Notes to the Consolidated Financial Statements

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

1 GENERAL

Bank of Communications Co., Ltd. (the "Bank") is a commercial and retail bank providing banking services mainly in the People's Republic of China ("PRC"). The Bank was reorganised as a joint stock national commercial bank on 1 April 1987, in accordance with the approval notice (Guo Fa (1986) No. 81) issued by the State Council of the PRC and the approval notice (Yin Fa (1987) No. 40) issued by the People's Bank of China ("PBOC"). Headquartered in Shanghai, the Bank operates 95 city level branches in the PRC. In addition, the Bank has branches in Hong Kong, New York, Tokyo, Singapore, and Seoul.

2 ACCOUNTING POLICIES

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

A Basis of presentation

The consolidated financial statements of the Group have been prepared in accordance with the International Financial Reporting Standards ("IFRS") The consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation of investment securities classified as available for sale, financial assets and financial liabilities held at fair value through profit or loss, property and equipment, investment properties and all derivative contracts, which are revalued at fair value.

Critical accounting estimates and judgments in applying accounting policies

The preparation of financial statements in conformity with IFRS and the disclosure requirements of the Hong Kong Companies Ordinance require the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies.

(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 profit and loss account, the Group makes judgment 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.

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

2 ACCOUNTING POLICIES *(Continued)*

A Basis of presentation *(Continued)*

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), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect reported fair value of financial instruments.

(3) *Income taxes*

The Group is subject to income taxes in numerous jurisdictions; principally, however in the China including Hong Kong Special Administrative Region. Significant estimates are required in determining the provision for income taxes. There are certain transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognizes liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. In particular, the deductibility of certain items in the Mainland China is subject to tax authority's 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. (Note 26)

(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. (Note 25).

The Group adopted the following amendments and interpretations that were effective as at 1 January 2006:

IAS 19 Amendment — Actuarial Gains and Losses, Group Plans and Disclosures;

IAS 21 Amendment — Net Investment in a Foreign Operation;

IFRIC 4 — Determining whether Arrangement contains a Lease;

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

2 ACCOUNTING POLICIES *(Continued)*

A Basis of presentation *(Continued)*

The application of above amendments and interpretations did not result in substantial changes to the Group's accounting policies and did not have a material impact on the Group's consolidated financial position as at the end of 2005 and 2006. Other amendments and interpretations that were effective as at 1 January 2006 are not applicable to the Group's accounting policies.

The Group has chosen not to early adopt the following standards and interpretations that were issued but not yet effective for accounting periods beginning on 1 January 2006:

IFRS 7 Financial instruments: Disclosure (effective 1 January 2007);

Amendments to IAS 1: Capital Disclosure (effective 1 January 2007);

IFRS 8 Operating Segments (effective 1 January 2008);

IFRIC 7 Applying the Restatement Approach under IAS 29 (effective 1 March 2006);

IFRIC 8 Scope of IFRS 2 (effective 1 May 2006);

IFRIC 9 Reassessment of embedded derivative (effective 1 June 2006);

IFRIC 10 Interim Financial Reporting and Impairment (effective 1 November 2006);

IFRIC 11 IFRS 2 — Group Treasury Share Transactions (effective 1 March 2007); and

IFRIC 12 Service Concession Arrangements (effective 1 January 2009).

The application of these new standards, amendments and interpretations will not have a material impact on the Group's consolidated financial position in the period of initial application.

Except for the adoption of the above amendments and interpretations which are effective for accounting periods commencing on or after 1 January 2006, the accounting policies and basis of preparation of the financial statements of the Group are consistent with those adopted in the Group's 2005 annual financial statements.

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

2 ACCOUNTING POLICIES *(Continued)*

B Subsidiary undertakings

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

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

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

In the stand alone financial statements of the Bank, the subsidiaries are measured at cost less provision for impairment, as the fair value of these subsidiaries cannot be reliably measured. The amount of impairment loss is included in the net profit or loss for the year. The Group applies a policy of treating transactions with minority interests as transactions with parties external the Group.

C Derivative financial instruments

Derivative financial instruments including foreign exchange contracts, currency and interest rate swaps, and other derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are obtained from quoted market prices, discounted cash flow models and options pricing models as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

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

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

2 ACCOUNTING POLICIES *(Continued)*

C Derivative financial instruments *(Continued)*

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

Certain derivative transactions, while considered as hedges under the Group's risk management policies, do not qualify for hedge accounting under the specific rules in IAS 39 and are therefore treated as derivatives held for trading.

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

D Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. Management determines the classification of its investments at initial recognition.

(a) *Financial assets at fair value through profit or loss*

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception.

A financial asset is classified in this category if it is acquired or incurred principally for the purpose of selling or repurchasing in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives are also categorized as held for trading unless they are designated as hedging instruments.

Financial assets and financial liabilities are designated at fair value through profit or loss when:

- doing so significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortised cost for loans and advances to customers or banks and debt securities in issue;

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

2 ACCOUNTING POLICIES *(Continued)*

D Financial assets *(Continued)*

(a) *Financial assets at fair value through profit or loss (Continued)*

- certain investments, such as equity investments, are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis are designated at fair value through profit and loss; and

- financial instruments, such as debt securities held, containing one or more embedded derivatives significantly modify the cash flows, are designated at fair value through profit and loss.

Gains and losses arising from changes in the fair value of derivatives that are managed in conjunction with designated financial assets or financial liabilities are included in gains and losses arising from trading activities.

(b) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (i) those that the entity intends to sell immediately or in the short term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; (ii) those that the entity upon initial recognition designates as available for sale; or (iii) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration. After initial recognition, loans and receivables are carried at amortised cost using the effective interest method, less any impairment allowances.

(c) *Held-to-maturity financial assets*

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. If the Group were to sell other than an insignificant amount of held-to-maturity assets, the entire category would be reclassified as available for sale.

(d) *Available-for-sale financial assets*

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates, equity prices or management intention.

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

2 ACCOUNTING POLICIES *(Continued)*

D Financial assets *(Continued)*

(d) *Available-for-sale financial assets (Continued)*

Purchases and sales of financial assets at fair value through profit or loss, held to maturity and available for sale are recognised on trade-date — the date on which the Group commits to purchase or sell the asset. Otherwise such transactions are treated as derivatives until settlement occurs, when they meet the definition of derivative.

Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit and loss are initially recognised at fair value, and transaction costs are expensed in the profit and loss account. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership. Financial liabilities are derecognised when they are extinguished — that is, when the obligation is discharged, cancelled or expires.

Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method. Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in gains and losses arising from trading activities in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in equity, until the financial asset is derecognised or impaired. At this time, the cumulative gain or loss previously recognised in equity is recognised in profit or loss. Interest earned whilst holding financial assets is reported as interest income using the effective interest rate method. Dividends receivable are included separately in dividend income when the entity's right to receive payment is established.

The fair values of quoted investments in active markets are based on current bid prices. If there is no active market for a financial asset, the Group establishes fair value using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

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

2 ACCOUNTING POLICIES *(Continued)*

E Impairment of financial assets

(a) *Assets carried at amortised cost*

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The estimated period between a loss occurring and its identification is determined by local management for each identified portfolio. In general, the periods used vary between three months and 12 months; in exceptional cases, longer periods are warranted.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the profit and loss account. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

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

2 ACCOUNTING POLICIES *(Continued)*

E Impairment of financial assets *(Continued)*

(a) *Assets carried at amortised cost (Continued)*

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the Group and historical loss experience for assets with credit risk characteristics similar to those in the Group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Group to reduce any differences between loss estimates and actual loss experience.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the profit and loss account in the impairment charge for credit losses.

(b) *Assets classified as available for sale*

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss — measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss — is removed from equity and recognised in the profit and loss account. Impairment losses recognised in the profit and loss account on equity instruments are not reversed through the profit and loss account. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the profit and loss account.

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

2 ACCOUNTING POLICIES *(Continued)*

F Interest income and expense

Interest income and expense are recognised in the profit and loss account for interest-bearing instruments on an accruals basis using the effective interest method. Interest income includes coupons earned on fixed income investment and trading securities and accrued discount and premium on treasury bills and other discounted instruments. Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

G Fee and commission income

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

H Sale/purchase and repurchase/resale agreements

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

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

I Property and equipment

All property, plant and equipment is initially measured at its cost, which includes expenditure that is directly attributable to the acquisition of the items.

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

2 ACCOUNTING POLICIES *(Continued)*

l Property and equipment *(Continued)*

Subsequent to initial recognition, the Group adopts a revaluation policy to carry all classes of property and equipment except for leasehold improvements at revaluation, being their fair value at the date of the revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Leasehold improvements continue to be stated at cost less accumulated impairment losses and depreciation.

Increases in the carrying amount arising on revaluation of property and equipment are credited to revaluation reserves in shareholders' equity. Decreases that offset previous increases of the same asset are charged against revaluation reserves; all other decreases are charged to the profit and loss account. The revaluation reserves are transferred directly to retained earnings when the relevant items of property and equipment are retired or disposed of.

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

Land and buildings	25–50 years
Leasehold improvements	3–10 years
Equipment and motor vehicles	3–8 years

No depreciation is provided against construction in progress.

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

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

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

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

2 ACCOUNTING POLICIES *(Continued)*

J Foreclosed assets

Foreclosed assets are initially recognised at fair value plus expenditure that is directly attributable to the acquisition of the items. An impairment loss is recognized in the profit and loss account whenever the carrying amount of such an asset exceeds its recoverable amount. Foreclosed assets are carried at cost less impairment.

K Land use rights

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

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

L Intangible assets

Intangible assets are recognized initially at its cost, which includes expenditure that is directly attributable to the acquisition of the items. Where payment for an intangible asset is deferred beyond normal credit terms, its cost is the cash price equivalent. Costs associated with maintaining computer software program are recognised as an expense as incurred. However, expenditure that enhances or extends the performance of computer software program beyond their original specifications is recognised as capital improvement and added to the original cost of the software. Amortization for intangible assets is calculated on a straight-line basis from the month of acquisition over the estimated useful period and is recognized in the profit and loss account. Intangible assets are stated at cost less accumulated amortization and impairment.

M Investment property

Property held to earn rentals which is not occupied by the Group is classified as investment property. Investment property comprises land and buildings.

Investment property is initially measured at its cost, which includes expenditure that is directly attributable to the acquisition of the items. Subsequent to initial recognition, the Group adopts the fair value model to account for its investment property. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. Where active market price information is not available, the Group uses alternative valuation methods such as discounted cash flow projections or recent prices on less active markets. These valuations are reviewed annually by an independent valuer. Changes in fair values are recorded in the profit and loss account.

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

2 ACCOUNTING POLICIES *(Continued)*

N Leases

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

O Cash and cash equivalents

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

P Provisions

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

Q Deferred income taxes

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

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

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

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

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

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

2 ACCOUNTING POLICIES *(Continued)*

R Borrowings

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

S Share capital

(1) *Share issue costs*

External costs directly attributable to the issue of new shares are deducted from equity net of any related income taxes.

(2) *Dividends on ordinary shares*

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

T Acceptances

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers. Acceptances are accounted for as financial guarantees and credit related commitments transactions and are disclosed as contingent liabilities and commitments.

U Employee benefits

(1) *Staff benefit and retirement benefit obligations*

Salaries and bonuses, housing benefits and costs for social security benefits are accrued in the financial period in which the services are rendered by employees of the Group. The Group also participates in various defined contribution retirement plans principally organised by municipal and provincial governments. The Group's contributions to these pension plans are charged to the profit and loss account in the financial period to which they relate.

(2) *Share-based compensation*

The Group operates a cash-settled, share-based compensation plan to certain senior management of the Bank. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense.

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

2 ACCOUNTING POLICIES *(Continued)*

U Employee benefits *(Continued)*

(2) *Share-based compensation (Continued)*

The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions. Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each balance sheet date, the Group revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the profit and loss account with a corresponding adjustment to the liability recognized.

V Foreign currency translation

(1) *Functional and presentation currency*

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

(2) *Transactions and balances*

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the profit and loss account.

Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in equity.

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

2 ACCOUNTING POLICIES *(Continued)*

V Foreign currency translation *(Continued)*

(3) *Group companies*

The results and financial position of all the group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

— Assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

— Income and expenses for each profit and loss account are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

— All resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings are taken to shareholders' equity. When a foreign operation is disposed of, or partially disposed of, such exchange differences are recognised in the profit and loss account as part of the gain or loss on sale.

W Contingent liabilities and contingencies

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

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

X Financial guarantee contracts

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

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

2 ACCOUNTING POLICIES *(Continued)*

X Financial guarantee contracts *(Continued)*

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

Y Fiduciary activities

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

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

Z Segment reporting

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

AA Offset financial assets and liabilities

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

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

3 USE OF FINANCIAL INSTRUMENTS

A Strategy in using financial instruments

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

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

B Credit risk

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

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

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.

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

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, so the group manages such credit risk together with loan portfolio.

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

Group

	Total assets	Total liabilities	Financial guarantees and credit related commitments
As at 31 December 2006			
Mainland China	**1,605,118**	**1,517,989**	**286,526**
Hong Kong	**97,111**	**93,743**	**21,570**
Others	**17,254**	**17,256**	**5,937**
Total	**1,719,483**	**1,628,988**	**314,033**
As at 31 December 2005			
Mainland China	1,326,468	1,246,177	227,747
Hong Kong	84,085	81,263	14,304
Others	12,886	12,853	3,859
Total	1,423,439	1,340,293	245,910

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

Bank

	Total assets	Total liabilities	Financial guarantees and credit related commitments
As at 31 December 2006			
Mainland China	**1,604,870**	**1,516,670**	**286,526**
Hong Kong	**95,213**	**92,642**	**21,570**
Others	**17,256**	**17,256**	**5,937**
Total	**1,717,339**	**1,626,568**	**314,033**
As at 31 December 2005			
Mainland China	1,326,026	1,244,705	227,747
Hong Kong	82,935	80,767	14,304
Others	12,886	12,853	3,859
Total	1,421,847	1,338,325	245,910

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.

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

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

Group and Bank

	31 December 2006	**%**	31 December 2005	%
Domestic regions				
— Beijing	**109,585**	**12**	84,298	11
— Jiangsu	**109,198**	**12**	93,247	12
— Shanghai	**98,816**	**11**	86,122	11
— Guangdong	**83,014**	**9**	66,002	9
— Zhejiang	**74,341**	**8**	56,634	7
— Shandong	**50,756**	**5**	46,956	6
— Henan	**35,956**	**4**	29,867	4
— Hubei	**33,868**	**4**	29,031	4
— Liaoning	**27,699**	**3**	26,920	4
— Others	**244,695**	**26**	204,238	26
Domestic regions total	**867,928**	**94**	723,315	94
Hong Kong and overseas countries	**56,897**	**6**	46,225	6
Interest receivables	**2,580**	**—**	1,834	—
Gross amount of loans and advances before allowance for impairment	**927,405**	**100**	771,374	100

A geographical region is reported where it contributes 3% 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).

(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):

Group and Bank

	31 December 2006	**%**	31 December 2005	%
Corporate loans				
Manufacturing				
— Petroleum and chemical	**41,227**	**4**	32,585	4
— Electronics	**26,917**	**3**	27,035	4
— Steel	**26,448**	**3**	24,540	3
— Machinery	**25,592**	**3**	22,763	3
— Textile	**20,420**	**2**	18,076	2
— Other manufacturing	**100,141**	**11**	85,360	11
Transportation	**93,035**	**10**	63,544	8
Trading	**81,945**	**9**	72,977	10
Services	**79,630**	**9**	56,024	7
Real estate	**65,962**	**7**	60,913	8
Utilities	**63,289**	**7**	51,812	7
Construction	**35,961**	**4**	25,958	3
Educations and scientific research	**25,521**	**3**	24,934	3
Post and telecommunications	**11,456**	**1**	15,768	2
Agriculture	**2,440**	**—**	4,698	1
Non-banking financial institutions	**13,020**	**1**	9,753	1
Others	**12,888**	**1**	7,871	1
Corporate loans total	**725,892**	**78**	604,611	78
Mortgage loans	**88,224**	**10**	78,264	10
Medium-term and long-term working capital loans	**17,626**	**2**	13,685	2
Short-term working capital loans	**10,321**	**1**	5,087	1
Car loans	**3,932**	**1**	3,961	1
Credit card advances	**2,731**	**—**	696	—
Loans secured by deposits	**1,284**	**—**	1,093	—
Others	**2,010**	**—**	1,267	—
Individual loans total	**126,128**	**14**	104,053	14
Discounted bills	**72,805**	**8**	60,876	8
Interest receivables	**2,580**	**—**	1,834	—
	75,385	**8**	62,710	8
Gross amount of loans and advances before allowance for impairment	**927,405**	**100**	771,374	100

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

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

B Credit risk *(Continued)*

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

Group and Bank

	31 December 2006	31 December 2005
Domestic		
Corporate entities		
State owned entities	**240,214**	198,276
Collective owned entities	**13,456**	11,022
Private unlimited companies	**47,733**	35,987
Private limited companies	**204,038**	163,673
Joint stock companies	**64,937**	63,723
Foreign invested enterprises	**83,408**	78,339
Other domestic entities	**31,226**	22,347
	685,012	573,367
Individuals	**112,129**	89,853
	797,141	663,220
Hong Kong and Overseas		
Corporate entities	**40,880**	31,244
Individuals	**13,999**	14,200
	54,879	45,444
Discounted bills	**72,805**	60,876
Interest receivables	**2,580**	1,834
Gross amount of loans and advances before allowance for impairment	**927,405**	771,374

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

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 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 currency to monitor the Group's currency risk.

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 the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board set limits on the level of exposure by currency, which are monitored regularly. The tables below summarize the Group's exposure to foreign currency exchange rate risk at the end of each year. The tables show the Group's assets and liabilities at carrying amounts in RMB, categorized by the original currency.

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

D Currency risk *(Continued)*

Group

	RMB	US Dollars	HK Dollars	Others	Total
As at 31 December 2006					
Assets					
Cash and balances with central banks	249,224	2,949	1,332	436	253,941
Due from other banks and financial institutions	70,367	37,773	6,495	3,988	118,623
Financial assets held for trading	8,346	1,849	2,385	415	12,995
Loans and advances to customers	821,997	43,954	38,515	5,841	910,307
Investment securities-loans and receivables	46,420	1,630	—	—	48,050
Investment securities-available-for-sale	296,890	27,583	5,912	9,438	339,823
Other assets, including deferred tax assets	46,007	(14,428)	3,415	750	35,744
Total assets	1,539,251	101,310	58,054	20,868	1,719,483
Liabilities					
Due to other banks and financial institutions	(149,445)	(15,374)	(1,228)	(2,619)	(168,666)
Financial liabilities held for trading	(101)	(2,448)	(6,024)	(151)	(8,724)
Due to customers	(1,287,404)	(67,489)	(51,300)	(14,138)	(1,420,331)
Other liabilities, including deferred tax liabilities	(27,326)	(560)	(3,374)	(7)	(31,267)
Total liabilities	(1,464,276)	(85,871)	(61,926)	(16,915)	(1,628,988)
Net position	74,975	15,439	(3,872)	3,953	90,495
Financial guarantees and credit related commitments	228,549	59,009	14,874	11,601	314,033

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

D Currency risk *(Continued)*

Bank

	RMB	US Dollars	HK Dollars	Others	Total
As at 31 December 2006					
Assets					
Cash and balances with central banks	249,224	2,949	582	436	253,191
Due from other banks and financial institutions	70,367	37,773	6,495	3,988	118,623
Financial assets held for trading	8,346	1,849	2,385	415	12,995
Loans and advances to customers	821,997	43,954	38,515	5,841	910,307
Investment securities-loans and receivables	46,420	1,630	—	—	48,050
Investment securities-available-for-sale	295,324	27,583	6,765	9,438	339,110
Investments in and due from subsidiaries	122	—	1,222	—	1,344
Other assets, including deferred tax assets	45,821	(14,428)	1,576	750	33,719
Total assets	1,537,621	101,310	57,540	20,868	1,717,339
Liabilities					
Due to other banks and financial institutions	(149,445)	(15,374)	(1,228)	(2,619)	(168,666)
Financial liabilities held for trading	(101)	(2,448)	(6,024)	(151)	(8,724)
Due to customers	(1,287,404)	(67,489)	(51,300)	(14,138)	(1,420,331)
Other liabilities, including deferred tax liabilities	(26,006)	(560)	(2,274)	(7)	(28,847)
Total liabilities	(1,462,956)	(85,871)	(60,826)	(16,915)	(1,626,568)
Net position	74,665	15,439	(3,286)	3,953	90,771
Financial guarantees and credit related commitments	228,549	59,009	14,874	11,601	314,033

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

D Currency risk *(Continued)*

Group

	RMB	US Dollars	HK Dollars	Others	Total
As at 31 December 2005					
Assets					
Cash and balances with central banks	136,606	2,401	848	454	140,309
Due from other banks and financial institutions	106,166	47,152	7,571	9,212	170,101
Financial assets held for trading	1	1,399	1,423	405	3,228
Loans and advances to customers	678,966	41,804	32,967	5,036	758,773
Investment securities-loans and receivables	26,527	1,845	—	—	28,372
Investment securities-available-for-sale	251,083	21,233	6,644	7,011	285,971
Other assets, including deferred tax assets	38,059	(2,993)	3,362	(1,743)	36,685
Total assets	1,237,408	112,841	52,815	20,375	1,423,439
Liabilities					
Due to other banks and financial institutions	(62,974)	(14,613)	(3,916)	(2,591)	(84,094)
Financial liabilities held for trading	(12)	(3,962)	(5,548)	(33)	(9,555)
Due to customers	(1,091,403)	(73,122)	(41,085)	(15,229)	(1,220,839)
Other liabilities, including deferred tax liabilities	(22,973)	(1,400)	(974)	(458)	(25,805)
Total liabilities	(1,177,362)	(93,097)	(51,523)	(18,311)	(1,340,293)
Net position	60,046	19,744	1,292	2,064	83,146
Financial guarantees and credit related commitments	184,775	45,206	9,867	6,062	245,910

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

D Currency risk *(Continued)*

Bank

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

(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.

The Group operates its business predominantly in Mainland China under the interest rate scheme regulated 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. It is normal practice for the interest rates of both interest-bearing assets and liabilities to move in the same direction. 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. Consequently, the Group is less vulnerable to interest rate risk. However, there is no guarantee that the PBOC will continue this practice in future.

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 amounts classified as "Due to customers up to one month" . These amounts classified as "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.

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

Group

	Up to 1 month	1–3 months	3–12 months	1–5 years	Over 5 years	Non-interest bearing	Total
As at 31 December 2006							
Assets							
Cash and balances with central banks	243,516	—	—	—	—	10,425	253,941
Due from other banks and financial institutions	88,653	15,204	14,255	—	—	511	118,623
Financial assets held for trading	2,659	1,785	4,916	1,977	1,266	392	12,995
Loans and advances to customers	77,609	153,949	385,356	149,154	144,239	—	910,307
Investment securities							
— loans and receivables	164	862	21,194	24,835	995	—	48,050
— available-for-sale	14,760	30,574	96,519	129,433	68,523	14	339,823
Other assets, including deferred tax assets	154	—	—	—	—	35,590	35,744
Total assets	427,515	202,374	522,240	305,399	215,023	46,932	1,719,483
Liabilities							
Due to other banks and financial institutions	(142,562)	(19,251)	(4,530)	(183)	(1,944)	(196)	(168,666)
Financial liabilities held for trading	(1,434)	(2,472)	(997)	(3,239)	(12)	(570)	(8,724)
Due to customers	(913,317)	(116,073)	(255,130)	(112,973)	(62)	(22,776)	(1,420,331)
Other liabilities, including deferred tax liabilities	(17)	—	(12,292)	—	—	(18,958)	(31,267)
Total liabilities	(1,057,330)	(137,796)	(272,949)	(116,395)	(2,018)	(42,500)	(1,628,988)
Total interest sensitivity gap	(629,815)	64,578	249,291	189,004	213,005	4,432	90,495

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

Bank

	Up to 1 month	1–3 months	3–12 months	1–5 years	Over 5 years	Non-interest bearing	Total
As at 31 December 2006							
Assets							
Cash and balances with central banks	243,515	—	—	—	—	9,676	253,191
Due from other banks and financial institutions	88,653	15,204	14,255	—	—	511	118,623
Financial assets held for trading	2,659	1,785	4,916	1,977	1,266	392	12,995
Loans and advances to customers	77,609	153,949	385,356	149,154	144,239	—	910,307
Investment securities							
— loans and receivables	164	862	21,194	24,835	995	—	48,050
— available-for-sale	15,613	30,574	96,519	129,433	66,957	14	339,110
Investments in and due from subsidiaries	—	—	—	—	—	1,344	1,344
Other assets, including deferred tax assets	—	—	—	—	—	33,719	33,719
Total assets	428,213	202,374	522,240	305,399	213,457	45,656	1,717,339
Liabilities							
Due to other banks and financial institutions	(142,562)	(19,251)	(4,530)	(183)	(1,944)	(196)	(168,666)
Financial liabilities held for trading	(1,434)	(2,472)	(997)	(3,239)	(12)	(570)	(8,724)
Due to customers	(913,317)	(116,073)	(255,130)	(112,973)	(62)	(22,776)	(1,420,331)
Other liabilities, including deferred tax liabilities	(17)	—	(12,292)	—	—	(16,538)	(28,847)
Total liabilities	(1,057,330)	(137,796)	(272,949)	(116,395)	(2,018)	(40,080)	(1,626,568)
Total interest sensitivity gap	(629,117)	64,578	249,291	189,004	211,439	5,576	90,771

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

Group

	Up to 1 month	1–3 months	3–12 months	1–5 years	Over 5 years	Non-interest bearing	Total
As at 31 December 2005							
Assets							
Cash and balances with central banks	131,290	—	—	—	—	9,019	140,309
Due from other banks and financial institutions	130,833	28,103	8,195	1,550	1,050	370	170,101
Financial assets held for trading	1,272	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
Total assets	344,462	204,208	438,990	222,041	167,246	46,492	1,423,439
Liabilities							
Due to other banks and financial institutions	(59,381)	(13,930)	(8,718)	—	(2,002)	(63)	(84,094)
Financial liabilities held for trading	(2,230)	(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)
Total liabilities	(852,847)	(127,206)	(228,132)	(90,057)	(3,919)	(38,132)	(1,340,293)
Total interest sensitivity gap	(508,385)	77,002	210,858	131,984	163,327	8,360	83,146

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

Bank

	Up to 1 month	1–3 months	3–12 months	1–5 years	Over 5 years	Non-interest bearing	Total
As at 31 December 2005							
Assets							
Cash and balances with central banks	131,290	—	—	—	—	8,739	140,029
Due from other banks and financial institutions	130,833	28,103	8,195	1,550	1,050	370	170,101
Financial assets held for trading	1,272	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	52,511	119	285,658
Investments in and due from subsidiaries	—	—	60	6	—	720	786
Other assets, including deferred tax assets	—	—	—	—	—	34,900	34,900
Total assets	344,462	204,208	439,050	222,047	166,933	45,147	1,421,847
Liabilities							
Due to other banks and financial institutions	(59,381)	(13,930)	(8,718)	—	(2,002)	(63)	(84,094)
Financial liabilities held for trading	(2,230)	(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)	—	(11,330)	(23,837)
Total liabilities	(852,847)	(127,206)	(228,132)	(90,057)	(3,919)	(36,164)	(1,338,325)
Total interest sensitivity gap	(508,385)	77,002	210,918	131,990	163,014	8,983	83,522

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

E Interest rate risk *(Continued)*

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

Group and Bank

	RMB	US Dollars	HK Dollars	Others
As at 31 December 2006				
Assets				
Balances with central banks	**1.39%**	**0.36%**	**0.18%**	**0.00%**
Due from other banks and financial institutions	**1.91%**	**4.98%**	**4.14%**	**3.43%**
Loans and advances to customers	**5.60%**	**4.88%**	**4.76%**	**2.12%**
Investment securities				
— loans and receivables	**2.62%**	**5.12%**	**NA**	**NA**
— available-for-sale	**2.98%**	**5.21%**	**3.44%**	**4.13%**
Liabilities				
Due to other banks and financial institutions	**1.62%**	**4.73%**	**3.48%**	**3.36%**
Due to customers	**1.54%**	**4.37%**	**3.45%**	**2.32%**
Subordinated term debt	**4.77%**	**NA**	**NA**	**NA**
As at 31 December 2005				
Assets				
Balances with central banks	1.60%	0.17%	0.19%	0.00%
Due from other banks and financial institutions	1.64%	4.23%	4.08%	3.88%
Loans and advances to customers	5.34%	4.38%	5.55%	2.20%
Investment securities				
— loans and receivables	2.98%	5.15%	N/A	N/A
— available-for-sale	2.85%	4.32%	3.44%	3.79%
Liabilities				
Due to other banks and financial institutions	1.43%	4.20%	4.02%	2.04%
Due to customers	1.55%	3.33%	3.37%	2.53%
Subordinated term debt	4.77%	NA	NA	NA

(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 at below 75% as required by the PBOC. 9% of the Group's total RMB denominated deposits and 4% of the total foreign currency denominated deposits must be deposited with central banks. The tables below analyze the assets and liabilities of the Group into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date.

Maturities of assets and liabilities

Group

	Up to 1 month	1–3 months	3–12 months	1–5 years	Over 5 years	Overdue	Total
As at 31 December 2006							
Assets							
Cash and balances with central banks	253,941	—	—	—	—	—	253,941
Due from other banks and financial institutions	88,807	15,378	14,418	—	—	20	118,623
Financial assets held for trading	2,644	1,394	4,953	2,509	1,495	—	12,995
Loans and advances to customers	64,025	129,257	387,041	170,539	143,649	15,796	910,307
Investment securities							
— loans and receivables	8	706	21,272	25,069	995	—	48,050
— available-for-sale	9,072	17,375	71,426	159,201	82,749	—	339,823
Other assets, including deferred tax assets	3,169	42	307	9,707	22,020	499	35,744
Total assets	421,666	164,152	499,417	367,025	250,908	16,315	1,719,483
Liabilities							
Due to other banks and financial institution	(141,442)	(20,566)	(4,531)	(183)	(1,944)	—	(168,666)
Financial liabilities held for trading	(3,689)	(522)	(925)	(3,421)	(167)	—	(8,724)
Due to customers	(922,735)	(119,151)	(262,212)	(114,035)	(2,198)	—	(1,420,331)
Other liabilities, including deferred tax liabilities	(14,431)	(2,046)	(1,523)	(12,963)	(304)	—	(31,267)
Total liabilities	(1,082,297)	(142,285)	(269,191)	(130,602)	(4,613)	—	(1,628,988)
Net liquidity gap	(660,631)	21,867	230,226	236,423	246,295	16,315	90,495

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk *(Continued)*

Bank

	Up to 1 month	1–3 months	3–12 months	1–5 years	Over 5 years	Overdue	Total
As at 31 December 2006							
Assets							
Cash and balances with central banks	253,191	—	—	—	—	—	253,191
Due from other banks and financial institutions	88,807	15,378	14,418	—	—	20	118,623
Financial assets held for trading	2,644	1,394	4,953	2,509	1,495	—	12,995
Loans and advances to customers	64,025	129,257	387,041	170,539	143,649	15,796	910,307
Investment securities							
— loans and receivables	8	706	21,272	25,069	995	—	48,050
— available-for-sale	9,924	17,375	71,426	159,201	81,184	—	339,110
Investments in and due from subsidiaries	—	—	—	—	1,344	—	1,344
Other assets, including deferred tax assets	2,352	42	307	9,707	20,812	499	33,719
Total assets	420,951	164,152	499,417	367,025	249,479	16,315	1,717,339
Liabilities							
Due to other banks and financial institution	(141,442)	(20,566)	(4,531)	(183)	(1,944)	—	(168,666)
Financial liabilities held for trading	(3,689)	(522)	(925)	(3,421)	(167)	—	(8,724)
Due to customers	(922,735)	(119,151)	(262,212)	(114,035)	(2,198)	—	(1,420,331)
Other liabilities, including deferred tax liabilities	(12,106)	(2,046)	(1,523)	(12,963)	(209)	—	(28,847)
Total liabilities	(1,079,972)	(142,285)	(269,191)	(130,602)	(4,518)	—	(1,626,568)
Net liquidity gap	(659,021)	21,867	230,226	236,423	244,961	16,315	90,771

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk *(Continued)*

Group

	Up to 1 month	1–3 months	3–12 months	1–5 years	Over 5 years	Overdue	Total
As at 31 December 2005							
Assets							
Cash and balances with central banks	140,309	—	—	—	—	—	140,309
Due from other banks and financial institutions	130,844	28,315	8,272	1,550	1,050	70	170,101
Financial assets held for trading	1,321	42	93	762	1,010	—	3,228
Loans and advances to customers	57,479	111,693	346,722	112,901	113,799	16,179	758,773
Investment securities							
— loans and receivables	14	717	1,763	25,394	484	—	28,372
— available-for-sale	3,876	17,428	57,111	138,465	69,091	—	285,971
Other assets, including deferred tax assets	6,858	853	2,593	4,815	20,797	769	36,685
Total assets	340,701	159,048	416,554	283,887	206,231	17,018	1,423,439
Liabilities							
Due to other banks and financial institution	(59,280)	(14,054)	(8,758)	—	(2,002)	—	(84,094)
Financial liabilities held for trading	(1,078)	(426)	(715)	(7,287)	(49)	—	(9,555)
Due to customers	(812,495)	(104,277)	(220,096)	(79,850)	(4,121)	—	(1,220,839)
Other liabilities, including deferred tax liabilities	(10,942)	(1,696)	(518)	(12,243)	(406)	—	(25,805)
Total liabilities	(883,795)	(120,453)	(230,087)	(99,380)	(6,578)	—	(1,340,293)
Net liquidity gap	(543,094)	38,595	186,467	184,507	199,653	17,018	83,146

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk *(Continued)*

Bank

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

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

F Liquidity risk *(Continued)*

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

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

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

G Fair values of financial assets and liabilities

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

(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)*

Group and Bank

	31 December 2006 Carrying Value	Fair Value	31 December 2005 Carrying Value	Fair Value
Financial assets				
Due from other banks and financial institutions	**118,623**	**118,623**	170,101	170,101
Loans and advances to customers	**910,307**	**910,307**	758,773	758,773
Investment securities				
— loans and receivables	**48,050**	**48,071**	28,372	29,189
— Due from/(to) subsidiaries	**125**	**125**	(136)	(136)
Financial liabilities				
Due to other banks and financial institutions	**168,666**	**168,666**	84,094	84,094
Due to customers	**1,420,331**	**1,420,726**	1,220,839	1,220,320
Subordinated term debt	**12,292**	**12,292**	12,292	12,292

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.

(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.

Subordinated term debt

The fair value of subordinated term debt with floating rate is approximately equal to its carrying value.

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

3 USE OF FINANCIAL INSTRUMENTS *(Continued)*

H Fiduciary activities

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

Group and Bank

	As at 31 December	
	2006	2005
Investment custody accounts	**190,248**	96,852

4 NET INTEREST INCOME

Group

	Year ended 31 December	
	2006	2005
Interest income		
Balances with central banks	**2,096**	1,815
Due from other banks and financial institutions	**6,141**	3,375
Trading securities	**—**	9
Loans and advances to customers	**45,321**	36,305
Investment securities	**10,855**	8,114
Others	**130**	62
	64,543	49,680
Interest expense		
Due to other banks and financial institutions	**(3,548)**	(1,548)
Due to customers	**(21,192)**	(16,541)
	(24,740)	(18,089)
Net interest income	**39,803**	31,591

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

4 NET INTEREST INCOME *(Continued)*

	Year ended 31 December	
	2006	2005
Interest income accrued on loans and advances to customers individually identified with impairment	**553**	740
Interest income accrued on amounts due from other banks and financial institutions with impairment	**—**	—

5 DIVIDEND INCOME

Group

	Year ended 31 December	
	2006	2005
Dividend income	**123**	45

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

6 GAINS LESS LOSSES ARISING FROM TRADING ACTIVITIES

Group

	Year ended 31 December	
	2006	2005
Foreign exchange	**253**	269
Interest rate instruments	**(310)**	151
	(57)	420

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/(expense) on interest rate instruments includes the results of marking securities held for trading, debt securities in issue, interest rate swaps, cross currency interest rate swaps, interest rate options and other interest rate derivatives to market.

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

7 OTHER OPERATING INCOME

Group

	Year ended 31 December	
	2006	2005
Profit on sales of land use rights and buildings	**54**	66
Sales of foreclosed assets and other assets	**148**	38
Revaluation surplus of investment property	**16**	46
Penalty income	**—**	9
Fund management Income	**118**	17
Other miscellaneous income	**702**	453
	1,038	629

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

8 IMPAIRMENT LOSSES ON LOANS AND ADVANCES

Group

	Year ended 31 December	
	2006	2005
Due from other banks and financial institutions and securities purchased under resale agreements, net *(Note 15(b))*	**(117)**	(149)
Loans and advances to customers *(Note 18(b))*	**5,748**	4,549
Less: recovery of loans previously written off	**(93)**	(102)
	5,538	4,298

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

9 OTHER OPERATING EXPENSES

Group

	Year ended 31 December	
	2006	2005
Staff costs *(Note 10)*	**7,391**	5,776
General and administrative expenses	**3,742**	3,080
Depreciation *(Note 20)*	**2,501**	2,364
Business tax and surcharges	**2,555**	2,109
Operating lease rentals	**849**	737
Impairment of other receivables	**311**	327
Regulator's supervision fee	**317**	259
Provision for/(Reversal of) outstanding litigation	**197**	(51)
Amortization of intangible assets	**136**	105
Revaluation deficit of property and equipment *(Note 20)*	**41**	9
Professional fees	**40**	34
Losses on sales of investment property	**5**	—
Amortization of land use rights	**3**	5
Others	**2,807**	3,258
	20,895	18,012

10 STAFF COSTS

Group

	Year ended 31 December	
	2006	2005
Salaries and bonus	**4,780**	3,678
Pension costs	**529**	431
Housing benefits and subsidies	**649**	535
Other social security and benefit costs	**1,433**	1,132
	7,391	5,776

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

11 DIRECTORS' EMOLUMENTS

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

	Year ended 31 December						
	2006						2005
Name	Emoluments	Salary	Discretionary bonuses	Other benefits	Employer's contribution to pension scheme	Total	Total
Executive directors							
Mr. Zhang, Jianguo	—	560,000	557,000	57,812	110,127	1,284,939	1,060,310
Mr. Li, Jun	—	832,000	445,600	86,544	117,502	1,481,646	799,853
Mr. Peng, Chun	—	768,000	445,600	86,207	102,086	1,401,893	301,433
Mr. Zhang, Jixiang	—	673,200	389,900	57,436	86,671	1,207,207	613,196
Mr. Qiao, Wei	NA	NA	NA	NA	NA	NA	433,285
Non-executive directors							
Mr. Jiang, Chaoliang	—	960,000	557,000	98,349	117,502	1,732,851	960,310
Mr. OR Ching Fai	NA	NA	NA	NA	NA	NA	2,000
Mr. Wang Dongshen	6,000	—	—	—	—	6,000	—
Mr. Fung Kwok Lun	NA	NA	NA	NA	NA	NA	2,000
Mr. Li Keping	6,000	—	—	—	—	6,000	6,000
Mr. Li Zexing	12,000	—	—	—	—	12,000	10,000
Mr. Hu, Huating	—	673,200	389,900	56,753	86,671	1,206,524	600,357
Mr. Gao Shiqing	4,000	—	—	—	—	4,000	2,000
Mr. Shen Weiming	6,000	—	—	—	—	6,000	4,000
Mr. Li Guanglin	4,000	—	—	—	—	4,000	6,000
Mr. Qian Ping	2,000	—	—	—	—	2,000	—
Mr. Xie Qingjian	—	200,000	—	—	—	200,000	150,000
Mr. Ian Ramsay Wilson	—	200,000	—	—	—	200,000	150,000
Mr. Thomas Joseph Manning	—	200,000	—	—	—	200,000	150,000
Mr. Hui Ho Ming Herbert	—	200,000	—	—	—	200,000	125,000
Mr. Chen Qingtai	—	200,000	—	—	—	200,000	125,000
Ms. Shi Meilun	2,000	—	—	—	—	2,000	NA
Supervisors							
Mr. Cui Leiping	—	960,000	557,000	98,627	117,502	1,733,129	955,998
Ms. Liu Sha	—	375,000	—	42,380	16,363	433,743	526,151
Ms. Chen Qing	—	375,000	90,000	559,654	82,046	1,106,700	525,791
Mr. Lee Jun	—	375,000	90,000	53,657	82,406	601,063	96,149
Ms. Yin Baoyu	NA	NA	NA	NA	NA	NA	583,760
Mr. Ning Jinbiao	6,000	—	—	—	—	6,000	6,000
Mr. Teng Tieqi	2,000	—	—	—	—	2,000	4,000
Mr. Ji Keliang	2,000	—	—	—	—	2,000	4,000
Mr. Liu Qiang	6,000	160,000	—	—	—	166,000	128,000
Ms. Chen Zheng	8,000	160,000	—	—	—	168,000	128,000
Total	66,000	7,871,400	3,522,000	1,197,419	918,876	13,575,695	8,458,593

*NA: Not applicable

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

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

11 DIRECTORS' EMOLUMENTS *(Continued)*

(b) Five Highest Paid Individuals

The five highest paid individuals in the Bank for the related years are as follows

	Year ended 31 December	
	2006	2005
Salary	**5**	5
Discretionary bonuses	**2**	1
Employer's contribution to pension scheme	**1**	1
	8	7

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

	Number of employees	
	2006	2005
RMB1,000,000–RMB1,500,000	**3**	4
RMB1,500,000–RMB2,000,000	**2**	1
	5	5

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

(c) Share-based compensation

In November 2005 and November 2006, Share Appreciation Rights ("SARs") were granted to several senior executives of head office under the long term incentive plan (as more fully described in Note 29). During the years 2006 and 2005, no SARs were exercised. Benefits arising from the granting of these SARs were recognized in the consolidated profit and loss account but not included in the directors' emoluments disclosed above.

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

12 INCOME TAX

Group

	Year ended 31 December	
	2006	2005
Current tax		
— Mainland China income tax	**6,706**	786
— Hong Kong profits tax	**188**	139
— Overseas taxation	**245**	2
	7,139	927
Deferred tax *(Note 26)*	**(2,003)**	2,673
	5,136	3,600

The provision for Mainland China income tax is calculated based on the statutory rate of 33% of the assessable income of the Bank and each of the subsidiaries established in Mainland China as determined in accordance with the relevant PRC income tax rules and regulations for the year ended 31 December 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 year ended 31 December 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 year ended 31 December 2006.

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

	Year ended 31 December	
	2006	2005
Profit before tax	**17,405**	12,843
Tax calculated at a tax rate of 33%	**5,744**	4,238
Effect of different tax rates in other countries	**(3)**	(58)
Tax credit arising from income not subject to tax *(Note 1)*	**(970)**	(1,020)
Tax effect of expenses that are not deductible for tax purposes *(Note 2)*	**365**	440
Income tax expense	**5,136**	3,600

Note 1: The income not subject to tax of the Group mainly represents interest income arising from treasury bonds, which is income tax free in accordance with the PRC tax regulation.

Note 2: The expenses that are not tax deductible of the Group mainly represents a portion of expenditure, such as payroll, entertainment expenses etc, which is over the tax deduction limits in accordance with PRC tax regulation.

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

13 BASIC AND DILUTED EARNINGS PER SHARE

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

	Year ended 31 December	
	2006	2005
Profit attributable to shareholders of the Bank	**12,274**	9,249
Weighted average number of ordinary shares in issue	**45,804**	42,581
Basic and diluted earnings per share (expressed in RMB per share)	**0.27**	0.22

14 CASH AND BALANCES WITH CENTRAL BANKS

Group

	As at 31 December	
	2006	2005
Cash	**10,415**	9,280
Balances with central banks other than mandatory reserve deposits	**139,443**	57,720
Included in cash and cash equivalents *(Note 35)*	**149,858**	67,000
Mandatory reserve deposits	**104,083**	73,309
	253,941	140,309

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

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

Bank

	As at 31 December	
	2006	2005
Cash	**9,665**	9,000
Balances with central banks other than mandatory reserve deposits	**139,443**	57,720
Included in cash and cash equivalents	**149,108**	66,720
Mandatory reserve deposits	**104,083**	73,309
	253,191	140,029

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

	As at 31 December	
	2006	2005
Mandatory reserve rate for deposits denominated in RMB	**9%**	7.5%
PBOC reserve rate for deposits denominated in foreign currencies	**4%**	3%

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

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

15 DUE FROM OTHER BANKS AND FINANCIAL INSTITUTIONS

(a) Due from other banks and financial institutions

Group and Bank

	As at 31 December	
	2006	2005
Placement with other banks and included in cash equivalents *(Note 35)*	**35,865**	34,305
Securities purchased under resale agreement	**25,972**	65,715
Less: allowance for impairment losses on securities purchased under resale agreement	**(10)**	(10)
	25,962	65,705
Loans purchased under resale agreement	**5,326**	11,062
Loans and advances to other banks	**45,342**	55,147
Loans to other financial institutions	**6,744**	4,615
	52,086	59,762
Less: Individual impairment allowance on amounts due from other banks and financial institutions	**(616)**	(733)
	51,470	59,029
	118,623	170,101

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

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

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

Group and Bank

	Year ended 31 December	
	2006	2005
Balance at beginning of the year	**743**	1,004
Reversal of impairment, net *(Note 8)*	**(117)**	(149)
Amounts transferred out during the year as uncollectible	**—**	(112)
Balance at end of the year	**626**	743

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

Group and Bank

	As at 31 December	
	2006	2005
Impaired amount of due from other banks and financial institutions	**626**	743
Impaired amount of due from other banks and financial institutions (percentage)	**0.53%**	0.44%

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

16 FINANCIAL ASSETS HELD FOR TRADING

Group and Bank

	As at 31 December	
	2006	2005
Derivative financial instruments *(Note 17)*	**392**	299
Government bonds		
— Listed in Hong Kong	**24**	1,294
— Listed outside Hong Kong	**83**	—
— Unlisted	**5,709**	—
Other debt securities		
— Listed in Hong Kong	**680**	611
— Unlisted — corporate bonds	**2,731**	146
— Unlisted — public sector	**46**	71
— Unlisted — banking sector	**3,330**	807
	12,995	3,228

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.

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

17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

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.

Group and Bank

	Contract/ notional Amount	Fair values Assets	Fair values Liabilities
As at 31 December 2006			
Foreign exchange derivatives			
Currency forwards	36,419	35	(70)
Currency swaps	61,281	126	(68)
Subtotal		161	(138)
Interest rate derivatives			
Forward rate agreements	3,748	3	—
Interest rate swaps	34,401	213	(370)
Cross currency interest rate swaps	1,038	7	(49)
OTC interest rate options	1,710	8	(11)
Subtotal		231	(430)
Total recognised derivatives		392	(568)

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

17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

Group and Bank

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

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

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

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

17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

Credit risk weighted amounts

Group and Bank

	As at 31 December	
	2006	2005
Derivatives		
— Exchange rate contracts	**264**	122
— Interest rate contracts	**101**	62
	365	184

The credit risk weighted amounts are the amounts calculated with reference to the guidelines issued by the China Banking Regulatory Commission ('CBRC') and are dependent on, amongst other factors, the creditworthiness of the counterparty and the maturity characteristics of each type of contract.

Replacement costs

Group and Bank

	As at 31 December	
	2006	2005
Derivatives		
— Exchange rate contracts	**161**	152
— Interest rate contracts	**231**	147
	392	299

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 contracts to market. Replacement cost is a close approximation of the credit risk for these contracts as of the balance sheet date.

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

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

17 DERIVATIVE FINANCIAL INSTRUMENTS *(Continued)*

Notional amounts of derivative financial instruments by original currency

Group and Bank

	RMB	US Dollars	HK Dollars	Others	Total
As at 31 December 2006					
Notional amount of derivative financial instruments	**38,662**	**79,145**	**11,958**	**8,832**	**138,597**
As at 31 December 2005					
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

Group and Bank

	As at 31 December	
	2006	2005
Loans and advances to customers	**927,405**	771,374
Less: collective impairment allowances	**(5,705)**	(4,520)
Individual impairment allowances	**(11,393)**	(8,081)
	910,307	758,773

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

18 LOANS AND ADVANCES TO CUSTOMERS *(Continued)*

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

Group and Bank

	As at 31 December	
	2006	2005
Balance at beginning of year	**12,601**	8,446
Impairment allowances for loans charged to profit and loss account	**8,980**	4,549
Reversal of impairment allowances for loans	**(3,232)**	—
Net impairment allowances for loans charged to profit and loss account	**5,748**	4,549
Loans written off during the year as uncollectible	**(1,147)**	(312)
Exchange difference	**(104)**	(82)
Balance at end of the year	**17,098**	12,601

(c) Individually identified loans with impairment:

Group and Bank

	As at 31 December	
	2006	2005
Individually identified loans with impairment	**23,477**	21,579
Individually identified loans with impairment to loans and advances to customers (percentage)	**2.53%**	2.80%

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

19 INVESTMENT SECURITIES

Group

	As at 31 December	
	2006	2005
Securities — loans and receivables		
Debt securities — at amortised cost		
— Unlisted	**48,050**	28,372
Securities — available-for-sale		
Debt securities — at fair value		
— Listed in Hong Kong	**9,497**	7,710
— Listed outside Hong Kong	**74,783**	47,003
— Unlisted	**254,284**	230,486
Equity securities — at fair value		
— Listed in Hong Kong	**531**	—
— Listed outside Hong Kong	**—**	2
— Unlisted	**728**	764
Equity securities at cost less impairment		
— Unlisted	**—**	6
	339,823	285,971

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

19 INVESTMENT SECURITIES *(Continued)*

Bank

	As at 31 December	
	2006	2005
Securities — loans and receivables		
Debt securities — at amortised cost		
— Unlisted	**48,050**	28,372
Securities — available-for-sale		
Debt securities — at fair value		
— Listed in Hong Kong	**9,497**	7,710
— Listed outside Hong Kong	**74,783**	47,003
— Unlisted	**254,284**	230,486
Equity securities — at fair value		
— Listed outside Hong Kong	**—**	2
— Unlisted	**546**	451
Equity securities at cost less impairment		
— Unlisted	**—**	6
	339,110	285,658

As certain unlisted equity securities held by the Group have no published quoted prices available or are not able to be benchmarked with similar financial instruments, or valuation techniques are not cost effective, the Group states such unlisted equity securities at cost less impairment.

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

19 INVESTMENT SECURITIES *(Continued)*

Gains less losses arising from investment securities comprise:

Group and Bank

	As at 31 December	
	2006	2005
Gains less losses arising from de-recognition of investment securities	**58**	359

The movement in investment securities may be summarized as follows:

Group

	Loans and receivables	Available-for-sale	Total
Balance at 1 January 2006	**28,372**	**285,971**	**314,343**
Additions	**23,020**	**463,634**	**486,654**
Disposals (sale or redemption)	**(3,282)**	**(406,593)**	**(409,875)**
Losses from changes in fair value	**—**	**(2,632)**	**(2,632)**
Exchange differences	**(60)**	**(557)**	**(617)**
At 31 December 2006	**48,050**	**339,823**	**387,873**

Bank

	Loans and receivables	Available-for-sale	Total
Balance at 1 January 2006	**28,372**	**285,658**	**314,030**
Additions	**23,020**	**463,634**	**486,654**
Disposals (sale or redemption)	**(3,282)**	**(406,869)**	**(410,151)**
Losses from changes in fair value	**—**	**(2,756)**	**(2,756)**
Exchange differences	**(60)**	**(557)**	**(617)**
At 31 December 2006	**48,050**	**339,110**	**387,160**

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

19 INVESTMENT SECURITIES *(Continued)*

Group

	Loans and receivables	Available-for-sale	Total
Balance at 1 January 2005	31,205	215,523	246,728
Additions	1,764	408,510	410,274
Disposals (sale or redemption)	(4,540)	(342,066)	(346,606)
Gain from changes in fair value	—	5,842	5,842
Exchange differences	(57)	(1,838)	(1,895)
At 31 December 2005	28,372	285,971	314,343

Bank

	Loans and receivables	Available-for-sale	Total
Balance at 1 January 2005	31,205	215,432	246,637
Additions	1,764	407,815	409,579
Disposals (sale or redemption)	(4,540)	(341,593)	(346,133)
Gain from changes in fair value	—	5,842	5,842
Exchange differences	(57)	(1,838)	(1,895)
At 31 December 2005	28,372	285,658	314,030

In 2004, the Group disposed of investment securities classified as held-to-maturity in the amount of RMB1.1 billion prior to their contractual maturity dates. As a result, the Group reclassified all its held-to-maturity investments with the amortised cost of RMB4,378 million to available-for-sale investments on 30 September 2004. The Group is also prohibited by Paragraph 9 of IAS 39 to classify any financial assets as held-to-maturity before 1 January 2007 and all investment securities purchased by the Group during 30 September 2004 to 31 December 2006 with the intention and ability to hold through maturity are classified as available-for-sale financial instruments in accordance with Paragraph 9 of IAS 39. As of 31 December 2006, the management of the Group has determined to reclassify its available-for-sale investment securities with the fair value and amortised cost of RMB228,560 million and RMB227,477 million respectively to held-to-maturity investments on 1 January 2007 when it becomes appropriate for the Group to carry these investment securities at amortised cost in accordance with Paragraph 54 of IAS 39.

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

19 INVESTMENT SECURITIES *(Continued)*

The investment securities are analysed by issuer as follows:

Group

	As at 31 December	
	2006	2005
Securities — loans and receivables		
— Central governments and central banks	**45,436**	26,527
— Public sector entities	**370**	464
— Banks and other financial institutions	**1,705**	1,381
— Corporate entities	**539**	—
	48,050	28,372
Securities — available-for-sale		
— Central governments and central banks	**144,405**	115,653
— Public sector entities	**2,119**	2,644
— Banks and other financial institutions	**178,495**	154,734
— Corporate entities	**14,804**	12,940
	339,823	285,971

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

19 INVESTMENT SECURITIES *(Continued)*

Bank

	As at 31 December 2006	2005
Securities — loans and receivables		
— Central governments and central banks	**45,436**	26,527
— Public sector entities	**370**	464
— Banks and other financial institutions	**1,705**	1,381
— Corporate entities	**539**	—
	48,050	28,372
Securities — available-for-sale		
— Central governments and central banks	**144,406**	115,653
— Public sector entities	**2,119**	2,644
— Banks and other financial institutions	**178,494**	154,734
— Corporate entities	**14,091**	12,627
	339,110	285,658

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

Group and Bank

	As at 31 December 2006	2005
Available-for-sale, at fair value		
— Unlisted	**1,329**	2,254

(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 year end to the contractual maturity dates is as follows:

Group and Bank

	As at 31 December	
	2006	2005
Up to 3 months	**—**	—
3 to 12 months	**1,066**	796
1 to 5 years	**263**	1,458
	1,329	2,254

20 PROPERTY AND EQUIPMENT

Group

	Land and Buildings	Construction in Progress	Equipment	Motor Vehicles	Leasehold Improvement	Total
Cost or valuation						
At 1 January 2006	**20,047**	**1,125**	**4,050**	**236**	**1,221**	**26,679**
Additions	**532**	**1,083**	**1,271**	**50**	**322**	**3,258**
Disposals	**(327)**	**(59)**	**(433)**	**(151)**	**(342)**	**(1,312)**
Transfers	**1,333**	**(1,333)**	**—**	**—**	**—**	**—**
Revaluation	**30**	**(29)**	**—**	**—**	**—**	**1**
At 31 December 2006	**21,615**	**787**	**4,888**	**135**	**1,201**	**28,626**
Accumulated depreciation						
At 1 January 2006	**—**	**—**	**(953)**	**(2)**	**(560)**	**(1,515)**
Charge for the period	**(826)**	**—**	**(1,349)**	**(67)**	**(259)**	**(2,501)**
Disposals	**9**	**—**	**413**	**145**	**290**	**857**
Revaluation	**817**	**—**	**—**	**—**	**—**	**817**
At 31 December 2006	**—**	**—**	**(1,889)**	**76**	**(529)**	**(2,342)**
Net book value						
At 31 December 2006	**21,615**	**787**	**2,999**	**211**	**672**	**26,284**
Carrying amount at 31 December 2006, if at cost	**12,946**	**685**	**2,823**	**191**	**672**	**17,317**

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

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

20 PROPERTY AND EQUIPMENT *(Continued)*

Bank

	Land and Buildings	Construction in Progress	Equipment	Motor Vehicles	Leasehold Improvement	Total
Cost or valuation						
At 1 January 2006	18,564	1,125	4,050	236	1,221	25,196
Additions	530	1,083	1,271	50	322	3,256
Disposals	(144)	(59)	(433)	(151)	(342)	(1,129)
Transfers	1,333	(1,333)	—	—	—	—
Revaluation	(28)	124	—	—	—	96
At 31 December 2006	20,255	940	4,888	135	1,201	27,419
Accumulated depreciation						
At 1 January 2006	—	—	(953)	(2)	(560)	(1,515)
Charge for the period	(826)	—	(1,349)	(67)	(259)	(2,501)
Disposals	13	—	413	145	290	861
Revaluation	813	—	—	—	—	813
At 31 December 2006	—	—	(1,889)	76	(529)	(2,342)
Net book value						
At 31 December 2006	20,255	940	2,999	211	672	25,077
Carrying amount at 31 December 2005, if at cost	12,181	685	2,823	191	672	16,552

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

20 PROPERTY AND EQUIPMENT *(Continued)*

Bank

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

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 2006 to revalue land and buildings, construction in progress, with reference to the open market value, 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 2006 to revalue lands and buildings, construction in progress, with reference to the open market value, 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 amounts expressed in millions of RMB unless otherwise stated.)

20 PROPERTY AND EQUIPMENT *(Continued)*

Group

	Year ended at 31 December 2006	2005
Revaluation surplus classified in equity, net of tax	**605**	541
Deferred tax liability *(Note 26)*	**244**	164
Revaluation deficit charged to profit and loss account *(Note 9)*	**(41)**	(9)
Exchange gain	**10**	19
	818	715

Bank

	As at 31 December 2006	2005
Revaluation surplus classified in equity, net of tax	**647**	339
Deferred tax liability *(Note 26)*	**294**	127
Revaluation deficit charged to profit and loss account	**(41)**	(56)
Exchange gain	**9**	19
	909	429

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

	As at 31 December 2006	2005
Net book value of land and buildings of Hong Kong Branch	**1,370**	1,370

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

21 OTHER ASSETS

Group

	As at 31 December	
	2006	2005
Settlement accounts	**264**	1,171
Other receivables	**4,681**	4,731
Less: impairment allowance	**(2,243)**	(2,167)
Foreclosed assets	**4,050**	5,483
Less: impairment allowance	**(2,906)**	(2,788)
Prepaid staff housing subsidies	**96**	214
Prepaid rental expenses	**314**	349
Land use rights	**592**	589
Intangible assets	**709**	296
Investment property	**145**	720
Others	**238**	1,968
	5,940	10,566

Bank

	As at 31 December	
	2006	2005
Settlement accounts	**264**	1,171
Other receivables	**3,962**	4,451
Less: impairment allowance	**(2,243)**	(2,167)
Foreclosed assets	**4,050**	5,483
Less: impairment allowance	**(2,906)**	(2,788)
Prepaid staff housing subsidies	**96**	214
Prepaid rental expenses	**314**	349
Land use rights	**592**	589
Intangible assets	**709**	296
Investment property	**143**	720
Others	**141**	1,946
	5,122	10,264

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

22 DUE TO OTHER BANKS AND FINANCIAL INSTITUTIONS

Group and Bank

	As at 31 December	
	2006	2005
Deposits from other banks and financial institutions	**127,831**	50,040
Loans from other banks and financial institutions	**40,835**	34,054
	168,666	84,094

23 FINANCIAL LIABILITIES HELD FOR TRADING

Group and Bank

	As at 31 December	
	2006	2005
Derivative financial instruments *(Note 17)*	**568**	301
Short position of securities held for trading	**2,228**	1,056
Debt securities in issue	**5,928**	8,198
	8,724	9,555

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

23 FINANCIAL LIABILITIES HELD FOR TRADING *(Continued)*

Debt securities in issue are:

	31 December 2006		31 December 2005	
	Amount	**Interest rate per annum (%)**	Amount	Interest rate per annum (%)
HKD short term Certificate of Deposit	**923**	**4.28%**	153	3.66%
HKD medium term Certificate of Deposit	**268**	**4.25%**	499	4.30%
USD short term Certificate of Deposit	**224**	**4.30%**	—	—
USD medium term Certificate of Deposit	**—**	**—**	199	4.04%
USD floating rate Certificate of deposit (maturing in November 2006)	**—**	**—**	1,577	LIBOR+0.08%
USD floating rate Certificate of Deposit (maturing in January 2007)	**1,154**	**3M LIBOR+0.20%**	1,186	3M LIBOR+0.20%
HKD floating rate Certificate of deposit (maturing in November 2008)	**909**	**HIBOR+0.18%**	936	HIBOR+0.18%
HKD fixed rate step-up rate Certificate of Deposit (maturing in May 2009)	**440**	**range from 3.10% to 4.60%**	453	range from 3.10% to 4.60%
HKD floating rate Certificate of Deposit (maturing in September 2008)	**404**	**HIBOR+0.26%**	417	HIBOR+0.26%
HKD fixed rate step-up rate Certificate of Deposit (maturing in November 2007)	**—**	**—**	245	range from 4.18% to 4.68%
USD floating rate Certificate of Deposit (maturing in June 2007)	**235**	**LIBOR+0.12%**	242	LIBOR+0.12%
HKD fixed rate step-up rate Certificate of Deposit (maturing in March 2006)	**—**	**—**	481	range from 1.95% to 2.70%
Others	**1,371**		1,810	
Total	**5,928**		8,198	

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

24 DUE TO CUSTOMERS

Group and Bank

	As at 31 December	
	2006	2005
Corporate current deposits	**457,839**	407,228
Corporate savings deposits	**5,878**	4,232
Corporate time deposits	**292,002**	231,275
Individual current deposits	**185,521**	162,757
Individual savings deposits	**14,182**	9,725
Individual time deposits	**288,896**	263,236
Pledged deposits	**115,650**	105,781
Certificates of deposit	**4,101**	696
Promissory notes	**3,250**	2,708
Customer margin deposits	**2,816**	1,642
Other deposits	**41,483**	23,544
Interest payable	**8,713**	8,015
	1,420,331	1,220,839
Including:		
Pledged deposits held as collateral for letters of credit	**5,066**	5,715

25 OTHER LIABILITIES

Group

	As at 31 December	
	2006	2005
Settlement accounts	**4,269**	4,509
Dividends payable	**2,020**	136
Staff benefits payables	**2,278**	1,692
Tax payable	**941**	816
Provision for outstanding litigation	**995**	938
Others	**5,648**	4,258
	16,151	12,349

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

25 OTHER LIABILITIES *(Continued)*

Bank

	As at 31 December	
	2006	2005
Settlement accounts	**4,269**	4,509
Dividends payable	**2,020**	136
Staff benefits payables	**2,278**	1,692
Tax payable	**931**	816
Provision for outstanding litigation	**995**	938
Others	**3,338**	2,414
	13,831	10,505

26 DEFERRED INCOME TAXES

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

Deferred income taxes are calculated on all temporary differences under the liability method using an effective tax rate of 17.5% for transactions in Hong Kong.

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

Group

	Year ended 31 December	
	2006	2005
Balance at beginning of the year	**542**	5,346
Credit/(debit) to profit and loss account	**2,003**	(2,673)
Available-for-sale securities		
— fair value remeasurement	**896**	(1,967)
Property revaluation	**(244)**	(164)
At end of the year	**3,197**	542

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

26 DEFERRED INCOME TAXES *(Continued)*

Bank

	Year ended 31 December	
	2006	2005
Balance at beginning of the year	**666**	5,453
Credit/(debit) to profit and loss account	**2,003**	(2,673)
Available-for-sale securities		
— fair value remeasurement	**918**	(1,967)
Property revaluation	**(294)**	(147)
At end of the year	**3,293**	666

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

Group

	As at 31 December	
	2006	2005
Deferred income tax liabilities		
Available-for-sale securities	**(380)**	(1,285)
Property revaluation reserve	**(1,738)**	(1,676)
Other temporary differences	**(271)**	(288)
	(2,389)	(3,249)
Deferred income tax assets		
Provision for loan losses	**2,229**	592
Impairment allowances for investments	**240**	392
Decelerated tax depreciation	**129**	128
Impairment of other assets	**2,987**	2,669
Available-for-sale securities	**1**	10
	5,586	3,791
Net deferred income tax assets	**3,197**	542

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

26 DEFERRED INCOME TAXES *(Continued)*

Bank

	As at 31 December	
	2006	2005
Deferred income tax liabilities		
Available-for-sale securities	**(358)**	(1,285)
Property revaluation reserve	**(1,654)**	(1,543)
Other temporary differences	**(271)**	(287)
	(2,283)	(3,115)
Deferred income tax assets		
Provision for loan losses	**2,229**	592
Impairment allowances for investments	**240**	392
Decelerated tax depreciation	**119**	118
Impairment of other assets	**2,987**	2,669
Available-for-sale securities	**1**	10
	5,576	3,781
Net deferred income tax assets	**3,293**	666

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

Group

	As at 31 December	
	2006	2005
Deferred tax assets	**3,520**	955
Deferred tax liabilities	**(323)**	(413)

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

26 DEFERRED INCOME TAXES *(Continued)*

Bank

	As at 31 December	
	2006	2005
Deferred tax assets	**3,520**	955
Deferred tax liabilities	**(227)**	(289)

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

Group

	As at 31 December	
	2006	2005
Provision for loan losses:		
Additional provisions for loan losses	**1,739**	198
Utilization	**(102)**	(33)
Sub-total	**1,637**	165
Impairment allowances for investments	**(152)**	(88)
Impairment of other assets	**318**	844
Utilization of tax loss carried forward	**—**	(3,631)
Accelerated depreciation	**—**	13
Decelerated depreciation	**1**	3
Depreciation/disposal of property and equipment	**183**	48
Other temporary differences	**16**	(27)
	2,003	(2,673)

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

27 RETIREMENT BENEFIT OBLIGATIONS

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

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

	Year ended 31 December	
	2006	2005
Expenses incurred for retirement benefit plans	**529**	431

28 SUBORDINATED TERM DEBT

Group and Bank

	As at 31 December	
	2006	2005
Floating rate subordinated debt — 2009	**12,000**	12,000
Interest payable	**292**	292
	12,292	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.

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

29 SHARE CAPITAL AND CAPITAL SURPLUS

Group

	Number of shares (in millions)	Ordinary shares of RMB1 each (RMB million)	Capital surplus (RMB million)	Total (RMB million)
At 31 December 2005/31 December 2006	45,804	45,804	21,540	67,344

Bank

	Number of shares (in millions)	Ordinary shares of RMB1 each (RMB million)	Capital surplus (RMB million)	Total (RMB million)
At 31 December 2005/31 December 2006	45,804	45,804	22,432	68,236

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

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

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

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

29 SHARE CAPITAL AND CAPITAL SURPLUS *(Continued)*

The shareholding structures of the Group and the Bank as at 31 December 2006 are as follow:

Group and Bank

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

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.

On 18 November 2005, the Board resolved to grant certain SARs under long term incentive plan. According to the resolution, the initial grant of SARs targeted at senior executives of the head office as at 23 June 2005. The exercise price of each SARs is HK$2.5, being the issue price of the H share at the time of its initial public offering. The amount of the initial grant of the SARs was 7.5 million shares. The SARs will be valid for a period of ten years from 23 June 2005, with a two-year vesting period.

On 3 November 2006, the Board resolved to grant certain SARs under long term incentive plan. According to the resolution, the grant of SARs targeted at senior executives of the head office as at 3 November 2006. The exercise price of each SARs is HK$6.13, being the closing price of the Group's H Share on the granting date. The amount of the grant of the SARs was 2.72 million shares. The SARs will be valid for a period of ten years from 3 November 2006, with a two-year vesting period.

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

29 SHARE CAPITAL AND CAPITAL SURPLUS *(Continued)*

Movements in the number of SARs outstanding are as follows

Group and Bank

	Year ended at 31 December	
	2006	2005
	Number of shares (In millions)	Number of shares (In millions)
Outstanding at beginning of the period	**8**	—
Granted	**3**	8
Outstanding at end of the period	**11**	8

The fair value of SARs using Binomial Option Pricing model at 31 December 2006 is RMB17 million (31 December 2005: RMB1 million).

30 RESERVES AND RETAINED EARNINGS

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

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. Such profit distribution is recognized in the balance sheet upon approval by the shareholders at the Annual General Meeting.

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, to the statutory general reserve through its profit appropriation. The statutory general reserve is an integral part of equity interest but not subject to dividend distribution. Such statutory general reserve is recognized in the balance sheet upon approval by the shareholders at the Annual General Meeting. Statutory reserve of Hongkong branch required by Hong Kong Monetary Authority ("HKMA") is also included in above statutory general reserve.

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

30 RESERVES AND RETAINED EARNINGS *(Continued)*

In accordance with the PRC legislation, after the statutory reserve has been transferred from the net distributable profit of the bank, discretionary reserve may be provided upon approval by the shareholders at the Annual General Meeting. Such discretionary reserve is recognized in the balance sheet upon approval by the shareholders at the Annual General Meeting.

On 8 March 2007, the Directors proposed the following profit appropriation, which is subject to the approval by shareholders at the Annual General Meeting:

	Year ended 31 December	
	2006	2005
Statutory reserve	**1,271**	899
Statutory general reserve	**6,208**	4,428
Discretionary reserve	**576**	—
	8,055	5,327

31 DIVIDENDS

	Year ended 31 December	
	2006	2005
Paid in the year	**1,665**	5

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 reserve of 10% of the net profit of the Bank as determined under PRC accounting regulations;

(iii) Allocations to statutory general reserve;

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

In accordance with the relevant regulations, the distributable profit is deemed to be the lesser of (i) the distributable profit determined in accordance with PRC GAAP and (ii) the distributable profit determined in accordance with IFRS.

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

31 DIVIDENDS *(Continued)*

The dividends are recognized in the balance sheet upon approval by the shareholders at the Annual General Meeting. At 31 December 2006, the aggregate amount of distributable profit was RMB12,635 million (2005: RMB8,991 million), being the distributable profit determined in accordance with IFRS (2005: PRC GAAP). On 8 March 2007, the directors proposed a cash dividend of RMB0.10 per share (2006: RMB0.08 per share), amounting to RMB4,580 million (2006: RMB3,664 million).

32 FINANCIAL GUARANTEES AND CREDIT RELATED COMMITMENTS, OTHER COMMITMENTS AND CONTINGENT LIBILITIES

Financial guarantees and credit related commitments

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

Group and Bank

	As at 31 December	
	2006	2005
Guarantees	**83,917**	49,623
Letters of credit	**28,375**	22,316
Acceptances	**166,094**	156,484
Other commitments with an original maturity of		
— Under 1 year	**24,694**	10,044
— 1 year and over	**10,953**	7,443
	314,033	245,910

Capital expenditure commitments

Group and Bank

	As at 31 December	
	2006	2005
Capital expenditure commitments for buildings	**335**	238

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

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

Operating lease commitments

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

Group and Bank

	As at 31 December	
	2006	2005
Not later than 1 year	**657**	555
Later than 1 year and not later than 5 years	**1,476**	1,320
Later than 5 years	**519**	466
	2,652	2,341

Commitments on security underwriting and bond acceptance

Group and Bank

	As at 31 December	
	2006	2005
Outstanding balance on security underwriting	**10,200**	—
Outstanding balance on bond acceptance *(Note 1)*	**24,523**	17,686

note 1: The Bank is entrusted by the Ministry of Finance ("MOF") to underwrite certain Certificates of Treasury Bond. The investors of Certificates of Treasury Bond have a right to redeem the bonds at par any time prior to maturity and the Bank is committed to redeem those bonds. The redemption price is the principal value of the Certificates of Treasury Bond plus unpaid interest.

The original maturities of these bonds vary from 1 to 5 years.

The MOF will not provide funding for the early redemption of these Certificates of Treasury Bond on a back-to-back basis but will pay interest through maturity and repay the principal at maturity.

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

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

Legal proceedings

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

Group and Bank

	As at 31 December	
	2006	2005
Outstanding claims	**2,058**	2,261
Provision for losses	**995**	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.

Group and Bank

	Pledged Assets As at 31 December		Related Liabilities As at 31 December	
	2006	2005	**2006**	2005
Balances with central banks	**104,083**	73,309	**—**	—
Investment securities	**3,548**	2,539	**2,346**	1,257
	107,631	75,848	**2,346**	1,257

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

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

Group and Bank

	As at 31 December	
	2006	2005
Financial guarantees and credit related commitments	**119,168**	179,746

The credit risk weighted amount refers to the amount as computed in accordance with the formula promulgated by the CBRC 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.

35 NOTES TO CONSOLIDATED CASH FLOW STATEMENT

(a) Analysis of changes in financing during the year

	Dividends	Share capital	Capital surplus	Subordinated term debt	Minority Interest
At 1 January 2006	**136**	**45,804**	**21,540**	**12,292**	**64**
Net cash outflow from financing/ other transferred out	**(1,780)**	**—**	**—**	**(636)**	**—**
Interest expense recognised on subordinated term debt	**—**	**—**	**—**	**636**	**—**
Net loss attributable to minority interest	**—**	**—**	**—**	**—**	**(5)**
Dividends	**3,664**	**—**	**—**	**—**	**—**
At 31 December 2006	**2,020**	**45,804**	**21,540**	**12,292**	**59**
At 1 January 2005	141	39,070	10,872	12,275	—
Net cash inflow/(outflow) from financing	(5)	6,734	10,668	(540)	70
Interest expense recognised on subordinated term debt	—	—	—	557	—
Net loss attributable to minority interest	—	—	—	—	(6)
At 31 December 2005	136	45,804	21,540	12,292	64

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

35 NOTES TO CONSOLIDATED CASH FLOW STATEMENT *(Continued)*

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

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

	As at 31 December	
	2006	2005
Cash and balances with central banks *(Note 14)*	**149,858**	67,000
Due from other banks and financial institutions *(Note 15)*	**35,865**	34,305
	185,723	101,305

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

36 PRINCIPAL SUBSIDIARIES

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

Name of subsidiaries	Place of incorporation and operation	Date of incorporation	Issued and fully paid up share capital	Bank equity interest %	Principal activities
Amiwell Company Limited	Hong Kong	30 Apr 1982	HKD2	100	Property holding and investment
Bank of Communications Trustee Limited	Hong Kong	13 Oct 1981	HKD50,000,000	100	Trustee Service
Bank of Communications (Nominee) Company Limited	Hong Kong	21 Aug 1981	HKD200,000	100	Investment holding
BCOM Finance (Hong Kong) Limited	Hong Kong	13 Mar 1979	HKD90,000,000	100	Deposit taking
BCOM Securities Company Limited	Hong Kong	3 Jun 1998	HKD175,000,000	100	Security dealing and brokerage
China Communications Insurance Company Limited	Hong Kong	1 Nov 2000	HKD250,000,000	100	General insurance and reinsurance
City Wisdom Limited	Hong Kong	19 Jul 2000	HKD10,000	100	Property holding
Eastern Sky Limited	Hong Kong	21 Aug 2000	HKD10,000	100	Property development
Expectation Investment Limited	Hong Kong	29 Jan 1997	HKD2	100	Investment holding
Kiu Fai Company Limited	Hong Kong	18 Mar 1967	HKD3,000,000	100	Property holding and investment holding
Right Master Investment Limited	Hong Kong	23 Dec 1998	HKD10,000	100	Property development
Star Wealthy Secretarial Company Limited	Hong Kong	23 Aug 1999	HKD2,000,000	100	Investment holding
Unique Profit Limited	Hong Kong	12 Jun 1998	HKD10,000	100	Property holding
Bank of Communications Charitable Foundation Limited	Hong Kong	19 Jun 2002	—	100	Charity fund
Creative Mart Limited	Hong Kong	12 May 1999	HKD100	100	Property development
Chiao Tung Developments Limited	Hong Kong	5 Feb 1985	HKD50,000,000	100	Investment holding
Career Computer (Shenzhen) Company Limited	PRC	22 Dec 1997	USD3,000,000	100	Development of computer software and hardware, electronic equipments and communication network
Bank of Communications Schroder Fund Management Co., Ltd.	PRC	4 Aug 2005	RMB200,000,000	65	Fund Management

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

36 PRINCIPAL SUBSIDIARIES *(Continued)*

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

All above principal subsidiaries are private companies.

For the year ended 31 December 2005 or 31 March 2006, all principal subsidiaries incorporated in Hong Kong as stated above were audited by KPMG. For the year ended 31 December 2006 or 31 March 2007, they are audited by PricewaterhouseCoopers Hong Kong CPAs 羅兵咸永道會計師事務所.

For the years ended 31 December 2005 and 2006, Career Computer (Shenzhen) Company Limited was audited by Shenzhen Peng Cheng CPAs Limited 深圳鵬城會計師事務所.

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

(b) Investment costs and balances with subsidiaries:

	Year ended 31 December	
	2006	2005
Investment cost — subsidiaries	**1,219**	922
Amount due from subsidiaries	**1,784**	1,207
Amount due to subsidiaries	**(1,659)**	(1,343)
Total	**1,344**	786

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

37 RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. The Group is subject to the control of the State Council of the PRC Government.

(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 year are as follows:

Treasury bonds

	Year ended 31 December	
	2006	2005
Purchase during the year	**54,840**	36,646
Redemption during the year	**(11,543)**	(22,091)
Interest income	**2,858**	2,267

	Year ended 31 December	
	2006	2005
Outstanding balance at beginning of the year	**79,368**	59,281
Outstanding at end of the year	**102,767**	79,368

(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.

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

37 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 year end, and the related expense and interest ranges for the year are as follows:

(i) *Loans and advances to customers*

	Year ended 31 December	
	2006	2005
Outstanding balance at beginning of the year	**207,715**	190,497
Outstanding balance at end of the year	**240,214**	207,715
Less: allowance for impairment losses	**(3,212)**	(2,313)
	237,002	205,402
Including: discounted bills	**8,439**	6,477
Interest rate range for discounted bills	**1.44%~5.74%**	3.24%~5.742%
Interest rate range of loans and advances other than discounted bills	**0.625%~18.72%**	0.57%~8.37%

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

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

37 RELATED PARTY TRANSACTIONS *(Continued)*

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

(i) *Loans and advances to customers (Continued)*

	Year ended 31 December	
	2006	2005
Maximum balance during the year	**240,214**	207,715
Provision for impairment during the year	**899**	442

(ii) *Investment securities*

	Year ended 31 December	
	2006	2005
Purchase during the year	**221,232**	206,665
Redemption during the year	**(40,549)**	(17,463)
Sales during the year	**(329,844)**	(180,824)
Interest income	**5,182**	3,132

	Year ended 31 December	
	2006	2005
Outstanding balance at beginning of the year	**137,424**	148,390
Outstanding balance at end of the year	**166,510**	137,424

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

37 RELATED PARTY TRANSACTIONS *(Continued)*

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

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

	Year ended 31 December	
	2006	2005
Outstanding balance at beginning of the year	**101,504**	39,140
Outstanding balance at end of the year	**31,502**	101,504
Less: allowance for impairment losses	**(616)**	(733)
	30,886	100,771

	Year ended 31 December	
	2006	2005
Maximum balance during the year	**70,768**	101,504
Provision for impairment reversed during the year	**(117)**	(149)

(iv) *Currency swap*

	Year ended 31 December	
	2006	2005
Notional amount	**8,679**	—
Fair value	**65**	—

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

37 RELATED PARTY TRANSACTIONS *(Continued)*

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

(v) *Due to other banks and financial institutions*

	Year ended 31 December	
	2006	2005
Outstanding balance at beginning of the year	**73,797**	20,894
Outstanding balance at end of the year	**89,864**	73,797

	Year ended 31 December	
	2006	2005
Maximum balance during the year	**163,245**	73,797

(vi) *Due to customers*

	Year ended 31 December	
	2006	2005
Outstanding balance at beginning of the year	**560,549**	112,197
Outstanding balance at end of the year	**273,099**	560,549

	Year ended 31 December	
	2006	2005
Maximum balance during the year	**560,549**	848,417

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

37 RELATED PARTY TRANSACTIONS *(Continued)*

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

(vii) *Financial guarantees and credit related commitments*

	As at 31 December	
	2006	2005
Guarantees	**29,609**	22,954
Letters of credit	**7,043**	6,111
Acceptances	**13,779**	19,673
Derivative transactions unsettled	**1,520**	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 the years ended 31 December 2005 and 2006, outstanding balances at the balance sheet date are as follows:

(i) *Loans*

	Year ended at 31 December	
	2006	2005
Outstanding at beginning of the year	**10**	9
Granted during the year	**26**	16
Repaid during the year	**(19)**	(15)
Outstanding at end of the year	**17**	10

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

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

37 RELATED PARTY TRANSACTIONS *(Continued)*

(c) Transactions with directors and senior management *(Continued)*

(ii) *Deposits*

	Year ended at 31 December 2006	2005
Outstanding at beginning of the year	**34**	29
Deposited during the year	**89**	129
Repaid during the year	**(90)**	(124)
Outstanding at end of the year	**33**	34

(d) Transactions with HSBC

As at 31 December 2006, the Hong Kong and Shanghai Banking Corporation Limited ("HSBC") holds 9,115 million shares of the bank which represents 19.9%. Transactions between the Group and HSBC are mainly banking activities under commercial terms and at market rates. Detail transaction volumes since the above share acquisition are set out below:

(i) *Placement with HSBC*

	Year ended 31 December 2006	2005
Outstanding at beginning of the year	**4,654**	100
Granted during the year	**363,308**	231,869
Repaid during the year	**(366,528)**	(227,315)
Outstanding at end of the year	**1,434**	4,654
Interest income	**34**	16

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

37 RELATED PARTY TRANSACTIONS *(Continued)*

(d) Transactions with HSBC *(Continued)*

(ii) *Deposits from HSBC*

	Year ended 31 December	
	2006	2005
Outstanding at beginning of the year	**2,318**	1,218
Deposited during the year	**124,264**	60,778
Repaid during the year	**(126,093)**	(59,678)
Outstanding at end of the year	**489**	2,318
Interest expense on deposits	**64**	36

(iii) *Investment securities*

	Year ended 31 December	
	2006	2005
Interest income	**28**	22

	As at 31 December	
	2006	2005
Outstanding balance	**1,395**	568

(iv) *Financial guarantees and credit related commitments*

	As at 31 December	
	2006	2005
Guarantees	**5**	7
Letters of credit	**218**	347
Derivative transactions unsettled	**5,739**	28,768

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

38 SEGMENTAL INFORMATION

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

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

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

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

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

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

(vi) Overseas — Including overseas subsidiaries and the branches in the following cities: Hong Kong, New York, Singapore, Seoul and Tokyo.

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

38 SEGMENTAL INFORMATION *(Continued)*

(a) Geographical segment information

	Northern China	North-eastern China	Eastern China	Central & Southern China	Western China	Overseas	Eliminations & Consolidated	Group Total
As at 31 December 2006								
Assets								
Cash and balances with central banks	51,808	3,910	180,153	11,046	6,007	1,017	—	253,941
Due from other banks and financial institutions	21,239	497	72,037	5,508	472	22,971	(4,101)	118,623
Financial assets held for trading	—	—	8,599	—	—	4,396	—	12,995
Loans and advances to customers	162,029	55,830	376,947	179,744	79,490	53,667	2,600	910,307
Investment securities								
— loans and receivables	2,564	1,514	38,788	3,384	1,800	—	—	48,050
— available-for-sale	31,462	17,042	228,981	27,449	10,221	24,668	—	339,823
Other assets	11,229	8,241	29,155	13,129	7,227	7,646	(40,883)	35,744
Segment assets	280,331	87,034	934,660	240,260	105,217	114,365	(42,384)	1,719,483
Liabilities								
Due to other banks and financial institutions	(70,829)	(1,277)	(76,127)	(12,608)	(2,150)	(5,675)	—	(168,666)
Financial liabilities held for trading	—	—	(419)	—	—	(8,305)	—	(8,724)
Due to customers	(257,469)	(129,916)	(533,531)	(291,467)	(137,982)	(69,647)	(319)	(1,420,331)
Other liabilities	(3,408)	(1,103)	(37,046)	(3,520)	(1,521)	(27,372)	42,703	(31,267)
Segment liabilities	(331,706)	(132,296)	(647,123)	(307,595)	(141,653)	(110,999)	42,384	(1,628,988)
Net on balance sheet position	(51,375)	(45,262)	287,537	(67,335)	(36,436)	3,366	—	90,495
Acquisition cost of property and equipment ("PPE") and intangible assets	491	283	1,970	647	325	92	2	3,810

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

38 SEGMENTAL INFORMATION *(Continued)*

(a) Geographical segment information *(Continued)*

	Northern China	North-eastern China	Eastern China	Central & Southern China	Western China	Overseas	Eliminations & Consolidated	Group Total
For the year ended 31 December 2006								
Interest income	10,545	4,574	36,034	11,870	5,253	5,602	(9,335)	64,543
Interest expense	(4,620)	(1,829)	(17,813)	(4,209)	(1,707)	(3,897)	9,335	(24,740)
Net interest income	5,925	2,745	18,221	7,661	3,546	1,705	—	39,803
Fee and commission income	387	233	1,355	578	261	662	—	3,476
Fee and commission expense	(79)	(39)	(169)	(98)	(45)	(173)	—	(603)
Net fee and commission income	308	194	1,186	480	216	489	—	2,873
Dividend income	2	—	75	9	—	37	—	123
Gains less losses arising from trading activities	276	63	(378)	158	31	(207)	—	(57)
Gains less losses arising from investment securities	41	—	6	—	—	11	—	58
Other operating income	132	37	554	136	43	136	—	1,038
(Reversal)/Impairment losses on loans and advances	(963)	(1,167)	(2,598)	(489)	(431)	110	—	(5,538)
Other operating expenses	(2,485)	(2,372)	(8,973)	(4,128)	(1,844)	(1,093)	—	(20,895)
Operating profit/(loss) before tax	3,236	(500)	8,093	3,827	1,561	1,188	—	17,405
Income tax	(1,348)	(270)	(1,057)	(1,466)	(604)	(391)	—	(5,136)
Net profit/(loss) for the year	1,888	(770)	7,036	2,361	957	797	—	12,269
Depreciation and amortization of property and equipment and intangible assets	(256)	(287)	(1,302)	(422)	(261)	(112)	—	(2,640)

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

38 SEGMENTAL INFORMATION *(Continued)*

(a) Geographical segment information *(Continued)*

	Northern China	North-eastern China	Eastern China	Central & Southern China	Western China	Overseas	Eliminations & Consolidated	Group Total
As at 31 December 2005								
Assets								
Cash and balances with central banks	11,289	4,361	108,266	10,427	5,360	606	—	140,309
Due from other banks and financial institutions	25,492	2,091	113,979	10,733	3,160	15,230	(584)	170,101
Financial assets held for trading	—	—	112	—	—	3,116	—	3,228
Loans and advances to customers	128,284	52,192	318,138	145,998	68,932	42,569	2,660	758,773
Investment securities								
— 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
Segment assets	210,270	81,977	769,196	205,936	94,266	96,971	(35,177)	1,423,439
Liabilities								
Due to other banks and financial institutions	(32,262)	(4,297)	(34,104)	(7,192)	(2,368)	(3,912)	41	(84,094)
Financial liabilities held for trading	—	—	(141)	—	—	(9,414)	—	(9,555)
Due to customers	(217,460)	(115,118)	(462,960)	(245,324)	(119,951)	(63,408)	3,382	(1,220,839)
Other liabilities	(4,909)	(2,759)	(22,485)	(6,827)	(3,197)	(17,382)	31,754	(25,805)
Segment liabilities	(254,631)	(122,174)	(519,690)	(259,343)	(125,516)	(94,116)	35,177	(1,340,293)
Net on balance sheet position	(44,361)	(40,197)	249,506	(53,407)	(31,250)	2,855	—	83,146
Acquisition cost of property and equipment ("PPE") and intangible assets	461	348	1,794	474	440	118	—	3,635

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

38 SEGMENTAL INFORMATION *(Continued)*

(a) Geographical segment information *(Continued)*

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

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

38 SEGMENTAL INFORMATION *(Continued)*

(b) Business segment information

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

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

	Corporate	Retail	Treasury	Others	Total
As at 31 December 2006					
Total carrying amount of segment assets	**736,304**	**133,685**	**815,778**	**33,716**	**1,719,483**
Segment revenue	**41,254**	**8,548**	**18,512**	**867**	**69,181**
Depreciation and amortization of PPE and intangible assets	**—**	**—**	**—**	**2,640**	**2,640**
Acquisition cost of PPE and intangible assets	**—**	**—**	**—**	**3,810**	**3,810**
As at 31 December 2005					
Total carrying amount of segment assets	612,441	112,593	663,733	34,672	1,423,439
Segment revenue	33,248	6,282	13,323	824	53,677
Depreciation and amortization of PPE and intangible assets	—	—	—	2,474	2,474
Acquisition cost of PPE and intangible assets	—	—	—	3,635	3,635

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

39 EVENTS AFTER THE BALANCE SHEET DATE

On 9 January 2007, the shareholders of the Group approved to issue no more than 4.5 billion Renminbi ordinary shares ('A shares') and to apply for a listing on Shanghai Stock Exchange. Such transaction is awaiting China Securities Regulatory Commission, CBRC and other regulators' approval.

On 9 January 2007, the shareholders of the Group also approved to issue subordinated loans amounting to RMB25 billion in inter-bank bond market of the PRC in March 2007. Such transaction has been approved by CBRC and PBOC.