Notes to the Consolidated Financial Statements

(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 People's Republic of China ("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 People's Bank of China ("PBOC"). Headquartered in Shanghai, the Bank operates 92 city level branches in the PRC. In addition, the Bank has branches in Hong Kong, New York, Tokyo, Singapore and Seoul.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

A Basis of presentation

The consolidated financial statements of the Group has been prepared in accordance with the International Financial Reporting Standards ("IFRS") The consolidated financial statements 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 at fair value through profit or loss, property and equipment, investment properties and all derivative contracts, which are revalued at fair value.

Critical accounting estimates and judgments in applying accounting policies

The preparation of financial statements 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.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

A Basis of presentation *(Continued)*

(1) Impairment losses on loans and advances

The Group reviews its loan portfolios to assess impairment on a quarterly basis, unless known circumstances indicate that impairment may have occurred as of an interim date. In determining whether an impairment loss should be recorded in the consolidated income statement, the Group makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group (e.g. payment delinquency or default), or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when estimating expected future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(2) Fair value of financial instruments

The fair values of financial instruments that are not quoted in active markets are determined by using valuation techniques. Valuation techniques used include discounted cash flows analysis and models. To the extent practical, models use only observable data, however areas such as credit risk (both own and counterparty's), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect reported fair value of financial instruments.

(3) Income taxes

The Group is subject to income taxes in numerous jurisdictions; principally, however in the Chinese Mainland and Hong Kong. Significant estimates are required in determining the provision for income taxes. There are certain transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. In particular, the deductibility of certain items in the Chinese Mainland is subject to government approval. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred income tax provisions in the period during which such a determination is made.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

A Basis of presentation *(Continued)*

(4) Provision for outstanding litigation

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.

The Group adopted the following IAS and IFRS, which are effective for accounting periods commencing on or after 1 January 2005:

IAS 1 (revised 2003)	Presentation of Financial Statements
IAS 8 (revised 2003)	Accounting Policies, Changes in Accounting Estimates and Errors
IAS 10 (revised 2003)	Events after the Balance Sheet Date
IAS 16 (revised 2003)	Property, Plant and Equipment
IAS 17 (revised 2003)	Leases
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 and Accounting for Investments in Subsidiaries
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
IAS 40 (revised 2003)	Investment Property
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 also early adopted relevant amendments to IAS 32, IAS 37, IAS 39 and IFRS 4 up to 18 August 2005. They are amendments on accounting treatments of a) Financial Guarantee Contracts, b) Cash Flow Hedge Accounting of Forecast Intragroup Transactions, and c) The Fair Value Option, which are effective for accounting periods commencing on or after 1 January 2006.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

A Basis of presentation *(Continued)*

The adoption of IAS 1, 8, 10, 16, 17, 21, 24, 27, 28, 32, 33, 40 (all revised 2003) and IFRS 2, 4, 5 (all issued 2004) did not result in changes to the Group's accounting policies. In summary:

– IAS 1, 8, 10, 16, 17, 27, 28, 32, 33, 40 (all revised 2003) and IFRS 2, 4, 5 (all issued 2004) had no material effect on the Group's policies.

– IAS 21 (revised 2003) had no material effect on the Group's policy. The functional currency of each of the consolidated entities has been re-evaluated based on the guidance to the revised standard.

  All the Group entities have the same functional currency as their measurement currency.

– IAS 24 (revised 2003) has affected the identification of related parties and some other related-party disclosures.

The adoption of IAS 39 (revised 2003) has resulted in a change in the accounting policy for financial assets, especially the accounting policy for investment securities-originated loans. Until 31 December 2004, debt securities that were purchased at original issuance without the intent to sell immediately or in the short term were classified as originated loans. In accordance with the provisions of IAS 39 (revised 2003), except for certain originated loans that are not quoted in an active market would be classified as "investment securities – loans and receivables", the originated loans should be classified as available-for-sale securities or trading securities according to the management's intention. The impact of the reclassification and its retrospective impact on the financial position of the Group at 1 January 2004 and 2005 are set out below:

	1 January 2005	1 January 2004
Decrease in originated loans	**(159,826)**	(104,670)
Increase in investment securities-available-for-sale	**125,495**	92,058
Increase in investment securities-loans and receivables	**31,205**	12,793
Increase in financial assets held for trading	**962**	–
(Decrease)/ Increase in revaluation reserve, net of tax	**(1,450)**	121
Increase in deferred tax assets/(liabilities)	**714**	(60)

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

A Basis of presentation *(Continued)*

The early adoption of amended IAS 32, IAS 37, IAS 39 and IFRS 4 did not result in changes to the Group's current accounting policies, but provide more specific guidance on the accounting of financial guarantee contracts.

There was no significant impact on opening retained earnings at 1 January 2005 and 2004 from the adoption of any of the above-mentioned standards.

Except for the adoption of the above IAS and IFRS which are effective for accounting periods commencing on or after 1 January 2005 and the early adoption of amended IAS32, IAS37, IAS39 and IFRS4, the accounting policies and basis of preparation of the financial statements of the Group are consistent with those adopted in the Group's 2004 annual accounts.

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.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

C Derivative financial instruments

Derivative financial instruments including foreign exchange contracts, currency and interest rate swaps, and other derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured 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.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e., the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Group recognises profits on day 1.

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 the profit and loss account. These embedded derivatives are measured at fair value with changes in fair value recognised in the profit and loss account.

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.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

D Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short team or if so designated by management. Derivatives are also categorized as held for trading unless they are designated as hedges.

Financial assets held for trading include 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. These securities are initially recognised at fair value and subsequently re-measured at fair value based on quoted bid prices. These securities are derecognised when the rights to receive cash flows from the trading securities have expired or when the Group has transferred substantially all risks and rewards of ownership. 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.

E 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.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

F 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.

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 financial assets held for 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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

H Investment securities

The Group classifies its investment securities in the following categories: loans and receivables and available-for-sale securities. Management determines the classification of its investments at initial recognition. Due to a 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. After such reclassification of investment securities, the Group may not recognise any held-to-maturity securities in the following two financial years. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership. Investment securities are initially recognised at fair value plus transaction costs and subsequently they are measured as follows:

(1) Loans and receivables

Loans and receivables are non-derivative debt securities with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. After initial recognition, loans and receivables are carried at amortised cost using the effective interest method, less any impairment allowances.

(2) Available-for-sale

Available-for-sale investments are those 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. After initial recognition, the available-for-sale securities 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.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

H Investment securities *(Continued)*

(2) Available-for-sale (Continued)

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.

The Group assesses at each balance sheet date whether there is objective evidence that an investment security or group of investment securities is impaired. An investment security or a group of investment securities is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the security (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the investment security or group of investment securities that can be reliably estimated. 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. If an available-for-sale security is impaired, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the profit and loss account.

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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

l Loans and advances to customers 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 and advances originatedby 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.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

J Property and equipment

Subsequent to initial recognition, the Group adopts a revaluation policy 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.

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. The revaluation reserves are transferred directly to retained earnings when the relevant items of property and equipment are retired or disposed of.

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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

K Foreclosed assets

Foreclosed assets are 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 programs are recognised as an expense as incurred. However, expenditure that enhances or extends the performance of computer software program beyond their original specifications is recognised as 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.

The Group adopts the fair value model to account for its investment property. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. Where active market price 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.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

O Leases

The leases entered into by the Group as lessee or lessor have been determined to be 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) and amounts due from other banks and financial institutions 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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

R Deferred income taxes *(Continued)*

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 fair value, 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 financial guarantees and credit related commitments transactions and are disclosed as contingent liabilities and commitments.

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

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) Functional and presentation currency

The Group's presentation 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 functional currency"). The consolidated financial statements are presented in Renminbi which is the functional currency of the parent.

(2) Transactions and balances

Foreign currency transactions are translated into the functional 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 presentation 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.

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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

W Foreign currency translation *(Continued)*

(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 the proceeds received. They are recorded in loans and advances to customers in the balance sheet, which is amortised into profit and loss account ratably over the guarantee period. Subsequently, they are carried at the higher of amortised carrying value or the provision required to meet the Group's guarantee obligation. The changes in carrying value are recorded in the profit and loss account under fee and commission income.

Notes to the Consolidated Financial Statements (Continued)

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

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.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

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.

AD Comparative

Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year.

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, 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 an 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 loans and advances but also financial guarantees and credit related commitments such as letters of credit, 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.

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

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 similar credit risk as loans.

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

Geographical concentrations of assets, liabilities and financial guarantees and credit related commitments:

Group

	Total assets	Total liabilities	Financial guarantees and credit related commitments
As at 31 December 2005			
Mainland China	**1,326,468**	**1,246,177**	**227,747**
Hong Kong	**84,085**	**81,263**	**14,304**
Others	**12,886**	**12,853**	**3,859**
Total	**1,423,439**	**1,340,293**	**245,910**
As at 31 December 2004			
Mainland China	1,038,044	988,055	152,330
Hong Kong	92,180	89,900	12,532
Others	13,781	13,947	2,773
Total	1,144,005	1,091,902	167,635

Bank

	Total assets	Total liabilities	Financial guarantees and credit related commitments
As at 31 December 2005			
Mainland China	**1,326,026**	**1,244,705**	**227,747**
Hong Kong	**82,935**	**80,767**	**14,304**
Others	**12,886**	**12,853**	**3,859**
Total	**1,421,847**	**1,338,325**	**245,910**
As at 31 December 2004			
Mainland China	1,037,545	986,573	152,330
Hong Kong	91,369	89,343	12,532
Others	13,781	13,947	2,773
Total	1,142,695	1,089,863	167,635

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

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

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

Group and Bank

	31 December 2005	**%**	31 December 2004	%
Domestic regions				
– Jiangsu	**93,247**	**12**	80,331	13
– Shanghai	**86,122**	**11**	68,611	11
– Beijing	**84,298**	**11**	71,565	11
– Guangdong	**66,002**	**9**	53,294	8
– Zhejiang	**56,634**	**7**	45,964	7
– Shandong	**46,956**	**6**	36,071	6
– Henan	**29,867**	**4**	28,579	4
– Liaoning	**26,920**	**4**	25,153	4
– Others	**233,269**	**30**	192,764	30
Domestic regions total	**723,315**	**94**	602,332	94
Hong Kong and overseas countries	**46,225**	**6**	36,452	6
Interest receivables	**1,834**	**–**	1,274	–
Gross amount of loans and advances before allowance for impairment	**771,374**	**100**	640,058	100

A geographical region is reported where it contributes 4% and more 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 assets. The Group's financial guarantees and credit related commitments mainly comprise acceptances and credit related commitments (Note 33).

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

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

Group and Bank

	31 December 2005	**%**	31 December 2004	%
Corporate loans				
Manufacturing				
– Steel	**24,540**	**3**	19,267	3
– Machinery	**22,763**	**3**	18,711	3
– Electronics	**27,035**	**4**	24,001	4
– Petroleum and chemical	**32,585**	**4**	27,929	5
– Textile	**18,076**	**2**	18,850	3
– Other manufacturing	**85,360**	**11**	71,263	11
Trading	**72,977**	**10**	67,846	11
Real estate	**60,913**	**8**	63,321	10
Transportation	**63,544**	**8**	43,436	7
Utilities	**51,812**	**7**	36,125	6
Services	**56,024**	**7**	33,978	5
Construction	**25,958**	**3**	20,916	3
Educations and scientific research	**24,934**	**3**	26,367	4
Post and telecommunications	**15,768**	**2**	15,114	2
Agriculture	**4,698**	**1**	2,082	–
Non-banking financial institutions	**9,753**	**1**	8,063	1
Others	**7,871**	**1**	11,742	2
Corporate loans total	**604,611**	**78**	509,011	80
Mortgage loans	**78,264**	**10**	63,978	10
Medium-term and long-term working capital loans	**13,685**	**2**	10,821	2
Car loans	**3,961**	**1**	5,113	1
Short-term working capital loans	**5,087**	**1**	3,718	–
Loans secured by deposits	**1,093**	**–**	–	–
Credit card advances	**696**	**–**	107	–
Others	**1,267**	**–**	2,040	–
Individual loans total	**104,053**	**14**	85,777	13
Discounted bills	**60,876**	**8**	43,996	7
Interest receivables	**1,834**	**–**	1,274	–
	62,710	**8**	45,270	7
Gross amount of loans and advances before allowance for impairment	**771,374**	**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.

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

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

Group and Bank

	31 December 2005	31 December 2004
Domestic		
Corporate entities		
State owned entities	**198,276**	178,533
Collective owned entities	**11,022**	11,484
Private unlimited companies	**35,987**	26,429
Private limited companies	**163,673**	132,148
Joint stock companies	**63,723**	56,894
Foreign invested enterprises	**78,339**	66,677
Other domestic entities	**22,347**	13,252
	573,367	485,417
Individuals	**89,853**	73,406
	663,220	558,823
Hong Kong and Overseas		
Corporate entities	**31,244**	23,594
Individuals	**14,200**	12,371
	45,444	35,965
Discounted bills	**60,876**	43,996
Interest receivables	**1,834**	1,274
Gross amount of loans and advances before allowance for impairment	**771,374**	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 mirroring with PBOC suggested interest rates, and the Group manages its interest rate risks by maintaining a minimum level of net interest spread between interest bearing assets and liabilities. Starting from 21 July 2005, China has reformed by moving into a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies. The change of exchange regime lead to an increase in volatility, therefore, the Board sets limits on the level of exposure by the currency to monitor the Group's currency risk.

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

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 Group takes on exposure to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board set limits on the level of exposure by currency, which are monitored regularly. The tables below summarize the Group's exposure to foreign currency exchange rate risk at the end of each year. The tables show the Group'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 2005					
Assets					
Cash and balances with central banks	136,606	2,401	848	454	140,309
Due from other banks and financial institutions	106,166	47,152	7,571	9,212	170,101
Financial assets held for trading	1	1,399	1,423	405	3,228
Loans and advances to customers	678,966	41,804	32,967	5,036	758,773
Investment securities-loans and receivables	26,527	1,845	–	–	28,372
Investment securities-available-for-sale	251,083	21,233	6,644	7,011	285,971
Other assets, including deferred tax assets	38,059	(2,993)	3,362	(1,743)	36,685
Total assets	1,237,408	112,841	52,815	20,375	1,423,439
Liabilities					
Due to other banks and financial institutions	(62,974)	(14,613)	(3,916)	(2,591)	(84,094)
Financial liabilities held for trading	(12)	(3,962)	(5,548)	(33)	(9,555)
Due to customers	(1,091,403)	(73,122)	(41,085)	(15,229)	(1,220,839)
Other liabilities, including deferred tax liabilities	(22,973)	(1,400)	(974)	(458)	(25,805)
Total liabilities	(1,177,362)	(93,097)	(51,523)	(18,311)	(1,340,293)
Net position	60,046	19,744	1,292	2,064	83,146
Financial guarantees and credit related commitments	184,775	45,206	9,867	6,062	245,910

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

D Currency risk *(Continued)*

Bank

	RMB	US Dollars	HK Dollars	Others	Total
As at 31 December 2005					
Assets					
Cash and balances with central banks	136,605	2,401	569	454	140,029
Due from other banks and financial institutions	106,166	47,152	7,571	9,212	170,101
Financial assets held for trading	1	1,399	1,423	405	3,228
Loans and advances to customers	678,966	41,804	32,967	5,036	758,773
Investment securities-loans and receivables	26,527	1,845	–	–	28,372
Investment securities-available-for-sale	250,987	21,233	6,427	7,011	285,658
Investments in and due from subsidiaries	(851)	–	1,637	–	786
Other assets, including deferred tax assets	37,575	(2,993)	2,061	(1,743)	34,900
Total assets	1,235,976	112,841	52,655	20,375	1,421,847
Liabilities					
Due to other banks and financial institutions	(62,974)	(14,613)	(3,916)	(2,591)	(84,094)
Financial liabilities held for trading	(12)	(3,962)	(5,548)	(33)	(9,555)
Due to customers	(1,091,403)	(73,122)	(41,085)	(15,229)	(1,220,839)
Other liabilities, including deferred tax liabilities	(21,500)	(1,400)	(479)	(458)	(23,837)
Total liabilities	(1,175,889)	(93,097)	(51,028)	(18,311)	(1,338,325)
Net position	60,087	19,744	1,627	2,064	83,522
Financial guarantees and credit related commitments	184,775	45,206	9,867	6,062	245,910

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

D Currency risk *(Continued)*

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
Financial assets held for trading	–	904	1,351	240	2,495
Loans and advances to customers	563,158	36,544	25,619	6,291	631,612
Investment securities-loans and receivables	28,911	2,294	–	–	31,205
Investment securities-available-for-sale	176,836	20,544	10,756	7,387	215,523
Other assets, including deferred tax assets	39,528	3,464	4,568	(1,814)	45,746
Total assets	971,440	103,667	48,874	20,024	1,144,005
Liabilities					
Due to other banks and financial institutions	(18,437)	(5,623)	(2,471)	(5,180)	(31,711)
Financial liabilities held for trading	–	(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 position	38,158	11,383	(135)	2,697	52,103
Financial guarantees and credit related commitments	110,034	42,077	9,376	6,148	167,635

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

D Currency risk *(Continued)*

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
Financial assets held for trading	–	904	1,351	240	2,495
Loans and advances to customers	563,158	36,544	25,619	6,291	631,612
Investment securities-loans and receivables	28,911	2,294	–	–	31,205
Investment securities-available-for-sale	176,746	20,544	10,755	7,387	215,432
Investments in and due from subsidiaries	219	–	1,057	–	1,276
Other assets, including deferred tax assets	38,797	3,464	2,929	(1,814)	43,376
Total assets	970,838	103,667	48,166	20,024	1,142,695
Liabilities					
Due to other banks and financial institutions	(18,437)	(5,623)	(2,471)	(5,180)	(31,711)
Financial liabilities held for trading	–	(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 position	38,884	11,383	(132)	2,697	52,832
Financial guarantees and credit related commitments	110,034	42,077	9,376	6,148	167,635

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

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, the interest rate framework within mainland China is set by the PBOC. According to the PBOC regulations, the ceiling for loan interest rates was adjusted from 30% to 70% above the stipulated interest rates on 1 January 2004 and finally was removed on 29 October 2004, whilst the floor is 10% below the stipulated rates. 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 financial guarantees and credit related commitments 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 financial guarantees and credit related commitments businesses which are not based upon these basic interest rates is not expected to be significant.

The 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 exposure to interest rate risks. The tables show the Group'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.

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

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 2005							
Assets							
Cash and balances with central banks	131,290	–	–	–	–	9,019	140,309
Due from other banks and financial institutions	130,833	28,103	8,195	1,550	1,050	370	170,101
Financial assets held for trading	1,401	29	114	714	970	–	3,228
Loans and advances to customers	70,237	138,190	348,928	89,503	111,915	–	758,773
Investment securities							
– loans and receivables	175	878	1,683	25,152	484	–	28,372
– available-for-sale	10,655	37,026	80,170	105,177	52,824	119	285,971
Other assets, including deferred tax assets	–	–	–	–	–	36,685	36,685
Total assets	344,591	204,226	439,090	222,096	167,243	46,193	1,423,439
Liabilities							
Due to other banks and financial institutions	(59,381)	(13,930)	(8,718)	–	(2,002)	(63)	(84,094)
Financial liabilities held for trading	(2,286)	(5,215)	(389)	(1,616)	(6)	(43)	(9,555)
Due to customers	(791,021)	(108,106)	(218,811)	(76,517)	(1,914)	(24,470)	(1,220,839)
Other liabilities, including deferred tax liabilities	(215)	–	(292)	(12,000)	–	(13,298)	(25,805)
Total liabilities	(852,903)	(127,251)	(228,210)	(90,133)	(3,922)	(37,874)	(1,340,293)
Total interest sensitivity gap	(508,312)	76,975	210,880	131,963	163,321	8,319	83,146

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

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 2005							
Assets							
Cash and balances with central banks	131,290	–	–	–	–	8,739	140,029
Due from other banks and financial institutions	130,833	28,103	8,195	1,550	1,050	370	170,101
Financial assets held for trading	1,401	29	114	714	970	–	3,228
Loans and advances to customers	70,237	138,190	348,928	89,503	111,915	–	758,773
Investment securities							
– loans and receivables	175	878	1,683	25,152	484	–	28,372
– available-for-sale	10,655	37,026	80,170	105,177	52,511	119	285,658
Investments in and due from subsidiaries	–	–	60	6	–	720	786
Other assets, including deferred tax assets	–	–	–	–	–	34,900	34,900
Total assets	344,591	204,226	439,150	222,102	166,930	44,848	1,421,847
Liabilities							
Due to other banks and financial institutions	(59,381)	(13,930)	(8,718)	–	(2,002)	(63)	(84,094)
Financial liabilities held for trading	(2,286)	(5,215)	(389)	(1,616)	(6)	(43)	(9,555)
Due to customers	(791,021)	(108,106)	(218,811)	(76,517)	(1,914)	(24,470)	(1,220,839)
Other liabilities, including deferred tax liabilities	(215)	–	(292)	(12,000)	–	(11,330)	(23,837)
Total liabilities	(852,903)	(127,251)	(228,210)	(90,133)	(3,922)	(35,906)	(1,338,325)
Total interest sensitivity gap	(508,312)	76,975	210,940	131,969	163,008	8,942	83,522

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

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
Financial assets held for trading	972	267	148	268	840	–	2,495
Loans and advances to customers	53,203	126,571	288,067	77,151	86,620	–	631,612
Investment securities							
– loans and receivables	512	952	2,423	26,656	662	–	31,205
– available-for-sale	13,175	34,517	76,695	61,282	29,830	24	215,523
Other assets, including deferred tax assets	–	–	–	–	–	45,746	45,746
Total assets	264,376	173,433	367,863	165,657	117,952	54,724	1,144,005
Liabilities							
Due to other banks and financial institutions	(22,978)	(5,161)	(1,602)	–	(1,956)	(14)	(31,711)
Financial liabilities held for trading	(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	(466,786)	99,131	190,004	95,719	112,959	21,076	52,103

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

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
Financial assets held for trading	972	267	148	268	840	–	2,495
Loans and advances to customers	53,203	126,571	288,067	77,151	86,620	–	631,612
Investment securities							
– loans and receivables	512	952	2,423	26,656	662	–	31,205
– available-for-sale	13,084	34,517	76,695	61,282	29,830	24	215,432
Investments in and due from subsidiaries	–	–	60	225	–	991	1,276
Other assets, including deferred tax assets	–	–	–	–	–	43,376	43,376
Total assets	264,285	173,433	367,923	165,882	117,952	53,220	1,142,695
Liabilities							
Due to other banks and financial institutions	(22,978)	(5,161)	(1,602)	–	(1,956)	(14)	(31,711)
Financial liabilities held for trading	(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	(466,877)	99,131	190,064	95,944	112,959	21,611	52,832

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

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 2005				
Assets				
Cash and balances with central banks	**1.60%**	**0.17%**	**0.19%**	**0.00%**
Due from other banks and financial institutions	**1.64%**	**4.23%**	**4.08%**	**3.88%**
Loans and advances to customers	**5.34%**	**4.38%**	**5.55%**	**2.20%**
Investment securities				
– loans and receivables	**2.98%**	**5.15%**	**N/A**	**N/A**
– available-for-sale	**2.85%**	**4.32%**	**3.44%**	**3.79%**
Liabilities				
Due to other banks and financial institutions	**1.43%**	**4.20%**	**4.02%**	**2.04%**
Due to customers	**1.55%**	**3.33%**	**3.37%**	**2.53%**
As at 31 December 2004				
Assets				
Cash and balances with central banks	1.82%	0.06%	0.00%	N/A
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				
– loans and receivables	2.96%	4.41%	N/A	N/A
– available-for-sale	3.62%	3.35%	2.01%	2.26%
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%

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk

The Group is exposed to daily calls on its available cash resources from overnight deposits, current accounts, matured deposits, loan draw downs, guarantees and from margin and other calls on cash settled derivatives. The Board set limits on the minimum proportion of 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 3% of the total foreign currency denominated deposits must be deposited with central banks. The tables below analyze the assets and liabilities of the Group 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	Over due	Total
As at 31 December 2005							
Assets							
Cash and balances with central banks	140,309	–	–	–	–	–	140,309
Due from other banks and financial institutions	130,844	28,315	8,272	1,550	1,050	70	170,101
Financial assets held for trading	1,321	42	93	762	1,010	–	3,228
Loans and advances to customers	57,479	111,693	346,722	112,901	113,799	16,179	758,773
Investment securities							
– loans and receivables	14	717	1,763	25,394	484	–	28,372
– available-for-sale	3,876	17,428	57,111	138,465	69,091	–	285,971
Other assets, including deferred tax assets	6,858	853	2,593	4,815	20,797	769	36,685
Total assets	340,701	159,048	416,554	283,887	206,231	17,018	1,423,439
Liabilities							
Due to other banks and financial institution	(59,280)	(14,054)	(8,758)	–	(2,002)	–	(84,094)
Financial liabilities held for trading	(1,078)	(426)	(715)	(7,287)	(49)	–	(9,555)
Due to customers	(812,495)	(104,277)	(220,096)	(79,850)	(4,121)	–	(1,220,839)
Other liabilities, including deferred tax liabilities	(10,942)	(1,696)	(518)	(12,243)	(406)	–	(25,805)
Total liabilities	(883,795)	(120,453)	(230,087)	(99,380)	(6,578)	–	(1,340,293)
Net liquidity gap	(543,094)	38,595	186,467	184,507	199,653	17,018	83,146

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk *(Continued)*

Bank

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Over due	Total
As at 31 December 2005							
Assets							
Cash and balances with central banks	140,029	–	–	–	–	–	140,029
Due from other banks and financial institutions	130,844	28,315	8,272	1,550	1,050	70	170,101
Financial assets held for trading	1,321	42	93	762	1,010	–	3,228
Loans and advances to customers	57,479	111,693	346,722	112,901	113,799	16,179	758,773
Investment securities							
– loans and receivables	14	717	1,763	25,394	484	–	28,372
– available-for-sale	3,876	17,428	57,111	138,465	68,778	–	285,658
Investments in and due from subsidiaries	–	–	60	6	720	–	786
Other assets, including deferred tax assets	6,555	853	2,593	4,815	19,315	769	34,900
Total assets	340,118	159,048	416,614	283,893	205,156	17,018	1,421,847
Liabilities							
Due to other banks and financial institution	(59,280)	(14,054)	(8,758)	–	(2,002)	–	(84,094)
Financial liabilities held for trading	(1,078)	(426)	(715)	(7,287)	(49)	–	(9,555)
Due to customers	(812,495)	(104,277)	(220,096)	(79,850)	(4,121)	–	(1,220,839)
Other liabilities, including deferred tax liabilities	(9,097)	(1,696)	(518)	(12,243)	(283)	–	(23,837)
Total liabilities	(881,950)	(120,453)	(230,087)	(99,380)	(6,455)	–	(1,338,325)
Net liquidity gap	(541,832)	38,595	186,527	184,513	198,701	17,018	83,522

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk *(Continued)*

Group

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Over due	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
Financial assets held for trading	974	254	145	286	836	–	2,495
Loans and advances to customers	43,804	104,553	285,017	97,181	87,421	13,636	631,612
Investment securities							
– loans and receivables	12	785	2,428	26,987	993	–	31,205
– available-for-sale	5,243	22,272	56,586	82,719	48,703	–	215,523
Other assets, including deferred tax assets	14,788	951	1,939	8,215	19,400	453	45,746
Total assets	269,825	140,285	346,765	215,688	157,353	14,089	1,144,005
Liabilities							
Due to other banks and financial institutions	(22,992)	(5,161)	(1,602)	–	(1,956)	–	(31,711)
Financial liabilities held for trading	(830)	(240)	(173)	(3,534)	(309)	–	(5,086)
Due to customers	(724,497)	(68,546)	(175,982)	(56,552)	(4,364)	–	(1,029,941)
Other liabilities, including deferred tax liabilities	(10,903)	(197)	(913)	(12,000)	(1,151)	–	(25,164)
Total liabilities	(759,222)	(74,144)	(178,670)	(72,086)	(7,780)	–	(1,091,902)
Net liquidity gap	(489,397)	66,141	168,095	143,602	149,573	14,089	52,103

Notes to the Consolidated Financial Statements (Continued)

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk *(Continued)*

Bank

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Over due	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
Financial assets held for trading	974	254	145	286	836	–	2,495
Loans and advances to customers	43,804	104,553	285,017	97,181	87,421	13,636	631,612
Investment securities							
– loans and receivables	12	785	2,428	26,987	993	–	31,205
– available-for-sale	5,152	22,272	56,586	82,719	48,703	–	215,432
Investments in and due from subsidiaries	–	–	60	153	1,063	–	1,276
Other assets, including deferred tax assets	13,959	951	1,939	8,215	17,859	453	43,376
Total assets	268,780	140,285	346,825	215,841	156,875	14,089	1,142,695
Liabilities							
Due to other banks and financial institution	(22,992)	(5,161)	(1,602)	–	(1,956)	–	(31,711)
Financial liabilities held for trading	(830)	(240)	(173)	(3,534)	(309)	–	(5,086)
Due to customers	(724,497)	(68,546)	(175,982)	(56,552)	(4,364)	–	(1,029,941)
Other liabilities, including deferred tax liabilities	(8,970)	(197)	(913)	(12,000)	(1,045)	–	(23,125)
Total liabilities	(757,289)	(74,144)	(178,670)	(72,086)	(7,674)	–	(1,089,863)
Net liquidity gap	(488,509)	66,141	168,155	143,755	149,201	14,089	52,832

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk *(Continued)*

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 balance sheet 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 2005		31 December 2004	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Financial assets				
Due from other banks and financial institutions	**170,101**	**170,101**	88,923	88,923
Loans and advances to customers	**758,773**	**758,773**	631,612	631,612
Investment securities – loans and receivables	**28,372**	**29,189**	31,205	31,130
Due from subsidiaries	**136**	**136**	66	66
Financial liabilities				
Due to other banks and financial institutions	**84,094**	**84,094**	31,711	31,711
Due to customers	**1,220,839**	**1,220,320**	1,029,941	1,029,286

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

G Fair values of financial assets and liabilities *(Continued)*

The fair values of those financial assets and liabilities such as amounts due from/ to other banks and financial institutions, 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 other banks and financial institutions, 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 loans and receivables, as available-for-sale securities are measured at fair value. The fair value is determined by following the hierarchy given below:

– 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.

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

G Fair values of financial assets and liabilities *(Continued)*

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	
	2005	2004
Investment custody accounts	**96,852**	71,662

Notes to the Consolidated Financial Statements (Continued)

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

4 NET INTEREST INCOME

Group

	Year ended 31 December	
	2005	2004
Interest income		
Balances with central banks	**1,815**	1,855
Due from other banks and financial institutions	**3,375**	2,231
Trading securities	**9**	6
Loans and advances to customers	**36,305**	28,287
Investment securities	**8,114**	5,885
Others	**62**	88
	49,680	38,352
Interest expense		
Due to other banks and financial institutions	**(1,548)**	(1,129)
Due to customers	**(16,541)**	(12,031)
	(18,089)	(13,160)
Net interest income	**31,591**	25,192

	Year ended 31 December	
	2005	2004
Interest income accrued on loans and advances to customers individually identified with impairment	**740**	1,431
Interest income accrued on amounts due from other banks and financial institutions with impairment	**–**	12

5 DIVIDEND INCOME

Group

	Year ended 31 December	
	2005	2004
Dividend income	**45**	55

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

6 GAINS LESS LOSSES ARISING FROM TRADING ACTIVITIES

Group

	Year ended 31 December	
	2005	2004
Foreign exchange	**207**	594
Interest rate instruments	**213**	(269)
	420	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/(expense) on interest rate instruments mainly include the results of marking interest rate and currency swaps and other derivatives to market.

Notes to the Consolidated Financial Statements (Continued)

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

7 OTHER OPERATING INCOME

Group

	Year ended 31 December	
	2005	2004
Profit on sales of land use rights and buildings	**66**	214
Sales of foreclosed assets and other assets	**38**	46
Revaluation surplus of investment property	**46**	–
Penalty income	**9**	19
Other miscellaneous income	**470**	354
	629	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	
	2005	2004
Due from other banks and financial institutions and securities purchased under resale agreements, net *(Note 15(b))*	**(149)**	324
Loans and advances to customers *(Note 18(b))*	**4,549**	3,041
Less: recovery of loans previously written off	**(102)**	(150)
	4,298	3,215

9 OTHER OPERATING EXPENSES

Group

	Year ended 31 December	
	2005	2004
Staff costs *(Note 10)*	**5,776**	4,660
General and administrative expenses	**3,080**	2,758
Depreciation *(Note 20)*	**2,364**	2,471
Business tax and surcharges	**2,109**	1,639
Operating lease rentals	**737**	747
Write-down/Impairment of other receivables	**327**	394
Regulator's supervision fee	**259**	185
(Reversal of)/Provision for outstanding litigation	**(51)**	633
Revaluation deficit of property and equipment *(Note 20)*	**9**	389
Revaluation deficit of investment property	**–**	32
Professional fees	**34**	159
Others	**3,368**	2,925
	18,012	16,992

10 STAFF COSTS

Group

	Year ended 31 December	
	2005	2004
Salaries and bonus	**3,678**	2,717
Pension costs	**431**	392
Housing benefits and subsidies	**535**	609
Other social security and benefit costs	**1,132**	942
	5,776	4,660

Notes to the Consolidated Financial Statements (Continued)

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

11 DIRECTORS' EMOLUMENTS

(a) Directors' and supervisors' emoluments (In RMB Yuan)

	Year ended 31 December						
	2005						2004
Name	Emoluments	Salary	Discretionary bonuses	Other benefits	Employer's contribution to pension scheme	Total	Total
Executive directors							
Mr. Zhang, Jianguo	–	54,420	673,812	196,647	135,431	1,060,310	703,825
Mr. Li, Jun	–	44,372	555,680	82,728	117,073	799,853	982,613
Mr. Peng, Chun	–	17,320	201,580	33,752	48,781	301,433	251,646
Mr. Zhang, Jixiang	–	50,236	462,632	56,689	43,639	613,196	222,411
Mr. Qiao, Wei	–	24,278	307,162	43,308	58,537	433,285	986,804
Mr. Xu, Junkang	N/A	N/A	N/A	N/A	N/A	N/A	733,914
Mr. Yin, Jieyan	N/A	N/A	N/A	N/A	N/A	N/A	610,733
Mr. Fang, Chengguo	N/A	N/A	N/A	N/A	N/A	N/A	601,792
Mr. Liu, Yuchang	N/A	N/A	N/A	N/A	N/A	N/A	505,656
Ms. Yin, Baoyu	N/A	N/A	N/A	N/A	N/A	N/A	212,886
Non-executive directors							
Mr. Jiang, Chaoliang	–	54,420	673,812	96,647	135,431	960,310	646,944
Mr. OR Ching Fai	2,000	–	–	–	–	2,000	2,000
Mr. Wang Dongshen	–	–	–	–	–	–	–
Mr. Fung Kwok Lun	2,000	–	–	–	–	2,000	2,000
Mr. Li Keping	6,000	–	–	–	–	6,000	2,000
Mr. Li Zexing	10,000	–	–	–	–	10,000	2,000
Mr. Hu, Huating	–	46,612	462,632	54,359	36,754	600,357	160,169
Mr. Gao Shiqing	2,000	–	–	–	–	2,000	2,000
Mr. Shen Weiming	4,000	–	–	–	–	4,000	2,000
Mr. Li Guanglin	6,000	–	–	–	–	6,000	2,000
Mr. Qian Ping	–	–	–	–	–	–	–
Mr. Xia Bin	N/A	N/A	N/A	N/A	N/A	N/A	20,000
Mr. Xie Qingjian	–	150,000	–	–	–	150,000	25,000
Mr. Ian Ramsay Wilson	–	150,000	–	–	–	150,000	25,000
Mr. Thomas Joseph Manning	–	150,000	–	–	–	150,000	25,000
Mr. Hui Ho Ming Herbert	–	125,000	–	–	–	125,000	N/A
Mr. Chen Qingtai	–	125,000	–	–	–	125,000	N/A

11 DIRECTORS' EMOLUMENTS *(Continued)*

(a) Directors' and supervisors' emoluments (In RMB Yuan) *(Continued)*

	Year ended 31 December						
	2005						2004
Name	Emoluments	Salary	Discretionary bonuses	Other benefits	Employer's contribution to pension scheme	Total	Total
Supervisors							
Mr. Cui Leiping	–	49,256	674,160	97,151	135,431	955,998	251,730
Ms. Liu Sha	–	44,438	427,800	31,387	22,526	526,151	24,288
Ms. Chen Qing	–	44,438	427,440	31,387	22,526	525,791	27,871
Mr. Lee Jun	–	11,080	61,521	8,013	15,535	96,149	N/A
Ms. Yin Baoyu	–	46,499	415,467	37,696	84,098	583,760	330,318
Mr. Ning Jinbiao	6,000	–	–	–	–	6,000	6,000
Ms. Dong Mei	N/A	N/A	N/A	N/A	N/A	N/A	4,000
Mr. Zhao Lijun	N/A	N/A	N/A	N/A	N/A	N/A	2,000
Mr. Teng Tieqi	4,000	–	–	–	–	4,000	2,000
Mr. Ji Keliang	4,000	–	–	–	–	4,000	4,000
Mr. Li Chao	N/A	N/A	N/A	N/A	N/A	N/A	20,000
Mr. Liu Qiang	8,000	120,000	–	–	–	128,000	49,333
Ms. Chen Zheng	8,000	120,000	–	–	–	128,000	25,333
Total	62,000	1,427,369	5,343,698	769,764	855,762	8,458,593	7,475,266

Above listed amounts only include emoluments of the Directors or Supervisors during their tenure of Director or Supervisor in the related years.

Notes to the Consolidated Financial Statements (Continued)

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

11 DIRECTORS' EMOLUMENTS *(Continued)*

(b) Five Highest Paid Individuals

The five highest paid individuals in the Bank for the related years are senior management of Hong Kong branch listed as follows:

	Year ended 31 December	
	2005	2004
Salary	**5**	5
Discretionary bonuses	**1**	1
Employer's contribution to pension scheme	**1**	–
	7	6

Emoluments of above five highest paid individuals in the Bank are within the following bands:

	Number of employees	
	2005	2004
RMB1,000,000-RMB1,500,000	**4**	4
RMB1,500,000-RMB2,000,000	**1**	1
	5	5

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

12 INCOME TAX EXPENSE

Group

	Year ended 31 December	
	2005	2004
Current tax		
– Mainland China income tax	**786**	141
– Hong Kong profits tax	**139**	75
– Overseas taxation	**2**	5
	927	221
Deferred tax *(Note 26)*	**2,673**	5,925
	3,600	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 year ended 31 December 2005.

Profits earned by the Hong Kong branch or subsidiaries in Hong Kong are subject to Hong Kong profits tax at the rate of 17.5%, on the estimated assessable profit for the year ended 31 December 2005. 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 year ended 31 December 2005.

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

12 INCOME TAX EXPENSE *(Continued)*

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	
	2005	2004
Profit before tax	**12,843**	7,750
Tax calculated at a tax rate of 33%	**4,238**	2,557
Effect of different tax rates in other countries	**(58)**	5
De-recognition of deferred tax assets in relation to loans disposed of *(Note 1)*	**–**	9,671
Recognition of deferred tax assets in relation to tax loss *(Note 2)*	**–**	(3,588)
Tax credit arising from income not subject to tax *(Note 3)*	**(1,020)**	(3,747)
Tax effect of expenses that are not deductible for tax purposes *(Note 4)*	**440**	1,248
Income tax expense	**3,600**	6,146

Notes:

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

2. The Group obtained written approvals from the Ministry of Finance ("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 amounting to RMB3,631 million (Note 26), being 33% of RMB11,002 million at 31 December 2004.

12 INCOME TAX EXPENSE *(Continued)*

Notes: (Continued)

3. 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. This amount of profit earned was income tax exempt in consideration of the loss incurred by the Bank on its disposal of impaired loans in June 2004.

4. Included in the amount of RMB1,248 million of expenses that are not deductible for tax purposes for the year ended 31 December 2004, is an amount of RMB756 million being the income tax on non-deductible staff cost & staff welfare. The Group obtained a written approval from the MOF and the tax authority on 7 February 2006, which granted a deductible limit for the Bank's staff cost of RMB3,315 million for the year ended 31 December 2005. Such approval led to a significant decrease of the income tax on non-deductible staff cost & staff welfare, approximately RMB1,050 million.

13 BASIC AND DILUTED EARNINGS PER SHARE

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

	Year ended 31 December	
	2005	2004
Profit attributable to shareholders of the Bank	**9,249**	1,604
Weighted average number of ordinary shares in issue	**42,581**	26,396
Basic and diluted earnings per share (expressed in RMB per share)	**0.22**	0.06

Notes to the Consolidated Financial Statements (Continued)

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

14 CASH AND BALANCES WITH CENTRAL BANKS

Group

	As at 31 December	
	2005	2004
Cash	**9,280**	8,616
Balances with central banks other than mandatory reserve deposits	**57,720**	58,215
Included in cash and cash equivalents *(Note 36)*	**67,000**	66,831
Mandatory reserve deposits	**73,309**	61,670
	140,309	128,501

Bank

	As at 31 December	
	2005	2004
Cash	**9,000**	8,491
Balances with central banks other than mandatory reserve deposits	**57,720**	58,215
Included in cash and cash equivalents	**66,720**	66,706
Mandatory reserve deposits	**73,309**	61,670
	140,029	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	
	2005	2004
Mandatory reserve rate for deposits denominated in RMB	**7.5%**	7.5%
Mandatory reserve rate for deposits denominated in foreign currency	**3%**	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	
	2005	2004
Placement with other banks and included in cash equivalents *(Note 36)*	**34,305**	8,926
Securities purchased under resale agreement	**65,715**	27,109
Less: allowance for impairment losses on securities purchased under resale agreement	**(10)**	(82)
	65,705	27,027
Loans purchased under resale agreement	**11,062**	2,395
Loans and advances to other banks	**55,147**	49,197
Loans to other financial institutions	**4,615**	2,300
	59,762	51,497
Less: Individual impairment allowance on amounts due from other banks and financial institutions	**(733)**	(922)
	59,029	50,575
	170,101	88,923

Notes to the Consolidated Financial Statements (Continued)

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

15 DUE FROM OTHER BANKS AND FINANCIAL INSTITUTIONS *(Continued)*

(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	
	2005	2004
Balance at beginning of the year	**1,004**	968
(Reversal of) /Provision for impairment, net *(Note 8)*	**(149)**	324
Amounts written-off/ transferred out during the year as uncollectible	**(112)**	(288)
Balance at end of the year	**743**	1,004

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

Group and Bank

	As at 31 December	
	2005	2004
Impaired amount of due from other banks and financial institutions	**743**	1,004
Impaired amount of due from other banks and financial institutions (percentage)	**0.44%**	1.12%

16 FINANCIAL ASSETS HELD FOR TRADING

Group and Bank

	As at 31 December	
	2005	2004
Derivative financial instruments *(Note 17)*	**299**	219
Government bonds-listed in Hong Kong	**1,294**	1,191
Other debt securities		
– Listed in Hong Kong	**611**	310
– Unlisted – corporate bonds	**146**	166
– Unlisted – public sector	**71**	96
– Unlisted – banking sector	**807**	513
	3,228	2,495

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).

Notes to the Consolidated Financial Statements (Continued)

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

17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

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 favourable (assets) or unfavourable (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	Fair values Liabilities
As at 31 December 2005			
Foreign exchange derivatives			
Currency forwards	**11,215**	**51**	**(43)**
Currency swaps	**23,234**	**99**	**(8)**
OTC currency options bought and sold	**335**	**2**	**(1)**
Subtotal		**152**	**(52)**
Interest rate derivatives			
Interest rate swaps	**24,791**	**108**	**(220)**
Cross currency interest rate swaps	**3,532**	**36**	**(26)**
OTC interest rate options	**565**	**3**	**(3)**
Subtotal		**147**	**(249)**
Total recognised derivatives		**299**	**(301)**

17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

Group and Bank

	Contract/ notional Amount	Fair values Assets	Liabilities
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	–
Subtotal		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	–
Subtotal		90	(388)
Total recognised derivatives		219	(577)

The tables above provide a detailed breakdown of the contractual or notional amounts and the fair values of the Group's derivative financial instruments outstanding at 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 undertakes its transactions in foreign exchange and interest rate contracts with other financial institutions and customers. Management has established limits of these contracts by counterparties, industry sectors and countries. Actual credit exposures and limits are regularly monitored and controlled by management.

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

17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

Credit risk weighted amounts

Group and Bank

	As at 31 December	
	2005	2004
Derivatives		
– Exchange rate contracts	**122**	171
– Interest rate contracts	**62**	30
– Other derivative contracts	**–**	4
	184	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	
	2005	2004
Derivatives		
– Exchange rate contracts	**184**	134
– Interest rate contracts	**83**	49
– Other derivative contracts	**–**	11
	267	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 Hong Kong Monetary Authority ("HKMA") because there are no relevant standards prescribed by IFRS. There was no relevant standard prescribed by the banking regulators for determining the credit risk weighted amounts of derivatives and the Group is not required to report credit risk weighted amounts of derivatives to the banking regulators.

17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

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 2005					
Notional amount of derivative financial instruments	**2,100**	**31,006**	**25,006**	**5,560**	**63,672**
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	
	2005	2004
Loans and advances to customers	**771,374**	640,058
Less: collective impairment allowances	**(4,520)**	(4,108)
individual impairment allowances	**(8,081)**	(4,338)
	758,773	631,612

Notes to the Consolidated Financial Statements (Continued)

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

18 LOANS AND ADVANCES TO CUSTOMERS *(Continued)*

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

Group and Bank

	As at 31 December	
	2005	2004
Balance at beginning of year	**8,446**	33,268
Impairment allowances for loans	**4,549**	3,041
Loans written off during the year as uncollectible	**(312)**	(928)
Exchange difference	**(82)**	–
Written back on disposal of impaired loans	**–**	(26,935)
Balance at end of the year	**12,601**	8,446

(c) Individually identified loans with impairment

Group and Bank

	As at 31 December	
	2005	2004
Individually identified loans with impairment	**21,579**	19,193
Individually identified loans with impairment to loans and advances to customers (percentage)	**2.80%**	3.00%

19 INVESTMENT SECURITIES

Group

	As at 31 December	
	2005	2004 restated
Securities – loans and receivables		
Debt securities – at amortised cost		
– Unlisted	**28,372**	31,205
Securities – available-for-sale		
Debt securities – at fair value		
– Listed in Hong Kong	**7,710**	5,715
– Listed outside Hong Kong	**47,003**	33,274
– Unlisted	**230,486**	176,012
Equity securities – at fair value		
– Listed outside Hong Kong	**2**	2
– Unlisted	**764**	429
Equity securities at cost less impairment		
– Unlisted	**6**	91
	285,971	215,523

Bank

	As at 31 December	
	2005	2004 restated
Securities – loans and receivables		
Debt securities – at amortised cost		
– Unlisted	**28,372**	31,205
Securities – available-for-sale		
Debt securities – at fair value		
– Listed in Hong Kong	**7,710**	5,715
– Listed outside Hong Kong	**47,003**	33,274
– Unlisted	**230,486**	176,012
Equity securities – at fair value		
– Listed outside Hong Kong	**2**	2
– Unlisted	**451**	429
Equity securities at cost less impairment		
– Unlisted	**6**	–
	285,658	215,432

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

19 INVESTMENT SECURITIES *(Continued)*

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.

Gains less losses arising from investment securities comprise:

Group and Bank

	As at 31 December	
	2005	2004
Gains less losses arising from de-recognition of investment securities	**359**	77

The movement in investment securities may be summarized as follows:

Group

	Originated loans/ Loans and receivables	Available-for-sale	Total
Previously reported balance at 1 January 2005	159,826	90,028	249,854
Reclassification upon the adoption of revised IAS 39	(127,659)	127,659	–
Transferred to financial assets held for trading upon the adoption of revised IAS 39	(962)	–	(962)
Revaluation upon the adoption of revised IAS 39	–	(2,164)	(2,164)
Adjusted balance at 1 January 2005, restated	31,205	215,523	246,728
Additions	1,764	408,510	410,274
Disposals (sale or redemption)	(4,540)	(342,066)	(346,606)
Gain from changes in fair value	–	5,842	5,842
Exchange differences	(57)	(1,838)	(1,895)
At 31 December 2005	28,372	285,971	314,343

19 INVESTMENT SECURITIES *(Continued)*

Bank

	Originated loans/ Loans and receivables	Available-for-sale	Total
Previously reported balance at 1 January 2005	159,826	89,937	249,763
Reclassification upon the adoption of revised IAS 39	(127,659)	127,659	–
Transferred to financial assets held for trading upon the adoption of revised IAS 39	(962)	–	(962)
Revaluation upon the adoption of revised IAS 39	–	(2,164)	(2,164)
Adjusted balance at 1 January 2005, restated	31,205	215,432	246,637
Additions	1,764	407,815	409,579
Disposals (sale or redemption)	(4,540)	(341,593)	(346,133)
Gain from changes in fair value	–	5,842	5,842
Exchange differences	(57)	(1,838)	(1,895)
At 31 December 2005	28,372	285,658	314,030

Notes to the Consolidated Financial Statements (Continued)

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

19 INVESTMENT SECURITIES *(Continued)*

The investment securities are analysed by issuer as follows:

Group

	As at 31 December	
	2005	2004
Securities – loans and receivables		
– Central governments and central banks	**26,527**	28,911
– Public sector entities	**464**	125
– Banks and other financial institutions	**1,381**	2,169
	28,372	31,205
Securities – available-for-sale		
– Central governments and central banks	**115,653**	108,582
– Public sector entities	**2,644**	2,398
– Banks and other financial institutions	**154,734**	99,640
– Corporate entities	**12,940**	4,903
	285,971	215,523

Bank

	As at 31 December	
	2005	2004
Securities – loans and receivables		
– Central governments and central banks	**26,527**	28,911
– Public sector entities	**464**	125
– Banks and other financial institutions	**1,381**	2,169
	28,372	31,205
Securities – available-for-sale		
– Central governments and central banks	**115,653**	108,582
– Public sector entities	**2,644**	2,398
– Banks and other financial institutions	**154,734**	99,640
– Corporate entities	**12,627**	4,812
	285,658	215,432

19 INVESTMENT SECURITIES *(Continued)*

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

Group and Bank

	As at 31 December	
	2005	2004
Available-for-sale, at fair value		
– Unlisted	**2,254**	3,221

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

Group and Bank

	As at 31 December	
	2005	2004
Up to 3 months	**–**	309
3 to 12 months	**796**	846
1 to 5 years	**1,458**	2,066
	2,254	3,221

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

20 PROPERTY AND EQUIPMENT

Group

	Land and Buildings	Construction in Progress	Equipment	Motor Vehicles	Leasehold improvement	Total
Cost or valuation						
At 1 January 2005	19,133	1,146	2,629	272	1,569	24,749
Additions	162	1,190	1,829	43	270	3,494
Disposals	(439)	(176)	(330)	(79)	(618)	(1,642)
Transfers	1,102	(1,024)	(78)	–	–	–
Revaluation	89	(11)	–	–	–	78
At 31 December 2005	20,047	1,125	4,050	236	1,221	26,679
Accumulated depreciation						
At 1 January 2005	–	–	–	–	(886)	(886)
Charge for the period	(792)	–	(1,254)	(70)	(248)	(2,364)
Disposals	155	–	301	68	574	1,098
Revaluation	637	–	–	–	–	637
At 31 December 2005	–	–	(953)	(2)	(560)	(1,515)
Net book value						
At 31 December 2005	20,047	1,125	3,097	234	661	25,164
Carrying amount at 31 December 2005, if at cost	11,835	975	3,001	211	661	16,683
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

20 PROPERTY AND EQUIPMENT *(Continued)*

Bank

	Land and Buildings	Construction in Progress	Equipment	Motor Vehicles	Leasehold improvement	Total
Cost or valuation						
At 1 January 2005	17,592	1,146	2,629	272	1,569	23,208
Additions	167	1,190	1,829	43	270	3,499
Disposals	(103)	(176)	(330)	(79)	(618)	(1,306)
Transfers	1,102	(1,024)	(78)	–	–	–
Revaluation	(194)	(11)	–	–	–	(205)
At 31 December 2005	18,564	1,125	4,050	236	1,221	25,196
Accumulated depreciation						
At 1 January 2005	–	–	–	–	(886)	(886)
Charge for the period	(792)	–	(1,254)	(70)	(248)	(2,364)
Disposals	158	–	301	68	574	1,101
Revaluation	634	–	–	–	–	634
At 31 December 2005	–	–	(953)	(2)	(560)	(1,515)
Net book value						
At 31 December 2005	18,564	1,125	3,097	234	661	23,681
Carrying amount at 31 December 2005, if at cost	10,964	975	3,001	211	661	15,812
Cost at 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

Notes to the Consolidated Financial Statements (Continued)

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

20 PROPERTY AND EQUIPMENT *(Continued)*

The Group's management had its land and buildings, construction in progress, equipment and motor vehicles revalued with reference to a valuation made on an open market and existing use basis by external valuer at 31 December 2004. Sallmanns (Far East) Ltd. (西門(遠東)有限公司) was the external valuer appointed for valuation at 31 December 2004. Pan-China Assets Appraisal Co., Ltd. (北京天健興業資產評估有限公司) was appointed as its external valuer for the Group's latest valuation exercise as at 31 December 2005 to revalue Land and buildings, construction in progress, while equipment and motor vehicles were not revalued due to their insignificance.

The revaluation reserve relating to revaluation of property and equipment is not distributable to shareholders.

Group

	Year ended at 31 December	
	2005	2004
Revaluation surplus classified in equity, net of tax	**541**	3,098
Deferred tax liability *(Note 26)*	**164**	1,458
Revaluation deficit charged to profit and loss account *(Note 9)*	**(9)**	(389)
Exchange gain	**19**	–
	715	4,167

Bank

	As at 31 December	
	2005	2004
Revaluation surplus classified in equity, net of tax	**339**	2,789
Deferred tax liability	**127**	1,341
Revaluation deficit charged to profit and loss account	**(56)**	(333)
Exchange gain	**19**	–
	429	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	
	2005	2004
Net book value of land and buildings of Hong Kong Branch	**1,370**	1,211

21 OTHER ASSETS

Group

	As at 31 December	
	2005	2004
Settlement accounts	**1,171**	5,124
Other receivables	**4,731**	4,383
Less: impairment allowance	**(2,167)**	(2,209)
Foreclosed assets	**5,483**	6,832
Less: impairment allowance	**(2,788)**	(1,785)
Prepaid staff housing subsidies	**214**	252
Prepaid rental expenses	**349**	356
Land use rights	**589**	630
Computer software	**296**	256
Investment property	**720**	708
Others	**1,968**	1,597
	10,566	16,144

Bank

	As at 31 December	
	2005	2004
Settlement accounts	**1,171**	5,124
Other receivables	**4,451**	3,723
Less: impairment allowance	**(2,167)**	(2,209)
Foreclosed assets	**5,483**	6,832
Less: impairment allowance	**(2,788)**	(1,785)
Prepaid staff housing subsidies	**214**	252
Prepaid rental expenses	**349**	356
Land use rights	**589**	630
Computer software	**296**	256
Investment property	**720**	708
Others	**1,946**	1,428
	10,264	15,315

Notes to the Consolidated Financial Statements (Continued)

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

22 DUE TO OTHER BANKS AND FINANCIAL INSTITUTIONS

Group and Bank

	As at 31 December	
	2005	2004
Due to central banks	**–**	28
Deposits from other banks and financial institutions	**50,040**	16,224
Loans from other banks and financial institutions	**34,054**	15,459
	84,094	31,711

23 FINANCIAL LIABILITIES HELD FOR TRADING

Group and Bank

	As at 31 December	
	2005	2004
Derivative financial instruments *(Note 17)*	**301**	577
Short position of securities held for trading	**1,056**	1,158
Debt securities in issue	**8,198**	3,351
	9,555	5,086

23 FINANCIAL LIABILITIES HELD FOR TRADING *(Continued)*

Debt securities in issue are:

Group and Bank

	As at 31 December 2005		As at 31 December 2004	
	Amount	Interest rate per Annum (%)	Amount	Interest rate per Annum (%)
HKD short term Certificate of Deposit	591	2.84	–	Not Applicable
HKD medium term Certificate of Deposit	2,546	3.25	760	3.23
USD medium term Certificate of Deposit	1,842	3.36	362	3.48
HKD floating rate Certificate of Deposit (maturing in June 2006)	417	HIBOR+0.06%	–	Not Applicable
HKD floating rate Certificate of Deposit (maturing in September 2006)	41	HIBOR+0.2%	426	HIBOR+0.20%
HKD floating rate Certificate of Deposit (maturing in March 2007)	178	First year 1.95% Remaining year 3M HIBOR + 0.15% (capped at 4.75%)	–	Not Applicable
HKD floating rate Certificate of Deposit (maturing in August 2008)	313	HIBOR+0.18%	–	Not Applicable
HKD floating rate Certificate of Deposit (maturing in September 2008)	105	HIBOR+0.26%	426	HIBOR+0.26%
HKD reverse Certificate of Deposit (maturing in May 2009)	6	First year 6.20% Remaining years 6.90% less 3M HIBOR (minimum at 0%)	138	6.9%-3M HIBOR

Notes to the Consolidated Financial Statements (Continued)

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

23 FINANCIAL LIABILITIES HELD FOR TRADING *(Continued)*

Group and Bank *(Continued)*

	As at 31 December 2005		As at 31 December 2004	
	Amount	**Interest rate per Annum (%)**	Amount	Interest rate per Annum (%)
USD floating rate Certificate of Deposit (maturing in May 2007)	**453**	**First year 3.1% Remaining year 3M LIBOR + 0.15% (capped at 5%)**	–	Not Applicable
USD floating rate Certificate of Deposit (maturing in June 2007)	**47**	**LIBOR+0.12%**	–	Not Applicable
HKD floating rate Certificate of deposit (maturing in November 2008)	**73**	**HIBOR+0.10%**	–	Not Applicable
HKD floating rate Certificate of deposit (maturing in November 2008)	**156**	**HIBOR+0.18%**	–	Not Applicable
USD floating rate Certificate of deposit (maturing in November 2006)	**35**	**LIBOR+0.08%**	–	Not Applicable
USD floating rate Certificate of deposit (maturing in November 2008)	**47**	**LIBOR+0.05%**	–	Not Applicable
USD floating rate Certificate of deposit (maturing in November 2008)	**162**	**LIBOR+0.18%**	–	Not Applicable
USD floating rate Certificate of Deposit (maturing in January 2007)	**1,186**	**LIBOR+0.20%**	1,239	LIBOR+0.20%
	8,198		3,351	

24 DUE TO CUSTOMERS

Group and Bank

	As at 31 December	
	2005	2004
Corporate current deposits	**407,228**	385,556
Corporate savings deposits	**4,232**	5,011
Corporate time deposits	**231,275**	186,216
Individual current deposits	**162,757**	143,461
Individual savings deposits	**9,725**	14,879
Individual time deposits	**263,236**	210,561
Pledged deposits	**105,781**	53,705
Certificates of deposit	**696**	–
Promissory notes	**2,708**	3,055
Customer margin deposits	**1,642**	2,075
Other deposits	**23,544**	18,815
Interest payable	**8,015**	6,607
	1,220,839	1,029,941
Including:		
Pledged deposits held as collateral for letters of credit	**5,715**	4,965

25 OTHER LIABILITIES

Group

	As at 31 December	
	2005	2004
Settlement accounts	**4,509**	4,971
Dividends payable	**136**	141
Staff benefits payables	**1,692**	1,604
Tax payable	**816**	655
Provision for outstanding litigation	**938**	989
Others	**4,258**	4,097
	12,349	12,457

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

25 OTHER LIABILITIES *(Continued)*

Bank

	As at 31 December	
	2005	2004
Settlement accounts	**4,509**	4,971
Dividends payable	**136**	141
Staff benefits payables	**1,692**	1,604
Tax payable	**816**	655
Provision for outstanding litigation	**938**	989
Others	**2,414**	2,165
	10,505	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 year 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 2005 (Year 2004: 17.5%) for transactions in Hong Kong.

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

Group

	Year ended 31 December	
	2005	2004 Restated
At beginning of the year	**4,632**	11,650
Reclassification into AFS securities	**714**	(60)
Adjusted balance at beginning of the year, restated	**5,346**	11,590
Charge to profit and loss account	**(2,673)**	(5,925)
Available-for-sale securities – fair value remeasurement	**(1,967)**	806
Property revaluation	**(164)**	(1,458)
Provision for investment	**–**	336
Exchange differences	**–**	(3)
At end of the year	**542**	5,346

26 DEFERRED INCOME TAXES *(Continued)*

Bank

	Year ended 31 December	
	2005	2004 Restated
At beginning of the year	**4,739**	11,650
Reclassification into AFS securities	**714**	(60)
Adjusted balance at beginning of the year, restated	**5,453**	11,590
Charge to profit and loss account	**(2,673)**	(5,935)
Available-for-sale securities – fair value remeasurement	**(1,967)**	806
Property revaluation	**(147)**	(1,341)
Provision for investment	**–**	336
Exchange differences	**–**	(3)
At end of the year	**666**	5,453

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

Group

	As at 31 December	
	2005	2004
Deferred income tax liabilities		
Available-for-sale securities	**(1,285)**	(53)
Accelerated tax depreciation	**–**	(13)
Property revaluation reserve	**(1,676)**	(1,560)
Other temporary differences	**(288)**	(261)
	(3,249)	(1,887)
Deferred income tax assets		
Provision for loan losses	**592**	427
Impairment allowances for investments	**392**	480
Decelerated tax depreciation	**128**	125
Impairment of other assets	**2,669**	1,825
Tax loss carried forward *(Note 12)*	**–**	3,631
Available-for-sale securities	**10**	745
	3,791	7,233
Net deferred income tax assets	**542**	5,346

Notes to the Consolidated Financial Statements (Continued)

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

26 DEFERRED INCOME TAXES *(Continued)*

Bank

	As at 31 December	
	2005	2004
Deferred income tax liabilities		
Available-for-sale securities	**(1,285)**	(53)
Accelerated tax depreciation	**–**	(13)
Property revaluation reserve	**(1,543)**	(1,443)
Other temporary differences	**(287)**	(261)
	(3,115)	(1,770)
Deferred income tax assets		
Provision for loan losses	**592**	427
Impairment allowances for investments	**392**	480
Decelerated tax depreciation	**118**	115
Impairment of other assets	**2,669**	1,825
Tax loss carried forward *(Note 12)*	**–**	3,631
Available-for-sale securities	**10**	745
	3,781	7,223
Net deferred income tax assets	**666**	5,453

26 DEFERRED INCOME TAXES *(Continued)*

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 2005	2004 Restated
Deferred tax assets	**955**	5,739
Deferred tax liabilities	**(413)**	(393)

Bank

	As at 31 December 2005	2004 Restated
Deferred tax assets	**955**	5,739
Deferred tax liabilities	**(289)**	(286)

The deferred tax charge in the profit and loss account comprises the following temporary differences:

Group

	As at 31 December 2005	2004
Provision for loan losses:		
Additional provisions for loan losses	**198**	879
Utilization	**(33)**	(23)
De-recognition of deferred tax assets in relation to loans disposed of *(Note 12)*	**–**	(9,671)
Sub-total	**165**	(8,815)
Impairment allowances for investments	**(88)**	(85)
Impairment of other assets	**844**	(682)
(Utilization of)/ Provision of tax loss carried forward *(Note 12)*	**(3,631)**	3,588
Accelerated tax depreciation	**13**	–
Decelerated tax depreciation	**3**	103
Depreciation/disposal of property and equipment	**48**	–
Other temporary differences	**(27)**	(34)
	(2,673)	(5,925)

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

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 period. 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 period 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 period when the payment is made.

	Year ended 31 December	
	2005	2004
Expenses incurred for retirement benefit plans	**431**	392

28 SUBORDINATED TERM DEBT

Group and Bank

	As at 31 December	
	2005	2004
Floating rate subordinated debt – 2009	**12,000**	12,000
Interest payable	**292**	275
	12,292	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 (in millions)	Ordinary shares of RMB1 each (RMB million)	Capital surplus (RMB million)	Total (RMB million)
At 1 January 2005	39,070	39,070	10,872	49,942
Issue of shares *(Note 1)*	6,734	6,734	11,259	17,993
Issuance cost	–	–	(591)	(591)
At 31 December 2005	45,804	45,804	21,540	67,344

Bank

	Number of shares (in millions)	Ordinary shares of RMB1 each (RMB million)	Capital surplus (RMB million)	Total (RMB million)
At 1 January 2005	39,070	39,070	11,764	50,834
Issue of shares *(Note 1)*	6,734	6,734	11,259	17,993
Issuance cost	–	–	(591)	(591)
At 31 December 2005	45,804	45,804	22,432	68,236

Note 1: On 23 June 2005, a total of 5,856 million shares were subscribed by various third parties at a price of HKD2.50 per share with a total consideration of HKD14,640 million (equivalent to RMB15,657 million). The excess over par value of RMB9,801 million was included in capital surplus while the issuance cost of RMB516 million was netted off against capital surplus.

On 4 July 2005, a total of 878 million shares were subscribed by the Hongkong and Shanghai Banking Corporation Limited ("HSBC") at a price of HKD2.5 per share with a total consideration of HKD2,195 million (equivalent to RMB2,336 million) as a result of the exercise of the over-allotment option. The excess over par value of RMB1,458 million was included in capital surplus while the issuance cost of RMB75 million was netted off against capital surplus.

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

29 SHARE CAPITAL AND CAPITAL SURPLUS *(Continued)*

Note 1: (Continued)

The share issuance cost contains underwriting commission and a proportion of listing related costs, i.e. professional charges, registration charges etc, which is attributable to the newly issued shares.

All the newly issued shares together with the shares held by the HSBC, the National Council For Social Security Fund and the China SAFE Investments Limited., are listed on the Hong Kong Stock Exchange.

The shareholding structures of the Bank immediately after the issue by the Bank of the Over-allotment Shares is as follows:

Group

	Number of shares (in millions)	**Approximated percentage of the Bank's issued share capital**
Domestic Shares in issue	22,740	49.65%
H shares offered under the Global Offering and converted from Domestic Shares	23,064	50.35%
Total number of shares	45,804	100.00%

Bank

	Number of shares (in millions)	**Approximated percentage of the Bank's issued share capital**
Domestic Shares in issue	22,740	49.65%
H shares offered under the Global Offering and converted from Domestic Shares	23,064	50.35%
Total number of shares	45,804	100.00%

29 SHARE CAPITAL AND CAPITAL SURPLUS *(Continued)*

Note 1: (Continued)

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 from shareholders; 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 RETAINED EARNINGS

Pursuant to the PRC regulations, the appropriation of profits to the discretionary reserve, the general and statutory 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.

In accordance with the PRC legislation, 10% of the net distributable profit of the Bank (Note 32), 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. On 28 March 2006, the Directors proposed to transfer 10% of its net income, as determined under the PRC accounting regulations, to the non-distributable statutory reserve with RMB899 million and such proposal has not been recognized in the balance sheet.

Pursuant to the PRC regulations, the Bank is required to transfer a certain amount of its net income, as determined based on the degree of overall unidentified loss exposure (normally no lower than 1% of the ending balance of risk assets by the end of 2009), to the general and statutory reserve through its profit appropriation. The general and statutory reserve is an integral part of equity interest but subject to dividend distribution. On 28 March 2006, the Directors proposed a general and statutory reserve of RMB4,428 million (2004: N/A) through its profit appropriation. The general and statutory reserve is subject to approval by the shareholders at the Annual General Meeting and has not been recognized in the balance sheet. Statutory reserve of Hongkong branch required by HKMA has been covered in above general and statutory reserve.

Notes to the Consolidated Financial Statements (Continued)

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

31 ESTABLISHMENT OF SUBSIDIARY

On 4 August 2005, the Bank has established the Bank of Communications Schroder Fund Management Co., Ltd. ("BOCOM Schroder") together with the other two third party investors. The BOCOM Schroder has a total paid in capital of RMB200 million, while the Bank holds its 65% equity interest.

32 DIVIDENDS

	Year ended 31 December	
	2005	2004
Paid in the year	**5**	8

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) Allocations to general provision reserve;

(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.

At 31 December 2005, the aggregate amount of profit available for profit distribution was RMB8,991 million (2004: N/A), being the retained profits determined in accordance with PRC GAAP. On 28 March 2006, the directors proposed a cash dividend of RMB0.08 per share (2004: N/A), amounting to RMB3,664 million (2004: N/A). The dividend is subject to approval by the shareholders at the Annual General Meeting and has not been recognized as a liability at the balance sheet date.

33 FINANCIAL GUARANTEES AND CREDIT RELATED COMMITMENTS, OTHER COMMITMENTS AND CONTINGENT LIABILITIES

Financial guarantees and credit related commitments

The following tables indicate the contractual amounts of the Group's financial guarantees and credit related commitments which the Group commits to extend to customers:

Group and Bank

	As at 31 December	
	2005	2004
Guarantees	**49,623**	30,867
Letters of credit	**22,316**	25,654
Acceptances	**156,484**	103,348
Other commitments with an original maturity of		
– Under 1 year	**10,044**	2,573
– 1 year and over	**7,443**	5,193
	245,910	167,635

Capital expenditure commitments

Group and Bank

	As at 31 December	
	2005	2004
Capital expenditure commitments for buildings	**238**	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	
	2005	2004
Not later than 1 year	**555**	499
Later than 1 year and not later than 5 years	**1,320**	1,141
Later than 5 years	**466**	532
	2,341	2,172

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

33 FINANCIAL GUARANTEES AND CREDIT RELATED COMMITMENTS, OTHER COMMITMENTS AND CONTINGENT LIBILITIES *(Continued)*

Legal proceedings

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

Group and Bank

	As at 31 December	
	2005	2004
Outstanding claims	**2,261**	2,601
Provision for losses	**938**	989

34 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	
	2005	2004	**2005**	2004
Balances with central banks	**73,309**	61,670	**–**	–
Investment securities	**200**	400	**200**	400
	73,509	62,070	**200**	400

35 CREDIT RISK WEIGHTED AMOUNT OF FINANCIAL GUARANTEES AND CREDIT RELATED COMMITMENTS

Group and Bank

	As at 31 December	
	2005	2004
Financial guarantees and credit related commitments	**179,746**	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.

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

36 NOTES TO CONSOLIDATED CASH FLOW STATEMENT

(a) Analysis of changes in financing during the year

	Dividends	Share capital	Capital surplus	Subordinated term debt	Minority Interest
At 1 January 2005	141	39,070	10,872	12,275	–
Net cash inflow/(outflow) from financing	(5)	6,734	10,668	(540)	70
Interest expense recognised on subordinated term debt	–	–	–	557	–
Net loss attributable to minority interest	–	–	–	–	(6)
At 31 December 2005	**136**	**45,804**	**21,540**	**12,292**	**64**
At 1 January 2004	149	17,108	11,035	–	–
Net cash inflow/(outflow) from financing	(8)	21,962	11,635	12,000	–
Impact of a Restructuring Transaction on capital surplus	–	–	(2,763)	–	–
Reserves offset against accumulated losses	–	–	(9,035)	–	–
Interest expense recognised on subordinated term debt	–	–	–	275	–
At 31 December 2004	141	39,070	10,872	12,275	–

(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	
	2005	**2004**
Cash and balances with central banks *(Note 14)*	**67,000**	66,831
Due from other banks and financial institutions *(Note 15)*	**34,305**	8,926
	101,305	75,757

37 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	30 Apr 1982	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

Notes to the Consolidated Financial Statements (Continued)

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

37 PRINCIPAL SUBSIDIARIES *(Continued)*

Name of subsidiaries	Place of incorporation and operation	Date of incorporation	Issued and fully paid up share capital	Group equity interest %	Principal activities
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
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
Bank of Communications Schroder Fund Management Co., Ltd.	PRC	4 Aug 2005	RMB200,000,000	65	Fund Management

All above principal subsidiaries are private companies.

For the year ended 31 December 2004 and 2005, or 31 March 2005 or 2006, all principal subsidiaries incorporated in Hong Kong as stated above were audited by KPMG.

For the years ended 31 December 2004 and 2005, Career Computer (Shenzhen) Company Limited was audited by Shenzhen Peng Cheng CPAs Limited 深圳鵬城會計師事務所.

37 PRINCIPAL SUBSIDIARIES *(Continued)*

The Bank of Communications Schroder Fund Management Co., Ltd. is audited by PricewatherhouseCoopers Zhong Tian CPAs Limited Co., 普華永道中天會計師事務所有限公司.

(b) Investment costs and balances with subsidiaries:

	Year ended 31 December	
	2005	2004
Investment cost – subsidiaries	**922**	1,210
Amount due from subsidiaries	**1,207**	1,262
Amount due to subsidiaries	**(1,343)**	(1,196)
Total	**786**	1,276

38 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.

(a) Financial Restructuring and Recapitalization with MOF in 2004

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.

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

38 RELATED PARTY TRANSACTIONS *(Continued)*

(a) Financial Restructuring and Recapitalization with MOF in 2004 *(Continued)*

- 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 in exchange for RMB20,700 million in a bill issued by the PBOC (the "Bills"). The Bills bear 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.

- On 30 June 2004, under the authority of Cai Jin【2004】No. 58 issued by the MOF, the MOF subscribed 5,000 million shares at par with a total consideration of RMB5,000 million.

- On 30 June 2004, China Central Huijin Investment Co., Ltd., subscribed 3,000 million shares at par with a total consideration of RMB3,000 million.

The Transferred Loans related to the Group are summarized below.

	Transferred Loans
Impaired loans:	
Doubtful loans	41,415
Loss loans	8,300
Loss loans written off previously but not yet approved by the tax authority	3,305
	53,020
Less: Allowance for impairment losses on loans and advances *(Note18(b))*	(26,935)
Allowance for impairment losses already written off	(3,305)
	22,780
Fair value of consideration received, net of tax	(20,017)
Carrying value in excess of fair value of consideration received	2,763

38 RELATED PARTY TRANSACTIONS *(Continued)*

(b) Transactions with the MOF

Apart from the above financial restructuring and recapitalization transaction with the MOF, the Group also 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 period end, and related income for the year are as follows:

Treasury bonds

	Year ended 31 December	
	2005	2004
Purchase during the year	**36,646**	16,634
Redemption during the year	**(22,091)**	(8,305)
Interest income	**2,267**	2,361

	Year ended 31 December	
	2005	2004
Outstanding balance at beginning of the year	**59,281**	50,023
Outstanding at end of the year	**79,368**	59,281

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

38 RELATED PARTY TRANSACTIONS *(Continued)*

(c) Transactions with other state controlled entities

The state controlled entities are those over which the PRC government directly holds over 50% of the outstanding shares or voting rights, and has the ability to control or the power to govern their financial or operational policies.

The Group is ultimately controlled by the PRC government, which also directly and indirectly controls a significant number of entities through its government authorities, agencies and affiliates. Accordingly, the Group is likely to have extensive transactions with other State-controlled entities. These transactions are conducted in the ordinary course of the Group's banking business on terms similar to those that would have been entered into with non-state-owned entities. The Group has also established its pricing strategy and approval processes for major products and services, such as loans, deposits, investment securities, money market transactions and financial guarantees and credit related commitments. Such pricing strategy and approval processes do not depend on whether the customers are state-owned entities or not. The volumes of related party transactions, outstanding balances and related provisions at the year end, and the related expense and interest ranges for the year are as follows:

(i) Loans and advances to customers

	Year ended 31 December	
	2005	2004
Outstanding balance at beginning of the year	**190,497**	191,081
Outstanding balance at end of the year	**207,715**	190,497
Less: allowance for impairment losses	**(2,313)**	(1,871)
	205,402	188,626
Including: discounted bills	**6,477**	11,762
Interest rate range for discounted bills	**3.24%~5.742%**	2.97%~5.742%
Interest rate range of loans and advances other than discounted bills	**0.57%~8.37%**	4.698%~6.732%

The loan interest rate range stated above covers interest rates for loans granted in various currencies and periods.

38 RELATED PARTY TRANSACTIONS *(Continued)*

(c) Transactions with other state controlled entities *(Continued)*

(i) Loans and advances to customers (Continued)

	Year ended 31 December	
	2005	2004
Maximum balance during the year	**207,715**	197,725
Provision for impairment recognized/(reversed) during the year	**442**	(1,239)

(ii) Investment securities

	Year ended 31 December	
	2005	2004
Purchase during the year	**206,665**	141,297
Redemption during the year	**(17,463)**	(14,210)
Sales during the year	**(180,824)**	(49,343)
Interest income	**3,132**	2,543

	Year ended 31 December	
	2005	2004
Outstanding balance at beginning of the year	**148,390**	117,555
Outstanding balance at end of the year	**137,424**	148,390

Notes to the Consolidated Financial Statements (Continued)

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

38 RELATED PARTY TRANSACTIONS *(Continued)*

(c) Transactions with other state controlled entities *(Continued)*

(iii) Due from other banks and financial institutions

	Year ended 31 December	
	2005	2004
Outstanding balance at beginning of the year	**39,140**	43,472
Outstanding balance at end of the year	**101,504**	39,140
Less: allowance for impairment losses	**(733)**	(994)
	100,771	38,146

	Year ended 31 December	
	2005	2004
Maximum balance during the year	**101,504**	54,120
Provision for impairment recognised/(reversed) during the year	**(149)**	324

(iv) Due to other banks and financial institutions

	Year ended 31 December	
	2005	2004
Outstanding balance at beginning of the year	**20,894**	10,125
Outstanding balance at end of the year	**73,797**	20,894

	Year ended 31 December	
	2005	2004
Maximum balance during the year	**73,797**	30,325

38 RELATED PARTY TRANSACTIONS *(Continued)*

(c) Transactions with other state controlled entities *(Continued)*

(v) Due to customers

	Year ended 31 December	
	2005	2004
Outstanding balance at beginning of the year	**112,197**	60,646
Outstanding balance at end of the year	**560,549**	112,197

	Year ended 31 December	
	2005	2004
Maximum balance during the year	**848,417**	134,520

(vi) Financial guarantees and credit related commitments

	As at 31 December	
	2005	2004
Guarantees	**22,954**	5,432
Letters of credit	**6,111**	14,492
Acceptances	**19,673**	9,703
Derivative transactions unsettled	**940**	3,899

Notes to the Consolidated Financial Statements (Continued)

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

38 RELATED PARTY TRANSACTIONS *(Continued)*

(d) 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 under commercial terms and at market rates 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 2004 and 2005, outstanding balances at the balance sheet date are as follows:

(i) Loans

	Year ended 31 December	
	2005	2004
Outstanding at beginning of the year	**9**	4
Granted during the year	**16**	8
Repaid during the year	**(15)**	(3)
Outstanding at end of the year	**10**	9

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

(ii) Deposits

	Year ended 31 December	
	2005	2004
Outstanding at beginning of the year	**29**	18
Deposited during the year	**129**	92
Repaid during the year	**(124)**	(81)
Outstanding at end of the year	**34**	29

38 RELATED PARTY TRANSACTIONS *(Continued)*

(e) Transactions with HSBC

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. On 23 June 2005 and 4 July 2005, HSBC further subscribed 462 million shares and 878 million shares at an issue price of HKD2.50 per share with a total consideration of HKD3,350 million (equivalent to RMB3,566 million). The excess over par value of HKD2,091 million (equivalent to RMB2,226 million) was included in capital surplus. Other transactions between the Group and HSBC are mainly banking activities under commercial terms and at market rates. Detail transaction volumes since the above share acquisition are set out below:

(i) Placement with HSBC

	Year ended 31 December 2005	Period from 18 August to 31 December 2004
Outstanding at beginning of the period/year	**100**	2,063
Granted during the period/year	**231,869**	57,658
Repaid during the period/year	**(227,315)**	(59,621)
Outstanding at end of the period/year	**4,654**	100
Interest income	**16**	4

(ii) Deposits from HSBC

	Year ended 31 December 2005	Period from 18 August to 31 December 2004
Outstanding at beginning of the period/year	**1,218**	985
Deposited during the period/year	**60,778**	14,530
Repaid during the period/year	**(59,678)**	(14,297)
Outstanding at end of the period/year	**2,318**	1,218
Interest expense on deposits	**36**	5

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

38 RELATED PARTY TRANSACTIONS *(Continued)*

(e) Transactions with HSBC *(Continued)*

(iii) Investment securities

	Year ended 31 December 2005	Period from 18 August to 31 December 2004
Interest income	**22**	8

	As at 31 December 2005	2004
Outstanding balance	**568**	414

(iv) Financial guarantees and credit related commitments

	As at 31 December 2005	2004
Guarantees	**7**	8
Letters of credit	**347**	17
Derivative transactions unsettled	**28,768**	10,943

39 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 overseas subsidiaries and the following branches: Hong Kong, New York, Singapore, Tokyo and Seoul.

39 SEGMENTAL INFORMATION

(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 2005								
Assets								
Cash and balances with central banks	11,289	4,361	108,266	10,427	5,360	606	–	140,309
Due from other banks and financial institutions	25,492	2,091	113,979	10,733	3,160	15,230	(584)	170,101
Financial assets held for trading	–	–	112	–	–	3,116	–	3,228
Loans and advances to customers	128,284	52,192	318,138	145,998	68,932	42,569	2,660	758,773
Investment securities								
– originated loans	130	78	28,091	35	38	–	–	28,372
– available-for-sale	21,760	14,523	193,042	23,020	8,737	24,889	–	285,971
Other assets	23,315	8,732	7,568	15,723	8,039	10,561	(37,253)	36,685
Total assets	210,270	81,977	769,196	205,936	94,266	96,971	(35,177)	1,423,439
Liabilities								
Due to other banks and financial institutions	(32,262)	(4,297)	(34,104)	(7,192)	(2,368)	(3,912)	41	(84,094)
Financial liabilities held for trading	–	–	(141)	–	–	(9,414)	–	(9,555)
Due to customers	(217,460)	(115,118)	(462,960)	(245,324)	(119,951)	(63,408)	3,382	(1,220,839)
Other liabilities	(4,909)	(2,759)	(22,485)	(6,827)	(3,197)	(17,382)	31,754	(25,805)
Total liabilities	(254,631)	(122,174)	(519,690)	(259,343)	(125,516)	(94,116)	35,177	(1,340,293)
Net on balance sheet position	(44,361)	(40,197)	249,506	(53,407)	(31,250)	2,855	–	83,146
Acquisition cost of property and equipment ("PPE") and intangible assets	461	348	1,794	474	440	118	–	3,635

Notes to the Consolidated Financial Statements (Continued)

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

39 SEGMENTAL INFORMATION *(Continued)*

(a) Geographical segment information *(Continued)*

	Northern China	North-eastern China	Eastern China	Central & Southern China	Western China	Overseas	Eliminations & Consolidated	Group Total
For the year ended 31 December 2005								
Interest income	8,205	3,912	27,416	9,281	4,271	3,028	(6,433)	49,680
Interest expense	(3,278)	(1,769)	(12,743)	(3,234)	(1,534)	(1,964)	6,433	(18,089)
Net interest income	4,927	2,143	14,673	6,047	2,737	1,064	–	31,591
Fee and commission income	321	190	930	470	186	447	–	2,544
Fee and commission expense	(50)	(38)	(128)	(81)	(33)	(105)	–	(435)
Net fee and commission income	271	152	802	389	153	342	–	2,109
Dividend income	–	–	39	3	–	3	–	45
Gains less losses arising from trading activities	218	54	(510)	125	24	509	–	420
Gains less losses arising from investment securities	103	–	258	17	–	(19)	–	359
Other operating income	33	18	249	58	33	238	–	629
Reversal/(Impairment) losses on loans and advances	(505)	(787)	(868)	(915)	(1,237)	14	–	(4,298)
Other operating expenses	(1,879)	(1,911)	(8,209)	(3,535)	(1,695)	(783)	–	(18,012)
Operating profit/(loss) before tax	3,168	(331)	6,434	2,189	15	1,368	–	12,843
Income tax	(1,046)	(216)	(609)	(1,113)	(392)	(224)	–	(3,600)
Net profit/(loss) for the year	2,122	(547)	5,825	1,076	(377)	1,144	–	9,243
Depreciation and amortization of property and equipment and intangible assets	238	288	1,149	428	244	127	–	2,474

39 SEGMENTAL INFORMATION *(Continued)*

(a) Geographical segment information *(Continued)*

	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
Financial assets held for trading	–	–	47	–	–	2,448	–	2,495
Loans and advances to customers	104,316	49,447	258,112	125,272	59,325	33,976	1,164	631,612
Investment securities								
– loans and receivables	114	7	30,711	225	148	–	–	31,205
– available-for-sale	18,957	11,793	128,227	19,257	9,642	27,647	–	215,523
Other assets	10,377	8,061	25,059	13,319	7,419	10,827	(29,316)	45,746
Total assets	152,212	74,823	583,286	174,297	83,245	105,961	(29,819)	1,144,005
Liabilities								
Due to other banks and financial institutions	(3,950)	(2,694)	(12,699)	(4,342)	(940)	(7,921)	835	(31,711)
Financial liabilities held for trading	–	–	(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	(29,104)	(30,009)	171,158	(40,366)	(21,690)	2,114	–	52,103
Acquisition cost of property and equipment and intangible assets	603	368	1,048	705	436	119	–	3,279

Notes to the Consolidated Financial Statements *(Continued)*

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

39 SEGMENTAL INFORMATION *(Continued)*

(a) Geographical segment information *(Continued)*

	Northern China	North-eastern China	Eastern China	Central & Southern China	Western China	Overseas	Eliminations & Consolidated	Group Total
Year ended 31 December 2004								
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
Reversal/(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/(loss) 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/(loss) for the year	715	(851)	376	1,475	(214)	103	–	1,604
Depreciation and amortization of property and equipment and intangible assets	290	321	1,151	464	285	112	–	2,623

39 SEGMENTAL INFORMATION *(Continued)*

(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 2005					
Total carrying amount of segment assets	**612,441**	**112,593**	**663,733**	**34,672**	**1,423,439**
Segment revenue	**33,248**	**6,282**	**13,323**	**824**	**53,677**
Depreciation and amortization of PPE and intangible assets	**–**	**–**	**–**	**2,474**	**2,474**
Acquisition cost of PPE and intangible assets	**–**	**–**	**–**	**3,635**	**3,635**
As at 31 December 2004					
Total carrying amount of segment assets	524,732	90,780	487,125	41,368	1,144,005
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

Notes to the Consolidated Financial Statements (Continued)

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

SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION

1 CAPITAL ADEQUACY AND LIQUIDITY RATIOS

Group

	As at 31 December	
	2005	2004
Capital adequacy ratio	**11.20%**	9.72%
Liquidity ratios: RMB current assets to RMB current liabilities	**63.23%**	66.30%
Foreign currency current assets to foreign currency current liabilities	**110.74%**	57.05%

The above capital adequacy and liquidity ratios are calculated in accordance with the formula promulgated by the PBOC and China Banking Regulatory Commission and based on PRC GAAP.

Notes to the Consolidated Financial Statements (Continued)

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

2 COMPONENTS OF CAPITAL BASE AFTER DEDUCTIONS

The capital base after deductions used in the calculation of the above capital adequacy ratio as at end of each period is analysed as below. All the figures included in the calculation are extracted from PRC GAAP statements of the Bank.

Group

	As at 31 December	
	2005	2004
Core capital:		
Paid up ordinary share capital	**45,934**	39,070
Reserves	**18,100**	34,948
Profit and loss account	**8,113**	(26,558)
Minority interest	**70**	–
	72,217	47,460
Supplementary capital:		
Reserves on revaluation of land and interests in land	**–**	–
Impairment allowances for impaired assets and regulatory reserves.	**10,935**	9,161
Term subordinated debt	**9,600**	12,000
Reserve-net profit of overseas branches retained	**–**	–
Gross value of supplementary capital	**20,535**	21,161
Eligible value of supplementary capital	**20,535**	21,161
Total capital base before deductions	**92,752**	68,621
Deductions:		
Unconsolidated equity investments	**(1,743)**	(1,894)
Total capital base after deductions	**91,009**	66,727

The “Unconsolidated equity investments” is calculated in accordance with the “Administrative Measures on the Capital Adequacy Ratio of Commercial Banks” issued by the China Banking Regulatory Commission on 23 February 2004.

3 CURRENCY CONCENTRATIONS

Group

	US Dollars	HK Dollars	Others	Total
As at 31 December 2005				
Spot assets	**110,330**	**46,980**	**20,069**	**177,379**
Spot liabilities	**(94,289)**	**(51,526)**	**(18,360)**	**(164,175)**
Forward purchases	**16,052**	**264**	**4,994**	**21,310**
Forward sales	**(14,821)**	**(337)**	**(7,630)**	**(22,788)**
Net options position	**282**	**–**	**–**	**282**
Net long/(short) position	**17,554**	**(4,619)**	**(927)**	**12,008**
Net structural position	**3,704**	**5,838**	**356**	**9,898**
As at 31 December 2004				
Spot assets	102,341	45,239	19,992	167,572
Spot liabilities	(93,178)	(50,001)	(17,439)	(160,618)
Forward purchases	26,649	21,886	1,679	50,214
Forward sales	(23,238)	(20,938)	(6,124)	(50,300)
Net options position	250	20	338	608
Net long/(short) position	12,824	(3,794)	(1,554)	7,476
Net structural position	2,132	4,722	133	6,987

The net options position is calculated using the model user approach as set out in the banking return of the HKMA. The net structural position of the Group includes the structural positions of the Bank's overseas branches, banking subsidiaries and other subsidiaries substantially involved in foreign exchange. Structural assets and liabilities include:

- Investments in fixed assets and premises, net of depreciation charges;
- Capital and statutory reserves of overseas branches;
- Investments in overseas subsidiaries and related companies; and
- Loan capital.

Notes to the Consolidated Financial Statements (Continued)

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

4 CROSS-BORDER CLAIMS

The Group is principally engaged in business operations within Mainland China, and regards all claims on third parties outside Mainland China as cross border claims.

Cross-border claims include loans and advances, balances and placements with banks and other financial institutions, holdings of trade bills and certificates of deposit and investment securities.

Cross-border claims have been disclosed by different country or geographical areas. A country or geographical area is reported where it constitutes 10% or more of the aggregate amount of cross-border claims, after taking into account any risk transfers. Risk transfer is only made if the claims are guaranteed by a party in a country which is different from that of the counterparty or if the claims are on an overseas branch of a bank whose head office is located in another country.

	Bank and other financial institutions	**Public sector entities**	**Others**	**Total**
As at 31 December 2005				
Asia Pacific excluding Mainland China	**35,778**	**3,317**	**35,187**	**74,282**
– of which attributed to Hong Kong	**2,815**	**3,146**	**31,530**	**37,491**
North and South America	**11,447**	**1,462**	**4,351**	**17,260**
Europe	**37,036**	**196**	**162**	**37,394**
	84,261	**4,975**	**39,700**	**128,936**
As at 31 December 2004				
Asia Pacific excluding Mainland China	29,201	500	4,550	34,251
– of which attributed to Hong Kong	22,219	–	1,724	23,943
North and South America	10,185	1,459	4,210	15,854
Europe	24,414	231	947	25,592
Middle East and Africa	–	–	49	49
	63,800	2,190	9,756	75,746

5 OVERDUE AND RESCHEDULED ASSETS

(a) Advances

(i) Gross amount of overdue loans

Group and Bank

	As at 31 December	
	2005	2004 Restated
Gross advances to customers which have been overdue for:		
– within 3 months	**5,250**	5,215
– between 3 and 6 months	**3,331**	2,958
– between 6 and 12 months	**4,912**	3,278
– over 12 months	**9,024**	4,942
	22,517	16,393
Percentage:		
– within 3 months	**0.68%**	0.82%
– between 3 and 6 months	**0.43%**	0.46%
– between 6 and 12 months	**0.64%**	0.51%
– over 12 months	**1.17%**	0.77%
	2.92%	2.56%
Gross advances to banks and other financial institutions which have been overdue for:		
– within 3 months	**–**	–
– between 3 and 6 months	**–**	–
– between 6 and 12 months	**–**	–
– over 12 months	**743**	1,004
	743	1,004
Percentage:		
– within 3 months	**–**	–
– between 3 and 6 months	**–**	–
– between 6 and 12 months	**–**	–
– over 12 months	**0.43%**	1.12%
	0.43%	1.12%

Notes to the Consolidated Financial Statements (Continued)

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

5 OVERDUE AND RESCHEDULED ASSETS *(Continued)*

(a) Advances *(Continued)*

(ii) *Overdue loans and advances to customers by geographical area*

Group and Bank

	As at 31 December	
	2005	2004 Restated
Domestic regions		
– Northern China	**2,748**	2,054
– North-eastern China	**3,646**	4,274
– Eastern China	**4,708**	3,756
– Central & Southern China	**5,710**	3,426
– Western China	**5,090**	2,458
	21,902	15,968
Hong Kong and overseas countries	**615**	425
	22,517	16,393

(iii) *Overdue and rescheduled loans*

Group and Bank

	As at 31 December 2005
Total rescheduled loans and advances to customers	**9,781**
Less: total overdue rescheduled loans and advances to customers	**(4,249)**
Total normal rescheduled loans and advances to customers	**5,532**
Percentage of normal part in total rescheduled loans	**57%**

5 OVERDUE AND RESCHEDULED ASSETS *(Continued)*

(b) Investment securities-available-for-sale

Group and Bank

	As at 31 December	
	2005	2004
Overdue for:		
– three months or less	**–**	41
– between 3 and 6 months	**–**	–
– between 6 and 12 months	**–**	–
– over 12 months	**–**	31
	–	72

Group and Bank

	As at 31 December	
	2005	2004
Foreclosed assets	**5,483**	6,832

Notes to the Consolidated Financial Statements (Continued)

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

6 BUSINESS SEGMENT INFORMATION

Group

	Fourth Quarter ended December 31, 2005				
	Corporate	Retail	Treasury	Others and unallocated	Total
External net interest income/(expense)	5,488	(160)	3,125	47	8,500
Internal net interest income/(expense)	545	2,198	(2,743)	–	–
Net interest income	6,033	2,038	382	47	8,500
Net fee and commission income	297	336	11	37	681
Dividend income	–	–	2	23	25
Gains less losses arising from trading activities	187	56	303	(7)	539
Gains less losses arising from investment securities	–	–	(18)	–	(18)
Other operating income	8	1	108	261	378
Impairment losses on loans and advances	(1,675)	7	100	–	(1,568)
Other operating expenses					
– depreciation and amortisation	–	–	–	(738)	(738)
– others	(2,574)	(1,414)	(239)	(914)	(5,141)
Operating profit before tax	2,276	1,024	649	(1,291)	2,658
Capital expenditure	–	–	–	1,413	1,413
Segment assets	612,441	112,593	663,733	34,672	1,423,439
Segment liabilities	776,898	443,180	106,702	13,513	1,340,293