



## **Bank of Communications Co., Ltd.**

(A joint stock company incorporated in the People's Republic of China with limited liability)

Stock Code: 3328

Interim Report 2006

# C O N T E N T S

Bank of Communications Co., Ltd.  
Interim Report 2006

I.	Financial Highlights	2
II.	Company Information	3
III.	Management Discussion and Analysis	4
IV.	Additional Information	17
V.	Independent Review Report	20
VI.	Unaudited Condensed Consolidated Interim Financial Information	21
VII.	Supplementary Unaudited Financial Information	81
VIII.	Reconciliation of Net Assets and Net Profit from PRC GAAP to IFRS	89

## I. FINANCIAL HIGHLIGHTS

(Amounts expressed in millions of RMB unless otherwise stated)

Item	Half-year ended 30 June 2006	Half-year ended 30 June 2005
<b>Operation indicators</b>		
Net interest income	<b>18,344</b>	14,942
Operating profit before tax	<b>9,257</b>	6,884
Net profit	<b>6,034</b>	4,605
Impairment losses on loans and advances	<b>(1,971)</b>	(1,918)
Return on total assets (Note 1)	<b>0.38%</b>	0.36%
Return on shareholders' equity (Note 2)	<b>7.17%</b>	6.17%
Basic and diluted earnings per share (in RMB)	<b>0.13</b>	0.12
	<b>30 June 2006</b>	31 December 2005
Shareholders' equity (Note 3)	<b>84,177</b>	83,082
Total assets	<b>1,588,988</b>	1,423,439
Net assets per share (in RMB)	<b>1.84</b>	1.81
Cost to income ratio (Note 4)	<b>44.36%</b>	51.24%
Impaired loan ratio (Note 5)	<b>2.48%</b>	2.80%
Tier-1 capital adequacy ratio (Note 6)	<b>8.39%</b>	8.78%
Capital adequacy ratio (Note 6)	<b>11.07%</b>	11.20%

Note 1: This ratio represents the net profit of the reporting period to the total assets at the end of the reporting period.

Note 2: This ratio represents the net profit of the reporting period to the shareholders' equity at the end of the reporting period.

Note 3: Bank shareholders' equity.

Note 4: This ratio represents the other operating expenses to the operating income (including net interest income, net fee and commission income, dividend income, gains less losses arising from trading activities, gains less losses arising from de-recognition of investment securities and other operating income).

Note 5: The impaired loan ratio represents the balance of impaired loan to the balance of loan before provision at the end of the reporting period.

Note 6: The ratio was calculated in accordance with the formula promulgated by the China Banking Regulatory Commission and the PRC GAAP.

## II. COMPANY INFORMATION

### LEGAL NAME

Bank of Communications Co., Ltd.

### DIRECTORS

#### *Executive Directors*

Li Jun  
Peng Chun  
Zhang Jixiang

#### *Non-Executive Directors*

Jiang Chaoliang (*Chairman of the Board of Directors*)  
Hu Huating  
Peter Wong Tung Shun  
Laura M. Cha  
Li Keping  
Li Zexing  
Gao Shiqing  
Shen Weiming  
Li Guanglin  
Qian Ping

#### *Independent Non-Executive Directors*

Xie Qingjian  
Ian Ramsay Wilson  
Thomas Joseph Manning  
Herbert Hui Ho Ming  
Chen Qingtai

### SUPERVISORS

Cui Leiping (*Chairman of the Board of Supervisors*)  
Ning Jinbiao  
Teng Tiej  
Ji Kelian  
Liu Qiang  
Chen Zheng  
Liu Sha  
Chen Qing  
Li Jun

### SECRETARY OF THE COMPANY

Zhang Jixiang

### AUTHORIZED REPRESENTATIVE

Zhang Jixiang

### DOMICILE OF THE COMPANY AND CONTACT FOR INVESTORS

188 Yin Cheng Zhong Lu, Shanghai  
Zip Code: 200120  
Tel: 86-21-58766688  
Fax: 86-21-58798398  
E-mail: dongban@bankcomm.com  
Website: www.bankcomm.com

### PLACE OF BUSINESS IN HONG KONG

20 Pedder Street, Central, Hong Kong

### AUDITORS

PricewaterhouseCoopers  
Deloitte Touche Tohmatsu CPA Ltd.

### HONG KONG LEGAL ADVISOR

Herbert Smith

### PRC LEGAL ADVISOR

King & Wood

### COMPLIANCE ADVISOR

Goldman Sachs (Asia) L.L.C.

### H-SHARE REGISTRAR

Computershare Hong Kong Investor Services Limited  
Rooms 1712-1716, 17th Floor, Hopewell Centre  
No.183, Queen's Road East, Hong Kong

### LISTING INFORMATION

Listing Place: The Stock Exchange of Hong Kong Limited  
Stock Type: H Share  
Stock Code: 3328

The Report is prepared in Chinese and English respectively. The English version is for reference only. In case of any inconsistency, the Chinese version shall prevail.

### III. MANAGEMENT DISCUSSION AND ANALYSIS

#### (I) BUSINESS OVERVIEW

During the first half of the year, the Group proactively responded to China's macro-economic adjustments, further enhanced its product innovation and achieved steady progress in the core business segments. Operationally, the Group did not only further optimize the business structure, but also launched more diversified products and services. Financially, impaired loan ratio declined, cost to income ratio improved further, and overall profitability continued to grow steadily.

By the end of the reporting period, the total assets of the Group reached RMB1,589 billion, representing an increase of RMB165.6 billion or 11.63% compared with the end of last year. The net profit reached RMB6.034 billion, representing an increase of RMB1.429 billion or 31.03% over the same period of last year. Return on total assets (annualized) reached 0.76% and return on shareholders' equity (annualized) reached 14.34%. The capital adequacy ratio reached 11.07% and the Tier-1 capital adequacy ratio reached 8.39%. Impaired loan ratio went down by 0.32 percentage points to 2.48% as compared with the end of last year.

The Group's outstanding performance has won itself the "Best Bank in China" for the year 2006 from *Euromoney*, one of the world's leading financial journals.

#### (II) OPERATION REVIEW

##### *Steady growth of loans and deposits and further expanded business*

By the end of the reporting period, the total outstanding loans to customers (before provision for impairment and including interests receivables, and the same hereinafter if not otherwise stated) amounted to RMB901.1 billion, increasing by RMB129.7 billion or 16.81% over the end of the previous year, among which, discounted bills amounted to RMB117.7 billion, representing an increase of RMB56.9 billion or 93.42% over the end of last year. Total deposits from customers (including interests payables, and the same hereinafter if not otherwise stated) reached RMB1,347 billion, representing an increase of RMB126.2 billion or 10.33% over the end of last year.

##### *Further improved loan customer and sector mix*

The Group's corporate loan customer structure at the mainland branches continued to improve. By the end of the reporting period, based on 10-category classification system, the proportion of loans to class 1-5 customers increased to 69.39%; the proportion of loans to 8-10 class customers dropped to 2.04%. Sector mix kept on improving as well, with loans to the service, petrochemical, transportation, and electric power sectors growing substantially and those to the real estate, steel, retail, hotel and restaurants and education being brought under effective control. Thus, the industrial distribution of loans was maintained at a reasonable level. "Zhan Ye Tong" ("SME Quick"), a new product developed by the Bank to provide packaged products and services to small and medium-sized enterprises ("SME"), was further promoted. By the end of the reporting period, the total number of SME clients increased by 1,081 over the end of last year and the balance of the loans to SME increased by RMB18.7 billion.

***Timely implementation of personal financial services strategy with more diversified retail products***

The Group established medium and long-term goals for retail business and reorganized the operational structure of the retail business at the head office level. An all-round cooperation with HSBC in the retail banking area began to unfold and HSBC support continued to evolve at management level. All these had greatly enhanced product innovation capability of the Bank. The number of dual-currency credit cards in force increased rapidly. By the end of the reporting period, the number of cards issued reached 1.08 million and the average card consumption, active cards ratio and interest-bearing principal ratio were maintained at a good level, indicating that the cards were of relatively high quality. “OTO Fortune” was introduced officially, through optimized resources allocation, as an up-market service platform for preferred customer segment.

***Further optimized structure of net operating income with proactive exploration of short-term corporate bonds underwriting***

As at the end of the reporting period, the net fee and commission income of the Group reached RMB1.296 billion, representing an increase of RMB418 million or 47.61% over the same period of last year. The net fee and commission income accounted for 6.42% of the net operating income, representing an increase of 1.24 percentage points over the same period of last year. Big efforts have also been made to develop high-end businesses including the underwriting of short-term corporate bonds. During the reporting period, the Group has acted as the lead underwriter for four short-term corporate bonds in a total amount of RMB22.3 billion.

***Product innovation going on with good momentum and the innovation capability further enhanced***

The Group was among the first batch of banks acquiring QDII business qualification and became the custodian bank for the first securitized lease assets in mainland China. The Group also timely introduced “Two-Currency Treasure”, a RMB personal wealth management product, which aimed at cross-managing RMB and foreign currencies and which proved to be a breakthrough in the field of RMB personal wealth management.

***Loan quality further improved along with enhanced risk management***

The Group further strengthened its internal control and risk management while various researches had also been done in managing credit, market and operational risks. The roles of various risk management tools have been brought into full play in identifying, early-warning and dispersing potential risks. The Group found out the case of Binhu Sub-Branch of Shenyang Branch and immediately took effective measures to lower the risk and reduce the losses. At the same time, pursuant to the principle of prudence, the Group made the provision of RMB100 million for the above case.

As at the end of the reporting period, the impaired loan ratio was 2.48%, down by 0.32 percentage points as compared with the end of last year. The credit cost ratio (annualized) was 0.44%, down by 0.08 percentage points over the same period of last year. The provision coverage for impaired loans increased from 58.39% at the end of last year to 63.46%, and if taking the total RMB4.428 billion of

general and statutory reserves into account, the Group's actual provision coverage for impaired loans would be 83.26% by the end of the reporting period. Furthermore, based on PRC regulator's standard, by the end of the reporting period, the provision coverage for non-performing loan ("NPL") was 111.65%, and if taking the total RMB4.428 billion of general and statutory reserves into account, the Group's actual provision coverage for NPL would be as high as 135.78%.

#### **Further strengthened cost control along with increased income**

While striving to improve operating income, the Group has also managed to control costs and expenses, thus the cost to income ratio continued to fall. By the end of the reporting period, the cost to income ratio was 44.36%, down by 3.70 percentage points over the same period of last year.

### **(III) FINANCIAL PERFORMANCE**

The Group's profitability continued to improve, and net interest spread recovered. By the end of the reporting period, the Group recorded a net profit of RMB6.034 billion, representing an increase of RMB1.429 billion or 31.03% over the same period of last year. Cost to income ratio was 44.36%, representing a decrease of 3.70 percentage points over the same period of last year. Net interest spread was 2.52%, representing a decrease of 6 basis points compared with that of last year and up by 8 basis points over the first quarter. Net interest margin was 2.57%, representing a decrease of 7 basis points as compared with that of last year and up by 6 basis points over the first quarter. Return on total assets (annualized) was 0.76%, up by 4 basis points over the same period of last year and return on shareholders' equity (annualized) was 14.34%, up by 2 percentage points over the same period of last year.

#### **1. Operating profit before tax**

The major components of operating profit before tax were net interest income and net fee and commission income. By the end of the reporting period, the Group recorded a net interest income of RMB18.344 billion, increasing by 22.77% over the same period of last year. The net interest income accounted for 90.90% of the total net operating income, up by 2.73 percentage points over the same period of last year. Net fee and commission income reached RMB1.296 billion, increasing by 47.61% over the same period of last year. Net fee and commission income accounted for 6.42% of the net operating income, increasing by 1.24 percentage points over the same period of last year.

The table below shows the details of the Group's sources of operating profits before tax for the periods indicated:

*(in millions of RMB)*

	<b>Half-Year ended 30 June</b>	
	<b>2006</b>	2005
Net interest income	<b>18,344</b>	14,942
Net fee and commission income	<b>1,296</b>	878
Impairment losses on loans and advances	<b>(1,971)</b>	(1,918)
Operating profit before tax	<b>9,257</b>	6,884

## 2. Net interest income

As at the end of reporting period, the Group recorded a net interest income of RMB18.344 billion, increasing by RMB3.402 billion or 22.77% as compared with the same period of last year.

The table below shows the major components of interest income, interest expenses and the associated net interest margin and net interest spread for the periods indicated:

(in millions of RMB, except percentages)

	<b>Half-year ended 30 June 2006</b>	Year ended 31 December 2005
<b>Interest income</b>		
Balances with central banks	<b>952</b>	1,815
Due from other banks and financial institutions	<b>2,990</b>	3,375
Trading securities	–	9
Loans and advances to customers	<b>20,797</b>	36,305
Investment securities	<b>4,809</b>	8,114
Others	<b>53</b>	62
<b>Total interest income</b>	<b>29,601</b>	49,680
<b>Interest expenses</b>		
Due to other banks and financial institutions	<b>1,541</b>	1,548
Due to customers	<b>9,716</b>	16,541
<b>Total interest expenses</b>	<b>11,257</b>	18,089
<b>Net interest income</b>	<b>18,344</b>	31,591
<b>Net interest spread<sup>(1)</sup></b>	<b>2.52%<sup>(3)</sup></b>	2.58%
<b>Net interest margin<sup>(2)</sup></b>	<b>2.57%<sup>(3)</sup></b>	2.64%

(1) This represents the difference between the average yield of total average interest-earning assets and average cost of total average interest-bearing liabilities.

(2) This represents the ratio of net interest income to the average interest-earning assets.

(3) Annualized indication rates: which are calculated by the interest rate (based on income and expense) for the first half year multiplied by 2, excluding the impact of personal wealth management products.

Although both the net interest spread and net interest margin dropped as compared with the end of last year, they picked up again over the first quarter. The main reasons are: firstly, the total loan outstanding against the daily average interest-earning assets rose from 55.31% of the first quarter to 56.67%; secondly, influenced by macro economic adjustments and the revived capital market that re-activated IPO and refinancing, money market interest rate went up substantially and thus greatly improved the yield of treasury operation; thirdly, the deposit cost ratio declined while the proportion of the total clients' deposits against the daily average interest-bearing liabilities rose from 92.67 % of the first quarter to 93.20 %, driving down the total cost of the liabilities.



The table below shows the average daily balance and the interest rates of our interest-earning assets and interest-bearing liabilities for the periods indicated:

(in millions of RMB, except percentages)

	Half-year ended 30 June 2006			Three months ended 31 March 2006			Year ended 31 December 2005		
	Average balance <sup>(1)</sup>	Interest income (expense)	Average yield (cost) <sup>(2)</sup>	Average balance <sup>(1)</sup>	Interest income (expense)	Average yield (cost) <sup>(2)</sup>	Average balance <sup>(1)</sup>	Interest income (expense)	Average yield (cost)
<b>Assets</b>									
Cash and balances with central banks	133,870	952	1.42%	132,131	465	1.41%	125,179	1,815	1.45%
Due from other banks and financial institutions	159,773	2,990	3.74%	170,537	1,421	3.33%	112,776	3,375	2.99%
Loans and advances to customers	807,482	20,797	5.15%	773,434	10,126	5.24%	694,903	36,305	5.22%
Investment securities and others	333,363	4,862	2.92%	322,257	2,326	2.89%	265,921	8,185	3.08%
Interest-earning assets	1,424,824 <sup>(3)</sup>	29,370 <sup>(3)</sup>	4.12%	1,398,359	14,338	4.10%	1,198,779	49,680	4.14%
Non-interest-earning assets	71,650			55,260			50,988		
Total assets	1,496,474			1,453,619			1,249,767		
<b>Liabilities and shareholders' equity</b>									
Due to customers	1,281,535	9,716	1.52%	1,242,252	4,853	1.56%	1,095,578	16,541	1.51%
Due to other banks and financial institutions	91,175	1,260	2.76%	85,970	556	2.59%	51,793	991	1.91%
Subordinated term debt	12,000	281	4.68%	12,309	142	4.61%	12,210	557	4.56%
Total interest-bearing liabilities	1,375,046 <sup>(3)</sup>	11,026 <sup>(3)</sup>	1.60%	1,340,531	5,551	1.66%	1,159,581	18,089	1.56%
Shareholders' equity and non-interest-bearing liabilities	121,428			113,088			90,186		
Liabilities and shareholders' equity	1,496,474			1,453,619			1,249,767		

(1) Daily average balance was calculated in accordance with PRC GAAP and adjusted in accordance with IFRS.

(2) Annualized indicators, which were calculated by the interest rates (based on income and expense) for the first half year multiplied by 2 or interest rates for the first quarter multiplied by 4.

(3) Exclude the impact of the personal wealth management products.

The table below shows the changes of interest income and interest expenses of the Group due to changes in volume and rates. Volume and rate variances have been calculated based on movements in average balances over these periods and changes in interest rates on interest-earning assets and interest-bearing liabilities.

(in millions of RMB)

	Comparison between half-year ended 30 June 2006 and year ended 31 December 2005 <sup>(1)</sup>			Comparison between 2005 and 2004		
	Increase/(Decrease) due to			Increase/(Decrease) due to		
	Volume	Interest rate	Net increase/(decrease)	Volume	Interest rate	Net increase/(decrease)
<b>Interest-earning assets</b>						
Cash and balances with central banks	126	(37)	89	221	(261)	(40)
Due from other banks and financial institutions	1,406	1,199	2,605	333	811	1,144
Loans and advances to customers	5,877	(588)	5,289	6,053	1,965	8,018
Investment securities and others	2,076	(537)	1,539	2,442	(236)	2,206
Change in interest income	9,485	37	9,522	9,049	2,279	11,328
<b>Interest-bearing liabilities</b>						
Due to customers	2,808	83	2,891	2,048	2,462	4,510
Due to other banks and financial institutions	753	776	1,529	325	(188)	137
Subordinated term debt	(10)	15	5	274	8	282
Change in Interest Expense	3,551	874	4,425	2,647	2,282	4,929

(1) In the comparison between the figures for the half-year ended 30 June 2006 and those for the year ended 31 December 2005, the formulae for calculating the impact of the changes in volume and interest rate on the changes in income and expenses were as follows:

Impact of changes in volume = (average balance for the first half year of 2006 - average balance of for the year ended 31 December 2005) \* average interest rate for the year ended 31 December 2005.

Impact of changes in interest rates = (annualized average interest rate for the first half year of 2006 - average interest rate for the year ended 31 December 2005) \* average balance for the first half year of 2006.

### 3. *Non-interest income*

As at the end of the reporting period, the Group recorded a non-interest income of RMB1.836 billion, representing a decrease of RMB169 million over the same period of last year, of which net fee and commission income amounted to RMB1.296 billion, representing an increase of RMB418 million or 47.61% over the same period of last year.

### 4. *Other operating expenses*

As at the end of the reporting period, other operating expenses of the Group were RMB8.952 billion, representing an increase of RMB807 million or 9.91% over the same period of last year, of which, the labour cost was RMB2.73 billion.

Cost to income ratio of the Group continued to decline, dropping from 48.06% of the same period of previous year to 44.36%, down by 3.70 percentage points as compared with the same period of last year or 6.88 percentage points as compared with that of last year. These achievements could be attributable to the Group's efforts in improving efficiency and strengthening cost control. The operating expenses increased by 9.91% over the same period of last year, which was 9.17 percentage points lower than the growth of 19.08% of net operating income.

### 5. *Impairment losses on loans and advances*

The Group's impairment losses on loans and advances consisted of the impairment losses on impaired loans and on advances to customers (less recovery of loans previously written off) and the provision for due from other banks and financial institutions as well as securities purchased under resale agreements.

The impairment losses on loans and advances increased slightly from RMB1.918 billion of the same period of last year to RMB1.971 billion of the reporting period.

As at the end of the reporting period, the credit cost ratio (annualized) was 0.44%, decreasing by 0.08 percentage points over the same period of last year.

### 6. *Income tax*

The table below shows the breakdown of the Group's current tax and deferred tax for the period indicated:

*(in millions of RMB)*

	<b>Half-year ended June 30</b>	
	<b>2006</b>	2005
Current tax	<b>3,520</b>	144
Deferred tax	<b>(298)</b>	2,135

The Group and its subsidiaries established in the PRC were subject to the PRC statutory tax rate of 33% for the period. The Group's Hong Kong Branch and its subsidiaries established in Hong Kong were subject to a tax rate of 17.5% for the period. The Group's other overseas branches were subject to the income tax rates of their respective jurisdictions where they were located.

**(IV) ASSETS**

As at the end of the reporting period, the total assets of the Group were RMB1,589 billion, representing an increase of 11.63% over the end of the previous year, of which: loans and advances to customers were RMB901.1 billion, growing by 16.81% over the end of last year; the securities investment was RMB363.8 billion, increasing by 15.73% over the end of last year.

The table below shows the major components of the total assets of the Group as of the dates indicated.

*(in millions of RMB)*

	<b>30 June 2006</b>	31 December 2005
Corporate loans <sup>(1)</sup>	<b>666,687</b>	604,611
Individual loans <sup>(1)</sup>	<b>114,503</b>	104,053
Discounted bills <sup>(1)</sup>	<b>117,747</b>	60,876
Interests receivables	<b>2,118</b>	1,834
<b>Gross amount of loans and advances before allowance for impairment</b>	<b>901,055</b>	771,374
Allowance for losses on loans and advances	<b>14,199</b>	12,601
<b>Loans and advances to customers</b>	<b>886,856</b>	758,773
<b>Financial assets held for trading</b>	<b>4,541</b>	3,228
<b>Investment securities</b>	<b>363,776</b>	314,343
<b>Cash and balances with central Banks</b>	<b>162,074</b>	140,309
<b>Due from other banks and financial institutions</b>	<b>135,680</b>	170,101

(1) Provision for impairment losses were not deducted from corporate loans, individual loans and discounted bills.

## 1. *Loans business*

The Group's loan business continued to grow in a steady and healthy way and loan to deposit ratio was maintained at an appropriate level. Facing the excessive market liquidity, the Group stepped up efforts to promote small business lending. Total small business loans increased by RMB18.70 billion over the end of the previous year, up by 0.58 percentage points to 10.95% against the total loans as compared with the beginning of the year.

### (1) Loans concentration by industries

The Group timely adjusted its credit policy and emphasized more on the segmentation of industry and business performance of corporate customers. The Group's loan portfolio embraced various industries with emphasis placing on manufacturing, transportation, public utility, trade and real estate, among which, loans to the manufacturing sector increased by RMB18.80 billion over the end of last year, accounting for 25.43% of the total loans; loans to transportation and utilities rose by RMB14.40 billion over the end of last year, accounting for 14.40% of the total loans; loans to the trading sector grew by RMB5.5 billion over the end of last year, accounting for 8.71% of the total loans; loans to the real estate sector increased by RMB3.2 billion over the end of last year, accounting for 7.12% of the total loans. Consumer loans grew by RMB10.5 billion over the end of last year, accounting for 12.71% of the total loans, of which mortgage loans grew by RMB5.8 billion over the end of last year, accounting for 9.33% of the total loans.

### (2) Customer structure of corporate loans

The credit structure continued to optimize. Based on the 10- category classification system, loans to class 1-5 customers accounted for 69.39% of the total, rising by 1.84 percentage points over the end of the previous year; loans to class 6-7 customers accounted for 20.36%, dropping by 6.41 percentage points over the end of the previous year, and loans to class 8-10 customers accounted for 2.04%, declining by 0.39 percentage points over the end of the previous year.

### (3) Borrower concentration

Pursuant to the existing banking laws and regulations, the total of credit extended to a single group customer shall not exceed 15% of the net capital of the bank, total loans extended to a single borrower shall not exceed 10% of the net capital of the bank. The Group was in compliance with these regulatory requirements.

### (4) Concentration by geographical location

The Group lays emphasis of its business on more developed Yangtze River Delta, Bohai Rim Economic Zone and the Pearl River Delta. Loans to the customers in the above areas remained stable, accounting for 64.27% and 64.24% of the total loans to the customers (before provision and excluding interest receivables) as at 31 December 2005 and 30 June 2006 respectively.

## (5) Loan quality

The risk management and internal control of the Group were further strengthened and loan quality continued to improve. Impaired loan is the concept under the International Financial Reporting Standards (the "IFRS"). A loan is impaired if there is objective evidence that full repayment under the original contractual terms is not possible.

As at the end of the reporting period, total impaired loan balance was RMB22.373 billion, increasing by RMB794 million over the end of last year; impaired loan ratio was 2.48%, decreasing by 0.32 percentage points over the end of last year; loan balance overdue for 90 days or above was RMB18.873 billion, increasing by 1.606 billion over the end of the previous year, of which trade bills overdue for 90 days or above were RMB350 million.

The table below shows the Group's individually identified impaired loans and loans overdue for 90 days or above, as of the dates indicated:

*(in millions of RMB, except percentages)*

	<b>30 June 2006</b>	31 December 2005
Individually identified impaired loans	<b>22,373</b>	21,579
Loan overdue for 90 days or above	<b>18,873</b>	17,267
Impaired loan ratio	<b>2.48%</b>	2.80%

The Group monitored the quality of loan portfolio in accordance with the 5-category loan classification guidelines set by the People's Bank of China. According to the guideline, commercial banks in the PRC are required to classify their loans into the following 5 categories: (1) "pass", (2) "special-mentioned", (3) "sub-standard", (4) "doubtful", (5) "loss". A loan is classified as "non-performing loan" if it is classified as "sub-standard", "doubtful" or "loss".

The table below shows the five-category loan classification as of the dates indicated:

(in millions of RMB except percentages)

	30 June 2006		31 December 2005	
	Amount	Proportion to total amount	Amount	Proportion to total amount
Pass	773,805	88.80%	652,653	85.52%
Special-mentioned	79,196	9.09%	92,473	12.11%
Sub-standard	10,740	1.23%	9,770	1.28%
Doubtful	7,189	0.83%	7,935	1.04%
Loss	421	0.05%	363	0.05%
Gross loans <sup>(1)</sup>	871,351	100.00%	763,194	100.00%
<b>NPL Ratio</b>		<b>2.11%</b>		2.37%

(1) Calculated under PRC GAAP

## 2. Treasury operation

The Group proactively adjusted its investment strategies according to the changing market conditions and further strengthened its treasury operation in inter-bank placements, investment securities, bond investments and derivative transactions to ensure the safety, liquidity and profitability of the funds. As of the end of the reporting period, the average treasury operation reached RMB627 billion, increasing by 24.44% over the end of last year, among which the average incremental investment securities and inter-bank lending of higher yield accounted for 92.94% of the total incremental treasury assets.

The Group further expanded treasury operation with active market participation. As at the end of the reporting period, the volume of RMB-dominated market transactions ranked the fourth in the market, maintaining the same position as the previous year. The Group continued its active role in the treasury operation.

## (V) LIABILITIES

As at the end of the reporting period, the total liabilities of the Group reached RMB1,504.7 billion, increasing by 12.27% over the end of the previous year; customer deposits amounted to RMB1,347 billion, growing by 10.33% over the end of the previous year. As the main source of funding of the Group, customer deposits accounted for 89.52% of total liabilities, dropping by 1.57 percentage points as compared with the end of last year. During the reporting period, corporate deposits grew by 10.04% and the retail deposits rose by 7.07%.

**(VI) PERFORMANCE BY GEOGRAPHY*****Geographical breakdown of performance***

A geographical segment refers to a specific economic environment under which the group operates and which gives rise to risks and returns that are different from other economic environments. As at the end of the reporting period, the net profit of the Group mainly came from Eastern China, Central China, Southern China and Northern China, totaling RMB5.484 billion and accounting for 90.87% of the net profit of the Group.

The table below shows the net profit and total revenue of the Group from each of the geographical segments for the periods indicated:

*(in millions of RMB)*

	<b>Half year ended 30 June 2006</b>		Half year ended 30 June 2005	
	<b>Net profit/ (loss)</b>	<b>Total revenue<sup>(1)</sup></b>	Net profit/ (loss)	Total revenue <sup>(1)</sup>
Northern China <sup>(2)</sup>	<b>1,244</b>	<b>5,217</b>	970	4,144
North-Eastern China <sup>(3)</sup>	<b>(343)</b>	<b>2,333</b>	(88)	2,049
Eastern China <sup>(4)</sup>	<b>2,702</b>	<b>17,270</b>	2,811	13,464
Central China and Southern China <sup>(5)</sup>	<b>1,538</b>	<b>5,799</b>	499	4,768
Western China <sup>(6)</sup>	<b>658</b>	<b>2,586</b>	(166)	2,223
Overseas <sup>(7)</sup>	<b>236</b>	<b>2,907</b>	579	1,963
Eliminations	–	<b>(4,412)</b>	–	(3,158)
<b>Total<sup>(8)</sup></b>	<b>6,035</b>	<b>31,700</b>	4,605	25,453

(1) Including the interest income, fee and commission income, dividend income, gains less losses arising from trading activities, gains less losses arising from de-recognition of investment securities.

(2) Including Beijing, Tianjin, Hebei, Shanxi and Inner Mongolia (the same hereinafter).

(3) Including Liaoning, Jilin and Heilongjiang (the same hereinafter).

(4) Including Shanghai, Jiangsu, Zhejiang, Anhui, Fujian, Jiangxi and Shandong (the same hereinafter).

(5) Including Henan, Hunan, Hubei, Guangdong and Guangxi (the same hereinafter).

(6) Including Chongqing, Sichuan, Guizhou, Yunnan, Tibet, Shaanxi, Gansu, Qinghai, Ningxia and Xinjiang (the same hereinafter).

(7) Including Hong Kong, New York, Singapore, Tokyo and Seoul (the same hereinafter).

(8) Including minority interest.



### **Geographical breakdown of loan balance**

The table below shows the loan balance by geographical segments on the indicated dates (before provision and excluding interests receivables).

*(in millions of RMB)*

	<b>30 June 2006</b>	31 December 2005
Northern China	<b>144,332</b>	129,729
North-Eastern China	<b>63,180</b>	53,962
Eastern China	<b>376,618</b>	320,533
Central China and Southern China	<b>177,967</b>	148,064
Western China	<b>78,352</b>	71,027
Overseas	<b>58,488</b>	46,225
Loan balance (before provision excluding interests receivables)	<b>898,937</b>	769,540

### **(VII) CLOSER COOPERATION WITH HSBC**

The Group's cooperation with HSBC expanded further into not only technical and business lines but also the overall operation and management. HSBC secondees at the Bank are now playing their important roles in helping the buildup of management information system, personal banking marketing and service teams as well as product designing and pricing. Following the first series of "De Li Bao" (a structured foreign exchange personal wealth management product), the two parties further improved the investment structure of the product and introduced the second series of "De Li Bao" to the market in July.

In June 2006, the first Bocom-HSBC Forum, a platform for communication and exchange of views on financial market development in China, was held jointly by the two banks with great success.

## **(VIII) OUTLOOK**

Looking into the second half of 2006, the economic and financial situation will undergo profound changes and the Chinese economy will continue to grow at a relatively rapid pace. Macro-economic adjustments will continue while opening-up and innovation of the financial market will further intensify competition in the industry. Facing both opportunities and challenges, the Group will respond to the changing situation in a more proactive way to ensure the continuous improvement of performance and efficiency.

The following will be done by the Group in the next half of the year: Firstly, to pay closer attention to the changes of macro economic adjustments and timely adjust the total volume as well as the pace of loan origination, thus to better allocate the credit resources by further optimizing credit structure by industry and client. Secondly, to continually improve the all-round risk management in an intensive way, closely monitoring the interest rate and foreign exchange rate movements to take precautions against potential risk; to expedite business process re-engineering and upgrade technical supports to better guard against operational risks as well as moral hazard problems. Thirdly, to establish a more advanced customer grading system to ensure the stability of corporate banking business through a better distribution of credit resources. Fourthly, to continually grow the retail and fee-based businesses in a proactive way by expediting the setting up of retail banking framework and production designing, thus to further enlarge the retail business market share and its revenue contribution to the Group's profit. Fifthly, to further expand the treasury operation and improve the efficiency of treasury operation by grasping the opportunity of the hiking interest rate.

## **IV. ADDITIONAL INFORMATION**

### **(I) DIRECTORS', SUPERVISORS' AND SENIOR MANAGEMENT'S INTERESTS**

As at 30 June 2006, none of the Bank's directors, supervisors, senior management and their associates held any interest or short positions in the shares, underlying shares and debentures of the Bank or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which were required to be notified to the Bank and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which are taken or deemed to have been taken under such provisions of the SFO), or which were required to be recorded in the register required to be kept by the Bank pursuant to Section 352 of the SFO, or which were required, pursuant to Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"), to be notified to the Bank and the Stock Exchange.

## (II) SUBSTANTIAL SHAREHOLDERS

As at 30 June 2006, the shareholders (other than the Bank's directors, supervisors and senior management) who had interests in the share capital of the Bank as recorded in the register required to be kept pursuant to section 336 of the SFO were as follows:

Name of substantial shareholders	Capacity	Number of domestic shares	Nature of interest (Note 1)	Approximate percentage of issued domestic shares (%)	Approximate percentage of total issued shares (%)
Ministry of Finance PRC	Beneficial owner	9,974,982,648	Long Position	43.87	21.78

Name of substantial shareholders	Capacity	Number of H-Shares	Nature of interest (Note 1)	Approximate percentage of total issued H-Shares (%)	Approximate percentage of total issued shares (%)
The Hongkong and Shanghai Banking Corporation Limited	Beneficial owner	9,115,002,580	Long Position	39.52	19.90
National Council for Social Security Fund	Beneficial owner	5,555,555,556	Long Position	24.09	12.13
China SAFE Investments Limited	Beneficial owner	3,000,000,000	Long Position	13.01	6.55

Note 1: Long positions held other than through share capital derivatives.

## (III) DIRECTORS

During the Period, Mr. William Fung Kwok Lun resigned as a non-executive director of the Bank on 1 June 2006 due to personal reasons. At the 12th session of the 4th Board of Directors meeting and the 2005 general meeting, Ms. Laura M. Cha was appointed as non-executive director of the Bank. Her term will end upon the expiration of the 4th Board of Directors. Ms. Laura M. Cha's qualification as a director has been approved by the China Banking Regulatory Commission on 22 July 2006.

Mr. Zhang Jianguo resigned as vice chairman, executive director and president of the Bank on 25 July 2006 due to personal reasons. At the same time, he ceased to be the authorised representative.

## (IV) PURCHASE, SALES OR REDEMPTION OF SHARES OF THE BANK

During the Period, neither the Bank nor any of its subsidiaries purchased, sold or redeemed any shares of the Bank.

**(V) COMPLIANCE WITH THE CODE PROVISIONS IN THE CODE ON CORPORATE GOVERNANCE PRACTICES**

The Group endeavors to establish high standard corporate governance, believing that good corporate governance is crucial to maximizing the value for our shareholders. In order to maintain a high standard of corporate governance, the Bank has established responsible, professional and accountable Board of Directors, Board of Supervisors, and an experienced senior management team. With the exception of the employee supervisors, the members of the Board of Directors and Board of Supervisors were elected by the shareholders at the general meeting of the Bank. The Bank has also set up four special committees under the Board of Directors, including a strategy committee, an audit committee, a risk management committee and a personnel and compensation committee. None of the Directors is aware of any information that would reasonably indicate that the Bank had not, for any part of the period ended 30 June 2006, been in compliance with the Code Provisions in the Code on Corporate Governance Practices as set out in Appendix 14 of the Listing Rules.

**(VI) DIRECTORS' COMPLIANCE WITH THE MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS OF LISTED ISSUERS**

The Group has adopted the Model Code as set out in Appendix 10 of the Listing Rules as the code of conduct regarding directors' securities transactions. The Bank has made specific enquiries of all directors and confirmed that they have complied with the required standards as set out in the Model Code for the period ended 30 June 2006.

**(VII) AUDIT COMMITTEE**

The Bank has set up an audit committee in accordance with the Code on Corporate Governance Practices as set out in Appendix 14 of the Listing Rules. The primary duties of the audit committee are to review the Bank's internal and external auditing work, to audit financial reports and to oversee implementation of internal control policy as well as the efficiency and compliance thereof. The audit committee consists of five members, including Herbert Hui Ho Ming (independent non-executive Director), Peter Wong Tung Shun (non-executive Director), Li Zexing (non-executive Director), Xie Qingjian (independent non-executive Director) and Chen Qingtai (independent non-executive Director), with independent non-executive Director Herbert Hui Ho Ming as chairman. The audit committee has reviewed the accounting standards and practices adopted by the Bank and discussed affairs regarding internal controls and financial reporting (including reviewing the Group's unaudited consolidated interim financial information) with the senior management.

**(VIII) APPROVAL OF INTERIM FINANCIAL REPORT**

During the Period, the consolidated interim financial information prepared by the Group in accordance with the IFRS for financial reports has been reviewed by PricewaterhouseCoopers and approved by the Board of Directors and the audit committee.

**(IX) PUBLICATION OF INFORMATION ON THE WEBSITE OF THE STOCK EXCHANGE**

The information as required by Appendix 16 of the Listing Rules will be submitted to the Stock Exchange before the stipulated date and published on its website ([www.hkex.com.hk](http://www.hkex.com.hk)) and the Bank's website ([www.bankcomm.com](http://www.bankcomm.com)).

## V. INDEPENDENT REVIEW REPORT



羅兵咸永道會計師事務所

**PricewaterhouseCoopers**  
22/F, Prince's Building  
Central, Hong Kong  
Telephone (852) 2289 8888  
Facsimile (852) 2810 9888  
www.pwchk.com

### TO THE BOARD OF DIRECTORS OF BANK OF COMMUNICATIONS CO., LTD.

*(incorporated in the People's Republic of China with limited liability)*

#### INTRODUCTION

We have been instructed by the Bank of Communications Co., Ltd. to review the condensed consolidated interim financial information set out on pages 21 to 88.

#### RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited require the preparation of condensed consolidated interim financial information to be in compliance with International Accounting Standard 34 "Interim Financial Reporting" issued by the International Accounting Standard Board and the relevant provisions thereof. The condensed consolidated interim financial information is the responsibility of, and has been approved by, the directors. It is our responsibility to form an independent conclusion, based on our review, on the condensed consolidated interim financial information and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

#### REVIEW WORK PERFORMED

We conducted our review in accordance with Statements of Auditing Standards 700 "Engagements to review interim financial reports" issued by the Hong Kong Institute of Certified Public Accountants. A review consists principally of making enquiries of group management and applying analytical procedures to the condensed consolidated interim financial information and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly, we do not express an audit opinion on the condensed consolidated interim financial information.

#### REVIEW CONCLUSION

On the basis of our review which does not constitute an audit, we are not aware of any material modifications that should be made to the condensed consolidated interim financial information for the six months ended 30 June 2006.

**PricewaterhouseCoopers**  
*Certified Public Accountants*

Hong Kong, 22 August 2006

## VI. UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION

### UNAUDITED CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

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

	Note	Three months ended		Half-year ended	
		30 June 2006	2005	30 June 2006	2005
Interest income		15,263	11,938	29,601	23,278
Interest expense		(5,706)	(4,360)	(11,257)	(8,336)
<b>Net interest income</b>	4	<b>9,557</b>	7,578	<b>18,344</b>	14,942
Fee and commission income		796	541	1,559	1,048
Fee and commission expense		(121)	(90)	(263)	(170)
<b>Net fee and commission income</b>		<b>675</b>	451	<b>1,296</b>	878
Dividend income	5	26	9	27	12
Gains less losses arising from trading activities	6	61	169	150	468
Gains less losses arising from de-recognition of investment securities	19	2	294	19	426
Other operating income	7	212	131	344	221
Impairment losses on loans and advances	8	(919)	(921)	(1,971)	(1,918)
Other operating expenses	9	(4,543)	(3,848)	(8,952)	(8,145)
<b>Operating profit before tax</b>		<b>5,071</b>	3,863	<b>9,257</b>	6,884
Income tax	12	(1,937)	(1,291)	(3,222)	(2,279)
<b>Net profit for the period</b>		<b>3,134</b>	2,572	<b>6,035</b>	4,605
<b>Attributable to:</b>					
Shareholders of the Bank		3,133	2,572	6,034	4,605
Minority interest		1	–	1	–
		<b>3,134</b>	2,572	<b>6,035</b>	4,605
<b>Basic and diluted earnings per share (in RMB)</b>	13	<b>0.07</b>	0.06	<b>0.13</b>	0.12

The accompanying notes presented on pages 26 to 80 form an integral part of this condensed consolidated interim financial information.

## UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEET

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

	<i>Note</i>	<b>30 June 2006</b>	31 December 2005
<b>ASSETS</b>			
Cash and balances with central banks	14	<b>162,074</b>	140,309
Due from other banks and financial institutions	15	<b>135,680</b>	170,101
Financial assets held for trading	16	<b>4,541</b>	3,228
Loans and advances to customers	18	<b>886,856</b>	758,773
Investment securities – loans and receivables	19	<b>44,463</b>	28,372
Investment securities – available-for-sale	19	<b>319,313</b>	285,971
Property and equipment	20	<b>24,630</b>	25,164
Deferred tax assets	26	<b>1,724</b>	955
Other assets	21	<b>9,707</b>	10,566
<b>Total assets</b>		<b>1,588,988</b>	1,423,439
<b>LIABILITIES</b>			
Due to other banks and financial institutions	22	<b>114,514</b>	84,094
Financial liabilities at fair value through profit or loss	23	<b>10,722</b>	9,555
Due to customers	24	<b>1,346,998</b>	1,220,839
Other liabilities	25	<b>17,472</b>	12,349
Current taxes		<b>2,714</b>	751
Deferred tax liabilities	26	<b>249</b>	413
Subordinated term debt	28	<b>12,077</b>	12,292
<b>Total liabilities</b>		<b>1,504,746</b>	1,340,293
<b>EQUITY</b>			
<b>Capital and reserves attributable to the Bank's shareholders</b>			
Share capital	29	<b>45,804</b>	45,804
Capital surplus	29	<b>21,540</b>	21,540
Other reserves		<b>10,352</b>	6,555
Retained earnings	30	<b>6,481</b>	9,183
		<b>84,177</b>	83,082
<b>Minority Interest</b>		<b>65</b>	64
<b>Total equity</b>		<b>84,242</b>	83,146
<b>Total equity and liabilities</b>		<b>1,588,988</b>	1,423,439

This condensed consolidated interim financial information was approved for issue by the Board of Directors on 22 August 2006 and signed on its behalf by:

Chairman of Board: Jiang Chaoliang

Chief Financial Officer: Yu Yali

The accompanying notes presented on pages 26 to 80 form an integral part of this condensed consolidated interim financial information.

## UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

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

	Share capital	Capital surplus	Statutory reserve	Discretionary reserve	Other reserves			Translation reserve on foreign operations	(Accumulated losses)/ Retained earnings	Minority interest	Total
					General and statutory reserve	Revaluation reserve for AFS securities	Revaluation reserve for properties				
	Note 29	Note 29	Note 30	Note 30	Note 30				Note 30		
<b>Balance at 1 January 2005</b>	39,070	10,872	-	-	-	(1,272)	3,579	-	(146)	-	52,103
Issue of shares	5,856	9,330	-	-	-	-	-	-	-	-	15,186
Issuance cost	-	(129)	-	-	-	-	-	-	-	-	(129)
Gains from changes in fair value of AFS securities, net of tax	-	-	-	-	-	2,928	-	-	-	-	2,928
Net profit	-	-	-	-	-	-	-	-	4,605	-	4,605
<b>Balance at 30 June 2005</b>	44,926	20,073	-	-	-	1,656	3,579	-	4,459	-	74,693
<b>Balance at 1 January 2006</b>	45,804	21,540	-	-	-	2,603	4,040	(88)	9,183	64	83,146
Dividends	-	-	-	-	-	-	-	-	(3,664)	-	(3,664)
Transfer to reserves	-	-	899	-	4,428	-	-	-	(5,327)	-	-
Losses from changes in fair value of AFS securities, net of tax	-	-	-	-	-	(1,301)	-	-	-	-	(1,301)
Translation difference on foreign operations	-	-	-	-	-	-	-	26	-	-	26
Revaluation reserve realization upon disposals	-	-	-	-	-	-	(255)	-	255	-	-
Net profit	-	-	-	-	-	-	-	-	6,034	1	6,035
<b>Balance at 30 June 2006</b>	45,804	21,540	899	-	4,428	1,302	3,785	(62)	6,481	65	84,242

The accompanying notes presented on pages 26 to 80 form an integral part of this condensed consolidated interim financial information.



## UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

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

	Half-year ended 30 June	
	2006	2005
<b>Cash flows from operating activities</b>		
Net profit before taxation:		
Adjustments for:	<b>9,257</b>	6,884
Impairment of loans and advances to customers	<b>2,042</b>	1,969
Write-back of due from banks and financial institutions	<b>(52)</b>	(18)
Impairment of other receivables	<b>422</b>	148
Depreciation of property and equipment	<b>1,240</b>	1,204
Amortization of prepaid staff subsidies	<b>99</b>	15
Amortization of prepaid rental expenses	<b>93</b>	88
Amortization of land use rights	<b>2</b>	3
Amortization of computer software	<b>60</b>	49
Net gains on investment securities	<b>(19)</b>	(426)
Gains on disposal of fixed assets	<b>(47)</b>	(15)
Losses on disposal of investment property	<b>10</b>	–
Interest expense for the issue of bonds	<b>281</b>	277
	<b>13,388</b>	10,178
Net increase in due from central banks	<b>(6,889)</b>	(6,122)
Net decrease/(increase) in due from other banks and financial institutions	<b>26,967</b>	(22,272)
Net increase in financial assets held for trading	<b>(1,313)</b>	(439)
Net increase in loans and advances to customers	<b>(130,125)</b>	(99,632)
Net (increase)/decrease in other assets	<b>(413)</b>	1,698
Net increase in due to other banks and financial institutions	<b>30,420</b>	4,368
Net increase in financial liabilities held for trading	<b>1,167</b>	1,558
Net increase in due to customers	<b>126,159</b>	117,568
Net increase in other liabilities	<b>1,389</b>	2,242
Net increase/(decrease) in business tax payable	<b>211</b>	(4)
Income tax paid	<b>(1,557)</b>	(34)
<b>Net cash from operating activities</b>	<b>59,404</b>	9,109

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	<b>2005</b>
<b>Cash flows from investing activities</b>		
Purchase of investment securities	<b>(278,055)</b>	(141,366)
Disposal or redemption of investment securities	<b>226,705</b>	145,028
Purchase of computer software	<b>(26)</b>	(33)
Disposal of computer software	<b>1</b>	–
Prepaid rental expenses	<b>(90)</b>	(84)
Disposal of land use rights	<b>6</b>	–
Purchase of property and equipment	<b>(918)</b>	(1,150)
Disposal of property and equipment	<b>253</b>	308
Disposal of investment property	<b>561</b>	–
<b>Net cash (used in)/from investing activities</b>	<b>(51,563)</b>	2,703
<b>Cash flows from financing activities</b>		
Issue of shares	–	15,057
Interest paid on issued bonds	<b>(496)</b>	(469)
Dividends paid	<b>(1)</b>	(2)
<b>Net cash (used in)/from financing activities</b>	<b>(497)</b>	14,586
<b>Effect of exchange rate changes on cash and cash equivalents</b>	<b>26</b>	–
<b>Net increase in cash and cash equivalents</b>	<b>7,370</b>	26,398
<b>Cash and cash equivalents at the beginning of the period</b>	<b>101,305</b>	75,757
<b>Cash and cash equivalents at the end of the period (Note 35)</b>	<b>108,675</b>	102,155
<b>Major non-cash transactions</b>		
Transfer from fixed assets to other assets	<b>6</b>	–
Transfer from other assets to fixed assets	–	57
<b>Supplementary information</b>		
Interest received	<b>29,317</b>	23,205
Interest paid	<b>(10,853)</b>	(6,856)

The accompanying notes presented on pages 26 to 80 form an integral part of this condensed consolidated interim financial information.

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION

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

### 1 GENERAL

Bank of Communications Co., Ltd. (the "Bank") is a commercial and retail bank providing banking services mainly in the 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 93 city branches in the PRC. In addition, the Bank has branches in Hong Kong SAR, New York, Tokyo, Singapore and Seoul.

### 2 BASIS OF PREPARATION AND ACCOUNTING POLICIES

#### A *Basis of preparation and accounting policies*

This unaudited condensed consolidated financial information has been prepared in accordance with International Accounting Standard ("IAS") 34 "Interim Financial Reporting" issued by the International Accounting Standard Board.

This condensed consolidated financial information should be read in conjunction with the 2005 annual financial statements.

The accounting policies and methods of computation used in the preparation of this condensed consolidated financial information are consistent with those used in the annual financial statements for the year ended 31 December 2005.

#### B *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 accounting policies of the Bank and its subsidiaries (collectively "the Group").

(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.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** *(Continued)*

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

**2 BASIS OF PREPARATION AND ACCOUNTING POLICIES** *(Continued)***B Critical accounting estimates and judgments in applying accounting policies** *(Continued)*

(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 various 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 Mainland China 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.

(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.

**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.

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

#### **B** *Credit risk*

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

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

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

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

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

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

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**3 USE OF FINANCIAL INSTRUMENTS** (Continued)**B Credit risk** (Continued)

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

	Total assets	Total liabilities	Financial guarantees and credit related commitments
<b>As at 30 June 2006</b>			
Mainland China	1,476,074	1,394,275	285,291
Hong Kong	96,896	94,456	17,918
Others	16,018	16,015	5,333
<hr/>			
Total	1,588,988	1,504,746	308,542
<hr/>			
<b>As at 31 December 2005</b>			
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
<hr/>			
Total	1,423,439	1,340,293	245,910
<hr/>			

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 UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(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):

	30 June 2006		31 December 2005	
		%		%
Domestic regions				
– Jiangsu	109,291	12	93,247	12
– Shanghai	103,583	11	86,122	11
– Beijing	89,810	10	84,298	11
– Guangdong	81,107	9	66,002	9
– Zhejiang	63,203	7	56,634	7
– Shandong	55,127	6	46,956	6
– Henan	34,790	4	29,867	4
– Liaoning	33,107	4	26,920	4
– Others	270,431	30	233,269	30
Domestic regions total	840,449	93	723,315	94
Hong Kong and overseas countries	58,488	7	46,225	6
Interest receivables	2,118	–	1,834	–
Gross amount of loans and advances before allowance for impairment	901,055	100	771,374	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 32).

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**3 USE OF FINANCIAL INSTRUMENTS** (Continued)

**B Credit risk** (Continued)

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

	30 June 2006		31 December 2005	
		%		%
Corporate loans				
Manufacturing				
– Petroleum and chemical	<b>44,587</b>	<b>5</b>	32,585	4
– Electronics	<b>26,989</b>	<b>3</b>	27,035	4
– Machinery	<b>23,464</b>	<b>3</b>	22,763	3
– Steel	<b>22,623</b>	<b>3</b>	24,540	3
– Textile	<b>19,043</b>	<b>2</b>	18,076	2
– Other manufacturing	<b>92,477</b>	<b>10</b>	85,360	11
Trading	<b>78,485</b>	<b>9</b>	72,977	10
Transportation	<b>73,871</b>	<b>8</b>	63,544	8
Services	<b>70,170</b>	<b>8</b>	56,024	7
Real estate	<b>64,144</b>	<b>7</b>	60,913	8
Utilities	<b>55,870</b>	<b>6</b>	51,812	7
Construction	<b>29,440</b>	<b>3</b>	25,958	3
Educations and scientific research	<b>26,322</b>	<b>3</b>	24,934	3
Post and telecommunications	<b>12,656</b>	<b>1</b>	15,768	2
Non-banking financial institutions	<b>11,614</b>	<b>1</b>	9,753	1
Agriculture	<b>2,008</b>	–	4,698	1
Others	<b>12,924</b>	<b>2</b>	7,871	1
Corporate loans total	<b>666,687</b>	<b>74</b>	604,611	78
Mortgage loans	<b>84,084</b>	<b>9</b>	78,264	10
Medium-term and long-term working capital loans				
Car loans	<b>3,846</b>	<b>1</b>	3,961	1
Short-term working capital loans	<b>5,546</b>	<b>1</b>	5,087	1
Loans secured by deposits	<b>1,206</b>	–	1,093	–
Credit card advances	<b>1,319</b>	–	696	–
Others	<b>3,020</b>	–	1,267	–
Individual loans total	<b>114,503</b>	<b>13</b>	104,053	14
Discounted bills	<b>117,747</b>	<b>13</b>	60,876	8
Interest receivables	<b>2,118</b>	–	1,834	–
	<b>119,865</b>	<b>13</b>	62,710	8
Gross amount of loans and advances before allowance for impairment	<b>901,055</b>	<b>100</b>	771,374	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 UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(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):

	<b>30 June 2006</b>	31 December 2005
<b>Domestic</b>		
Corporate entities		
State owned entities	<b>213,298</b>	198,276
Collective owned entities	<b>11,746</b>	11,022
Private unlimited companies	<b>41,058</b>	35,987
Private limited companies	<b>184,091</b>	163,673
Joint stock companies	<b>65,757</b>	63,723
Foreign invested enterprises	<b>79,913</b>	78,339
Other domestic entities	<b>28,950</b>	22,347
	<b>624,813</b>	573,367
Individuals	<b>99,427</b>	89,853
	<b>724,240</b>	663,220
<b>Hong Kong and overseas</b>		
Corporate entities	<b>41,874</b>	31,244
Individuals	<b>15,076</b>	14,200
	<b>56,950</b>	45,444
Discounted bills	<b>117,747</b>	60,876
Interest receivables	<b>2,118</b>	1,834
	<b>901,055</b>	771,374
Gross amount of loans and advances before allowance for impairment	<b>901,055</b>	771,374

#### **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 its foreign exchange rate management 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.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**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 period. The tables show the Group's assets and liabilities at carrying amounts in RMB, categorized by the original currency.

	RMB	US Dollars	HK Dollars	Others	Total
<b>As at 30 June 2006</b>					
<b>Assets</b>					
Cash and balances with central banks	157,650	2,896	1,026	502	162,074
Due from other banks and financial institutions	72,903	42,698	10,972	9,107	135,680
Financial assets held for trading	42	1,973	2,164	362	4,541
Loans and advances to customers	797,295	43,297	40,294	5,970	886,856
Investment securities-loans and receivables	42,631	1,832	-	-	44,463
Investment securities-available-for-sale	281,773	22,520	6,707	8,313	319,313
Other assets, including deferred tax assets	41,074	(3,333)	753	(2,433)	36,061
<b>Total assets</b>	<b>1,393,368</b>	<b>111,883</b>	<b>61,916</b>	<b>21,821</b>	<b>1,588,988</b>
<b>Liabilities</b>					
Due to other banks and financial institutions	(93,871)	(16,059)	(1,925)	(2,659)	(114,514)
Financial liabilities at fair value through profit or loss	(33)	(3,954)	(6,701)	(34)	(10,722)
Due to customers	(1,206,795)	(73,019)	(51,338)	(15,846)	(1,346,998)
Other liabilities, including deferred tax liabilities	(29,235)	(1,006)	(2,220)	(51)	(32,512)
<b>Total liabilities</b>	<b>(1,329,934)</b>	<b>(94,038)</b>	<b>(62,184)</b>	<b>(18,590)</b>	<b>(1,504,746)</b>
<b>Net position</b>	<b>63,434</b>	<b>17,845</b>	<b>(268)</b>	<b>3,231</b>	<b>84,242</b>
<b>Financial guarantees and credit related commitments</b>					
	236,378	51,116	11,762	9,286	308,542

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

#### D Currency risk *(Continued)*

	RMB	US Dollars	HK Dollars	Others	Total
<b>As at 31 December 2005</b>					
<b>Assets</b>					
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
<b>Total assets</b>	<b>1,237,408</b>	<b>112,841</b>	<b>52,815</b>	<b>20,375</b>	<b>1,423,439</b>
<b>Liabilities</b>					
Due to other banks and financial institutions	(62,974)	(14,613)	(3,916)	(2,591)	(84,094)
Financial liabilities at fair value through profit or loss	(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)
<b>Total liabilities</b>	<b>(1,177,362)</b>	<b>(93,097)</b>	<b>(51,523)</b>	<b>(18,311)</b>	<b>(1,340,293)</b>
<b>Net position</b>	<b>60,046</b>	<b>19,744</b>	<b>1,292</b>	<b>2,064</b>	<b>83,146</b>
<b>Financial guarantees and credit related commitments</b>	<b>184,775</b>	<b>45,206</b>	<b>9,867</b>	<b>6,062</b>	<b>245,910</b>

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** *(Continued)*

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

**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, there is no ceiling for loan interest rates, whilst the floor for loan interest rates 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 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.

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 UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

#### *E Interest rate risk (Continued)*

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
<b>As at 30 June 2006</b>							
<b>Assets</b>							
Cash and balances with central banks	153,168	-	-	-	-	8,906	162,074
Due from other banks and financial institutions	102,031	18,871	13,804	600	-	374	135,680
Financial assets held for trading	1,759	5	240	1,294	922	321	4,541
Loans and advances to customers	82,804	182,251	378,576	119,154	124,071	-	886,856
Investment securities							
- loans and receivables	407	535	19,139	23,885	497	-	44,463
- available-for-sale	18,577	37,840	76,856	115,442	70,596	2	319,313
Other assets, including deferred tax assets	-	-	-	-	-	36,061	36,061
<b>Total assets</b>	<b>358,746</b>	<b>239,502</b>	<b>488,615</b>	<b>260,375</b>	<b>196,086</b>	<b>45,664</b>	<b>1,588,988</b>
<b>Liabilities</b>							
Due to other banks and financial institutions	(70,700)	(29,449)	(12,084)	-	(2,053)	(228)	(114,514)
Financial liabilities at fair value through profit or loss	(2,121)	(6,560)	(1,639)	(86)	(1)	(315)	(10,722)
Due to customers	(838,972)	(110,820)	(277,710)	(98,934)	(1,103)	(19,459)	(1,346,998)
Other liabilities, including deferred tax liabilities	(115)	-	(5)	(12,000)	-	(20,392)	(32,512)
<b>Total liabilities</b>	<b>(911,908)</b>	<b>(146,829)</b>	<b>(291,438)</b>	<b>(111,020)</b>	<b>(3,157)</b>	<b>(40,394)</b>	<b>(1,504,746)</b>
<b>Total interest sensitivity gap</b>	<b>(553,162)</b>	<b>92,673</b>	<b>197,177</b>	<b>149,355</b>	<b>192,929</b>	<b>5,270</b>	<b>84,242</b>

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**3 USE OF FINANCIAL INSTRUMENTS** (Continued)

**E Interest rate risk** (Continued)

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
<b>As at 31 December 2005</b>							
<b>Assets</b>							
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	1,272	11	14	659	973	299	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
<b>Total assets</b>	<b>344,462</b>	<b>204,208</b>	<b>438,990</b>	<b>222,041</b>	<b>167,246</b>	<b>46,492</b>	<b>1,423,439</b>
<b>Liabilities</b>							
Due to other banks and financial institutions	(59,381)	(13,930)	(8,718)	-	(2,002)	(63)	(84,094)
Financial liabilities at fair value through profit or loss	(2,230)	(5,170)	(311)	(1,540)	(3)	(301)	(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)
<b>Total liabilities</b>	<b>(852,847)</b>	<b>(127,206)</b>	<b>(228,132)</b>	<b>(90,057)</b>	<b>(3,919)</b>	<b>(38,132)</b>	<b>(1,340,293)</b>
<b>Total interest sensitivity gap</b>	<b>(508,385)</b>	<b>77,002</b>	<b>210,858</b>	<b>131,984</b>	<b>163,327</b>	<b>8,360</b>	<b>83,146</b>

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (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:

	RMB	US Dollars	HK Dollars	Others
<b>As at 30 June 2006</b>				
<b>Assets</b>				
Cash and balances with central banks	1.46%	0.19%	0.07%	N/A
Due from other banks and financial institutions	1.96%	5.01%	4.34%	4.47%
Loans and advances to customers	5.21%	5.06%	5.61%	2.20%
Investment securities				
– loans and receivables	2.64%	5.35%	N/A	N/A
– available-for-sale	2.93%	5.31%	4.20%	3.92%
<b>Liabilities</b>				
Due to other banks and financial institutions	1.63%	4.92%	3.98%	1.71%
Due to customers	1.50%	4.07%	3.51%	2.72%
<b>As at 31 December 2005</b>				
<b>Assets</b>				
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%
<b>Liabilities</b>				
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%

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**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 less than 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

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Overdue	Total
<b>As at 30 June 2006</b>							
<b>Assets</b>							
Cash and balances with central banks	162,074	-	-	-	-	-	162,074
Due from other banks and financial institutions	102,248	18,994	13,838	600	-	-	135,680
Financial assets held for trading	1,776	26	281	1,454	1,004	-	4,541
Loans and advances to customers	69,739	156,322	376,375	142,349	125,683	16,388	886,856
Investment securities							
- loans and receivables	167	455	19,139	24,205	497	-	44,463
- available-for-sale	8,202	15,768	56,688	152,283	86,372	-	319,313
Other assets, including deferred tax assets	6,846	730	2,977	4,488	20,328	692	36,061
<b>Total assets</b>	<b>351,052</b>	<b>192,295</b>	<b>469,298</b>	<b>325,379</b>	<b>233,884</b>	<b>17,080</b>	<b>1,588,988</b>
<b>Liabilities</b>							
Due to other banks and financial institution	(69,683)	(30,454)	(12,324)	-	(2,053)	-	(114,514)
Financial liabilities at fair value through profit or loss	(1,823)	(612)	(4,405)	(3,880)	(2)	-	(10,722)
Due to customers	(855,637)	(107,767)	(279,534)	(100,770)	(3,290)	-	(1,346,998)
Other liabilities, including deferred tax liabilities	(17,661)	(1,769)	(304)	(12,556)	(222)	-	(32,512)
<b>Total liabilities</b>	<b>(944,804)</b>	<b>(140,602)</b>	<b>(296,567)</b>	<b>(117,206)</b>	<b>(5,567)</b>	<b>-</b>	<b>(1,504,746)</b>
<b>Net liquidity gap</b>	<b>(593,752)</b>	<b>51,693</b>	<b>172,731</b>	<b>208,173</b>	<b>228,317</b>	<b>17,080</b>	<b>84,242</b>



## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

#### F Liquidity risk *(Continued)*

Maturities of assets and liabilities *(Continued)*

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Overdue	Total
<b>As at 31 December 2005</b>							
<b>Assets</b>							
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
<b>Total assets</b>	<b>340,701</b>	<b>159,048</b>	<b>416,554</b>	<b>283,887</b>	<b>206,231</b>	<b>17,018</b>	<b>1,423,439</b>
<b>Liabilities</b>							
Due to other banks and financial institution	(59,280)	(14,054)	(8,758)	-	(2,002)	-	(84,094)
Financial liabilities at fair value through profit or loss	(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)
<b>Total liabilities</b>	<b>(883,795)</b>	<b>(120,453)</b>	<b>(230,087)</b>	<b>(99,380)</b>	<b>(6,578)</b>	<b>-</b>	<b>(1,340,293)</b>
<b>Net liquidity gap</b>	<b>(543,094)</b>	<b>38,595</b>	<b>186,467</b>	<b>184,507</b>	<b>199,653</b>	<b>17,018</b>	<b>83,146</b>

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.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**3 USE OF FINANCIAL INSTRUMENTS** (Continued)**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.

	30 June 2006		31 December 2005	
	Carrying value	Fair value	Carrying value	Fair value
<b>Financial assets</b>				
Due from other banks and financial institutions	135,680	135,680	170,101	170,101
Loans and advances to customers	886,856	886,856	758,773	758,773
Investment securities				
– loans and receivables	44,463	45,197	28,372	29,189
<b>Financial liabilities</b>				
Due to other banks and financial institutions	114,514	114,514	84,094	84,094
Due to customers	1,346,998	1,346,620	1,220,839	1,220,320

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.

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

(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)*

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.

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.

	<b>As at 30 June 2006</b>	As at 31 December 2005
Investment custody accounts	<b>124,555</b>	96,852

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**4 NET INTEREST INCOME**

	Three months ended		Half-year ended	
	30 June		30 June	
	2006	2005	2006	2005
<b>Interest income</b>				
Balances with central banks	487	431	952	926
Due from other banks and financial institutions	1,569	755	2,990	1,470
Trading securities	–	–	–	84
Loans and advances to customers	10,671	8,732	20,797	16,879
Investment securities	2,522	1,971	4,809	3,810
Others	14	49	53	109
	<b>15,263</b>	11,938	<b>29,601</b>	23,278
<b>Interest expense</b>				
Due to other banks and financial institutions	(844)	(463)	(1,541)	(866)
Due to customers	(4,862)	(3,897)	(9,716)	(7,470)
	<b>(5,706)</b>	(4,360)	<b>(11,257)</b>	(8,336)
<b>Net interest income</b>	<b>9,557</b>	7,578	<b>18,344</b>	14,942

	Half-year ended 30 June	
	2006	2005
Interest income accrued on loans and advances to customers individually identified with impairment	337	405
Interest income accrued on amounts due from other banks and financial institutions with impairment	–	–

**5 DIVIDEND INCOME**

	Half-year ended 30 June	
	2006	2005
Dividend income	27	12

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

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 6 GAINS LESS LOSSES ARISING FROM TRADING ACTIVITIES

	Half-year ended 30 June	
	2006	2005
Foreign exchange	171	194
Interest rate instruments	(21)	274
	<b>150</b>	468

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

Net income on interest rate instruments includes the results of marking securities held for trading, debt securities in issue, structured deposit, interest rate swaps, cross currency interest rate swaps, interest rate options and other interest rate derivatives to market.

### 7 OTHER OPERATING INCOME

	Half-year ended 30 June	
	2006	2005
Profit on sales of land use rights and buildings	47	15
Sales of foreclosed assets and other assets	3	–
Penalty income	–	8
Other miscellaneous income	294	198
	<b>344</b>	221

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

### 8 IMPAIRMENT LOSSES ON LOANS AND ADVANCES

	Three months ended 30 June		Half-year ended 30 June	
	2006	2005	2006	2005
Due from other banks and financial institutions and securities purchased under resale agreements, net <i>(Note 15(b))</i>	(21)	(7)	(52)	(18)
Loans and advances to customers <i>(Note 18(b))</i>	949	960	2,042	1,969
Less: recovery of loans previously written off	(9)	(32)	(19)	(33)
	<b>919</b>	921	<b>1,971</b>	1,918

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**9 OTHER OPERATING EXPENSES**

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Staff costs (Note 10)	<b>2,730</b>	2,309
Depreciation (Note 20)	<b>1,240</b>	1,204
Operating lease rentals	<b>431</b>	393
General and administrative expenses	<b>1,600</b>	1,403
Impairment of other receivables	<b>422</b>	148
Business tax and surcharges	<b>1,198</b>	969
Regulator's supervision fee	<b>153</b>	129
(Reversal)/Provision for outstanding litigation	<b>(200)</b>	181
Professional fees	<b>18</b>	27
Losses on sales of investment property	<b>10</b>	–
Others	<b>1,350</b>	1,382
	<b>8,952</b>	8,145

**10 STAFF COSTS**

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Salaries and bonus	<b>1,663</b>	1,372
Pension costs	<b>256</b>	248
Housing benefits and subsidies	<b>255</b>	282
Other social security and benefit costs	<b>556</b>	407
	<b>2,730</b>	2,309

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 11 DIRECTORS' EMOLUMENTS

Details of the directors', the supervisors' and the senior management's emoluments are as follows:

	Half-year ended 30 June	
	2006	2005
Fees	6	7

The numbers of directors, supervisors and senior management whose annual emoluments fell within the following band are set out below:

	Half-year ended 30 June	
	2006	2005
Nil – RMB1,000,000	33	34

No directors waived or agreed to waive any emolument during the period.

In 2006, RMB250,000 was accrued for independent non-executive directors' emolument (2005: RMB200,000).

### 12 INCOME TAX

	Three months ended		Half-year ended	
	30 June		30 June	
	2006	2005	2006	2005
Current tax				
– Mainland China income tax	1,946	40	3,210	66
– Hong Kong profits tax	46	58	83	76
– Overseas taxation	226	1	227	2
	2,218	99	3,520	144
Deferred tax ( <i>Note 26</i> )	(281)	1,192	(298)	2,135
	1,937	1,291	3,222	2,279

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 half-year ended 30 June 2006.

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 half-year ended 30 June 2006. 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 half-year ended 30 June 2006.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**12 INCOME TAX** (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:

	Three months ended		Half-year ended	
	30 June		30 June	
	2006	2005	2006	2005
Profit before tax	<b>5,071</b>	3,863	<b>9,257</b>	6,884
Tax calculated at a tax rate of 33%	<b>1,674</b>	1,275	<b>3,055</b>	2,272
Effect of different tax rates in other countries	<b>24</b>	(24)	<b>23</b>	(19)
Tax credit arising from income not subject to tax	<b>(178)</b>	(263)	<b>(409)</b>	(482)
Tax effect of expenses that are not deductible for tax purposes	<b>417</b>	303	<b>553</b>	508
Income tax expense	<b>1,937</b>	1,291	<b>3,222</b>	2,279

**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 period.

	Half-year ended 30 June	
	2006	2005
Profit attributable to shareholders of the Bank	<b>6,034</b>	4,605
Weighted average number of ordinary shares in issue	<b>45,804</b>	39,326
Basic and diluted earnings per share (expressed in RMB per share)	<b>0.13</b>	0.12

**14 CASH AND BALANCES WITH CENTRAL BANKS**

	30 June	31 December
	2006	2005
Cash	<b>8,906</b>	9,280
Balances with central banks other than mandatory reserve deposits	<b>72,970</b>	57,720
Included in cash and cash equivalents (Note 35)	<b>81,876</b>	67,000
Mandatory reserve deposits	<b>80,198</b>	73,309
	<b>162,074</b>	140,309



## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 14 CASH AND BALANCES WITH CENTRAL BANKS *(Continued)*

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.

	<b>30 June 2006</b>	31 December 2005
Mandatory reserve rate for deposits denominated in RMB	<b>7.5%</b>	7.5%
Mandatory reserve rate for deposits denominated in foreign currency	<b>3%</b>	3%

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*

	<b>30 June 2006</b>	31 December 2005
Placement with other banks and included in cash equivalents <i>(Note 35)</i>	<b>26,799</b>	34,305
Securities purchased under resale agreement	<b>32,704</b>	65,715
Less: allowance for impairment losses on securities purchased under resale agreement	<b>(10)</b>	(10)
	<b>32,694</b>	65,705
Loans purchased under resale agreement	<b>12,081</b>	11,062
Loans and advances to other banks	<b>60,774</b>	55,147
Loans to other financial institutions	<b>4,013</b>	4,615
	<b>64,787</b>	59,762
Less: individual impairment allowance on amounts due from other banks and financial institutions	<b>(681)</b>	(733)
	<b>64,106</b>	59,029
	<b>135,680</b>	170,101

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** *(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*

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
<b>Balance at beginning of the period</b>	<b>743</b>	1,004
Reversal of impairment, net <i>(Note 8)</i>	<b>(52)</b>	(18)
<b>Balance at end of the period</b>	<b>691</b>	986

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

	<b>30 June 2006</b>	31 December 2005
Impaired amount of due from other banks and financial institutions	<b>691</b>	743
Impaired amount of due from other banks and financial institutions (percentage)	<b>0.51%</b>	0.44%

**16 FINANCIAL ASSETS HELD FOR TRADING**

	<b>30 June 2006</b>	31 December 2005
Derivative financial instruments <i>(Note 17)</i>	<b>321</b>	299
Government bonds-listed in Hong Kong	<b>1,989</b>	1,294
Other debt securities		
– Listed in Hong Kong	<b>671</b>	611
– Unlisted – corporate bonds	<b>742</b>	146
– Unlisted – public sector	<b>45</b>	71
– Unlisted – banking sector	<b>773</b>	807
	<b>4,541</b>	3,228

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 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. Foreign currency and interest rate futures are contractual obligations to receive or pay a net amount based on changes in currency rates or interest rates or to buy or sell foreign currency or a financial instrument on a future date at a specified price, established in an organised financial market. The credit risk is negligible, as futures contracts are collateralised by cash or marketable securities, and changes in the futures contract value are settled daily with the exchange. Forward rate agreements are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contracted rate of interest and the current market rate, based on a notional principal amount.

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

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

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Group's exposure to credit or price risks. The derivative instruments become 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.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**17 DERIVATIVE FINANCIAL INSTRUMENTS** (Continued)

	Contract/Notional amount	Fair values	
		Assets	Liabilities
<b>As at 30 June 2006</b>			
<b>Foreign exchange derivatives</b>			
Currency forwards	23,399	28	(67)
Currency swaps	33,025	21	(18)
OTC currency options bought and sold	978	4	(3)
		53	(88)
<b>Interest rate derivatives</b>			
Interest rate swaps	36,154	245	(204)
Cross currency interest rate swaps	1,055	10	(10)
OTC interest rate options	800	10	(10)
Forward rate agreements	2,399	–	(3)
Futures	1,051	3	–
		268	(227)
<b>Equity derivatives</b>	14	–	–
<b>Total recognised derivatives</b>		321	(315)
<b>As at 31 December 2005</b>			
<b>Foreign exchange derivatives</b>			
Currency forwards	11,215	51	(43)
Currency swaps	23,234	99	(8)
OTC currency options bought and sold	335	2	(1)
		152	(52)
<b>Interest rate derivatives</b>			
Interest rate swaps	24,791	108	(220)
Cross currency interest rate swaps	3,532	36	(26)
OTC interest rate options	565	3	(3)
		147	(249)
<b>Total recognised derivatives</b>		299	(301)

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

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 period 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 for these contracts by counterparties, industry sectors and countries. Actual credit exposures and limits are regularly monitored and controlled by management.

#### *Credit risk weighted amounts*

	<b>30 June 2006</b>	31 December 2005
Derivatives		
– Exchange rate contracts	<b>146</b>	122
– Interest rate contracts	<b>110</b>	62
	<b>256</b>	184

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*

	<b>30 June 2006</b>	31 December 2005
Derivatives		
– Exchange rate contracts	<b>53</b>	184
– Interest rate contracts	<b>268</b>	83
	<b>321</b>	267

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.

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

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**17 DERIVATIVE FINANCIAL INSTRUMENTS** (Continued)*Notional amounts of derivative financial instruments by original currency (net position)*

	RMB	US Dollars	HK Dollars	Others	Total
<b>As at 30 June 2006</b>					
Notional amount of derivative financial instruments	9,641	67,268	14,861	7,105	98,875
<b>As at 31 December 2005</b>					
Notional amount of derivative financial instruments	2,100	31,006	25,006	5,560	63,672

**18 LOANS AND ADVANCES TO CUSTOMERS***(a) Loans and advances to customers*

	30 June 2006	31 December 2005
Loans and advances to customers	901,055	771,374
Less: collective impairment allowances	(5,009)	(4,520)
individual impairment allowances	(9,190)	(8,081)
	<b>886,856</b>	758,773

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

	Half-year ended 30 June 2006	2005
<b>Balance at beginning of period</b>	<b>12,601</b>	8,446
Impairment allowances for loans charged to profit and loss account	3,351	1,969
Reversal of impairment allowances for loans	(1,309)	–
Net impairment allowances for loans charged to profit and loss account	2,042	1,969
Loans written off during the period as uncollectible	(432)	(106)
Exchange difference	(12)	–
<b>Balance at end of the period</b>	<b>14,199</b>	10,309

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

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

### 18 LOANS AND ADVANCES TO CUSTOMERS (Continued)

#### (c) Individually identified loans with impairment

	<b>30 June 2006</b>	31 December 2005
Individually identified loans with impairment	<b>22,373</b>	21,579
Individually identified loans with impairment to loans and advances to customers (percentage)	<b>2.48%</b>	2.80%

### 19 INVESTMENT SECURITIES

	<b>30 June 2006</b>	31 December 2005
<b>Securities – loans and receivables</b>		
Debt securities – at amortised cost		
– Unlisted	<b>44,463</b>	28,372
<b>Securities – available-for-sale</b>		
Debt securities – at fair value		
– Listed in Hong Kong	<b>7,879</b>	7,710
– Listed outside Hong Kong	<b>63,703</b>	47,003
– Unlisted	<b>246,949</b>	230,486
Equity securities – at fair value		
– Listed outside Hong Kong	–	2
– Unlisted	<b>781</b>	764
Equity securities at cost less impairment		
– Unlisted	<b>1</b>	6
	<b>319,313</b>	285,971

As certain unlisted equity securities held by the Group have no published quoted prices available, are not able to be benchmarked with similar financial instruments, and 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:

	<b>Half-year ended 30 June 2006</b>	2005
Gains less losses arising from de-recognition of investment securities	<b>19</b>	426

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**19 INVESTMENT SECURITIES** (Continued)

The movement in investment securities may be summarized as follows:

	<b>Loans and receivables</b>	<b>Available-for-sale</b>	<b>Total</b>
At 1 January 2006	28,372	285,971	314,343
Additions	18,395	259,499	277,894
Disposals (sale or redemption)	(2,287)	(224,399)	(226,686)
Losses from changes in fair value	–	(1,936)	(1,936)
Exchange differences	(17)	178	161
At 30 June 2006	44,463	319,313	363,776

The investment securities are analysed by issuer as follows:

	<b>30 June 2006</b>	31 December 2005
<b>Securities – loans and receivables</b>		
– Central governments and central banks	42,631	26,527
– Public sector entities	461	464
– Banks and other financial institutions	1,371	1,381
	44,463	28,372
<b>Securities – available-for-sale</b>		
– Central governments and central banks	141,093	115,653
– Public sector entities	2,568	2,644
– Banks and other financial institutions	158,917	154,734
– Corporate entities	16,735	12,940
	319,313	285,971

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

	<b>30 June 2006</b>	31 December 2005
<b>Available-for-sale, at fair value</b>		
– Unlisted	1,978	2,254



## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 19 INVESTMENT SECURITIES *(Continued)*

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

	<b>30 June 2006</b>	31 December 2005
Up to 3 months	<b>330</b>	–
3 to 12 months	<b>826</b>	796
1 to 5 years	<b>822</b>	1,458
	<b>1,978</b>	2,254

### 20 PROPERTY AND EQUIPMENT

	Land and buildings	Construction in progress	Equipment	Motor vehicles	Leasehold improvement	Total
<b>Cost or valuation</b>						
At 1 January 2006	20,047	1,125	4,050	236	1,221	26,679
Additions	175	344	252	19	128	918
Disposals	(163)	(31)	(64)	(26)	(271)	(555)
Transfers	246	(246)	–	–	–	–
At 30 June 2006	20,305	1,192	4,238	229	1,078	27,042
<b>Accumulated depreciation</b>						
At 1 January 2006	–	–	(953)	(2)	(560)	(1,515)
Charge for the period	(424)	–	(660)	(38)	(118)	(1,240)
Disposals	7	–	50	24	262	343
At 30 June 2006	(417)	–	(1,563)	(16)	(416)	(2,412)
<b>Net book value</b>						
At 30 June 2006	19,888	1,192	2,675	213	662	24,630
<b>Carrying amount</b>						
at 30 June 2006, if at cost	11,847	1,052	2,616	191	662	16,368

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**20 PROPERTY AND EQUIPMENT** (Continued)

	Land and buildings	Construction in progress	Equipment	Motor vehicles	Leasehold improvement	Total
<b>Cost or valuation</b>						
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
<b>Accumulated depreciation</b>						
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)
<b>Net book value</b>						
At 31 December 2005	20,047	1,125	3,097	234	661	25,164
<b>Carrying amount</b>						
<b>at 31 December 2005, if at cost</b>	11,835	975	3,001	211	661	16,683

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 (excluding Hong Kong Branch) 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.

CB Richard Ellis Ltd. was appointed as the external valuer for the Hong Kong Branch's latest valuation exercise as at 31 December 2005 to revalue lands and buildings, construction in progress, while the 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.

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

	30 June 2006	31 December 2005
Net book value of land and buildings of Hong Kong Branch	1,326	1,370

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 21 OTHER ASSETS

	<b>30 June 2006</b>	31 December 2005
Settlement accounts	1,174	1,171
Other receivables	5,558	4,731
Less: impairment allowance	<b>(2,354)</b>	(2,167)
Foreclosed assets	5,008	5,483
Less: impairment allowance	<b>(3,141)</b>	(2,788)
Prepaid staff housing subsidies	115	214
Prepaid rental expenses	346	349
Land use rights	587	589
Computer software	261	296
Investment property	149	720
Others	2,004	1,968
	<b>9,707</b>	10,566

### 22 DUE TO OTHER BANKS AND FINANCIAL INSTITUTIONS

	<b>30 June 2006</b>	31 December 2005
Deposits from other banks and financial institutions	59,442	50,040
Loans from other banks and financial institutions	55,072	34,054
	<b>114,514</b>	84,094

### 23 FINANCIAL LIABILITIES AT FAIR VALUE THROUGH PROFIT OR LOSS

	<b>30 June 2006</b>	31 December 2005
<b>Financial liabilities held for trading</b>		
– Derivative financial instruments <i>(Note 17)</i>	315	301
– Short position of securities held for trading	1,971	1,056
– Debt securities in issue	8,432	8,198
<b>Financial liabilities at fair value through profit or loss</b>		
– Structured deposit	4	–
	<b>10,722</b>	9,555

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**23 FINANCIAL LIABILITIES AT FAIR VALUE THROUGH PROFIT OR LOSS** (Continued)

Debt securities in issue are:

	30 June 2006		31 December 2005	
	Amount	Interest rate per annum (%)	Amount	Interest rate per annum (%)
HKD short term Certificate of Deposit	706	4.17%	591	2.84%
HKD medium term Certificate of Deposit	603	4.24%	759	3.59%
USD short term Certificate of Deposit	30	4.20%	-	-
USD medium term Certificate of Deposit	545	3.78%	1,842	3.36%
HKD fixed rate step-up rate Certificate of Deposit (maturing in October 2007)	66	range from 2.35% to 2.80%	481	range from 2.35% to 2.80%
HKD fixed rate step-up rate Certificate of Deposit (maturing in November 2007)	241	range from 4.18% to 4.68%	88	range from 4.18% to 4.68%
HKD fixed rate step-up rate Certificate of Deposit (maturing in March 2008)	86	range from 2.83% to 3.83%	38	range from 2.83% to 3.83%
HKD fixed rate step-up rate Certificate of Deposit (maturing in May 2009)	446	range from 3.10% to 4.60%	244	range from 3.10% to 4.60%
HKD fixed rate step-up rate Certificate of Deposit (maturing in October 2009)	46	range from 2.80% to 4.30%	936	range from 2.80% to 4.30%
HKD floating rate Certificate of Deposit (maturing in June 2006)	-	-	417	HIBOR + 0.06%
HKD floating rate Certificate of Deposit (maturing in September 2006)	414	HIBOR + 0.2%	41	HIBOR + 0.2%
HKD floating rate Certificate of Deposit (maturing in March 2007)	38	First year 1.95% Remaining year 3M HIBOR + 0.15% (capped at 4.75%)	178	First year 1.95% Remaining year 3M HIBOR + 0.15% (capped at 4.75%)
HKD floating rate Certificate of Deposit (maturing in August 2008)	156	HIBOR + 0.18%	313	HIBOR + 0.18%

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION (Continued)

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

### 23 FINANCIAL LIABILITIES AT FAIR VALUE THROUGH PROFIT OR LOSS (Continued)

	30 June 2006		31 December 2005	
	Amount	Interest rate per annum (%)	Amount	Interest rate per annum (%)
HKD floating rate Certificate of Deposit (maturing in September 2008)	416	HIBOR + 0.26%	105	HIBOR + 0.26%
HKD reverse Certificate of Deposit (maturing in May 2009)	118	First year 6.20% Remaining years 6.90% less 3M HIBOR (minimum at 0%)	6	First year 6.20% Remaining years 6.90% less 3M HIBOR (minimum at 0%)
USD floating rate Certificate of Deposit (maturing in May 2007)	90	First year 3.1% Remaining year 3M LIBOR + 0.15% (capped at 5%)	453	First year 3.1% Remaining year 3M LIBOR + 0.15% (capped at 5%)
USD floating rate Certificate of Deposit (maturing in June 2007)	241	LIBOR + 0.12%	47	LIBOR + 0.12%
HKD floating rate Certificate of deposit (maturing in November 2008)	6	First year HIBOR Remaining years 4.4%	73	First year HIBOR Remaining years 4.4%
HKD floating rate Certificate of deposit (maturing in February 2008)	52	HIBOR + 0.10%	-	-
HKD floating rate Certificate of deposit (maturing in March 2008)	104	HIBOR + 0.10%	-	-
HKD floating rate Certificate of deposit (maturing in March 2008)	103	HIBOR + 0.10%	-	-
HKD floating rate Certificate of deposit (maturing in March 2008)	103	HIBOR + 0.12%	-	-
HKD floating rate Certificate of deposit (maturing in November 2008)	933	HIBOR + 0.18%	156	HIBOR + 0.18%
USD floating rate Certificate of deposit (maturing in November 2006)	1,570	LIBOR + 0.08%	35	LIBOR + 0.08%

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**23 FINANCIAL LIABILITIES AT FAIR VALUE THROUGH PROFIT OR LOSS** (Continued)

	30 June 2006		31 December 2005	
	Amount	Interest rate per annum (%)	Amount	Interest rate per annum (%)
USD floating rate Certificate of deposit (maturing in November 2008)	19	First year LIBOR + 0.05% Remaining year 4.5%	47	First year LIBOR + 0.05% Remaining year 4.5%
USD floating rate Certificate of deposit (maturing in November 2008)	105	LIBOR + 0.18%	162	LIBOR + 0.18%
USD floating rate Certificate of Deposit (maturing in January 2007)	1,195	LIBOR + 0.20%	1,186	LIBOR + 0.20%
	<b>8,432</b>		<b>8,198</b>	

**24 DUE TO CUSTOMERS**

	30 June 2006	31 December 2005
Corporate current deposits	432,048	407,228
Corporate savings deposits	5,892	4,232
Corporate time deposits	269,334	231,275
Individual current deposits	166,516	162,757
Individual savings deposits	10,968	9,725
Individual time deposits	289,052	263,236
Pledged deposits	132,282	105,781
Certificates of deposit	1,533	696
Promissory notes	2,333	2,708
Customer margin deposits	1,651	1,642
Other deposits	27,251	23,544
Interest payable	8,138	8,015
	<b>1,346,998</b>	<b>1,220,839</b>
Including:		
Pledged deposits held as collateral for letters of credit	4,817	5,715

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 25 OTHER LIABILITIES

	<b>30 June</b>	31 December
	<b>2006</b>	2005
Settlement accounts	<b>6,088</b>	4,509
Dividends payable	<b>3,799</b>	136
Staff benefits payables	<b>1,167</b>	1,692
Tax payable	<b>1,027</b>	816
Provision for outstanding litigation	<b>598</b>	938
Others	<b>4,793</b>	4,258
	<b>17,472</b>	12,349

### 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 period 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 period ended 30 June 2006 (Year 2005: 17.5%) for transactions in Hong Kong.

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

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
At beginning of the period	<b>542</b>	5,346
Credit/(Charge) to profit and loss account	<b>298</b>	(2,135)
Available-for-sale securities		
– fair value remeasurement	<b>635</b>	(1,479)
At end of the period	<b>1,475</b>	1,732

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**26 DEFERRED INCOME TAXES** (Continued)

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

	<b>30 June 2006</b>	31 December 2005
<b>Deferred income tax liabilities</b>		
Available-for-sale securities	<b>(656)</b>	(1,285)
Property revaluation reserve	<b>(1,519)</b>	(1,676)
Other temporary differences	<b>(254)</b>	(288)
	<b>(2,429)</b>	(3,249)
<b>Deferred income tax assets</b>		
Provision for loan losses	<b>729</b>	592
Impairment allowances for investments	<b>330</b>	392
Decelerated tax depreciation	<b>127</b>	128
Impairment of other assets	<b>2,702</b>	2,669
Available-for-sale securities	<b>16</b>	10
	<b>3,904</b>	3,791
<b>Net deferred income tax assets</b>	<b>1,475</b>	542

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

	<b>30 June 2006</b>	31 December 2005
Deferred tax assets	<b>1,724</b>	955
Deferred tax liabilities	<b>(249)</b>	(413)



## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 26 DEFERRED INCOME TAXES *(Continued)*

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

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Provision for loan losses:		
Additional provisions for loan losses	<b>137</b>	–
Utilization	–	(274)
<hr/>		
Sub-total	<b>137</b>	(274)
(Reversal of)/impairment allowances for investments	<b>(62)</b>	91
Impairment of other assets	<b>33</b>	712
Provision of tax loss carried forward	–	(2,676)
Accelerated tax depreciation	–	3
Decelerated tax depreciation	<b>(1)</b>	–
Depreciation/disposal of property and equipment	<b>157</b>	–
Other temporary differences	<b>34</b>	9
<hr/>		
	<b>298</b>	(2,135)
<hr/>		

### 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.

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Expenses incurred for retirement benefit plans	<b>256</b>	248
<hr/>		

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**28 SUBORDINATED TERM DEBT**

	<b>30 June 2006</b>	31 December 2005
Floating rate subordinated debt – 2009	<b>12,000</b>	12,000
Interest payable	<b>77</b>	292
	<b>12,077</b>	12,292

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**

	<b>Number of shares (in millions)</b>	<b>Ordinary shares of RMB1 each (RMB million)</b>	<b>Capital surplus (RMB million)</b>	<b>Total (RMB million)</b>
At 1 January 2006 and 30 June 2006	45,804	45,804	21,540	67,344

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 31), 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 resolved 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 resolution was approved by the shareholders at the Annual General Meeting on 22 June 2006.

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 30 RESERVES AND RETAINED EARNINGS *(Continued)*

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 not subject to dividend distribution. On 28 March 2006, the Directors proposed a general and statutory reserve of RMB4,428 million through its profit appropriation. The general and statutory reserve was approved by the shareholders at the Annual General Meeting on 22 June 2006. Statutory reserve of Hong Kong branch required by HKMA has been covered in above general and statutory reserve.

### 31 DIVIDENDS

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Paid in the period	<b>1</b>	2

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, 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, amounting to RMB3,664 million. The dividend was approved by the shareholders at the Annual General Meeting on 22 June 2006.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**32 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:

	<b>30 June 2006</b>	31 December 2005
Guarantees	<b>73,060</b>	49,623
Letters of credit	<b>23,049</b>	22,316
Acceptances	<b>187,897</b>	156,484
Other commitments with an original maturity of		
– under 1 year	<b>14,424</b>	10,044
– 1 year and over	<b>10,112</b>	7,443
	<b>308,542</b>	245,910

*Capital expenditure commitments*

	<b>30 June 2006</b>	31 December 2005
Capital expenditure commitments	<b>76</b>	238

*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:

	<b>30 June 2006</b>	31 December 2005
Not later than 1 year	<b>584</b>	555
Later than 1 year and not later than 5 years	<b>1,438</b>	1,320
Later than 5 years	<b>456</b>	466
	<b>2,478</b>	2,341

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 32 FINANCIAL GUARANTEES AND CREDIT RELATED COMMITMENTS, OTHER COMMITMENTS AND CONTINGENT LIABILITIES *(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 period/year are as follows:

	<b>30 June 2006</b>	31 December 2005
Outstanding claims	<b>2,309</b>	2,261
Provision for losses	<b>598</b>	938

### 33 ASSETS PLEDGED

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

	<b>Pledged assets</b>		<b>Related liabilities</b>	
	<b>30 June 2006</b>	31 December 2005	<b>30 June 2006</b>	31 December 2005
Balances with central banks	<b>80,198</b>	73,309	–	–
Investment securities	<b>3,894</b>	2,539	<b>2,632</b>	1,257
	<b>84,092</b>	75,848	<b>2,632</b>	1,257

### 34 CREDIT RISK WEIGHTED AMOUNT OF FINANCIAL GUARANTEES AND CREDIT RELATED COMMITMENTS

	<b>30 June 2006</b>	31 December 2005
Financial guarantees and credit related commitments	<b>116,269</b>	179,746

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.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**35 NOTES TO CONSOLIDATED CASH FLOW STATEMENT****(a) Analysis of changes in financing during the period**

	Dividends	Share capital	Capital surplus	Subordinated term debt	Minority interest
At 1 January 2006	136	45,804	21,540	12,292	64
Net cash outflow from financing	(1)	-	-	(496)	-
Interest expense recognised on subordinated term debt	-	-	-	281	-
Net profit attributable to minority interest	-	-	-	-	1
Dividends	3,664	-	-	-	-
At 30 June 2006	3,799	45,804	21,540	12,077	65
At 1 January 2005	141	39,070	10,872	12,275	-
Net cash outflow from financing	(2)	5,856	9,201	(469)	-
Interest expense recognised on subordinated term debt	-	-	-	277	-
At 30 June 2005	139	44,926	20,073	12,083	-

**(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:

	30 June 2006	31 December 2005
Cash and balances with central banks (Note 14)	81,876	67,000
Due from other banks and financial institutions (Note 15)	26,799	34,305
	108,675	101,305

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 36 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) Transactions with the MOF*

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

Treasury bonds

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Purchase during the period	<b>24,575</b>	7,399
Redemption during the period	<b>(7,528)</b>	(18,947)
Interest income	<b>1,210</b>	1,207
	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Outstanding balance at beginning of the period	<b>79,368</b>	59,281
Outstanding at end of the period	<b>94,024</b>	53,536

#### *(b) 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.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**36 RELATED PARTY TRANSACTIONS** (Continued)**(b) Transactions with other state controlled entities** (Continued)

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 period end, and the related expense and interest ranges for periods ended 30 June 2005 and 2006 are as follows:

## (i) Loans and advances to customers

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Outstanding balance at beginning of the period	<b>207,715</b>	190,497
Outstanding balance at end of the period	<b>225,259</b>	207,005
Less: allowance for impairment losses	<b>(2,578)</b>	(2,138)
	<b>222,681</b>	204,867
Including: discounted bills	<b>11,961</b>	6,704
Interest rate range for discounted bills	<b>1.44%~4.8%</b>	2.97%~5.74%
Interest rate range of loans and advances other than discounted bills	<b>0.625%~8.775%</b>	2%~9.396%

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

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Maximum balance during the period	<b>225,259</b>	215,789
Provision for impairment recognized/(reversed) during the period	<b>265</b>	(267)



## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 36 RELATED PARTY TRANSACTIONS *(Continued)*

#### *(b) Transactions with other state controlled entities (Continued)*

##### (ii) Investment securities

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	<b>2005</b>
Purchase during the period	<b>157,098</b>	104,311
Redemption during the period	<b>(20,832)</b>	(35,488)
Sales during the period	<b>(147,165)</b>	(61,974)
Interest income	<b>2,924</b>	1,915
	<b>Half-year ended 30 June</b>	
	<b>2006</b>	<b>2005</b>
Outstanding balance at beginning of the period	<b>137,424</b>	148,390
Outstanding balance at end of the period	<b>240,285</b>	154,781

##### (iii) Due from other banks and financial institutions

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	<b>2005</b>
Outstanding balance at beginning of the period	<b>101,504</b>	39,140
Outstanding balance at end of the period	<b>70,308</b>	78,841
Less: allowance for impairment losses	<b>(681)</b>	(976)
	<b>69,627</b>	77,865
	<b>Half-year ended 30 June</b>	
	<b>2006</b>	<b>2005</b>
Maximum balance during the period	<b>101,504</b>	78,841
Provision for impairment (reversed)/recognised during the period	<b>(52)</b>	18

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**36 RELATED PARTY TRANSACTIONS** (Continued)**(b) Transactions with other state controlled entities** (Continued)

(iv) Currency swap

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Notional amount	<b>3,878</b>	–
Fair value	<b>5</b>	–

(v) Due to other banks and financial institutions

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Outstanding balance at beginning of the period	<b>73,797</b>	20,894
Outstanding balance at end of the period	<b>104,511</b>	26,923

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Maximum balance during the period	<b>104,511</b>	26,923

(vi) Due to customers

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Outstanding balance at beginning of the period	<b>560,549</b>	112,197
Outstanding balance at end of the period	<b>315,638</b>	186,504

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Maximum balance during the period	<b>560,549</b>	224,361

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 36 RELATED PARTY TRANSACTIONS *(Continued)*

#### *(b) Transactions with other state controlled entities (Continued)*

(vii) Financial guarantees and credit related commitments

	<b>30 June 2006</b>	31 December 2005
Guarantees	<b>70,981</b>	22,954
Letters of credit	<b>6,115</b>	6,111
Acceptances	<b>18,466</b>	19,673
Derivative transactions unsettled	<b>1,201</b>	940

#### *(c) 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 six months ended 30 June 2005 and 2006, outstanding balances at the balance sheet date are as follows:

(i) Loans

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Outstanding at beginning of the period	<b>10</b>	9
Granted during the period	<b>14</b>	6
Repaid during the period	<b>(9)</b>	(3)
Outstanding at end of the period	<b>15</b>	12

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

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**36 RELATED PARTY TRANSACTIONS** (Continued)**(c) Transactions with directors and senior management** (Continued)

## (ii) Deposits

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Outstanding at beginning of the period	<b>34</b>	29
Deposited during the period	<b>51</b>	13
Repaid during the period	<b>(58)</b>	(20)
	<hr/>	
Outstanding at end of the period	<b>27</b>	22

**(d) Transactions with HSBC**

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

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Outstanding at beginning of the period	<b>4,654</b>	100
Granted during the period	<b>134,021</b>	113,490
Repaid during the period	<b>(136,727)</b>	(111,914)
	<hr/>	
Outstanding at end of the period	<b>1,948</b>	1,676
	<hr/>	
Interest income	<b>10</b>	3

## (ii) Deposits from HSBC

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Outstanding at beginning of the period	<b>2,318</b>	1,218
Deposited during the period	<b>49,083</b>	32,737
Repaid during the period	<b>(49,642)</b>	(32,012)
	<hr/>	
Outstanding at end of the period	<b>1,759</b>	1,943
	<hr/>	
Interest expense on deposits	<b>30</b>	7

## NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION *(Continued)*

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

### 36 RELATED PARTY TRANSACTIONS *(Continued)*

#### *(d) Transactions with HSBC (Continued)*

##### (iii) Investment securities

	<b>Half-year ended 30 June</b>	
	<b>2006</b>	2005
Interest income	<b>4</b>	16
	<b>30 June</b>	31 December
	<b>2006</b>	2005
Outstanding balance	<b>727</b>	568

##### (iv) Financial guarantees and credit related commitments

	<b>30 June</b>	31 December
	<b>2006</b>	2005
Guarantees	<b>4</b>	7
Letters of credit	<b>381</b>	347
Derivative transactions unsettled	<b>7,962</b>	28,768

### 37 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.

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**37 SEGMENTAL INFORMATION** (Continued)

**(a) Geographical segment information**

	Northern China	North- eastern China	Eastern China	Central and Southern China	Western China	Overseas	Eliminations and Consolidated	Total
<b>As at 30 June 2006</b>								
<b>Assets</b>								
Cash and balances with central banks	5,431	3,027	139,734	9,443	3,850	589	-	162,074
Due from other banks and financial institutions	25,794	2,022	83,068	5,323	2,150	19,762	(2,439)	135,680
Financial assets held for trading	-	-	61	-	-	4,480	-	4,541
Loans and advances to customers	142,706	60,888	373,443	175,792	76,224	55,506	2,297	886,856
Investment securities								
- loans and receivables	1,508	1,967	38,190	1,616	1,182	-	-	44,463
- available-for-sale	28,915	17,253	212,252	24,931	11,003	24,959	-	319,313
Other assets	22,342	6,762	17,336	12,686	7,302	7,618	(37,985)	36,061
<b>Total assets</b>	<b>226,696</b>	<b>91,919</b>	<b>864,084</b>	<b>229,791</b>	<b>101,711</b>	<b>112,914</b>	<b>(38,127)</b>	<b>1,588,988</b>
<b>Liabilities</b>								
Due to other banks and financial institutions	(30,010)	(9,491)	(55,886)	(11,306)	(2,514)	(5,307)	-	(114,514)
Financial liabilities at fair value through profit or loss	-	-	(145)	-	-	(10,577)	-	(10,722)
Due to customers	(239,203)	(123,778)	(512,880)	(272,065)	(127,872)	(71,200)	-	(1,346,998)
Other liabilities	(2,813)	(1,242)	(37,637)	(3,613)	(1,947)	(23,387)	38,127	(32,512)
<b>Total liabilities</b>	<b>(272,026)</b>	<b>(134,511)</b>	<b>(606,548)</b>	<b>(286,984)</b>	<b>(132,333)</b>	<b>(110,471)</b>	<b>38,127</b>	<b>(1,504,746)</b>
<b>Net on balance sheet position</b>	<b>(45,330)</b>	<b>(42,592)</b>	<b>257,536</b>	<b>(57,193)</b>	<b>(30,622)</b>	<b>2,443</b>	<b>-</b>	<b>84,242</b>
<b>Acquisition cost of property and equipment ("PPE") and intangible assets</b>								
	148	120	341	192	120	23	-	944

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**37 SEGMENTAL INFORMATION** (Continued)

(a) **Geographical segment information** (Continued)

	Northern China	North- eastern China	Eastern China	Central and Southern China	Western China	Overseas	Eliminations and Consolidated	Total
<b>For the half-year ended</b>								
<b>30 June 2006</b>								
Interest income	4,831	2,187	16,666	5,407	2,435	2,487	(4,412)	29,601
Interest expense	(2,101)	(910)	(8,311)	(1,925)	(654)	(1,768)	4,412	(11,257)
<b>Net interest income</b>	<b>2,730</b>	<b>1,277</b>	<b>8,355</b>	<b>3,482</b>	<b>1,781</b>	<b>719</b>	<b>-</b>	<b>18,344</b>
Fee and commission income	160	100	621	248	123	307	-	1,559
Fee and commission expense	(27)	(15)	(81)	(48)	(14)	(78)	-	(263)
<b>Net fee and commission income</b>	<b>133</b>	<b>85</b>	<b>540</b>	<b>200</b>	<b>109</b>	<b>229</b>	<b>-</b>	<b>1,296</b>
Dividend income	2	-	7	8	-	10	-	27
Gains less losses arising from trading activities	132	34	(117)	81	16	4	-	150
Gains less losses arising from investment securities	15	-	4	-	-	-	-	19
Other operating income	77	12	89	55	12	99	-	344
Reversal/(impairment) losses on loans and advances	(277)	(512)	(979)	(151)	(110)	58	-	(1,971)
Other operating expenses	(1,018)	(1,105)	(3,759)	(1,572)	(841)	(657)	-	(8,952)
<b>Operating profit/(loss) before tax</b>	<b>1,794</b>	<b>(209)</b>	<b>4,140</b>	<b>2,103</b>	<b>967</b>	<b>462</b>	<b>-</b>	<b>9,257</b>
Income tax	(550)	(134)	(1,438)	(565)	(309)	(226)	-	(3,222)
<b>Net profit/(loss) for the period</b>	<b>1,244</b>	<b>(343)</b>	<b>2,702</b>	<b>1,538</b>	<b>658</b>	<b>236</b>	<b>-</b>	<b>6,035</b>
<b>Depreciation and amortization of property and equipment and intangible assets</b>	<b>121</b>	<b>142</b>	<b>631</b>	<b>208</b>	<b>133</b>	<b>67</b>	<b>-</b>	<b>1,302</b>

**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**37 SEGMENTAL INFORMATION** (Continued)**(a) Geographical segment information** (Continued)

	Northern China	North- eastern China	Eastern China	Central and Southern China	Western China	Overseas	Eliminations and Consolidated	Total
<b>As at 31 December 2005</b>								
<b>Assets</b>								
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								
- loans and receivables	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
<b>Total assets</b>	<b>210,270</b>	<b>81,977</b>	<b>769,196</b>	<b>205,936</b>	<b>94,266</b>	<b>96,971</b>	<b>(35,177)</b>	<b>1,423,439</b>
<b>Liabilities</b>								
Due to other banks and financial institutions	(32,262)	(4,297)	(34,104)	(7,192)	(2,368)	(3,912)	41	(84,094)
Financial liabilities at fair value through profit or loss	-	-	(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)
<b>Total liabilities</b>	<b>(254,631)</b>	<b>(122,174)</b>	<b>(519,690)</b>	<b>(259,343)</b>	<b>(125,516)</b>	<b>(94,116)</b>	<b>35,177</b>	<b>(1,340,293)</b>
<b>Net on balance sheet position</b>	<b>(44,361)</b>	<b>(40,197)</b>	<b>249,506</b>	<b>(53,407)</b>	<b>(31,250)</b>	<b>2,855</b>	<b>-</b>	<b>83,146</b>
<b>Acquisition cost of property and equipment ("PPE") and intangible assets</b>								
	461	348	1,794	474	440	118	-	3,635



**NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED INTERIM FINANCIAL INFORMATION** (Continued)

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

**37 SEGMENTAL INFORMATION** (Continued)

(a) **Geographical segment information** (Continued)

	Northern China	North- eastern China	Eastern China	Central and Southern China	Western China	Overseas	Eliminations and Consolidated	Total
<b>For the half-year ended</b>								
<b>30 June 2005</b>								
Interest income	3,840	1,943	12,535	4,482	2,121	1,515	(3,158)	23,278
Interest expense	(1,502)	(819)	(5,978)	(1,459)	(725)	(1,011)	3,158	(8,336)
<b>Net interest income</b>	2,338	1,124	6,557	3,023	1,396	504	-	14,942
Fee and commission income	133	79	402	205	75	154	-	1,048
Fee and commission expense	(28)	(18)	(48)	(38)	(11)	(27)	-	(170)
<b>Net fee and commission income</b>	105	61	354	167	64	127	-	878
Dividend income	-	-	10	-	-	2	-	12
Gains less losses arising from trading activities	85	21	148	50	9	155	-	468
Gains less losses arising from investment securities	72	-	344	7	-	3	-	426
Other operating income	14	6	25	24	18	134	-	221
Reversal/(impairment) losses on loans and advances	(193)	(338)	(319)	(496)	(681)	109	-	(1,918)
Other operating expenses	(961)	(832)	(3,348)	(1,830)	(787)	(387)	-	(8,145)
<b>Operating profit before tax</b>	1,460	42	3,771	945	19	647	-	6,884
Income tax	(490)	(130)	(960)	(446)	(185)	(68)	-	(2,279)
<b>Net profit/(loss) for the period</b>	970	(88)	2,811	499	(166)	579	-	4,605
<b>Depreciation and amortization of property and equipment and intangible assets</b>	123	147	601	209	121	56	-	1,257

## VII. SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION

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

• Capital Adequacy and Liquidity Ratios	82
• Components of Capital Base after Deductions	83
• Currency concentrations	84
• Cross-border Claims	85
• Overdue and Rescheduled Assets	86

## VII. SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION *(Continued)*

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

### 1 CAPITAL ADEQUACY AND LIQUIDITY RATIOS

	<b>30 June 2006</b>	31 December 2005
Capital adequacy ratio	<b>11.07%</b>	11.20%
Liquidity ratios:		
RMB current assets to RMB current liabilities	<b>67.46%</b>	63.23%
Foreign currency current assets to foreign currency current liabilities	<b>94.27%</b>	110.74%

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.

**VII. SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION** *(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.

	<b>30 June 2006</b>	31 December 2005
Core capital:		
Paid up ordinary share capital <i>(Note 1)</i>	<b>45,804</b>	45,934
Reserves	<b>18,011</b>	18,100
Profit and loss account	<b>14,252</b>	8,113
Minority interest	<b>71</b>	70
	<b>78,138</b>	72,217
Supplementary capital:		
Reserves on revaluation of land and interests in land	<b>3,855</b>	–
Impairment allowances for impaired assets and regulatory reserves	<b>12,204</b>	10,935
Term subordinated debt	<b>9,600</b>	9,600
Reserve-net profit of overseas branches retained	<b>–</b>	–
Gross value of supplementary capital	<b>25,659</b>	20,535
Eligible value of supplementary capital	<b>25,659</b>	20,535
Total capital base before deductions	<b>103,797</b>	92,752
Deductions:		
Unconsolidated equity investments	<b>(1,894)</b>	(1,743)
Total capital base after deductions	<b>101,903</b>	91,009

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.

*Note 1:* The amount of RMB130 million represents a variation in the treatment of subsidiary equity in accordance with regulatory policy.

## VII. SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION *(Continued)*

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

### 3 CURRENCY CONCENTRATIONS

<b>As at 30 June 2006</b>	<b>US Dollars</b>	<b>HK Dollars</b>	<b>Others</b>	<b>Total</b>
Spot assets	<b>108,769</b>	<b>56,030</b>	<b>21,338</b>	<b>186,137</b>
Spot liabilities	<b>(94,631)</b>	<b>(62,196)</b>	<b>(18,655)</b>	<b>(175,482)</b>
Forward purchases	<b>27,412</b>	<b>151</b>	<b>3,727</b>	<b>31,290</b>
Forward sales	<b>(20,131)</b>	<b>(284)</b>	<b>(7,255)</b>	<b>(27,670)</b>
Net long/(short) position	<b>21,419</b>	<b>(6,299)</b>	<b>(845)</b>	<b>14,275</b>
Net structural position	<b>3,707</b>	<b>5,897</b>	<b>548</b>	<b>10,152</b>
As at 31 December 2005	US Dollars	HK Dollars	Others	Total
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

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.

**VII. SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION** *(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.

	<b>Bank and other financial institutions</b>	<b>Public sector entities</b>	<b>Others</b>	<b>Total</b>
<b>As at 30 June 2006</b>				
Asia Pacific excluding Mainland China	<b>27,402</b>	<b>4,017</b>	<b>43,686</b>	<b>75,105</b>
– of which attributed to Hong Kong	<b>1,901</b>	<b>3,871</b>	<b>40,991</b>	<b>46,763</b>
North and South America	<b>13,717</b>	<b>1,348</b>	<b>3,487</b>	<b>18,552</b>
Europe	<b>42,435</b>	<b>205</b>	<b>105</b>	<b>42,745</b>
	<b>83,554</b>	<b>5,570</b>	<b>47,278</b>	<b>136,402</b>
<b>As at 31 December 2005</b>				
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

## VII. SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION *(Continued)*

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

### 5 OVERDUE AND RESCHEDULED ASSETS

#### (a) Advances

(i) Gross amount of overdue loans

	<b>30 June 2006</b>	31 December 2005
Gross advances to customers which have been overdue for:*		
– within 3 months	<b>4,074</b>	5,250
– between 3 and 6 months	<b>2,595</b>	3,331
– between 6 and 12 months	<b>5,164</b>	4,912
– over 12 months	<b>11,114</b>	9,024
	<b>22,947</b>	22,517
Percentage:		
– within 3 months	<b>0.45%</b>	0.68%
– between 3 and 6 months	<b>0.29%</b>	0.43%
– between 6 and 12 months	<b>0.57%</b>	0.64%
– over 12 months	<b>1.24%</b>	1.17%
	<b>2.55%</b>	2.92%
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	<b>691</b>	743
	<b>691</b>	743
Percentage:		
– within 3 months	–	–
– between 3 and 6 months	–	–
– between 6 and 12 months	–	–
– over 12 months	<b>0.51%</b>	0.44%
	<b>0.51%</b>	0.44%

## VII. SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION *(Continued)*

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

### 5 OVERDUE AND RESCHEDULED ASSETS *(Continued)*

#### *(a) Advances (Continued)*

##### (i) Gross amount of overdue loans *(Continued)*

\* Included in the gross overdue advances to customers as at 30 June 2006, there are trade bills which have been overdue for:

	<b>30 June 2006</b>
– within 3 months	<b>268</b>
– between 3 and 6 months	<b>84</b>
– between 6 and 12 months	<b>47</b>
– over 12 months	<b>219</b>
	<b>618</b>

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

	<b>30 June 2006</b>	31 December 2005
Domestic regions		
– Northern China	<b>3,420</b>	2,748
– North-eastern China	<b>4,346</b>	3,646
– Eastern China	<b>5,644</b>	4,708
– Central & Southern China	<b>5,399</b>	5,710
– Western China	<b>3,667</b>	5,090
	<b>22,476</b>	21,902
Hong Kong and overseas countries	<b>471</b>	615
	<b>22,947</b>	22,517



## VII. SUPPLEMENTARY UNAUDITED FINANCIAL INFORMATION *(Continued)*

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

### 5 OVERDUE AND RESCHEDULED ASSETS *(Continued)*

#### *(a) Advances (Continued)*

(iii) Overdue and rescheduled loans

	<b>30 June 2006</b>	31 December 2005
Total rescheduled loans and advances to customers	<b>5,876</b>	9,781
Less: total overdue rescheduled loans and advances to customers	<b>(3,682)</b>	(4,249)
<hr/>		
Total normal rescheduled loans and advances to customers	<b>2,194</b>	5,532
<hr/>		
Percentage of normal part in total rescheduled loans	<b>37%</b>	57%
<hr/>		

*(b)* As at 31 December 2005 and 30 June 2006, the Group has no overdue available-for-sale investment securities.

#### *(c) Foreclosed assets*

	<b>30 June 2006</b>	31 December 2005
Foreclosed assets	<b>5,008</b>	5,483
<hr/>		

## VIII. RECONCILIATION OF NET ASSETS AND NET PROFIT FROM PRC GAAP TO IFRS

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

Under PRC GAAP, the Bank has implemented <Financial instrument recognition and measurement (draft)> since 1 January 2006. The Bank retrospectively restated the 2005 fiscal year's financial reports under PRC GAAP due to this accounting policy change. The reconciliation of net assets and net profits from PRC GAAP to IFRS after the restatement is listed as follows:

	Net assets		Net profit		
	30 June 2006	31 December 2005 Restated	Half-year ended 30 June 2006	Year ended 31 December 2005 Restated	
<b>PRC GAAP figures</b>	<b>82,997</b>	<b>81,202</b>	<b>6,477</b>	<b>9,416</b>	
<b>Adjustments for accounting standard differences:</b>					
1.	Revaluation surplus from fixed assets and investment properties	3,852	4,197	(329)	(182)
2.	Differences arising from the transfer of the non-performing loans to China Cinda Asset Management Corporation	(665)	(760)	95	206
3.	Consolidated adjustments	(979)	(801)	(8)	(19)
4.	Deferred taxes	(724)	(901)	2	334
5.	Translation difference on foreign currency net position	-	-	(24)	(371)
6.	Others	(304)	145	(179)	(135)
<b>IFRS figures</b>	<b>84,177</b>	<b>83,082</b>	<b>6,034</b>	<b>9,249</b>	

### Explanation of the adjustments for accounting standard differences:

#### 1. REVALUATION SURPLUS/DEFICIT FROM FIXED ASSETS AND INVESTMENT PROPERTIES

In 2005, the Bank carried out a further revaluation exercise on fixed assets and investment properties for the purpose of the preparation of its IFRS financial statements, which was not a statutory valuation nor was it approved by the Ministry of Finance of the PRC. The valuation surplus/deficit arising from the 2004 valuation has been reflected in IFRS accounts, while it is not recognised in PRC GAAP financial statements. The differences arising from fixed assets and investment property valuation exercise in 2005 have been reflected as accounting standard differences accordingly. Such difference will be depreciated during the remaining beneficiary period.

## VIII. RECONCILIATION OF NET ASSETS AND NET PROFIT FROM PRC GAAP TO IFRS *(Continued)*

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

### 2. DIFFERENCES ARISING FROM THE TRANSFER OF THE NON-PERFORMING LOANS TO CHINA CINDA ASSET MANAGEMENT CORPORATION

On 27 June 2004, the Bank disposed of non-performing loans (the "Transferred Loans") to China Cinda Asset Management Corporation in exchange for a bill issued by the People's Bank of China (the "Bill"). The amount of carrying value of the Transferred Loans in excess of the fair value of the Bill, net of tax, was offset against capital surplus in its IFRS financial statements. The discount will be amortized and recorded as interest income during the remaining beneficiary periods of the Bill.

### 3. CONSOLIDATION ADJUSTMENTS

Subsidiaries, which are those companies and other entities (including Special Purpose Entities) in which the Group, directly or indirectly, has control, are consolidated in the Bank's IFRS financial statements. However, under PRC GAAP, it is allowed not to consolidate subsidiaries which are intended to be disposed of in the near future.

### 4. DEFERRED TAXES

In both PRC GAAP and IFRS financial statements prepared by the Bank, 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. Accordingly, all adjustments on accounting standard differences also gave rise to deferred taxation differences.

### 5. TRANSLATION DIFFERENCE ON FOREIGN CURRENCY NET POSITION

Translation difference on foreign currency net position under PRC GAAP is recognized in equity, while it is recognized as foreign exchange gain or loss in profit and loss under IFRS.

### 6. OTHERS

All other differences are adjustments with minor amounts.