 4,097 |
| | 8,144 | 8,584 | 12,457 |

*Bank*

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Settlement accounts | 4,798 | 4,620 | 4,971 |
| Dividends payable | 386 | 149 | 141 |
| Staff benefits payables | 1,196 | 1,327 | 1,604 |
| Tax payable | 219 | 413 | 655 |
| Provision for outstanding litigation | — | 356 | 989 |
| Others | 1,310 | 1,181 | 2,165 |
| | 7,909 | 8,046 | 10,525 |

## 26 DEFERRED INCOME TAXES

Deferred income taxes are calculated on all temporary differences under the liability method using an effective tax rate of 33% for the relevant periods for transactions in Mainland China.

Deferred income taxes are calculated on all temporary differences under the liability method using an effective tax rate of 17.5% for the year ended 31 December 2004 (2003: 17.5%; 2002: 16%) for transactions in Hong Kong.

The movement in the deferred income tax account is as follows:

*Group*

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| At beginning of the year | 12,870 | 11,304 | 11,650 |
| Credit/(Charge) to profit and loss account | (1,517) | 432 | (5,925) |
| Available-for-sale securities | | | |
| – fair value remeasurement | (49) | 16 | 32 |
| – transfer to net profit | — | — | — |
| Property revaluation (Note 20) | — | (102) | (1,458) |
| Provision for investments | — | — | 336 |
| Exchange differences | — | — | (3) |
| At end of the year | 11,304 | 11,650 | 4,632 |

***Bank***

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| At beginning of the year | 12,870 | 11,304 | 11,650 |
| Credit/(Charge) to profit and loss account | (1,517) | 432 | (5,935) |
| Available-for-sale securities | | | |
| – fair value remeasurement | (49) | 16 | 32 |
| – transfer to net profit | — | — | — |
| Property revaluation (Note 20) | — | (102) | (1,341) |
| Provision for investments | — | — | 336 |
| Exchange differences | — | — | (3) |
| At end of the year | 11,304 | 11,650 | 4,739 |

Deferred income tax assets and liabilities are attributable to the following items:

***Group***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Deferred income tax liabilities** | | | |
| Available-for-sale securities | (70) | (54) | (53) |
| Accelerated tax depreciation | (529) | (13) | (13) |
| Property revaluation reserve | — | (102) | (1,560) |
| Other temporary differences | (164) | (224) | (261) |
| | (763) | (393) | (1,887) |
| **Deferred income tax assets** | | | |
| Provision for loan losses | 9,658 | 9,242 | 427 |
| Provision for investments | 193 | 229 | 480 |
| Decelerated tax depreciation | — | 22 | 125 |
| Impairment of other assets | 2,193 | 2,507 | 1,825 |
| Tax loss carried forward (Note 12) | 23 | 43 | 3,631 |
| Available-for-sale securities | — | — | 31 |
| | 12,067 | 12,043 | 6,519 |
| **Net deferred income tax assets** | 11,304 | 11,650 | 4,632 |

***Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| **Deferred income tax liabilities** | | | |
| Available-for-sale securities | (70) | (54) | (53) |
| Accelerated tax depreciation | (529) | (13) | (13) |
| Property revaluation reserve | — | (102) | (1,443) |
| Other temporary differences | (164) | (224) | (261) |
| | (763) | (393) | (1,770) |
| **Deferred income tax assets** | | | |
| Provision for loan losses | 9,658 | 9,242 | 427 |
| Provision for investments | 193 | 229 | 480 |
| Decelerated tax depreciation | — | 22 | 115 |
| Impairment of other assets | 2,193 | 2,507 | 1,825 |
| Tax loss carried forward (Note 12) | 23 | 43 | 3,631 |
| Available-for-sale securities | — | — | 31 |
| | 12,067 | 12,043 | 6,509 |
| **Net deferred income tax assets** | 11,304 | 11,650 | 4,739 |

The above net deferred income tax assets are disclosed separately on the balance sheet based on different responsible taxation authorities:

***Group***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Deferred tax assets | 11,304 | 11,712 | 5,025 |
| Deferred tax liabilities | — | (62) | (393) |

***Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Deferred tax assets | 11,304 | 11,712 | 5,025 |
| Deferred tax liabilities | — | (62) | (286) |

The deferred tax credit/(charge) in the profit and loss account comprises the following temporary differences:

***Group***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Provision for loan losses: | | | |
| Additional provisions for loan losses | (228) | 1,031 | 879 |
| Recognition of deferred tax asset not previously recognized (Note 12) | 119 | 1,295 | — |
| Utilization | (769) | (2,742) | (23) |
| De-recognition of deferred tax assets in relation to loans disposed of (Note 12) | — | — | (9,671) |
| Sub-total | (878) | (416) | (8,815) |
| Provisions for investments | 19 | 36 | (85) |
| Impairment of other assets | (472) | 314 | (682) |
| Tax loss carried forward (Note 12) | (38) | 20 | 3,588 |
| Accelerated tax depreciation | (120) | 516 | — |
| Decelerated tax depreciation | — | 22 | 103 |
| Other temporary differences | (28) | (60) | (34) |
| | (1,517) | 432 | (5,925) |

## 27 RETIREMENT BENEFIT OBLIGATIONS

The Group participates in various defined contribution retirement benefit plans organised by municipal and provincial governments in Mainland China under which it is required to make monthly contributions to these plans at rates ranging from 10% to 27% of the employees' basic salary for the Relevant Periods. The Group currently has no additional significant cost for the payment of retirement and other post-retirement benefits of employees other than the monthly contributions described above. The Group's contributions to these pension plans are charged to the profit and loss account in the year to which they relate.

Retirement benefit obligations of the Group in locations other than Mainland China, which are immaterial to the Group, are made in accordance with the relevant local policies and regulations. They are accounted for in the profit and loss account in the year when the payment is made.

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Expenses incurred for retirement benefit plans | 193 | 306 | 392 |

## 28 SUBORDINATED TERM DEBT

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Floating rate subordinated debt – 2009 | — | — | 12,000 |
| Interest payable | — | — | 275 |
| | — | — | 12,275 |

The floating rate subordinated term debt bears interest at the rate of 1 year fixed deposit rate set by the PBOC plus 2.52% and will mature in July 2009.

## 29 SHARE CAPITAL AND CAPITAL SURPLUS

### *Group*

| | Number of shares | Ordinary shares of RMB1 each | Capital surplus | Total |
|---|---|---|---|---|
| | (in millions) | (RMB million) | (RMB million) | (RMB million) |
| At 1 January 2002 | 15,910 | 15,910 | 5,455 | 21,365 |
| Donation received | — | — | 1 | 1 |
| Issue of shares (note 1) | 1,123 | 1,123 | 1,123 | 2,246 |
| At 31 December 2002/ 1 January 2003 | 17,033 | 17,033 | 6,579 | 23,612 |
| Issue of shares (note 2) | 75 | 75 | 75 | 150 |
| Capitalization of revaluation surplus (note 3) | — | — | 4,381 | 4,381 |
| At 31 December 2003/ 1 January 2004 | 17,108 | 17,108 | 11,035 | 28,143 |
| Restructuring transactions with government (note 4) | 13,556 | 13,556 | 1,681 | 15,237 |
| Restructuring transactions with third parties (note 4) | 8,406 | 8,406 | 7,191 | 15,597 |
| Reserves offset against accumulated losses (note 5) | — | — | (9,035) | (9,035) |
| At 31 December 2004 | 39,070 | 39,070 | 10,872 | 49,942 |

### *Bank*

| | Number of shares | Ordinary shares of RMB1 each | Capital surplus | Total |
|---|---|---|---|---|
| | (in millions) | (RMB million) | (RMB million) | (RMB million) |
| At 1 January 2002 | 15,910 | 15,910 | 5,455 | 21,365 |
| Donation received | — | — | 1 | 1 |
| Issue of shares (note 1) | 1,123 | 1,123 | 1,123 | 2,246 |
| At 31 December 2002/ 1 January 2003 | 17,033 | 17,033 | 6,579 | 23,612 |
| Issue of shares (note 2) | 75 | 75 | 75 | 150 |
| Capitalization of revaluation surplus (note 3) | — | — | 4,381 | 4,381 |
| At 31 December 2003/ 1 January 2004 | 17,108 | 17,108 | 11,035 | 28,143 |
| Restructuring transactions with government (note 4) | 13,556 | 13,556 | 2,573 | 16,129 |
| Restructuring transactions with third parties (note 4) | 8,406 | 8,406 | 7,191 | 15,597 |
| Reserves offset against accumulated losses (note 5) | — | — | (9,035) | (9,035) |
| At 31 December 2004 | 39,070 | 39,070 | 11,764 | 50,834 |

The total authorized numbers of ordinary shares as of 31 December 2002, 2003 and 2004 are the same as numbers of issued capital at those balance sheet dates. All issued shares are fully paid.

Note 1:

During the year ended 31 December 2002, the Bank increased the number of issued ordinary shares from 15,910 million shares to 17,033 million shares. Details of the increase are as follows:

- On 3 August 2001, the Bank's Directors passed a resolution to capitalize dividends payable to the MOF amounting to RMB2,006 million, which represented 70% of the profit contributed by overseas branches for the years prior to 1998 and attributable to the MOF. Accordingly, 1,003 million shares were issued to MOF at RMB2 each. Both share capital and capital surplus were increased by RMB1,003 million in 2002 with the ratification from MOF as stated in Cai Jin [2003] No. 68 issued on 22 July 2003.

- According to Cai Jin [2002] No. 158 issued by MOF on 1 November 2002, MOF agreed to capitalise dividends receivable from the Bank amounting to RMB240 million by subscribing 120 million shares at RMB2 each. Share capital and capital surplus were increased by RMB120 million and RMB120 million respectively.

Note 2:

During the year ended 31 December 2003, the Bank further increased the number of issued ordinary shares from 17,033 million shares to 17,108 million shares. Details of the increase are as follows:

- According to Cai Jin [2003] No. 99 issued by MOF on 6 November 2003, MOF agreed to capitalise dividends receivable from the Bank amounting to RMB150 million by subscribing 75 million shares at RMB2 per share. Share capital and capital surplus were increased by RMB75 million and RMB75 million respectively.

Note 3:

The Group changed its accounting policy on property and equipment on 31 December 2003 from a cost basis to a valuation basis, and accordingly recorded a revaluation surplus amounting to RMB4,862 million. MOF has mandated that RMB4,381 million be regarded as capital contribution to the Bank in the notice Cai Jin [2003] No. 103 "The approval on revaluation increase of property and equipment of Bank of Communications Co., Ltd." on 26 December 2003. Accordingly, the Bank recorded a transfer of revaluation reserve to capital surplus during the year.

Note 4:

On June 24, 2004, the PBOC, with the approval of the State Council, issued Yin Fu [2004] "Approval on the Packaged Capital Restructuring Program of Bank of Communications by the PBOC" (the "Restructuring Package"), approving a series of financial restructuring transactions (each, individually, a "Restructuring Transaction") intended to increase the Bank's capital and resolve certain impaired loans. The detailed impact of the Restructuring Package is stated in Note 1.

Note 5:

In accordance with Cai Jin [2004] No.57. "Notice on Financial Reform and Restructuring of the Bank of Communications Co., Ltd." issue by the MOF and the Bank's resolution on capital expansion, financial restructuring and foreign strategic investors approved in the annual general shareholder's meeting held on 20 June 2004, the Bank utilised its statutory reserves, discretionary reserves, statutory welfare reserves and capital surplus to offset against its accumulated losses as at 30 June 2004.

Generally, transactions of the following nature are recorded in the capital surplus:

(i) share premium arising from the issue of shares at prices in excess of their par value;
(ii) donations received; and
(iii) any other items required by the PRC regulations to be so treated.

Capital surplus can be utilized to offset prior years' accumulated losses, for the issue of bonus shares or for increasing paid-up capital as approved by the Directors.

## 30 RESERVES AND ACCUMULATED LOSSES

In accordance with the PRC legislation, 10% of the net profit of the Bank, as determined under the PRC accounting regulations, is required to be transferred to a non-distributable statutory reserve until such time when this reserve represents 50% of the share capital of the Bank.

Pursuant to the PRC regulations, the Bank is required to transfer 5% to 10% of its net income, as determined under the PRC accounting regulations, to the statutory welfare reserve. This fund can only be used to provide staff welfare facilities and other collective benefits to the Bank's employees. This fund is non-distributable other than in liquidation.

Pursuant to the PRC regulations, the appropriation of profits to the discretionary reserve and the distribution of dividends in each year are based on the recommendations of the Directors and are subject to the passing of resolutions to be considered at the Bank's Annual General Meeting to be held subsequent to each year end.

## 31 DIVIDENDS

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Declared in the year | 3,011 | 636 | — |
| Rate of dividend proposed on ordinary shares (Rmb/per share) | 0.065 | 0.04 | — |
| Paid in the year | 758 | 723 | 8 |
| Capitalization of declared dividends without cash movements | 2,006 | 150 | — |

Under PRC Company Law and the Bank's Articles of Association, the net profit after tax as reported in the PRC statutory financial statements can only be distributed as dividends after allowances for the following:

(i) Making up prior year's cumulative losses, if any;

(ii) Allocations to the non-distributable statutory accumulation reserve of 10% of the net profit of the Bank;

(iii) Allocation to the statutory welfare reserve of 5% to 10% of the net profit of the Bank;

(iv) Allocations to the discretionary revenue reserve fund if approved by the Bank's Annual General Meeting. These funds forms part of the shareholder's equity.

In accordance with the relevant regulations, after the Bank's initial public offering, the net profit after tax of the Group for the purpose of profit distribution is deemed to be the lesser of (i) the retained profits determined in accordance with PRC GAAP and (ii) the retained profit determined in accordance with IFRS.

## 32 CONTINGENT LIABILITIES AND COMMITMENTS

### Contingent liabilities

The following tables indicate the contractual amounts of the Group's and the Bank's off-balance sheet financial instruments which the Group commits to extend to customers:

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Guarantees | 14,657 | 21,912 | 30,867 |
| Issuance of letters of credit | 14,621 | 21,943 | 25,654 |
| Acceptances | 44,674 | 73,017 | 103,348 |
| Other commitments with an original maturity of | | | |
| – under 1 year or which are unconditionally cancellable | 2,626 | 1,006 | 2,573 |
| – 1 year and over | 7,290 | 3,681 | 5,193 |
| | 83,868 | 121,559 | 167,635 |

**Capital expenditure commitments**

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Capital expenditure commitments for buildings | 233 | 215 | 490 |

**Operating lease commitments**

Where the Group is the lessee, the future minimum lease payments under non-cancelable operating leases in respect of buildings are as follows:

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Not later than 1 year | 598 | 559 | 499 |
| Later than 1 year and not later than 5 years | 1,273 | 1,229 | 1,141 |
| Later than 5 years | 589 | 574 | 532 |
| | 2,460 | 2,362 | 2,172 |

**Legal proceedings**

A number of legal proceedings are initiated by third parties against the Group as defendant. The total outstanding claims at end of each year are as follows:

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Outstanding claims | 2,185 | 2,174 | 2,601 |
| Provision for losses | — | 356 | 989 |

The Group evaluates the losses, if any, arising from outstanding claims made by third parties on a regular basis. Provision for losses is made by the Group in the financial statements when it is probable that an outflow of resources is required to settle the claims. The Group believes that the provision made is adequate to meet the settlement obligations.

## 33 ASSETS PLEDGED

Assets are pledged as collateral under repurchase agreements with other banks and financial institutions and for security deposits relating to local futures, options and stock exchange memberships. Mandatory reserve deposits are also held with local central banks in accordance with statutory requirements. These deposits are not available to finance the Group's day to day operations.

***Group and Bank***

| | Pledged Assets as at 31 December | | | Related Liabilities as at 31 December | | |
|---|---|---|---|---|---|---|
| | 2002 | 2003 | 2004 | 2002 | 2003 | 2004 |
| Balances with central banks | 34,357 | 50,246 | 61,670 | — | — | — |
| Investment securities | — | 450 | 400 | — | 450 | 400 |
| | 34,357 | 50,696 | 62,070 | — | 450 | 400 |

## 34 CREDIT RISK WEIGHTED AMOUNT OF OFF BALANCE SHEET EXPOSURES

***Group and Bank***

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Contingent liabilities and commitments | 55,048 | 105,200 | 124,156 |

The credit risk weighted amount refers to the amount as computed in accordance with the Hong Kong Banking Ordinance and depends on the status of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% for contingent liabilities and commitments.

The above credit risk weighted amounts are calculated in accordance with the formula promulgated by the HKMA because there are no relevant standards prescribed by IFRS (note 1).

The credit risk weighted amounts stated above have taken into account of the effects of bilateral netting arrangements.

note 1:

The credit risk weighted amount as set out below refers to the amount as computed in accordance with the formula promulgated by the China Banking Regulatory Commission.

**Group and Bank**

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Contingent liabilities and commitments | 44,213 | 81,966 | 124,406 |

## 35 NOTES TO CONSOLIDATED CASH FLOW STATEMENT

*(a) Analysis of changes in financing during the year*

| | Dividends | Share capital | Capital surplus | Subordinated term debt |
|---|---|---|---|---|
| At 1 January 2002 | 139 | 15,910 | 5,455 | — |
| Net cash inflow/(outflow) from financing | (758) | 120 | 120 | — |
| Capitalisation of dividends payable | (2,006) | 1,003 | 1,003 | — |
| Dividends | 3,011 | — | — | — |
| Donation | — | — | 1 | — |
| At 31 December 2002/1 January 2003 | 386 | 17,033 | 6,579 | — |
| Net cash inflow/(outflow) from financing | (723) | — | — | — |
| Capitalisation of dividends payable | (150) | 75 | 75 | — |
| Capitalization of revaluation surplus | — | — | 4,381 | — |
| Dividends | 636 | — | — | — |
| At 31 December 2003/1 January 2004 | 149 | 17,108 | 11,035 | — |
| Impact of a Restructuring Transaction on capital surplus (Note 1) | — | — | (2,763) | — |
| Reserves offset against accumulated losses | — | — | (9,035) | — |
| Net cash inflow/(outflow) from financing | (8) | 21,962 | 11,635 | 12,000 |
| At 31 December 2004 | 141 | 39,070 | 10,872 | 12,000 |

*(b) Analysis of the balance of cash and cash equivalents*

For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances with original maturities of less than 90 days, used for the purpose of meeting short-term cash commitments:

| | As at 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Cash and balances with central banks (Note 14) | 48,953 | 62,826 | 66,831 |
| Due from other banks and financial institutions (Note 15) | 4,217 | 14,462 | 8,926 |
| | 53,170 | 77,288 | 75,757 |

## 36 PRINCIPAL SUBSIDIARIES

*(a) Particulars of the principal subsidiaries are as follows:*

| Name of subsidiaries | Place of incorporation and operation | Date of incorporation | Issued and fully paid up share capital | Group equity interest % | Principal activities |
|---|---|---|---|---|---|
| Amiwell Company Limited | Hong Kong | 18 Mar 1980 | HKD2 | 100 | Property holding and investment |
| Bank of Communications Trustee Limited | Hong Kong | 13 Oct 1981 | HKD50,000,000 | 100 | Trustee Service |
| Bank of Communications (Nominee) Company Limited | Hong Kong | 21 Aug 1981 | HKD200,000 | 100 | Investment holding |
| BCOM Finance (Hong Kong) Limited | Hong Kong | 13 Mar 1979 | HKD90,000,000 | 100 | Deposit taking |
| BCOM Securities Company Limited | Hong Kong | 3 Jun 1998 | HKD175,000,000 | 100 | Security dealing and brokerage |
| China Communications Insurance Company Limited | Hong Kong | 1 Nov 2000 | HKD250,000,000 | 100 | General insurance and reinsurance |
| City Wisdom Limited | Hong Kong | 19 Jul 2000 | HKD10,000 | 100 | Property holding |
| Eastern Sky Limited | Hong Kong | 21 Aug 2000 | HKD10,000 | 100 | Property development |
| Expectation Investment Limited | Hong Kong | 29 Jan 1997 | HKD2 | 100 | Investment holding |
| Kiu Fai Company Limited | Hong Kong | 18 Mar 1967 | HKD3,000,000 | 100 | Property holding and investment holding |
| Right Master Investment Limited | Hong Kong | 23 Dec 1998 | HKD10,000 | 100 | Property development |
| Star Wealthy Secretarial Company Limited | Hong Kong | 23 Aug 1999 | HKD2,000,000 | 100 | Investment holding |
| Unique Profit Limited | Hong Kong | 12 Jun 1998 | HKD10,000 | 100 | Property holding |
| Bank of Communications Charitable Foundation Limited | Hong Kong | 19 Jun 2002 | — | 100 | Charity fund |
| Bank of Communications Finance Building Company Limited | PRC | 16 Sep 1992 | USD80,000,000 | 100 | Property development |
| Creative Mart Limited* | Hong Kong | 12 May 1999 | HKD100 | 100 | Property development |
| Chiao Tung Developments Limited* | Hong Kong | 5 Feb 1985 | HKD50,000,000 | 100 | Investment holding |
| Career Computer (Shenzhen) Company Limited* | PRC | 22 Dec 1997 | USD3,000,000 | 100 | Development of computer software and hardware, electronic equipments and communication network |

* Indirectly held by the Bank

All above principal subsidiaries are private companies.

For the year ended 31 December 2002 or 31 March 2003, all principal subsidiaries incorporated in Hong Kong as stated above were audited by Deloitte Touche Tohmatsu.

For the year ended 31 December 2003 or 31 March 2004, all principal subsidiaries incorporated in Hong Kong as stated above were audited by KPMG.

For the years ended 31 December 2002, 2003 and 2004, Career Computer (Shenzhen) Company Limited was audited by Shenzhen Peng Cheng CPAs Limited 深圳鵬程會計師事務所.

Bank of Communications Finance Building Company Limited was audited by Shanghai Shangkuai CPAs 上海上會會計師事務所 for the years ended 31 December 2002 and 2003, and it was liquidated subsequently.

*(b) Investment costs and balances with subsidiaries:*

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Investment cost–subsidiaries | 1,512 | 1,426 | 1,210 |
| Amount due from subsidiaries | 1,124 | 1,368 | 1,262 |
| Amount due to subsidiaries | (238) | (592) | (1,196) |
| Total | 2,398 | 2,202 | 1,276 |

## 37 RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. The Group is subject to the control of the State Council of the PRC Government through the MOF. In accordance with a specific exemption in IAS, the Group does not accumulate or disclose transactions with other PRC Government owned or controlled enterprises as related party transactions.

**Transactions with the MOF**

The Group enters into banking transactions with the MOF in the normal course of business. These include the purchase and redemption of investment securities issued by the MOF. The volumes of related party transactions, outstanding balances at the year end, and related income for the year are as follows:

**Investment securities**

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Purchase during the year | 13,280 | 13,213 | 16,634 |
| Redemption during the year | 6,249 | 7,265 | 8,305 |
| Outstanding at end of the year | 45,364 | 50,023 | 59,281 |
| Interest income | 1,861 | 1,940 | 2,364 |

Other than the abovementioned banking transactions between the Group and the MOF, the Group has also entered into capital transactions with the MOF during the Relevant Periods as set out in Notes 1 and 29.

**Transactions with directors and senior management**

The Group enters into banking transactions with directors and senior management in the normal course of business. These include loans and deposits, which are carried out at rates charged to third party customers of the Company except that loans and deposits have been made to and taken from senior management of the Hong Kong branch at preferential rates. The volumes of related party transactions during each of the years ended 31 December 2002, 2003 and 2004, outstanding balances at the balance sheet date are as follows:

**Loans**

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Outstanding at beginning of the year | 1 | 5 | 4 |
| Granted during the year | 6 | 4 | 8 |
| Repaid during the year | (3) | (5) | (3) |
| Outstanding at end of the year | 4 | 4 | 9 |
| Maximum aggregate amount of relevant loans outstanding during the year | 6 | 8 | 11 |

No interest income and allowance for impairment have been recognised in respect of loans granted to directors and senior management.

**Deposits**

| | Year ended 31 December | | |
|---|---|---|---|
| | 2002 | 2003 | 2004 |
| Outstanding at beginning of the year | 10 | 16 | 18 |
| Deposited during the year | 40 | 17 | 92 |
| Repaid during the year | (34) | (15) | (81) |
| Outstanding at end of the year | 16 | 18 | 29 |
| Interest expense on deposits | 1 | — | 1 |

**Transactions with HSBC**

On 18 August 2004, HSBC subscribed 7,775 million shares and became the second largest shareholder of the Bank (Notes 1 and 29). Transactions between the Group and HSBC are mainly banking activities at rates charged to third party customers of the Group. Detail transaction volumes since the above share acquisition are set below:

| Balance sheet items: | As at 31 December 2004 |
|---|---|
| Placement with HSBC | 100 |
| Deposits from HSBC | 34 |
| Loans from HSBC | 1,184 |
| Investment securities issued by HSBC | 414 |
| Interest payable | 1 |

| Profit and loss items: | Period from 18 August to 31 December 2004 |
|---|---|
| Interest income | 6 |
| Interest expense | 6 |

| Off-balance sheet exposures: | As at 31 December 2004 |
|---|---|
| Guarantees | 8 |
| Issuance of letters of credit | 17 |
| Derivative transactions unsettled | 10,943 |

## 38 SEGMENTAL INFORMATION

(a) The following table sets out the segmental information of the Group's operating results, assets and liabilities. The geographical segments are:

(i) Northern China – Including the following provinces: Beijing, Tianjin, Hebei, Shanxi, Inner Mongolia;

(ii) North Eastern China – Including the following provinces: Liaoning, Jilin, Heilongjiang;

(iii) Eastern China – Including head office and the following provinces: Shanghai, Jiangsu, Zhejiang, Anhui, Fujian, Jiangxi and Shandong;

(iv) Central & Southern China – Including the following provinces: Henan, Hunan, Hubei, Guangdong, Guangxi, Hainan;

(v) Western China – Including the following provinces: Chongqing, Sichuan, Guizhou, Yunnan, Tibet, Shanxi, Gansu, Qinghai, Ningxia and Xinjiang;

(vi) Overseas – Including the following branches, representative offices and overseas subsidiaries: Hong Kong, New York, Singapore and Tokyo.

*a) Geographical segment information*

| | Northern China | North-eastern China | Eastern China | Central & Southern China | Western China | Overseas | Eliminations & Consolidated | Group Total |
|---|---|---|---|---|---|---|---|---|
| **As at 31 December 2002** | | | | | | | | |
| **Assets** | | | | | | | | |
| Cash and balances with central banks | 7,988 | 4,228 | 57,718 | 8,685 | 4,389 | 302 | — | 83,310 |
| Due from other banks and financial institutions | 7,337 | 863 | 80,942 | 7,392 | 1,748 | 14,976 | (15,965) | 97,293 |
| Trading securities | — | — | — | — | — | 141 | — | 141 |
| Loans and advances to customers | 49,675 | 39,548 | 154,661 | 80,244 | 43,658 | 27,367 | — | 395,153 |
| Investment securities | | | | | | | | |
| – originated loans | 7,959 | 6,788 | 57,430 | 12,392 | 5,158 | 4,330 | — | 94,057 |
| – available-for-sale | 47 | 26 | 680 | 148 | 24 | 13,714 | — | 14,639 |
| – held-to-maturity | 156 | — | 6,400 | 44 | — | 1,342 | — | 7,942 |
| Other assets | 13,021 | 5,211 | 7,305 | 8,169 | 3,673 | 3,974 | (1,885) | 39,468 |
| **Total assets** | 86,183 | 56,664 | 365,136 | 117,074 | 58,650 | 66,146 | (17,850) | 732,003 |
| **Liabilities** | | | | | | | | |
| Due to other banks and financial institutions | (1,856) | (2,477) | (20,425) | (4,885) | (865) | (3,758) | 9,584 | (24,682) |
| Trading liabilities | — | — | — | — | — | (180) | — | (180) |
| Due to customers | (98,888) | (74,822) | (252,369) | (137,989) | (75,579) | (49,506) | — | (689,153) |
| Other liabilities | (2,482) | (476) | (764) | (949) | (553) | (11,596) | 8,266 | (8,554) |
| **Total liabilities** | (103,226) | (77,775) | (273,558) | (143,823) | (76,997) | (65,040) | 17,850 | (722,569) |
| **Net on balance sheet position** | (17,043) | (21,111) | 91,578 | (26,749) | (18,347) | 1,106 | — | 9,434 |
| **Acquisition cost of property and equipment ("PPE") and intangible assets** | 258 | 442 | 1,179 | 585 | 212 | 76 | — | 2,752 |
| Off balance sheet and credit commitments | 14,068 | 4,347 | 29,088 | 14,336 | 6,670 | 15,359 | — | 83,868 |
| Interest income | 3,463 | 2,295 | 14,595 | 5,173 | 2,837 | 2,032 | (4,517) | 25,878 |
| Interest expense | (1,247) | (1,190) | (7,292) | (2,046) | (994) | (1,018) | 4,517 | (9,270) |
| **Net interest income** | 2,216 | 1,105 | 7,303 | 3,127 | 1,843 | 1,014 | — | 16,608 |
| Fee and commission income | 127 | 77 | 397 | 171 | 78 | 217 | — | 1,067 |
| Fee and commission expense | (30) | (25) | (116) | (36) | (19) | (28) | — | (254) |
| **Net fee and commission income** | 97 | 52 | 281 | 135 | 59 | 189 | — | 813 |
| Dividend income | — | — | 44 | — | — | 49 | — | 93 |
| Gains less losses arising from trading activities | 60 | 20 | 181 | 52 | 12 | 39 | — | 364 |
| Gains less losses arising from investment securities | — | — | — | — | — | 8 | — | 8 |
| Other operating income | 16 | 18 | 151 | 55 | 15 | 31 | — | 286 |
| Impairment losses on loans and advances | 233 | (1,350) | (167) | 553 | 11 | (227) | — | (947) |
| Other operating expenses | (1,350) | (1,780) | (2,602) | (2,721) | (1,540) | (742) | — | (10,735) |
| **Operating profit before tax** | 1,272 | (1,935) | 5,191 | 1,201 | 400 | 361 | — | 6,490 |
| Income tax | (66) | (6) | (1,768) | (97) | (66) | (58) | — | (2,061) |
| **Net profit for the year** | 1,206 | (1,941) | 3,423 | 1,104 | 334 | 303 | — | 4,429 |
| **Depreciation and amortization of PPE and intangible assets** | 154 | 280 | 780 | 278 | 143 | 82 | — | 1,717 |

| | Northern China | North-eastern China | Eastern China | Central & Southern China | Western China | Overseas | Eliminations & Consolidated | Group Total |
|---|---|---|---|---|---|---|---|---|
| **As at 31 December 2003** | | | | | | | | |
| **Assets** | | | | | | | | |
| Cash and balances with central banks | 6,714 | 5,891 | 82,531 | 10,790 | 6,384 | 762 | — | 113,072 |
| Due from other banks and financial institutions | 16,079 | 781 | 45,368 | 2,654 | 896 | 40,277 | (6,120) | 99,935 |
| Trading securities | — | — | — | — | — | 3,106 | — | 3,106 |
| Loans and advances to customers | 71,793 | 44,707 | 209,885 | 106,201 | 53,192 | 29,445 | 1,452 | 516,675 |
| Investment securities | | | | | | | | |
| – originated loans | 8,922 | 7,072 | 64,859 | 13,399 | 5,932 | 4,486 | — | 104,670 |
| – available-for-sale | 242 | 600 | 19,861 | 1,059 | 410 | 14,515 | — | 36,687 |
| – held-to-maturity | 365 | — | 4,469 | 43 | 1 | 1,843 | — | 6,721 |
| Other assets | 8,469 | 4,727 | 16,764 | 7,683 | 4,730 | 6,217 | (3,536) | 45,054 |
| **Total assets** | 112,584 | 63,778 | 443,737 | 141,829 | 71,545 | 100,651 | (8,204) | 925,920 |
| **Liabilities** | | | | | | | | |
| Due to other banks and financial institutions | (1,234) | (1,697) | (9,622) | (3,348) | (804) | (7,360) | 2,915 | (21,150) |
| Trading liabilities | — | — | — | — | — | (3,463) | — | (3,463) |
| Due to customers | (133,272) | (87,936) | (315,417) | (169,246) | (89,424) | (78,864) | — | (874,159) |
| Other liabilities | (2,021) | (832) | 478 | (1,775) | (959) | (9,247) | 5,289 | (9,067) |
| **Total liabilities** | (136,527) | (90,465) | (324,561) | (174,369) | (91,187) | (98,934) | 8,204 | (907,839) |
| **Net on balance sheet position** | (23,943) | (26,687) | 119,176 | (32,540) | (19,642) | 1,717 | — | 18,081 |
| **Acquisition cost of PPE and intangible assets** | 373 | 334 | 1,019 | 553 | 194 | 61 | — | 2,534 |
| Off balance sheet and credit commitments | 22,879 | 7,543 | 47,150 | 24,090 | 8,703 | 11,194 | — | 121,559 |
| Interest income | 4,291 | 2,775 | 15,919 | 6,126 | 3,126 | 1,918 | (4,176) | 29,979 |
| Interest expense | (1,507) | (1,286) | (7,477) | (2,230) | (1,131) | (850) | 4,176 | (10,305) |
| **Net interest income** | 2,784 | 1,489 | 8,442 | 3,896 | 1,995 | 1,068 | — | 19,674 |
| Fee and commission income | 153 | 103 | 518 | 243 | 97 | 304 | — | 1,418 |
| Fee and commission expense | (33) | (27) | (89) | (57) | (19) | (36) | — | (261) |
| **Net fee and commission income** | 120 | 76 | 429 | 186 | 78 | 268 | — | 1,157 |
| Dividend income | 1 | — | 62 | — | — | 19 | — | 82 |
| Gains less losses arising from trading activities | 91 | 35 | 222 | 67 | 16 | 71 | — | 502 |
| Gains less losses arising from investment securities | — | — | — | — | — | (2) | — | (2) |
| Other operating income | 14 | 7 | 166 | 56 | 36 | 248 | — | 527 |
| Impairment losses on loans and advances | (566) | (957) | (1,432) | (1,263) | (686) | (211) | — | (5,115) |
| Other operating expenses | (1,290) | (1,929) | (4,916) | (2,661) | (1,277) | (617) | — | (12,690) |
| **Operating profit before tax** | 1,154 | (1,279) | 2,973 | 281 | 162 | 844 | — | 4,135 |
| Income tax | (574) | (148) | 1,914 | (508) | (265) | (178) | — | 241 |
| **Net profit for the year** | 580 | (1,427) | 4,887 | (227) | (103) | 666 | — | 4,376 |
| **Depreciation and amortization of PPE and intangible assets** | 172 | 205 | 664 | 350 | 199 | 80 | — | 1,670 |

| | Northern China | North-eastern China | Eastern China | Central & Southern China | Western China | Overseas | Eliminations & Consolidated | Group Total |
|---|---|---|---|---|---|---|---|---|
| **As at 31 December 2004** | | | | | | | | |
| **Assets** | | | | | | | | |
| Cash and balances with central banks | 7,930 | 5,090 | 96,658 | 13,494 | 4,870 | 459 | — | 128,501 |
| Due from other banks and financial institutions | 10,518 | 425 | 44,472 | 2,730 | 1,841 | 30,604 | (1,667) | 88,923 |
| Trading securities | — | — | 46 | — | — | 1,487 | — | 1,533 |
| Loans and advances to customers | 104,316 | 49,447 | 258,112 | 125,272 | 59,325 | 33,976 | 1,164 | 631,612 |
| Investment securities | | | | | | | | |
| – originated loans | 11,515 | 10,563 | 103,547 | 16,731 | 8,728 | 8,742 | — | 159,826 |
| – available-for-sale | 7,747 | 1,398 | 56,781 | 3,055 | 1,181 | 19,866 | — | 90,028 |
| – held-to-maturity | — | — | — | — | — | — | — | — |
| Other assets | 10,377 | 8,061 | 24,345 | 13,319 | 7,419 | 10,827 | (29,316) | 45,032 |
| **Total assets** | 152,403 | 74,984 | 583,961 | 174,601 | 83,364 | 105,961 | (29,819) | 1,145,455 |
| **Liabilities** | | | | | | | | |
| Due to other banks | (3,950) | (2,694) | (12,699) | (4,342) | (940) | (7,921) | 835 | (31,711) |
| Trading liabilities | — | — | (95) | — | — | (4,991) | — | (5,086) |
| Due to customers | (173,255) | (99,297) | (378,278) | (204,813) | (101,139) | (74,897) | 1,738 | (1,029,941) |
| Other liabilities | (4,111) | (2,841) | (21,056) | (5,508) | (2,856) | (16,038) | 27,246 | (25,164) |
| **Total liabilities** | (181,316) | (104,832) | (412,128) | (214,663) | (104,935) | (103,847) | 29,819 | (1,091,902) |
| **Net on balance sheet position** | (28,913) | (29,848) | 171,833 | (40,062) | (21,571) | 2,114 | — | 53,553 |
| **Acquisition cost of PPE and intangible assets** | 603 | 368 | 1,048 | 705 | 436 | 119 | — | 3,279 |
| Off balance sheet and credit commitments | 32,995 | 8,090 | 70,981 | 29,505 | 10,759 | 15,305 | — | 167,635 |
| Interest income | 6,135 | 3,296 | 19,996 | 7,575 | 3,658 | 2,090 | (4,398) | 38,352 |
| Interest expense | (2,178) | (1,406) | (9,082) | (2,504) | (1,317) | (1,071) | 4,398 | (13,160) |
| **Net interest income** | 3,957 | 1,890 | 10,914 | 5,071 | 2,341 | 1,019 | — | 25,192 |
| Fee and commission income | 232 | 150 | 711 | 367 | 138 | 398 | — | 1,996 |
| Fee and commission expense | (42) | (31) | (105) | (70) | (23) | (50) | — | (321) |
| **Net fee and commission income** | 190 | 119 | 606 | 297 | 115 | 348 | — | 1,675 |
| Dividend income | — | 7 | 16 | 1 | — | 31 | — | 55 |
| Gains less losses arising from trading activities | 125 | 36 | 177 | 94 | 19 | (126) | — | 325 |
| Gains less losses arising from investment securities | 1 | — | 73 | — | — | 3 | — | 77 |
| Other operating income | 56 | 52 | 138 | 80 | 29 | 278 | — | 633 |
| Impairment losses on loans and advances | (680) | (952) | (864) | 85 | (604) | (200) | — | (3,215) |
| Other operating expenses | (2,062) | (1,796) | (6,708) | (3,423) | (1,753) | (1,250) | — | (16,992) |
| **Operating profit before tax** | 1,587 | (644) | 4,352 | 2,205 | 147 | 103 | — | 7,750 |
| Income tax | (872) | (207) | (3,976) | (730) | (361) | — | — | (6,146) |
| **Net profit for the period** | 715 | (851) | 376 | 1,475 | (214) | 103 | — | 1,604 |
| **Depreciation and amortization of PPE and intangible assets** | 290 | 321 | 1,151 | 464 | 285 | 112 | — | 2,623 |

*b) Business segment information*

The Group is engaged predominantly in banking and related financial activities. It comprises retail banking, corporate banking, treasury and other classes of business.

Corporate banking mainly comprises corporate loans, bills, trade finance, corporate deposits and remittance. Retail banking mainly comprises retail loans, retail deposits, credit card and remittance. Treasury mainly comprises money market placements and takings, investment in securities, and securities sold subject to linked repurchase agreements ('repos'). The 'Others' business mainly comprises other items which cannot be categorized as above business segments.

| | Corporate | Retail | Treasury | Others | Total |
|---|---|---|---|---|---|
| **As at 31 December 2002** | | | | | |
| Total carrying amount of segment assets | 360,920 | 35,964 | 295,904 | 39,215 | 732,003 |
| Segment revenue | 19,393 | 1,265 | 6,752 | 286 | 27,696 |
| Depreciation and amortization of PPE and intangible assets | — | — | — | 1,717 | 1,717 |
| Acquisition cost of PPE and intangible assets | — | — | — | 2,752 | 2,752 |
| **As at 31 December 2003** | | | | | |
| Total carrying amount of segment assets | 459,689 | 59,573 | 359,436 | 47,222 | 925,920 |
| Segment revenue | 22,143 | 2,492 | 7,348 | 523 | 32,506 |
| Depreciation and amortization of PPE and intangible assets | — | — | — | 1,670 | 1,670 |
| Acquisition cost of PPE and intangible assets | — | — | — | 2,534 | 2,534 |
| **As at 31 December 2004** | | | | | |
| Total carrying amount of segment assets | 524,732 | 90,780 | 488,575 | 41,368 | 1,145,455 |
| Segment revenue | 26,226 | 4,187 | 10,324 | 701 | 41,438 |
| Depreciation and amortization of PPE and intangible assets | — | — | — | 2,623 | 2,623 |
| Acquisition cost of PPE and intangible assets | — | — | — | 3,279 | 3,279 |

## 39 DISPOSAL OF IMPAIRED LOANS

The Transferred Loans related to both the Bank and the Group are summarized below.

***Group***

| | Loans to customers | Loans to subsidiaries | Total |
|---|---|---|---|
| Impaired loans: | | | |
| Doubtful loans | 40,085 | 1,330 | 41,415 |
| Loss loans | 8,276 | 24 | 8,300 |
| Loss loans written off previously but not yet approved by the tax authority | 3,305 | — | 3,305 |
| | 51,666 | 1,354 | 53,020 |
| Less: Allowance for impairment losses on loans and advances (Note18(b)) | (26,935) | — | (26,935) |
| Allowance for impairment losses already written off | (3,305) | — | (3,305) |
| | 21,426 | 1,354 | 22,780 |
| Fair value of consideration received, net of tax (Note 1) | | | (20,017) |
| Carrying value in excess of fair value of consideration received | | | 2,763 |

***Bank***

| | Loans to customers | Loans to subsidiaries | Total |
|---|---|---|---|
| Impaired loans: | | | |
| Doubtful loans | 40,085 | 1,330 | 41,415 |
| Loss loans | 8,276 | 24 | 8,300 |
| Loss loans written off previously but not yet approved by the tax authority | 3,305 | — | 3,305 |
| | 51,666 | 1,354 | 53,020 |
| Less: Allowance for impairment losses on loans and advances (Note18(b)) | (26,935) | — | (26,935) |
| Allowance for impairment losses on loans to subsidiaries | — | (892) | (892) |
| Allowance for impairment losses already written off | (3,305) | — | (3,305) |
| | 21,426 | 462 | 21,888 |
| Fair value of consideration received, net of tax (Note 1) | | | (20,017) |
| Carrying value in excess of fair value of consideration received | | | 1,871 |

**BANK OF COMMUNICATIONS CO., LTD.**

**SECTION VII: SUBSEQUENT ACCOUNTS**
(All amounts expressed in millions of RMB unless otherwise stated.)

## VII SUBSEQUENT ACCOUNTS

No audited accounts of the Group, the Bank or any of its subsidiaries have been prepared in respect of any period subsequent to 31 December 2004 up to the date of this report. Save as disclosed in this report, no dividend or other distribution has been declared, made or paid by the Bank or any of its subsidiaries in respect of any period subsequent to 31 December 2004.

Yours faithfully
**PricewaterhouseCoopers**
Certified Public Accountants
Hong Kong