Consolidated Income Statement

For the year ended 31 December 2006 (Amount in millions of Renminbi, unless otherwise stated)

	Note	2006	2005
Interest income	V.2	**215,334**	167,948
Interest expense	V.2	**(93,963)**	(66,940)
Net interest income		**121,371**	101,008
Fee and commission income	V.3	**17,139**	12,698
Fee and commission expense	V.3	**(2,816)**	(3,451)
Net fee and commission income		**14,323**	9,247
Net trading (losses)/gains	V.4	**(1,544)**	4,283
Net gains/(losses) on investment securities	V.5	**1,132**	(582)
Other operating income	V.6	**13,096**	11,150
Impairment losses on loans and advances	V.17	**(12,342)**	(11,486)
Operating expenses and others	V.7	**(68,731)**	(59,984)
Operating profit		**67,305**	53,636
Share of results of associates and joint ventures	V.21	**632**	175
Profit before income tax		**67,937**	53,811
Income tax expense	V.10	**(19,673)**	(22,253)
Profit for the year		**48,264**	31,558
Attributable to:			
Equity holders of the Bank		**42,830**	25,921
Minority interest		**5,434**	5,637
		48,264	31,558
Earnings per share for profit attributable to the equity holders of the Bank during the year (Expressed in Renminbi per ordinary share) — Basic and diluted	V.11	**0.18**	0.14
Dividends	V.36		
Dividends declared and paid during the year		**—**	12,737
Dividends proposed after the balance sheet date		**10,154**	1,375
		10,154	14,112

The accompanying notes form an integral part of these financial statements.

Consolidated Balance Sheet

As at 31 December 2006 (Amount in millions of Renminbi, unless otherwise stated)

	Note	As at 31 December	
		2006	2005
ASSETS			
Cash and due from banks	V.12	**39,812**	41,082
Balances with central banks	V.13	**379,631**	316,941
Placements with banks and other financial institutions	V.14	**399,138**	332,099
Government certificates of indebtedness for bank notes issued	V.26	**36,626**	35,586
Precious metals		**42,083**	26,974
Trading assets and other financial instruments at fair value through profit or loss	V.15	**115,828**	111,782
Derivative financial instruments	V.16	**24,837**	16,808
Loans and advances to customers, net	V.17	**2,337,726**	2,152,112
Investment securities	V.18		
— available-for-sale		**815,178**	602,221
— held-to-maturity		**461,140**	607,459
— loans and receivables		**500,336**	361,851
Investment in associates and joint ventures	V.21	**5,931**	5,061
Property and equipment	V.22	**86,200**	62,417
Investment property	V.23	**8,221**	8,511
Deferred income tax assets	V.33	**21,396**	20,504
Other assets	V.24	**53,570**	38,640
Total assets		**5,327,653**	4,740,048

	Note	As at 31 December	
		2006	2005
LIABILITIES			
Due to banks and other financial institutions		**178,777**	134,217
Due to central banks	V.25	**42,374**	30,055
Bank notes in circulation	V.26	**36,823**	35,731
Certificates of deposit and placements from banks and other financial institutions		**146,908**	212,626
Derivative financial instruments and liabilities at fair value through profit or loss	V.27	**113,048**	91,174
Due to customers	V.28	**4,091,118**	3,699,464
Bonds issued	V.29	**60,173**	60,179
Other borrowings	V.30	**63,398**	52,164
Current tax liabilities		**18,149**	23,459
Retirement benefit obligations	V.31	**7,444**	7,052
Deferred income tax liabilities	V.33	**3,029**	2,136
Other liabilities	V.34	**153,456**	136,272
Total liabilities		**4,914,697**	4,484,529
EQUITY			
Capital and reserves attributable to equity holders of the Bank			
Share capital	V.35	**253,839**	209,427
Capital reserve	V.35	**66,617**	(5,954)
Statutory reserves	V.36	**10,380**	5,987
General and regulatory reserves	V.36	**13,934**	5,109
Undistributed profits	V.36	**38,425**	10,188
Reserve for fair value changes of available-for-sale securities	V.37	**2,009**	1,899
Currency translation differences		**(2,071)**	(237)
Treasury shares	V.35	**(216)**	—
		382,917	226,419
Minority interest		**30,039**	29,100
Total equity		**412,956**	255,519
Total equity and liabilities		**5,327,653**	4,740,048

Approved and authorized for issue by the Board of Directors on 22 March 2007.

Xiao Gang
Director

Li Lihui
Director

The accompanying notes form an integral part of these financial statements.

Balance Sheet

As at 31 December 2006 (Amount in millions of Renminbi, unless otherwise stated)

	Note	As at 31 December 2006	As at 31 December 2005
ASSETS			
Cash and due from banks	V.12	**37,842**	38,275
Balances with central banks	V.13	**354,881**	284,373
Placements with banks and other financial institutions	V.14	**303,002**	243,654
Government certificates of indebtedness for bank notes issued	V.26	**1,713**	1,641
Precious metals		**40,542**	25,238
Trading assets and other financial instruments at fair value through profit or loss	V.15	**76,581**	82,082
Derivative financial instruments	V.16	**16,363**	11,329
Loans and advances to customers, net	V.17	**1,971,865**	1,788,742
Investment securities	V.18		
— available-for-sale		**706,739**	542,142
— held-to-maturity		**287,398**	415,143
— loans and receivables		**458,606**	343,910
Investment in subsidiaries	V.20	**45,451**	45,080
Investment in associates and joint ventures	V.21	**21**	45
Property and equipment	V.22	**49,473**	48,061
Investment property	V.23	**620**	461
Deferred income tax assets	V.33	**21,843**	20,389
Other assets	V.24	**30,272**	25,837
Total assets		**4,403,212**	3,916,402

The accompanying notes form an integral part of these financial statements.

	Note	As at 31 December	
		2006	2005
LIABILITIES			
Due to banks and other financial institutions		**164,376**	124,948
Due to central banks	V.25	**42,349**	30,030
Bank notes in circulation	V.26	**1,909**	1,786
Certificates of deposits and placements from banks and other financial institutions		**146,596**	215,923
Derivative financial instruments and liabilities at fair value through profit or loss	V.27	**91,084**	76,323
Due to customers	V.28	**3,358,565**	3,009,187
Bonds issued	V.29	**60,173**	60,179
Other borrowings	V.30	**46,006**	52,164
Current tax liabilities		**16,757**	22,440
Retirement benefit obligations	V.31	**7,444**	7,052
Deferred income tax liabilities	V.33	**32**	23
Other liabilities	V.34	**112,527**	112,534
Total liabilities		**4,047,818**	3,712,589
EQUITY			
Capital and reserves attributable to equity holders of the Bank			
Share capital	V.35	**253,839**	209,427
Capital reserve	V.35	**66,166**	(6,054)
Statutory reserves	V.36	**9,714**	5,465
General and regulatory reserves	V.36	**11,393**	2,618
Undistributed profits/(accumulated losses)	V.36	**14,385**	(8,709)
Reserve for fair value changes of available-for-sale securities	V.37	**(1,038)**	280
Currency translation differences		**935**	786
Total equity		**355,394**	203,813
Total equity and liabilities		**4,403,212**	3,916,402

Approved and authorized for issue by the Board of Directors on 22 March 2007.

Xiao Gang
Director

Li Lihui
Director

The accompanying notes form an integral part of these financial statements.

Consolidated Statement of Changes in Equity

For the year ended 31 December 2006 (Amount in millions of Renminbi, unless otherwise stated)

		Attributable to equity holders of the Bank									
	Note	Share capital	Capital reserve	Statutory reserves	General and regulatory reserves	Undistributed profits	Reserve for fair value changes of available-for-sale securities	Currency translation differences	Treasury shares	Minority interest	Total
At 1 January 2006		209,427	(5,954)	5,987	5,109	10,188	1,899	(237)	—	29,100	255,519
Issue of ordinary shares	V.35	44,412	72,567	—	—	—	—	—	—	—	116,979
Net profit		—	—	—	—	42,830	—	—	—	5,434	48,264
Appropriation to statutory reserves	V.36	—	—	4,393	—	(4,393)	—	—	—	—	—
Appropriation to general reserve and regulatory reserve	V.36	—	—	—	8,828	(8,828)	—	—	—	—	—
Net change in fair value of available-for-sale securities, net of tax	V.37	—	—	—	—	—	110	—	—	33	143
Exercise of subsidiary share options	V.32	—	—	—	—	—	—	—	—	33	33
Purchase of treasury shares	V.35	—	—	—	—	—	—	—	(216)	—	(216)
Dividends	V.36	—	—	—	—	(1,375)	—	—	—	(3,391)	(4,766)
Currency translation differences		—	—	—	—	—	—	(1,834)	—	(1,087)	(2,921)
Others		—	4	—	(3)	3	—	—	—	(83)	(79)
At 31 December 2006		253,839	66,617	10,380	13,934	38,425	2,009	(2,071)	(216)	30,039	412,956

The accompanying notes form an integral part of these financial statements.

For the year ended 31 December 2005 (Amount in millions of Renminbi, unless otherwise stated)

		Attributable to equity holders of the Bank									
	Note	Share capital	Capital reserve	Statutory reserves	General and regulatory reserves	Undistributed profits	Reserve for fair value changes of available-for-sale securities	Currency translation differences	Treasury shares	Minority interest	Total
At 1 January 2005		186,390	(10,432)	3,140	419	16,547	2,730	1,961	—	27,152	227,907
Issue of ordinary shares	V.35	23,037	3,964	—	—	—	—	—	—	—	27,001
Net profit		—	—	—	—	25,921	—	—	—	5,637	31,558
Appropriation to Statutory reserves	V.36	—	—	2,847	—	(2,847)	—	—	—	—	—
Appropriation to general reserve and regulatory reserve	V.36	—	—	—	4,690	(4,690)	—	—	—	—	—
Net change in fair value of available-for-sale securities, net of tax	V.37	—	—	—	—	—	1,423	—	—	(110)	1,313
Exercise of subsidiary share options	V.32	—	—	—	—	—	—	—	—	17	17
Capital contribution from Huijin	V.35	—	500	—	—	—	—	—	—	—	500
Adoption of equity accounting for investment in associates	V.21; V.36	—	—	—	—	2,194	(2,254)	—	—	—	(60)
Dividends	V.36	—	—	—	—	(26,937)	—	—	—	(2,954)	(29,891)
Currency translation differences		—	—	—	—	—	—	(2,198)	—	(642)	(2,840)
Others		—	14	—	—	—	—	—	—	—	14
At 31 December 2005		209,427	(5,954)	5,987	5,109	10,188	1,899	(237)	—	29,100	255,519

The accompanying notes form an integral part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December 2006 (Amount in millions of Renminbi, unless otherwise stated)

	Note	2006	2005
Cash flows from operating activities			
Profit before income tax		**67,937**	53,811
Adjustments:			
Impairment losses on loans and advances		**12,342**	11,486
Reversal of impairment losses on other assets		**(125)**	(457)
Depreciation of property and equipment		**5,209**	5,186
Amortization of intangible assets and other assets		**817**	1,128
Net gains on disposal of property and equipment and other assets		**(569)**	(665)
Net gains on disposal of investments in subsidiaries, associates and joint ventures		**(789)**	(320)
Share of results of associates and joint ventures		**(632)**	(175)
Interest expense arising from bonds issued		**2,840**	2,611
Net changes in operating assets and liabilities:			
Net increase in balances with central banks		**(69,063)**	(41,130)
Net decrease in due from banks and placements with banks and other financial institutions		**5,266**	56,168
Net increase in loans and advances to customers		**(197,956)**	(90,679)
Net increase in investment securities		**(151,786)**	(375,150)
Net (increase)/decrease in other assets		**(13,878)**	1,139
Net increase in due to banks and other financial institutions		**44,560**	22,429
Net increase/(decrease) in due to central banks		**12,319**	(36,683)
Net (decrease)/increase in certificates of deposits and placements from banks and other financial institutions		**(65,718)**	71,539
Net increase in due to customers		**391,654**	361,016
Net increase/(decrease) in other liabilities		**14,514**	(10,274)
Net cash from operating activities		**56,942**	30,980
Income tax paid		**(25,536)**	(17,249)
Net cash inflow from operating activities		**31,406**	13,731

The accompanying notes form an integral part of these financial statements.

	Note	2006	2005
Cash flows from investing activities			
Acquisition of a subsidiary, net of cash acquired	V.42	**(5,373)**	—
Payment for increase of investments in subsidiaries, associates and joint ventures		**(185)**	(3,187)
Proceeds from disposal of investments in subsidiaries, associates and joint ventures		**1,120**	2,264
Proceeds from disposal of property and equipment, intangible assets and other assets		**1,732**	4,291
Dividends received		**320**	310
Purchase of property and equipment, intangible assets and other assets		**(7,425)**	(5,951)
Net cash outflow from investing activities		**(9,811)**	(2,273)
Net cash inflow before financing activities		**21,595**	11,458
Cash flows from financing activities			
Proceeds from issuance of ordinary shares		**117,423**	27,001
Cash received from issuance of subordinated bonds		**—**	33,930
Proceeds from minority equity holders of a subsidiary upon exercise of subsidiary share options		**33**	17
Proceeds from minority equity holders of subsidiaries		**55**	—
Payment of interest on bonds issued		**(2,774)**	(1,485)
Dividend paid to equity holders of the Bank		**(1,375)**	(26,937)
Dividend paid to minority interest		**(3,391)**	(2,954)
Purchases of treasury shares		**(216)**	—
Payment of share issuance costs		**(413)**	—
Net cash inflow from financing activities		**109,342**	29,572
Effect of exchange rate changes on cash and cash equivalents		**(8,105)**	(10,060)
Net increase in cash and cash equivalents		**122,832**	30,970
Cash and cash equivalents as at 1 January	V.39	**397,112**	366,142
Cash and cash equivalents as at 31 December	V.39	**519,944**	397,112

The accompanying notes form an integral part of these financial statements.

Notes to the Financial Statements

For the year ended 31 December 2006 (Amount in millions of Renminbi, unless otherwise stated)

I GENERAL INFORMATION AND PRINCIPAL ACTIVITIES

The Bank, formerly known as Bank of China, was founded on 5 February 1912. From its formation until 1949, the Bank performed various functions of a central bank, foreign exchange bank and commercial bank specializing in trade finance. Following the founding of the People's Republic of China (the "PRC") in 1949, the Bank was designated as a specialized foreign exchange bank. Since 1994, the Bank has evolved into a state-owned commercial bank. In accordance with the Master Implementation Plan for the Joint Stock Reform ("Joint Stock Reform Plan") approved by the State Council of the PRC, the Bank was converted into a joint stock commercial bank on 26 August 2004 and its name was changed from Bank of China to Bank of China Limited.

The PRC Government, through Central SAFE Investments Limited ("Huijin"), owned 83.15% of the ordinary shares of the Bank as of 31 December 2005 with the remaining shares owned by strategic investors. During 2006, the Bank issued 8,514,415,652 ordinary shares to the National Council for Social Security Fund ("NCSSF") and 35,897,384,000 ordinary shares through offerings related to listings on the Stock Exchange of Hong Kong Limited ("Hong Kong Stock Exchange") and the Shanghai Stock Exchange. Huijin owned 67.49% of the Bank's outstanding ordinary shares as at 31 December 2006. The Bank remains a state-controlled joint stock commercial bank. See Note V 35.

The Bank is licensed as a financial institution by the China Banking Regulatory Commission (the "CBRC") [No. B10311000H0001] and is registered as a business enterprise with the State Administration of Industry and Commerce of the PRC [No. 1000001000134].

The Group provides a full range of corporate banking, personal banking, treasury operations, investment banking, insurance and related financial services to its customers in the PRC, Hong Kong Special Administrative Region of the PRC ("Hong Kong"), Macau Special Administrative Region of the PRC ("Macau") and other major international financial centers.

The Head Office of the Bank and its branches operating in the PRC are referred to as Domestic Operations. Branches and subsidiaries domiciled outside the PRC, including those located in Hong Kong and Macau, are referred to as Overseas Operations.

The Bank's principal regulator is the CBRC. The Overseas Operations of the Group are subject to the supervision of local regulators.

These financial statements have been approved by the Board of Directors on 22 March 2007.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES

1 Basis of presentation

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

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and have been prepared under the historical cost convention as modified by the revaluation of available-for-sale investment securities, investment property, financial assets and financial liabilities at fair value through profit or loss and derivative financial instruments.

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note IV.

(1) *Amendments and interpretations to published standards effective in 2006 and relevant to the Group's operations*

- IAS 19 (Amendment), Employee Benefits, was effective for accounting periods beginning on or after 1 January 2006. It introduces the option of an alternative recognition approach for actuarial gains and losses. It imposes additional recognition requirements for multi-employer plans where insufficient information is available to apply defined benefit accounting. It also adds new disclosure requirements. The Group does not intend to adopt this option and the effect of this amendment is limited to the format and extent of disclosures presented in the financial statements.

- IAS 21 (Amendment), Net Investment in a Foreign Operation, requires that exchange differences on monetary items forming a part of the net investment in a foreign operation should be reclassified as equity, whether or not the monetary item is denominated in the functional currency of either the reporting entity or the foreign operation. An additional example is included to clarify that sister-company loans can form part of a group's net investment in a foreign operation. This amendment was effective for annual periods beginning on or after 1 January 2006, and had no material effect on the Group's results of operations or financial position.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

1 Basis of presentation (Continued)

(1) *Amendments and interpretations to published standards effective in 2006 and relevant to the Group's operations (Continued)*

- IAS 39 (Amendment), The Fair Value Option, was effective for accounting periods beginning on or after 1 January 2006. This amendment restricts the circumstances under which the fair value option in IAS 39 can be used, as compared to the previously existing provisions of IAS 39. The adoption of this amendment to IAS 39 does not have a material effect on the Group's results of operations or financial position. The Group's use of the fair value option in the past had complied with the more restrictive provisions of the amendment to IAS 39.

- IAS 39 and IFRS 4 (Amendments), Financial Guarantee Contracts, are effective for accounting periods beginning on or after 1 January 2006. These amendments require any new or existing financial guarantee contracts that were previously not accounted for under IFRS 4 to be accounted for under IAS 39. The adoption of these amendments did not have a material impact on the Group's results of operations or financial position. No material amounts of financial guarantees were accounted for under IFRS 4.

(2) *Standards, amendments and interpretations that are not yet effective and have not been adopted early by the Group*

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

- IFRS 7, Financial Instruments: Disclosures and IAS 1, Presentation of Financial Statements — Capital Disclosures (Amendment), are effective for annual periods beginning on or after 1 January 2007. IFRS 7 introduces certain new disclosures relating to financial instruments while incorporating many of the requirements presently in IAS 32. IFRS 7 will supersede IAS 30 Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and the disclosure requirements of IAS 32 Financial Instruments: Disclosure and Presentation. The Group has assessed the impact of IFRS 7 and the amendment to IAS 1 and concluded that the key impact will be more qualitative and quantitative disclosures primarily related to fair value measurement and risk management. The adoption of this standard will have no effect on the Group's results of operations or financial position. The Group will apply IFRS 7 and the amendment to IAS 1 from annual periods beginning 1 January 2007.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

1 Basis of presentation (Continued)

(2) *Standards, amendments and interpretations that are not yet effective and have not been adopted early by the Group (Continued)*

- IFRS 8, Operating Segments is effective for annual periods beginning on or after 1 January 2009. IFRS 8 supersedes IAS 14, Segment Reporting, under which segments were identified and reported on the basis of a risk and return analysis. Items were reported on the basis of the accounting policies used for external reporting. Under IFRS 8, segments are components of an entity regularly reviewed by an entity's chief operating decision-maker. Items are reported based on internal reporting. This interpretation is not expected to have a material effect on the Group's operating results or financial position.

(3) *Standards, amendments and interpretations that are not yet effective and have not been early adopted by the Group*

- IFRIC 8, Scope of IFRS 2 is effective for annual periods beginning on or after 1 May 2006. IFRIC 8 requires consideration of transactions involving the issuance of equity instruments — where the identifiable consideration received is less than the fair value of the equity instruments issued — to establish whether or not they fall within the scope of IFRS 2. This interpretation is not expected to have a material effect on the Group's operating results or financial position.

- IFRIC 9, Reassessment of Embedded Derivatives is effective for annual periods beginning on or after 1 June 2006 and requires an entity to assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required. This interpretation is not expected to have a material effect on the Group's operating results or financial position.

- IFRIC 10, Interim Financial Reporting and Impairment is effective for annual periods beginning on or after 1 November 2006 and prohibits the impairment losses recognized in an interim period on goodwill, investments in equity instruments and investments in financial assets carried at cost to be reversed at a subsequent balance sheet date. This interpretation is not expected to have a material effect on the Group's operating results or financial position.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

1 Basis of presentation (Continued)

(3) *Standards, amendments and interpretations that are not yet effective and have not been early adopted by the Group (Continued)*

- IFRIC 11, IFRS 2 — Group and Treasury Share Transactions is effective for annual periods beginning on of after 1 March 2007 and clarifies the accounting by a subsidiary when its employees receive shares of its parent as equity-settled or cash-settled transactions. It also addresses the accounting for share-based payment transactions involving two or more entities within one group. This interpretation is not expected to have a material effect on the Group's operating results or financial position.

2 Group accounts

(1) *Consolidation*

(a) *Subsidiaries*

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets (including intangible assets) acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized directly in the income statement.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

2 Group accounts (Continued)

(1) *Consolidation (Continued)*

(a) *Subsidiaries (Continued)*

Inter-company transactions, balances and unrealized gains on transactions between group companies are eliminated; unrealized losses are also eliminated unless the transaction provides evidence of impairment of the assets transferred. Where necessary, accounting policies of subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

In the Bank's balance sheets, investment in subsidiaries is stated at cost less allowance for impairment losses. The results of subsidiaries are accounted for by the Bank on the basis of dividends received or receivable.

(b) *Transactions with minority interests*

The Group applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Disposal to minority interests results in gains and losses to the Group that is recorded in the income statement. Purchases from minority interests result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

(c) *Associates and joint ventures*

Associates are entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

Joint ventures exist where the Group has a contractual arrangement with one or more parties to undertake economic activities which are subject to joint control. These economic activities typically, though not necessarily, are undertaken through separately established entities.

Investments in associates and joint ventures are accounted for using the equity method of accounting and are initially recognized at cost. The Group's investment in associates and joint ventures includes goodwill, net of accumulated impairment loss.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

2 Group accounts (Continued)

(1) *Consolidation (Continued)*

(c) *Associates and joint ventures (Continued)*

The Group's share of the post-acquisition profits or losses of associates and joint ventures is recognized in the income statement, and its share of post-acquisition movements in reserves is recognized in reserves. The cumulative post-acquisition movements are adjusted against the cost of the investment. When the Group's share of losses in an associate or joint venture equals or exceeds its interest in the associate or joint venture, the Group does not recognize further losses unless the Group has incurred obligations or made payments on behalf of the associate or joint venture.

Unrealized gains on transactions between the Group and its associates and joint ventures are eliminated to the extent of the Group's interest in the associates or joint ventures; unrealized losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred.

In the Bank's balance sheets, the investments in associated companies and joint ventures are stated at cost less allowance for impairment losses. The results of associated companies and joint ventures are accounted for by the Bank on the basis of dividends received or receivable.

(2) *Segment reporting*

A business segment is a group of assets and operations engaged in providing products and services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products and services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

3 Derivative financial instruments

Derivatives are initially recognized at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and through the use of valuation techniques, including discounted cash flow models and option pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

3 Derivative financial instruments (Continued)

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 recognizes profits on day one.

Certain derivatives embedded in other financial instruments, such as the conversion option in a convertible bond, are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried as at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognized in the income statement unless the Group chooses to designate the hybrid contracts at fair value through profit or loss.

While certain derivative transactions are intended to provide effective economic hedges of specific interest rate and foreign exchange risks, they do not qualify for hedge accounting under the specific requirements of IAS 39 and are treated as derivatives held for trading with changes in fair value reported as net trading (losses)/gains. The Group has no derivative positions that are designated as hedging instruments.

4 Foreign currency translation

(1) *Functional and presentation currency*

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The financial statements are presented in RMB, which is the Bank's functional and presentation currency.

(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 recognized in the income statement.

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

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

4 Foreign currency translation (Continued)

(3) *Group companies*

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

i. assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;

ii. income and expenses for each income statement are translated at average exchange rates; and

iii. all resulting exchange differences are recognized as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities and monetary items that are part of the net investment in foreign entities are recognized in equity. When a foreign entity is sold, these exchange differences are recognized in the income statement, as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

5 Interest income and expense

Interest income and expense are recognized in the income statement for all instruments measured at amortized cost using the effective interest method.

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all amounts paid or received by the Group that are an integral part of the effective interest rate, including transaction costs and all other premiums or discounts.

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 recognized using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

6 Fee and commission income

Fees and commissions are recognized on an accrual basis when the related service has been provided.

Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognized as an adjustment to the effective interest rate on the loan. Loan syndication fees are recognized as revenue when the related syndication arrangement has been completed and the Group has retained no part of the loan package for itself or has retained a part at the same effective interest rate as that of other participants.

Commission and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party, such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses, are generally recognized on completion of the underlying transaction.

Portfolio and other management advisory and service fees are recognized based on the applicable service contracts, usually on a time-apportionate basis. Fund management fees and custodian service fees are recognized ratably over the period that the service is provided.

7 Financial assets

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

(1) *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 which has been acquired or received principally for the purpose of selling or repurchasing in the near term or 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, is classified as held-for-trading. All derivatives are also classified as held for trading.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

7 Financial assets (Continued)

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

A financial asset, other than one held for trading, is classified as financial assets at fair value through profit or loss if it meets the criteria set out below and is so designated by management:

- the designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring the financial assets or liabilities or recognizing the gains and losses on them on different bases; or

- applies to a group of financial assets, financial liabilities or both that is managed and its performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and where information about that group of financial instruments is provided internally on that basis to key management personnel; or

- relates to financial instruments containing one or more embedded derivatives that significantly modifies the cash flows resulting from those financial instruments.

These assets are recognized initially at fair value, with transaction costs taken directly to the income statement on the trade date, the date on which the Group commits to purchase or sell the asset, and are subsequently remeasured at fair value.

Gains and losses from changes in the fair value of such assets (excluding interest accruals) are reported in net trading (losses)/gains. The accrual of interest is reported in interest income.

(2) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, including balances with central banks, placements with banks and other financial institutions, investment securities classified as loans and receivables and loans and advances to customers. They arise when the Group advances cash directly to a borrower or issuer with no intention of trading the receivables. Loans and advances to customers are recognized when cash is advanced to borrowers. Regular way purchases and sales of loans and receivables are recognized on the trade date. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortized cost using the effective interest rate, less allowances for impairment losses.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

7 Financial assets (Continued)

(2) *Loans and receivables (Continued)*

The Group transfers (or "re-discounts") certain trade bills to banks and other financial institutions. These trade bills are derecognized on transfer when all risks and rewards have been transferred. When the criteria for derecognition have not been met, the related transactions are accounted for as secured borrowings and an obligation is recorded as placements from banks and other financial institutions, as appropriate.

(3) *Held-to-maturity*

Financial assets classified as held-to-maturity are non-derivative financial assets traded in active markets, with fixed or determinable payments and fixed maturities that the Group's management has both the positive intention and the ability to hold to maturity. Were the Group to sell other than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available-for-sale investments. They are initially recorded at fair value plus any directly attributable transaction costs on the trade date, the date on which the Group commits to purchase the asset, and are subsequently measured at amortized cost using the effective interest rate, less allowance for impairment losses.

(4) *Available-for-sale*

Financial assets classified as available-for-sale are non-derivatives that are either designated as such or are not classified in any of the other categories. They are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Available-for-sale financial assets are initially recorded at fair value plus any directly attributable transaction costs on the trade date, the date on which the Group commits to purchase the asset and are subsequently re-measured at fair value. Gains and losses arising from changes in the fair value of financial assets classified as available-for-sale are recognized directly in equity, until the financial asset is derecognized or impaired at which time the cumulative gain or loss previously recognized in equity should be recognized in profit or loss. Interest calculated using the effective interest method is recognized in the income statement. Dividends on equity instruments classified as available-for-sale are recognized in the income statement when the Group's right to receive payment is established.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

7 Financial assets (Continued)

(4) *Available-for-sale (Continued)*

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available-for-sale are analyzed between translation differences resulting from changes in amortized cost of the securities and other changes in the carrying amount of the securities. The translation differences on monetary securities are recognized in income statement; translation differences on non-monetary securities are recognized in equity. Changes in the fair value of monetary and non-monetary securities classified as available-for-sale are recognized in equity.

(5) *Derecognition of financial assets*

Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

(6) *Determination of fair value*

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active or the security is unlisted, the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

8 Insurance contracts

(1) *Insurance contracts classification, recognition and measurement*

The Group's insurance subsidiaries issue insurance contracts that transfer significant insurance risk. As a general guideline, the Group defines as significant insurance risk the possibility of having to pay benefits on the occurrence of an insured event that are at least 10% more than the benefit payable if the insured event did not occur. The Group issues general insurance contracts, which cover casualty and property insurance risk, and long term business insurance contracts, which insure events associated with human life (for example death, or survival) over a long duration. The Group does not separately measure embedded derivatives that meet the definition of an insurance contract or options to surrender insurance contracts for a fixed amount (or an amount based on a fixed amount and an interest rate).

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

8 Insurance contracts (Continued)

(1) *Insurance contracts classification, recognition and measurement (Continued)*

Premiums on general insurance contracts are recognized as revenue (earned premiums) proportionally over the period of coverage. The portion of premium received on in-force contracts that relates to unexpired risks at the balance sheet date is reported as the unearned premium liability. Premiums are recognized before the deduction of commissions.

Claims and loss adjustment expenses are charged to the income statement as incurred based on the estimated liability for compensation owed to contract holders or third parties damaged by the contract holders. They include direct and indirect claims settlement costs and arise from events that have occurred up to the balance sheet date even if they have not yet been reported to the Group.

Premiums on long-term business insurance contracts are recognized as revenue when they become payable by the contract holders. Premiums are recognized before the deduction of commissions. Benefits and claims are recorded as an expense when they are incurred. A liability for contractual benefits that are expected to be incurred in the future is recorded when premiums are recognized. For certain long-term insurance contracts (linked long term insurance contracts) with embedded derivatives linking payments on the contract to units of an investment fund set up by the Group with the consideration received from the contract holders, the liability is adjusted for all changes in the fair value of the underlying assets, and includes a liability for contractual benefits that are expected to be incurred in the future which is recorded when the premiums are recognized.

(2) *Deferred policy acquisition costs ("DAC")*

Commissions and other acquisition costs for general insurance contracts that vary with and are related to securing new contracts and renewing existing contracts are capitalized as DAC, an intangible asset. All other costs are recognized as expenses when incurred. The DAC is subsequently amortized over the terms of the policies as premiums are earned.

(3) *Liability adequacy test*

At each balance sheet date, liability adequacy tests are performed to ensure the adequacy of the insurance contract liabilities (including unearned premium in the case of general insurance contracts). Any deficiency is immediately charged to the income statement, with a provision established for losses arising from the liability adequacy test.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

9 Sale and repurchase agreements

Securities and bills sold subject to repurchase agreements ("repos") are recorded as investment securities or loans and advances to customers. The counterparty liability is included in Placements from banks and other financial institutions or Due to central banks, as appropriate. Securities and bills purchased under agreements to resell ("reverse repos") are recorded as Placements with banks and other financial institutions, as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

Securities lending transactions are generally secured, with collateral taking the form of securities or cash advanced or received. Securities lent to counterparties are retained in the financial statements. Cash collateral advanced or received is recorded as an asset or a liability respectively.

10 Foreclosed assets

Foreclosed assets are accounted as "Assets held for sale" and reported in "Other assets" and the relevant loans are derecognized. The foreclosed assets are measured at lower of carrying amount and net realizable value.

11 Precious metals and precious metals swaps

Precious metals comprise gold, silver and other precious metals. Precious metals that are not related to the Group's precious metals trading activities are carried at cost. Precious metals that are related to the Group's trading activities are initially recognized at cost and subsequently re-measured at their respective market prices at the balance sheet date. Marked-to-market gains or losses on precious metals related to the Group's trading activities are included in Net trading (losses)/gains.

The Group receives all risks and rewards of ownership related to bullion deposited with the Group as bullion deposits, including the right to freely pledge or transfer, and it records the gold bullion received as an asset. A liability to return the amount of gold bullion deposited is also recognized. This obligation is measured at cost unless the Group does not possess sufficient gold bullion to meet the obligation giving rise to the liability. To the extent the liability exceeds the related asset, the open position is marked to market.

Gold bullion and other precious metals sold subject to linked repurchase agreements are not derecognized and the related counter-party liability is recorded as Placements from banks and other financial institutions or Due to central bank, as appropriate.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

12 Impairment of financial assets

(1) *Assets carried at amortized 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 if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the 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. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Group about the following loss events:

(i) significant financial difficulty of the issuer or obligor;

(ii) a breach of contract, such as a default or delinquency in interest or principal payments;

(iii) the Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;

(iv) it becoming probable that the borrower will enter into bankruptcy or other financial reorganization;

(v) the disappearance of an active market for that financial asset because of financial difficulties; or

(vi) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

— adverse changes in the payment status of borrowers in the group; or

— national or local economic conditions that correlate with defaults on the assets in the group.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

12 Impairment of financial assets (Continued)

(1) *Assets carried at amortized cost (Continued)*

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant. The Group then performs a collective assessment for all other financial assets that are not individually significant or for which impairment has not yet been identified. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, 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 recognized are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments has been incurred, 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 recognized in the income statement. 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. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralized 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 assessment of impairment, financial assets are grouped on the basis of similar and relevant 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.

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 exist currently.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

12 Impairment of financial assets (Continued)

(1) *Assets carried at amortized cost (Continued)*

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period. 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 uncollectable, it is written off against the related allowances 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. Subsequent recoveries of amounts previously written off decrease the amount of the allowances for loan impairment in the income statement.

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 recognized (such as an improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognized in the income statement.

(2) *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 losses, measured as the difference between the acquisition cost (net of any principal repayment and amortization) and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss, is removed from equity and recognized in the income statement. 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 recognized in the income statement, the impairment loss is reversed through the income statement. With respect to equity instruments, such reversals are made through the available-for-sale reserve within equity.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

13 Intangible assets

(1) *Goodwill*

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary/associate at the date of acquisition. Goodwill on acquisition of subsidiaries is included in intangible assets. Goodwill on acquisition of associates is included in investment in associates and is tested annually for impairment as part of the overall balance. Separately recognized goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business acquisition in which the goodwill arose.

(2) *Other intangible assets*

Other intangible assets principally comprise computer software; and options and firm orders for aircraft.

Computer software is stated at cost less accumulated amortization and impairment. These costs are amortized on a straight-line basis over their estimated useful lives with the amortization recognized in the income statement. When the estimated recoverable amount of an intangible asset is lower than its carrying amount, an impairment loss is recognized in the income statement.

Options and firm orders for aircraft which arose from the acquisition of a subsidiary are initially recorded at fair value at the date of acquisition. The value of such options and firm orders, which are not amortized, will be added to the cost of aircraft when the related aircraft are purchased. The value of options is charged to the income statement upon expiry if they are not exercised.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

14 Impairment of investment in subsidiaries and associates and non-financial assets

Assets that have an indefinite useful life or are not yet available for use are not subject to amortization, but are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Assets other than goodwill that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

15 Property and equipment

(1) *Buildings, improvements, equipment and motor vehicles*

Buildings comprise primarily branches and office premises. All buildings, improvements, equipment and motor vehicles are stated at historical cost less accumulated depreciation and impairment. Historical cost includes expenditures that are directly attributable to the acquisition of the items.

Subsequent costs are included in an asset's carrying amount or are recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

Depreciation is calculated on the straight-line method to write down the cost of such assets to their residual values over their estimated useful lives as follows:

Buildings	15–50 years
Improvements	Shorter of economic useful life or remaining lease term
Equipment	3–15 years
Motor vehicles	4–6 years

The residual values and useful lives of assets are reviewed, and adjusted if appropriate, at each balance sheet date.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

15 Property and equipment (Continued)

(1) ***Buildings, improvements, equipment and motor vehicles (Continued)***

Buildings, improvements, equipment and motor vehicles are periodically reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains and losses on disposals are determined by comparing proceeds with carrying amount, relevant taxes and expenses. These are included in the income statement.

(2) ***Aircraft***

Aircraft are stated at cost less accumulated depreciation and any impairment loss. The cost of aircraft is stated net of manufacturers' credits. Modifications, improvements and all other costs associated with maintaining the aircraft in a serviceable state are capitalized.

Aircraft are depreciated using the straight-line method over a period of 25 years, being the expected useful life, less the years of their service at the time of purchase to an estimated residual value.

Aircraft are periodically reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Gains and losses on disposal of the aircraft are determined by comparing proceeds with carrying amount, relevant taxes and expenses. These are included in the income statement.

(3) ***Construction in progress***

Construction in progress consists of assets under construction or being installed and is stated at cost. Cost includes equipment cost, cost of construction, installation and other direct costs. Items classified as construction in progress are transferred to property and equipment when such assets are ready for their intended use, and the depreciation charge commences from the following month after such assets are transferred to property and equipment.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

15 Property and equipment (Continued)

(3) *Construction in progress (Continued)*

Impairment losses are recognized for idle projects with respect to which management has determined that resumption in the foreseeable future is not probable, including those projects that are the subject of litigation. The impairment loss is equal to the extent to which the estimated recoverable amount of a specific project is less than its carrying amount. Impairment losses are charged to the income statement.

16 Investment property

Investment property, principally consisting of office buildings, is held to generate rental income over the long term or earn capital gains or both and is not occupied by the Group. Investment property is carried at fair value, representing open market value determined periodically by independent appraisers. Changes in fair values are recorded in the income statement as part of other operating income.

17 Leases

(1) *Operating lease*

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. The total payments made under operating leases (net of any incentives received from the lessor) which include land use rights with payments that are separately identifiable at inception of the lease are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognized as an expense in the period in which termination takes place.

Where the Group is the lessor under operating leases, the assets subject to the operating lease are accounted for as property and equipment and investment property. Rental income (net of any incentives given to the lessees) is recognized on a straight-line basis over the lease term.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

17 Leases (Continued)

(2) *Finance lease*

Leases of assets where the Group has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the present value of the minimum lease payments at the inception of the lease term. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against the income statement.

When assets are leased out under a finance lease, the present value of the lease payments is recognized as a receivable. The difference between the gross receivables and the present value of the receivables is recognized as unearned finance income.

Lease income is recognized over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

18 Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with an original maturity of less than three months, including: cash, non-restricted balances with central banks, due from banks, placements with banks and other financial institutions, and short-term bills and notes classified as investment securities.

19 Provisions

Provisions are recognized 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.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

20 Financial liabilities

Financial liabilities are classified into two categories: financial liabilities at fair value through profit or loss and other financial liabilities. All financial liabilities are classified at inception and recognised initially at fair value.

(1) *Financial liabilities at fair value through profit or loss*

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

A financial liability is classified as held for trading if it is incurred principally for the purpose of repurchasing in the short term. It is carried at fair value and any gains and losses from changes in fair value are recognised in the income statement.

A financial liability is typically classified as fair value through profit or loss at inception if it meets the following criteria:

- the designation eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mismatch") that would otherwise arise from measuring the financial assets or financial liabilities or recognising the gains and losses on them on different bases;

- a group of financial assets and/or financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and this is the basis on which information about the financial assets and/or financial liabilities is provided internally to the key management personnel; or

- relates to financial instruments containing one or more embedded derivative that significantly modifies the cash flows resulting from those financial instruments.

Financial liabilities designated as at fair value through profit or loss, including deposits received from customers that are embedded with certain derivatives, are designated as such at inception. Financial liabilities designated at fair value through profit or loss are carried at fair value. Any gains and losses (excluding interest accruals) from changes in fair value are recognised in the income statement and reported in Net trading (losses)/gains. The accrual of interest is reported in Interest expenses.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

20 Financial liabilities (Continued)

(2) *Other financial liabilities*

Other financial liabilities including borrowings are recognized initially at fair value, net of transaction costs incurred. Other financial liabilities are subsequently stated at amortized cost; any difference between proceeds net of transaction costs and the redemption value is recognized in the income statement over the period of the other financial liabilities using the effective interest method.

If the Group purchases its own debt, it is removed from the consolidated balance sheet, and the difference between the carrying amount of a liability and the consideration paid is included in the income statement.

21 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

22 Employee benefits

(1) *Defined contribution plans*

In accordance with the policies of relevant state and local governments, domestic employees participate in various defined contribution retirement schemes administered by local Labour and Social Security Bureaus. Domestic Operations contribute to pension and insurance schemes administered by the local pension and insurance agencies using applicable contribution rates stipulated in the relevant local regulations. Upon retirement, the local Labour and Social Security Bureaus are responsible for the payment of the basic retirement benefits to the retired employees. In addition to these basic staff pension schemes, domestic employees can also voluntarily participate in a contribution retirement benefit program established by the Bank during 2005 ("the Annuity Plan"). The Bank contributes to the Annuity Plan based on certain percentages of the employees' gross salaries.

All eligible employees in Overseas Operations participate in local defined contribution schemes. Overseas Operations contribute to these defined contribution plans based on certain percentages of the employees' basic salaries.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

22 Employee benefits (Continued)

(1) *Defined contribution plans (Continued)*

Contributions made by the Group to the retirement schemes described above are recorded as an expense in the income statement as accrued. Forfeited contributions by those employees who leave the schemes prior to the full vesting of their contributions are used to reduce the existing level of contributions or retained in the retirement schemes in accordance with the requirements of the respective defined contribution plans. The Group has no further legal obligation to pay additional pensions even if the defined contribution schemes in which the Group's employees participate are not sufficient to fund withdrawals by participants.

(2) *Retirement benefit obligations*

Historically, the Group has paid supplemental retirement benefits to all retired domestic employees and early retirement benefits to those employees who accepted an early retirement arrangement. Supplemental retirement benefits include supplemental pension income payments and medical expense coverage, the amounts of which are calculated based on the difference between the basic benefits received and enhanced benefit levels determined by management from time to time. Early retirement benefits have been paid to those employees who accept voluntary retirement before the normal retirement date, as approved by management. The related benefit payments are made from the date of early retirement through the normal retirement date.

The Group has recorded a liability for its obligation related to supplemental and early retirement obligations to retired and early retired employees. No liability has been recorded related to benefits that current domestic employees may receive in the future, as the Group has not incurred a constructive obligation to pay such benefits. In connection with the implementation of the Joint Stock Reform Plan, management has undertaken a comprehensive re-design of its employee compensation including establishing the Annuity Plan. A number of the elements of this re-design are consistent with and reinforce management's position that the Group has had no obligation to pay supplemental retirement benefits to current domestic employees. These include relevant amendments to the domestic employee policy handbook and a written acknowledgement by domestic employees of a clarification of the Group's obligations only to fund the mandatory payments to state administered defined contribution.

All employees who retired after 1 January 2004 are eligible to make withdrawals from the Annuity Plan fund from 1 January 2006.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

22 Employee benefits (Continued)

(2) *Retirement benefit obligations (Continued)*

The liability related to the supplemental benefit obligation for employees who retired prior to 31 December 2003 and early retirement obligations existing at each year-end with respect to early retired employees, is calculated by the independent actuaries using the projected unit credit method and recorded as a liability under Retirement benefit obligations in the balance sheet. The present value of the liability is determined through estimated future cash outflows using interest rates of RMB treasury bills which have terms to maturity approximating the terms of the related liability. Actuarial gains and losses, changes in actuarial assumptions and amendments to pension plans are charged or credited to the income statement immediately as they occur. Past-service costs are recognized immediately in the income statement.

(3) *Housing funds*

Pursuant to local government regulations, all domestic employees participate in various local housing funds administered by local governments. Domestic Operations contribute on a monthly basis to these funds based on certain percentages of the salaries of the employees. These payments are expensed as incurred.

(4) *Share-based compensation*

(a) *Equity-settled share-based compensation schemes*

The Group operates a number of equity-settled share-based compensation schemes. The fair value of the employee services received in exchange for the grant of the options under these schemes is recognized as an expense over the vesting period, with a corresponding increase in equity. 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. The fair value of the equity instruments is measured at grant date, and is not subsequently re-measured. 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 entity revises its estimates of the number of options that are expected to become exercisable. It recognizes the impact of the revision of original estimates, if any, in the income statement, with a corresponding adjustment to equity over the remaining vesting period.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

22 Employee benefits (Continued)

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

(b) *Cash-settled share-based compensation scheme*

The Bank also operates a cash-settled, share appreciation rights plan. The related cost of services received from the employees and the liability to pay for such services are measured at fair value and recognized over the vesting period as the employees render services. Fair value is established at the grant date and until the liability is settled, the fair value is re-measured at each reporting date with any changes in fair value recognized in profit or loss for the period. Fair value is determined by using an appropriate valuation model.

The total amount to be expensed over the vesting period is determined by reference to the fair value of the rights granted, excluding the impact of any non-market vesting conditions. Non-market conditions are included in the assumptions about the number of rights that are expected to vest. At each balance sheet date, the entity revises its estimates of the number of rights that are expected to vest. It recognizes the impact of the revision to original estimates, if any, in the income statement, with a corresponding adjustment to liability.

(5) *Bonus plans*

The Group recognizes a liability and an expense for bonuses, taking into consideration its business performance and profit attributable to the Bank's equity holders. The Group recognizes a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

23 Deferred income taxes

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

23 Deferred income taxes (Continued)

The principal temporary differences arise from asset impairment allowances, depreciation of property and equipment, revaluation of certain financial assets and liabilities including derivative contracts, provisions for pension and benefit costs and tax losses carried forward. However, deferred income tax is not recognized if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Deferred income tax assets are recognized to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

Deferred income tax is provided on temporary differences arising from investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the difference will not reverse in the foreseeable future.

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

Deferred income 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 recognized in the income statement together with the deferred gain and loss.

24 Share capital

Ordinary shares are classified as equity when there is no contractual obligation to transfer cash or other financial assets. Consideration received on the issuance of shares in excess of the share cost is reported in the Capital reserve.

(1) ***Share issue costs***

Incremental costs directly attributable to the issue of new ordinary shares are shown in equity as a deduction, net of tax, from the proceeds.

(2) ***Dividends***

Dividends are recognized as liabilities in the period in which they are approved by the Bank's equity holders.

Dividends for the year that are declared after the balance sheet date are addressed in the subsequent event note to the financial statements.

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

24 Share capital (Continued)

(3) *Treasury shares*

Where the Bank or other members of the Group purchase the Bank's ordinary shares, treasury shares are recorded at the amount of consideration paid and deducted from total shareholders' equity until they are cancelled, sold or reissued. Where such shares are subsequently sold or reissued, any consideration received is included in shareholders' equity.

25 Acceptances

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers. The Group expects most acceptances to be settled simultaneously with the reimbursement from the customers. Acceptances are accounted for as off-balance sheet transactions and are disclosed as Credit commitments in Note V.38 (6).

26 Fiduciary activities

The Group commonly acts as a custodian, trustee or in other fiduciary capacities, that result in its holding or placing of assets on behalf of securities investment funds, social security funds, insurance companies, qualified foreign institutional investors, annuity schemes and other institutions. These assets are excluded from these financial statements, as they are not assets of the Group.

The Group also administers entrusted loans on behalf of third-party lenders. In this regard, the Group grants loans to borrowers, as an intermediary, at the direction of 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 purpose, amounts, interest rates, and repayment schedule. The Group charges a commission related to its activities in connection with the entrusted loans, but the risk of loss is borne by the third-party lenders. Entrusted loans are not recognized in the financial statements of the Group.

27 Contingent liabilities

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 recognized because it is not probable that an outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

(Amount in millions of Renminbi, unless otherwise stated)

II SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (Continued)

27 Contingent liabilities (Continued)

A contingent liability is not recognized as a provision 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 recognized as a provision.

28 Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.

Financial guarantees are initially recognized in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the Group's liabilities under such guarantees are measured at the higher of the initial measurement, less amortization calculated to recognize in the income statement the fee income earned on a straight line basis over the life of the guarantee and the best estimate of the expenditure required to settle any financial obligation arising at the balance sheet date. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the judgment of management.

Any increase in the liability relating to guarantees is taken to the income statement under other operating expenses.

29 Comparative figures

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the current year. These reclassifications do not have any impact to the Group's or the Bank's total assets, total liabilities and total shareholders' equity as at 31 December 2005 and the Group's profit for the year then ended.

III FINANCIAL RISK MANAGEMENT

1 Strategy in using financial instruments

This section presents information about the Group's exposure to and its management and control of risks, in particular the primary risks associated with its use of financial instruments:

— credit risk is the risk of loss resulting from client or counterparty default and arises on credit exposure in all forms, including settlement risk;

— market risk is exposure to observable market variables such as interest rates, exchange rates and equity markets;

— funding and liquidity risk is the risk that the Group is unable to meet its payment obligations when due, or that it is unable, on an ongoing basis, to borrow funds in the market on an unsecured, or even secured basis at an acceptable price to fund actual or proposed commitments.

2 Credit risk

Credit risk is increased when counterparties are concentrated in the same industries or geographical regions. The Group operates in the PRC, Hong Kong and Macau, and other international locations. Each of these has its own unique characteristics in terms of economic development and of its financial markets. Therefore, each area presents 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 individual borrowers.

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

The primary purpose of credit-related commitments is to ensure that funds are available to a customer, as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans and advances. Guarantee deposits are received by the Group to lessen the credit risks related to certain of these commitments provided by the Group. When received, such deposits are typically established as a certain percentage of the notional amount of a guarantee, standby letter of credit or other credit related commitment. The percentage of such deposits over the related credit commitments is determined by the creditworthiness of the related customer.

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

3 Concentrations of operating income, assets, liabilities and off-balance sheet items

The geographical concentrations of the Group's operating income, assets, liabilities, and credit commitments are set forth below:

As at and for the year ended 31 December 2006

Group

	Total operating income	Total assets	Total liabilities	Credit commitments	Capital expenditure
Chinese Mainland[1]	**108,510**	**4,287,692**	**3,921,219**	**884,607**	**5,954**
Hong Kong and Macau	**37,669**	**1,084,078**	**980,389**	**203,476**	**1,406**
Other overseas locations	**2,744**	**214,766**	**204,675**	**61,297**	**52**
Elimination[1]	**(545)**	**(258,883)**	**(191,586)**	**(61,558)**	**—**
	148,378	**5,327,653**	**4,914,697**	**1,087,822**	**7,412**

As at and for the year ended 31 December 2005

Group

	Total operating income	Total assets	Total liabilities	Credit commitments	Capital expenditure
Chinese Mainland[1]	91,396	3,797,520	3,586,428	699,066	5,379
Hong Kong and Macau	30,590	969,872	872,995	182,334	660
Other overseas locations	3,120	186,995	178,855	52,434	67
Elimination[1]	—	(214,339)	(153,749)	(38,072)	—
	125,106	4,740,048	4,484,529	895,762	6,106

(1) Includes investments in subsidiaries and related elimination. These are excluded in the presentation of segment asset disclosure and related elimination in Note V.1.

Total operating income includes net interest income, net fee and commission income, net trading (losses)/gains, net gains on investment securities and other operating income.

(2) Over 90% of the Bank's operating income, assets, liabilities and credit commitments are attributable to the Chinese Mainland segment and therefore no geographical analysis is presented for the Bank.

III FINANCIAL RISK MANAGEMENT (Continued)

3 Concentrations of operating income, assets, liabilities and off-balance sheet items (Continued)

Geographical concentrations of risk for loans and advances to customers (gross) are as follows:

Group

	As at 31 December			
	2006		2005	
		%		%
Chinese Mainland	**1,990,400**	**82**	1,800,142	81
Hong Kong and Macau	**379,532**	**16**	379,071	17
Other overseas locations	**62,087**	**2**	56,052	2
Gross amounts of loans and advances before allowance for impairment losses	**2,432,019**	**100**	2,235,265	100

Bank

	As at 31 December			
	2006		2005	
		%		%
Chinese Mainland	**1,990,400**	**96**	1,800,142	96
Hong Kong and Macau	**15,149**	**1**	14,866	1
Other overseas locations	**59,278**	**3**	53,315	3
Gross amounts of loans and advances before allowance for impairment losses	**2,064,827**	**100**	1,868,323	100

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

3 Concentrations of operating income, assets, liabilities and off-balance sheet items (Continued)

The economic sector concentration of risk for loans and advances to customers (gross) based on the Group's classification system are as follows:

Group

	As at 31 December			
	2006		2005	
		%		%
Chinese Mainland				
Corporate loans				
Manufacturing	**556,032**	**23**	491,117	22
Commerce and services	**257,853**	**11**	255,460	12
Energy, mineral and agriculture	**240,314**	**10**	210,281	10
Transportation and logistics	**182,398**	**8**	165,396	8
Real estate	**113,589**	**5**	96,390	4
Public utilities	**105,933**	**4**	91,924	4
Financial services	**53,333**	**2**	77,237	3
Construction	**34,676**	**1**	30,089	1
Others	**2,692**	**—**	2,290	—
Corporate loan total	**1,546,820**	**64**	1,420,184	64
Personal loans				
Mortgage loans	**337,834**	**14**	286,829	13
Credit card advances	**2,876**	**—**	1,929	—
Others	**102,870**	**4**	91,200	4
Personal loan total	**443,580**	**18**	379,958	17
Total for Chinese Mainland	**1,990,400**	**82**	1,800,142	81

III FINANCIAL RISK MANAGEMENT (Continued)

3 Concentrations of operating income, assets, liabilities and off-balance sheet items (Continued)

Group (Continued)

	As at 31 December			
	2006		2005	
		%		%
Hong Kong and Macau				
Corporate loans				
Real estate	**94,391**	**4**	86,419	3
Manufacturing	**35,853**	**1**	34,285	2
Commerce and services	**33,443**	**1**	35,137	2
Transportation and logistics	**24,481**	**1**	21,783	1
Energy, mineral and agriculture	**12,256**	**1**	12,429	1
Financial services	**12,107**	**1**	14,367	1
Construction	**4,053**	**—**	4,874	—
Others	**25,328**	**1**	27,613	1
Corporate loan total	**241,912**	**10**	236,907	11
Personal loans				
Mortgage loans	**117,972**	**5**	125,514	6
Credit card advances	**5,516**	**—**	4,856	—
Others	**14,132**	**1**	11,794	—
Personal loan total	**137,620**	**6**	142,164	6
Total for Hong Kong and Macau	**379,532**	**16**	379,071	17
Other overseas locations	**62,087**	**2**	56,052	2
Gross amounts of loans and advances before allowance for impairment losses	**2,432,019**	**100**	2,235,265	100

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

3 Concentrations of operating income, assets, liabilities and off-balance sheet items (Continued)

Bank

	As at 31 December			
	2006		2005	
		%		%
Corporate loans				
Manufacturing	**568,398**	**27**	498,363	26
Commerce and services	**268,522**	**13**	267,967	14
Energy, mineral and agriculture	**248,865**	**12**	218,777	12
Transportation and logistics	**188,606**	**9**	173,003	9
Real estate	**127,287**	**6**	105,794	6
Public utilities	**106,141**	**5**	91,924	5
Financial services	**60,969**	**3**	82,566	4
Construction	**34,866**	**2**	31,203	2
Others	**12,398**	**1**	14,336	1
Corporate loan total	**1,616,052**	**78**	1,483,933	79
Personal loans				
Mortgage loans	**341,576**	**17**	290,342	16
Credit card advances	**2,942**	**—**	1,929	—
Others	**104,257**	**5**	92,119	5
Personal loan total	**448,775**	**22**	384,390	21
Gross amounts of loans and advances before allowance for impairment losses	**2,064,827**	**100**	1,868,323	100

Over 90% of the Bank's gross balances of loans and advances are attributable to the Chinese Mainland segment and therefore no geographical segment analysis is presented.

III FINANCIAL RISK MANAGEMENT (Continued)

3 Concentrations of operating income, assets, liabilities and off-balance sheet items (Continued)

Gross loans and advances to customers analyzed by customer type:

Group

	As at 31 December	
	2006	2005
Chinese Mainland		
Corporate entities	**1,331,824**	1,224,873
Individuals	**443,580**	379,958
Trade bills	**214,996**	195,311
	1,990,400	1,800,142
Hong Kong, Macau and other overseas		
Corporate entities	**267,837**	262,363
Individuals	**139,164**	143,045
Trade bills	**34,618**	29,715
	441,619	435,123
Gross amounts of loans and advances before allowance for impairment losses	**2,432,019**	2,235,265

Bank

	As at 31 December	
	2006	2005
Chinese Mainland		
Corporate entities	**1,331,824**	1,224,873
Individuals	**443,580**	379,958
Trade bills	**214,996**	195,311
	1,990,400	1,800,142
Hong Kong, Macau and other overseas		
Corporate entities	**54,351**	53,893
Individuals	**5,195**	4,432
Trade bills	**14,881**	9,856
	74,427	68,181
Gross amounts of loans and advances before allowance for impairment losses	**2,064,827**	1,868,323

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

4 Market risk

The Group takes on exposure to market risks. Market risk is the risk of potential loss to earnings or cash flows that may result from the Group's on and off-balance-sheet positions as a result of adverse changes in market prices (such as interest rates, exchange rates, equity prices and commodity prices). The principal types of market risk for the Group are interest rate risk and exchange rate risk. The Group controls its market risk with risk limits approved by the Board of Directors in respect of its trading and banking book (including investment book). Market risk in its trading book is monitored and controlled by establishing an overall Value at Risk limit and stop loss limits. Based on the different characteristics of specific products, the qualifications of the dealers and position amounts, stop loss limits are established for each trading desk and each dealer. On each trading day, the position and profit or loss of trading desks are monitored to identify transactions that are in excess of authorized limits. The market risk in its investment book is controlled and managed at both portfolio and product levels by establishing different types of limits including duration, concentration, Value at Risk limit, present value of a basis point change in interest rates and stress tests limit.

The management of the specific market risks is summarized below in Note III.5 and Note III.6.

5 Currency risk

The Group conducts the majority of its business in RMB, with certain transactions denominated in USD, Hong Kong dollars ("HKD") and, to a much lesser extent, other currencies. The exchange rates of the RMB to the USD and HKD respectively are set by the People's Bank of China ("PBOC") and have fluctuated in the last decade within a narrow band of less than 1% prior to July 2005. On 21 July 2005, the PRC Government introduced a managed floating exchange rate system to allow the value of the RMB to fluctuate within a regulated band based on market supply and demand and by reference to a basket of currencies. On the same day, the value of the RMB appreciated by approximately 2% against the USD. The PRC Government in the future may make further adjustments to the exchange rate system.

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

The Group's net foreign currency positions as at 31 December 2006 and 31 December 2005 are analyzed below:

	Foreign Currency Position			
	As at 31 December 2006		As at 31 December 2005	
	RMB billion	**USD billion equivalent***	RMB billion	USD billion equivalent*
Net on-balance sheet foreign currency position of the Group	**669**	**86**	485	60
Less: Net off-balance sheet foreign currency position of the Group	**(433)**	**(55)**	(171)	(21)
Net foreign currency position of the Group	**236**	**31**	314	39
Less: Foreign currency denominated net investments in foreign operations (ii)	**(114)**	**(15)**	(106)	(13)
Net position (excluding structural position in foreign operations)	**122**	**16**	208	26

The key movements of the Group's net foreign currency position during 2006 are analyzed as follows:

	Foreign Currency Position			
USD billion equivalent*	**Net on-balance sheet position**	**Net off-balance sheet position**	**Net investments in foreign operations (ii)**	**Net position**
Opening position as at 1 January 2006	**60**	**(21)**	**(13)**	**26**
— Proceeds from a global offering	**11**	**—**	**—**	**11**
— Spot transactions to reduce foreign currency position (i)	**(26)**	**—**	**—**	**(26)**
— Funding swap transactions (i)	**42**	**(42)**	**—**	**—**
— Funding swap transactions expired	**(4)**	**4**	**—**	**—**
— Others	**3**	**4**	**(2)**	**5**
Closing position as at 31 December 2006	**86**	**(55)**	**(15)**	**16**

* The Group's foreign currency position expressed in USD equivalent in the above tables comprises all net foreign currency exposures as of 31 December 2006 and 2005 based on the respective year-end closing foreign exchange rates of each currency with the USD.

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

(i) The Group endeavors to manage its sources and uses of foreign currencies to minimize potential mismatches in accordance with management directives. However, the Group's ability to manage its foreign currency positions in relation to the RMB is limited as RMB is not a freely convertible currency. The PRC government's current foreign currency regulations require the conversion of foreign currency to be approved by relevant PRC government authorities. The Bank has significant foreign currency positions, which arose largely through foreign currency capital contributions from the equity holders and its foreign currency operations.

In 2005, the Bank entered into a foreign currency option agreement with Huijin ("Huijin option"), having a notional amount of USD18 billion, to economically hedge a portion of its net foreign currency position (see Note V.16(2)).

During the year ended 31 December 2006, the Bank has entered into certain foreign exchange spot transactions, having an aggregate notional amount of USD26.3 billion (2005: Nil), to further reduce its net foreign currency position.

During the year ended 31 December 2006, the Bank has also entered into a series of USD/RMB funding swaps, having an aggregate notional amount of USD41.5 billion (2005: USD4.2 billion), with maturities of either 1 year or 3 years to benefit from the interest differentials between USD and RMB. These USD/RMB funding swaps have no impact on the Group's net foreign currency position. As at 31 December 2006, the outstanding notional amount of these transactions amounted to USD41.5 billion (2005: USD4.2 billion) and the fair value of these outstanding positions as at 31 December 2006 amounted to RMB2.2 billion (2005: RMB0.01 billion). See Note V.16(1).

Subsequent to the balance sheet date and up to the date of this report, the Bank has exercised three tranches of the Huijin option and sold USD4.5 billion to Huijin for RMB at the exchange rate as agreed in the foreign currency option agreement. In addition, the Bank has entered into foreign exchange spot transactions of USD6.8 billion to further reduce its net foreign currency position after the balance sheet date (Note V.43).

Concurrently, the Bank entered into Cross Currency Interest Rate Swap contracts ("CIRS") with a notional amount of USD11.3 billion after the balance sheet date. Under the CIRS, the Bank swapped in USD with RMB at the applicable spot rates and agreed to settle the USD in exchange for RMB after one year. Interest is exchanged on a quarterly basis over the life of the CIRS based on market rates (Note V.43).

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

(ii) The Group's net investments in foreign operations represent the net assets/liabilities of overseas subsidiaries, branches or associated undertakings, the functional currencies of which are currencies other than RMB. The results of operations and financial position of these operations are translated into RMB, for reporting purposes with all exchange differences arising from the translation recognized under the "Currency translation differences" as a separate component of equity. These exchange differences therefore do not impact the consolidated profit or loss of the Group.

The following table illustrates the potential impact to the income statement for a 1 per cent fluctuation in the foreign currency exchange rates against RMB based on the net position of the Group excluding the net structural position in foreign operations as set forth above:

	31 December 2006 Profit/(loss)	31 December 2005 Profit/(loss)
1% appreciation/depreciation in foreign currency exchange rates relative to the RMB	**+/- 1,220**	+/- 2,080

The above sensitivity analysis in response to potential movements in the foreign currency exchange rates against RMB is for illustrative purposes and only represents simple scenarios applied to the Bank's net outstanding foreign currency position as at the respective date. Such analysis does not take into account the correlation effect of changes in different foreign currencies, any further actions that may have been or could be taken by management after the balance sheet date, subject to the approval by the PRC government, to mitigate the effect of exchange differences, nor for any consequential changes in the foreign currency positions.

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

The table below summarizes the Group's exposure to foreign currency exchange rate risk as at 31 December 2006 and 2005. Included in the table are the carrying amounts of the assets and liabilities of the Group and the Bank along with off-balance sheet positions and credit commitments in RMB equivalent, categorized by the original currency. Option products are included in net off-balance sheet position using notional amounts.

Group

	As at 31 December 2006							
	RMB	USD	HKD	EURO	JPY	GBP	Others	Total
Assets								
Cash and due from banks	20,313	9,174	4,478	2,020	1,691	658	1,478	39,812
Balances with central banks	349,839	19,556	2,322	425	4,865	—	2,624	379,631
Placements with banks and other financial institutions	50,136	185,382	111,652	20,085	8,346	6,984	16,553	399,138
Government certificates of indebtedness for bank notes issued	—	—	34,913	—	—	—	1,713	36,626
Precious metals	—	—	1,541	—	—	—	40,542	42,083
Trading assets and other financial instruments at fair value through profit or loss	34,273	38,772	23,677	8,688	6,491	80	3,847	115,828
Derivative financial instruments	7,418	9,161	7,694	150	88	174	152	24,837
Loans and advances to customers, net	1,614,521	329,663	316,546	33,913	21,422	4,468	17,193	2,337,726
Investment securities								
— available-for-sale	313,323	398,383	45,325	31,962	10,684	2,870	12,631	815,178
— held-to-maturity	180,914	192,383	63,521	6,325	—	1,794	16,203	461,140
— loans and receivables	350,159	76,235	43,609	—	13,520	1,065	15,748	500,336
Investments in associates and joint ventures	2,461	762	2,708	—	—	—	—	5,931
Property and equipment	47,346	22,538	12,864	134	1,064	511	1,743	86,200
Investment property	—	—	7,601	—	—	—	620	8,221
Deferred income tax assets	21,200	4	73	—	37	—	82	21,396
Other assets	14,343	21,303	13,987	1,252	307	227	2,151	53,570
Total assets	3,006,246	1,303,316	692,511	104,954	68,515	18,831	133,280	5,327,653

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

Group

	As at 31 December 2006							
	RMB	USD	HKD	EURO	JPY	GBP	Others	Total
Liabilities								
Due to banks and other financial institutions	99,311	27,643	5,044	2,542	8,322	270	35,645	178,777
Due to central banks	—	36,598	5,776	—	—	—	—	42,374
Bank notes in circulation	—	—	34,914	—	—	—	1,909	36,823
Certificates of deposits and placements from banks and other financial institutions	78,497	59,308	5,037	2,397	120	147	1,402	146,908
Derivative financial instruments and liabilities at fair value through profit or loss	9,688	73,876	28,083	282	78	762	279	113,048
Due to customers	2,902,584	420,197	572,423	42,529	44,032	23,210	86,143	4,091,118
Bonds issued	60,000	173	—	—	—	—	—	60,173
Other borrowings	—	40,014	—	15,247	3,984	786	3,367	63,398
Current tax liabilities	16,072	223	1,269	13	13	3	556	18,149
Retirement benefit obligations	7,444	—	—	—	—	—	—	7,444
Deferred income tax liabilities	—	806	2,178	—	—	—	45	3,029
Other liabilities	88,800	25,753	33,339	2,190	968	556	1,850	153,456
Total liabilities	3,262,396	684,591	688,063	65,200	57,517	25,734	131,196	4,914,697
Net on-balance sheet position	(256,150)	618,725	4,448	39,754	10,998	(6,903)	2,084	412,956
Net off-balance sheet position	439,850	(468,346)	79,804	(37,825)	(13,762)	7,222	156	7,099
Credit commitments	505,383	345,814	152,091	51,404	16,424	4,440	12,266	1,087,822

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

Bank

	As at 31 December 2006							
	RMB	USD	HKD	EURO	JPY	GBP	Others	Total
Assets								
Cash and due from banks	19,674	8,757	3,952	1,932	1,604	615	1,308	37,842
Balances with central banks	326,117	19,389	2,269	425	4,865	—	1,816	354,881
Placements with banks and other financial institutions	50,932	173,541	29,164	22,310	8,408	6,360	12,287	303,002
Government certificates of indebtedness for bank notes issued	—	—	—	—	—	—	1,713	1,713
Precious metals	—	—	—	—	—	—	40,542	40,542
Trading assets and other financial instruments at fair value through profit or loss	31,497	30,533	—	6,437	6,324	—	1,790	76,581
Derivative financial instruments	7,418	8,391	61	126	88	169	110	16,363
Loans and advances to customers, net	1,609,963	274,178	22,619	31,003	19,735	3,476	10,891	1,971,865
Investment securities								
— available-for-sale	312,925	336,857	12,343	27,613	10,684	750	5,567	706,739
— held-to-maturity	180,914	92,451	10,915	2,540	—	13	565	287,398
— loans and receivables	350,159	73,668	10,546	—	13,520	761	9,952	458,606
Investments in subsidiaries	—	1,413	43,155	45	—	—	838	45,451
Investments in associates and joint ventures	—	10	—	—	—	—	11	21
Property and equipment	46,668	215	—	134	1,064	511	881	49,473
Investment property	—	—	—	—	—	—	620	620
Deferred income tax assets	21,742	4	—	—	37	—	60	21,843
Other assets	14,044	12,803	1,280	1,062	302	115	666	30,272
Total assets	2,972,053	1,032,210	136,304	93,627	66,631	12,770	89,617	4,403,212

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

Bank

	As at 31 December 2006							
	RMB	USD	HKD	EURO	JPY	GBP	Others	Total
Liabilities								
Due to banks and other financial institutions	84,378	29,206	3,960	2,412	8,460	320	35,640	164,376
Due to central banks	—	36,573	5,776	—	—	—	—	42,349
Bank notes in circulation	—	—	—	—	—	—	1,909	1,909
Certificates of deposits and placements from banks and other financial institutions	78,156	57,015	7,102	3,163	142	147	871	146,596
Derivative financial instruments and liabilities at fair value through profit or loss	9,688	66,257	13,913	243	78	753	152	91,084
Due to customers	2,891,429	268,327	69,661	36,405	40,242	11,075	41,426	3,358,565
Bonds issued	60,000	173	—	—	—	—	—	60,173
Other borrowings	—	24,000	—	15,247	3,984	786	1,989	46,006
Current tax liabilities	16,058	223	—	9	13	3	451	16,757
Retirement benefit obligations	7,444	—	—	—	—	—	—	7,444
Deferred income tax liabilities	—	20	—	—	—	—	12	32
Other liabilities	87,583	17,979	2,467	1,986	879	418	1,215	112,527
Total liabilities	3,234,736	499,773	102,879	59,465	53,798	13,502	83,665	4,047,818
Net on-balance sheet position	(262,683)	532,437	33,425	34,162	12,833	(732)	5,952	355,394
Net off-balance sheet position	439,686	(407,017)	22,467	(32,369)	(15,426)	1,170	(4,795)	3,716
Credit commitments	502,965	310,418	11,297	48,725	15,890	4,323	8,610	902,228

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

Group

	As at 31 December 2005							
	RMB	USD	HKD	EURO	JPY	GBP	Others	Total
Assets								
Cash and due from banks	17,632	12,507	5,016	1,688	1,422	540	2,277	41,082
Balances with central banks	274,107	13,503	10,655	852	15,826	—	1,998	316,941
Placements with banks and other financial institutions	71,563	124,632	95,603	13,023	474	5,573	21,231	332,099
Government certificates of indebtedness for bank notes issued	—	—	33,945	—	—	—	1,641	35,586
Precious metals	—	—	1,736	—	—	—	25,238	26,974
Trading assets and other financial instruments at fair value through profit or loss	29,051	41,333	15,592	12,061	8,260	143	5,342	111,782
Derivative financial instruments	—	11,493	4,552	149	548	57	9	16,808
Loans and advances to customers, net	1,411,382	346,718	315,727	34,443	24,866	4,192	14,784	2,152,112
Investment securities								
— available-for-sale	230,512	284,807	29,829	28,884	13,891	5,128	9,170	602,221
— held-to-maturity	271,612	232,005	78,267	7,376	921	1,777	15,501	607,459
— loans and receivables	305,762	8,230	31,166	1,723	—	—	14,970	361,851
Investments in associates and joint ventures	4,547	31	483	—	—	—	—	5,061
Property and equipment	46,004	289	12,850	135	1,121	480	1,538	62,417
Investment property	—	—	8,040	—	—	—	471	8,511
Deferred income tax assets	20,177	24	86	—	30	—	187	20,504
Other assets	14,520	11,251	9,757	1,025	618	247	1,222	38,640
Total assets	2,696,869	1,086,823	653,304	101,359	67,977	18,137	115,579	4,740,048

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

Group

	As at 31 December 2005							
	RMB	USD	HKD	EURO	JPY	GBP	Others	Total
Liabilities								
Due to banks and other financial institutions	67,518	22,498	8,351	2,319	7,571	236	25,724	134,217
Due to central banks	1,084	24,162	4,650	29	—	32	98	30,055
Bank notes in circulation	—	—	33,945	—	—	—	1,786	35,731
Certificates of deposits and placements from banks and other financial institutions	142,106	55,077	8,065	2,081	3,968	278	1,051	212,626
Derivative financial instruments and liabilities at fair value through profit or loss	—	70,625	19,552	420	384	117	76	91,174
Due to customers	2,531,878	438,881	527,118	46,854	37,565	26,634	90,534	3,699,464
Bonds issued	60,000	179	—	—	—	—	—	60,179
Other borrowings	—	28,370	—	16,251	4,665	1,092	1,786	52,164
Current tax liabilities	21,728	191	946	15	—	10	569	23,459
Retirement benefit obligations	7,052	—	—	—	—	—	—	7,052
Deferred income tax liabilities	—	—	2,114	—	—	—	22	2,136
Other liabilities	95,714	17,028	19,571	1,510	1,139	518	792	136,272
Total liabilities	2,927,080	657,011	624,312	69,479	55,292	28,917	122,438	4,484,529
Net on-balance sheet position	(230,211)	429,812	28,992	31,880	12,685	(10,780)	(6,859)	255,519
Net off-balance sheet position	173,666	(229,776)	73,943	(29,586)	(16,344)	15,331	15,197	2,431
Credit commitments	394,938	295,280	137,425	30,874	21,185	2,049	14,011	895,762

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

Bank

	As at 31 December 2005							
	RMB	USD	HKD	EURO	JPY	GBP	Others	Total
Assets								
Cash and due from banks	17,167	9,617	6,046	1,593	1,256	489	2,107	38,275
Balances with central banks	251,430	13,415	1,787	852	15,826	—	1,063	284,373
Placements with banks and other financial institutions	72,014	101,144	34,644	14,326	3,909	2,497	15,120	243,654
Government certificates of indebtedness for bank notes issued	—	—	—	—	—	—	1,641	1,641
Precious metals	—	—	—	—	—	—	25,238	25,238
Trading assets and other financial instruments at fair value through profit or loss	28,069	33,978	—	9,881	8,260	71	1,823	82,082
Derivative financial instruments	—	10,449	156	118	540	57	9	11,329
Loans and advances to customers, net	1,409,349	295,757	19,143	30,114	22,347	3,346	8,686	1,788,742
Investment securities								
— available-for-sale	230,361	255,249	6,740	26,286	13,891	4,089	5,526	542,142
— held-to-maturity	271,612	125,084	13,268	3,125	670	452	932	415,143
— loans and receivables	305,762	6,428	20,994	1,723	—	—	9,003	343,910
Investments in subsidiaries	17	404	42,762	45	—	—	1,852	45,080
Investments in associates and joint ventures	—	1	—	—	—	—	44	45
Property and equipment	44,991	288	—	135	1,121	480	1,046	48,061
Investment property	—	—	—	—	—	—	461	461
Deferred income tax assets	20,177	24	—	—	30	—	158	20,389
Other assets	14,649	8,132	850	855	289	101	961	25,837
Total assets	2,665,598	859,970	146,390	89,053	68,139	11,582	75,670	3,916,402

III FINANCIAL RISK MANAGEMENT (Continued)

5 Currency risk (Continued)

Bank

	As at 31 December 2005							
	RMB	USD	HKD	EURO	JPY	GBP	Others	Total
Liabilities								
Due to banks and other financial institutions	54,790	24,790	9,149	2,159	7,979	304	25,777	124,948
Due to central banks	1,084	24,137	4,650	29	—	32	98	30,030
Bank notes in circulation	—	—	—	—	—	—	1,786	1,786
Certificates of deposits and placements from banks and other financial institutions	141,669	52,839	14,013	2,310	3,958	548	586	215,923
Derivative financial instruments and liabilities at fair value through profit or loss	—	67,509	7,828	418	382	117	69	76,323
Due to customers	2,522,232	295,557	68,398	39,533	34,625	12,568	36,274	3,009,187
Bonds issued	60,000	179	—	—	—	—	—	60,179
Other borrowings	—	28,370	—	16,251	4,665	1,092	1,786	52,164
Current tax liabilities	21,723	191	1	13	—	10	502	22,440
Retirement benefit obligations	7,052	—	—	—	—	—	—	7,052
Deferred income tax liabilities	—	—	—	—	—	—	23	23
Other liabilities	94,645	12,913	1,543	1,336	784	338	975	112,534
Total liabilities	2,903,195	506,485	105,582	62,049	52,393	15,009	67,876	3,712,589
Net on-balance sheet position	(237,597)	353,485	40,808	27,004	15,746	(3,427)	7,794	203,813
Net off-balance sheet position	173,671	(163,490)	28,235	(24,826)	(19,716)	7,902	(1,654)	122
Credit commitments	393,498	263,040	5,588	28,823	20,340	1,997	10,678	723,964

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk

The Group takes on exposure to the effects of changes in the prevailing level of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. Currently, interest rates for RMB loans and deposits in the PRC are set by the PBOC. The PBOC establishes RMB benchmark interest rates, which create a floor for RMB loan rates and a cap for RMB deposit rates. The Group's Domestic Operations are subject to an interest rate scheme regulated by the PBOC. It is normal practice for the interest rates of both interest-bearing assets and liabilities to move in tandem, although the timing of such movements may not be synchronized. This significantly mitigates the exposure of the Group to RMB interest rate risk. However, there is no guarantee that the PBOC will continue this practice in future.

The Group is proactive in managing its exposure to foreign currency interest rates. It monitors changes in foreign currency interest rates closely. In order to control its foreign currency interest rate risk exposure, the Group will adjust foreign currency interest levels on loans and deposits where necessary. It may also use financial instruments as economic hedges against this exposure.

The tables below summarize the Group's exposure to interest rates, showing the carrying amounts of the assets and liabilities of the Group and the Bank, categorized by the earlier of contractual re-pricing or maturity dates at the carrying amounts.

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Group

	As at 31 December 2006						
	Less than 1 month	Between 1 to 3 months	Between 4 to 12 months	Between 1 to 5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and due from banks	7,724	—	—	—	—	32,088	39,812
Balances with central banks	352,873	—	—	—	—	26,758	379,631
Placements with banks and other financial institutions	265,023	106,212	27,783	120	—	—	399,138
Government certificates of indebtedness for bank notes issued	—	—	—	—	—	36,626	36,626
Precious metals	—	—	—	—	—	42,083	42,083
Trading assets and other financial instruments at fair value through profit or loss	8,409	17,950	17,787	35,507	29,405	6,770	115,828
Derivative financial instruments	—	—	—	—	—	24,837	24,837
Loans and advances to customers, net	766,022	391,764	1,128,407	26,320	18,942	6,271	2,337,726
Investment securities							
— available-for-sale	119,182	86,881	143,113	249,999	208,133	7,870	815,178
— held-to-maturity	56,479	93,807	116,519	121,376	72,959	—	461,140
— loans and receivables	52,744	62,973	92,151	249,868	42,600	—	500,336
Investments in associates and joint ventures	—	—	—	—	—	5,931	5,931
Property and equipment	—	—	—	—	—	86,200	86,200
Investment property	—	—	—	—	—	8,221	8,221
Deferred income tax assets	—	—	—	—	—	21,396	21,396
Other assets	193	—	—	—	—	53,377	53,570
Total assets	1,628,649	759,587	1,525,760	683,190	372,039	358,428	5,327,653

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Group

	As at 31 December 2006						
	Less than 1 month	Between 1 to 3 months	Between 4 to 12 months	Between 1 to 5 years	Over 5 years	Non-interest bearing	Total
Liabilities							
Due to banks and other financial institutions	142,042	260	991	—	—	35,484	178,777
Due to central banks	15,497	5,077	21,757	—	—	43	42,374
Bank notes in circulation	—	—	—	—	—	36,823	36,823
Certificates of deposits and placements from banks and other financial institutions	82,335	39,415	15,636	8,939	—	583	146,908
Derivative financial instruments and liabilities at fair value through profit or loss	27,010	22,408	34,485	3,303	6,772	19,070	113,048
Due to customers	2,484,610	453,841	842,988	268,310	428	40,941	4,091,118
Bonds issued	—	9,000	—	42,000	9,173	—	60,173
Other borrowings	4,466	8,792	18,400	13,618	14,372	3,750	63,398
Current tax liabilities	—	—	—	—	—	18,149	18,149
Retirement benefit obligations	—	—	—	—	—	7,444	7,444
Deferred income tax liabilities	—	—	—	—	—	3,029	3,029
Other liabilities	—	—	—	—	—	153,456	153,456
Total liabilities	2,755,960	538,793	934,257	336,170	30,745	318,772	4,914,697
Total interest sensitivity gap	(1,127,311)	220,794	591,503	347,020	341,294	39,656	412,956

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Bank

	As at 31 December 2006						
	Less than 1 month	Between 1 to 3 months	Between 4 to 12 months	Between 1 to 5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and due from banks	10,155	—	—	—	—	27,687	37,842
Balances with central banks	328,444	—	—	—	—	26,437	354,881
Placements with banks and other financial institutions	215,369	59,793	27,720	120	—	—	303,002
Government certificates of indebtedness for bank notes issued	—	—	—	—	—	1,713	1,713
Precious metals	—	—	—	—	—	40,542	40,542
Trading assets and other financial instruments at fair value through profit or loss	3,734	12,013	15,037	30,675	15,122	—	76,581
Derivative financial instruments	—	—	—	—	—	16,363	16,363
Loans and advances to customers, net	459,068	358,013	1,116,522	19,922	14,754	3,586	1,971,865
Investment securities							
— available-for-sale	113,450	71,593	137,711	222,824	160,448	713	706,739
— held-to-maturity	29,676	52,625	83,130	77,475	44,492	—	287,398
— loans and receivables	48,966	48,310	68,861	249,869	42,600	—	458,606
Investments in subsidiaries	—	—	—	—	—	45,451	45,451
Investments in associates and joint ventures	—	—	—	—	—	21	21
Property and equipment	—	—	—	—	—	49,473	49,473
Investment property	—	—	—	—	—	620	620
Deferred income tax assets	—	—	—	—	—	21,843	21,843
Other assets	192	—	—	—	—	30,080	30,272
Total assets	1,209,054	602,347	1,448,981	600,885	277,416	264,529	4,403,212

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Bank

	As at 31 December 2006						
	Less than 1 month	Between 1 to 3 months	Between 4 to 12 months	Between 1 to 5 years	Over 5 years	Non-interest bearing	Total
Liabilities							
Due to banks and other financial institutions	129,396	—	—	—	—	34,980	164,376
Due to central banks	15,497	5,077	21,757	—	—	18	42,349
Bank notes in circulation	—	—	—	—	—	1,909	1,909
Certificates of deposits and placements from banks and other financial institutions	78,339	42,201	19,084	6,972	—	—	146,596
Derivative financial instruments and liabilities at fair value through profit or loss	21,154	18,822	31,606	3,085	6,772	9,645	91,084
Due to customers	1,891,308	370,618	817,744	267,573	115	11,207	3,358,565
Bonds issued	—	9,000	—	42,000	9,173	—	60,173
Other borrowings	1,736	1,115	11,572	13,619	14,372	3,592	46,006
Current tax liabilities	—	—	—	—	—	16,757	16,757
Retirement benefit obligations	—	—	—	—	—	7,444	7,444
Deferred income tax liabilities	—	—	—	—	—	32	32
Other liabilities	—	—	—	—	—	112,527	112,527
Total liabilities	2,137,430	446,833	901,763	333,249	30,432	198,111	4,047,818
Total interest sensitivity gap	(928,376)	155,514	547,218	267,636	246,984	66,418	355,394

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Group

	As at 31 December 2005						
	Less than 1 month	Between 1 to 3 months	Between 4 to12 months	Between 1 to 5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and due from banks	11,624	—	—	—	—	29,458	41,082
Balances with central banks	282,601	1,019	20	—	—	33,301	316,941
Placements with banks and other financial institutions	219,459	95,367	17,224	49	—	—	332,099
Government certificates of indebtedness for bank notes issued	—	—	—	—	—	35,586	35,586
Precious metals	—	—	—	—	—	26,974	26,974
Trading assets and other financial instruments at fair value through profit or loss	6,678	13,594	20,951	44,592	21,456	4,511	111,782
Derivative financial instruments	—	—	—	—	—	16,808	16,808
Loans and advances to customers, net	739,411	309,707	1,046,662	30,557	21,685	4,090	2,152,112
Investment securities							
— available-for-sale	83,297	39,436	132,426	222,989	114,862	9,211	602,221
— held-to-maturity	73,197	120,609	184,638	155,890	73,125	—	607,459
— loans and receivables	29,505	16,996	12,965	259,785	42,600	—	361,851
Investments in associates and joint ventures	—	—	—	—	—	5,061	5,061
Property and equipment	—	—	—	—	—	62,417	62,417
Investment property	—	—	—	—	—	8,511	8,511
Deferred income tax assets	—	—	—	—	—	20,504	20,504
Other assets	—	—	—	—	—	38,640	38,640
Total assets	1,445,772	596,728	1,414,886	713,862	273,728	295,072	4,740,048

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Group

	As at 31 December 2005						
	Less than 1 month	Between 1 to 3 months	Between 4 to12 months	Between 1 to 5 years	Over 5 years	Non-interest bearing	Total
Liabilities							
Due to banks and other financial institutions	105,902	—	—	—	—	28,315	134,217
Due to central banks	29,911	20	—	—	—	124	30,055
Bank notes in circulation	—	—	—	—	—	35,731	35,731
Certificates of deposits and placements from banks and other financial institutions	78,728	51,316	75,595	3,899	—	3,088	212,626
Derivative financial instruments and liabilities at fair value through profit or loss	12,207	22,678	26,291	8,151	5,609	16,238	91,174
Due to customers	2,111,931	478,588	835,252	240,849	1,279	31,565	3,699,464
Bonds issued	—	9,000	—	42,000	9,179	—	60,179
Other borrowings	1,827	1,283	13,096	15,978	15,790	4,190	52,164
Current tax liabilities	—	—	—	—	—	23,459	23,459
Retirement benefit obligations	—	—	—	—	—	7,052	7,052
Deferred income tax liabilities	—	—	—	—	—	2,136	2,136
Other liabilities	—	—	—	—	—	136,272	136,272
Total liabilities	2,340,506	562,885	950,234	310,877	31,857	288,170	4,484,529
Total interest sensitivity gap	(894,734)	33,843	464,652	402,985	241,871	6,902	255,519

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Bank

	As at 31 December 2005						
	Less than 1 month	Between 1 to 3 months	Between 4 to12 months	Between 1 to 5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and due from banks	12,963	—	—	—	—	25,312	38,275
Balances with central banks	251,351	—	—	—	—	33,022	284,373
Placements with banks and other financial institutions	160,496	64,610	13,197	5,351	—	—	243,654
Government certificates of indebtedness for bank notes issued	—	—	—	—	—	1,641	1,641
Precious metals	—	—	—	—	—	25,238	25,238
Trading assets and other financial instruments at fair value through profit or loss	2,587	7,675	17,506	40,731	13,583	—	82,082
Derivative financial instruments	—	—	—	—	—	11,329	11,329
Loans and advances to customers, net	447,603	265,919	1,032,329	21,545	17,256	4,090	1,788,742
Investment securities							
— available-for-sale	78,067	31,481	130,426	201,875	97,088	3,205	542,142
— held-to-maturity	42,279	70,698	147,654	98,065	56,447	—	415,143
— loans and receivables	24,763	11,368	5,393	259,785	42,601	—	343,910
Investments in subsidiaries	—	—	—	—	—	45,080	45,080
Investments in associates and joint ventures	—	—	—	—	—	45	45
Property and equipment	—	—	—	—	—	48,061	48,061
Investment property	—	—	—	—	—	461	461
Deferred income tax assets	—	—	—	—	—	20,389	20,389
Other assets	—	—	—	—	—	25,837	25,837
Total assets	1,020,109	451,751	1,346,505	627,352	226,975	243,710	3,916,402

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Bank

	As at 31 December 2005						
	Less than 1 month	Between 1 to 3 months	Between 4 to12 months	Between 1 to 5 years	Over 5 years	Non-interest bearing	Total
Liabilities							
Due to banks and other financial institutions	97,279	—	—	—	—	27,669	124,948
Due to central banks	29,910	20	—	—	—	100	30,030
Bank notes in circulation	—	—	—	—	—	1,786	1,786
Certificates of deposits and placements from banks and other financial institutions	83,104	53,078	75,041	2,524	—	2,176	215,923
Derivative financial instruments and liabilities at fair value through profit or loss	10,384	20,494	24,783	5,309	5,609	9,744	76,323
Due to customers	1,625,628	327,602	810,211	237,830	720	7,196	3,009,187
Bonds issued	—	9,000	—	42,000	9,179	—	60,179
Other borrowings	1,827	1,283	13,096	15,978	15,790	4,190	52,164
Current tax liabilities	—	—	—	—	—	22,440	22,440
Retirement benefit obligations	—	—	—	—	—	7,052	7,052
Deferred income tax liabilities	—	—	—	—	—	23	23
Other liabilities	—	—	—	—	—	112,534	112,534
Total liabilities	1,848,132	411,477	923,131	303,641	31,298	194,910	3,712,589
Total interest sensitivity gap	**(828,023)**	**40,274**	**423,374**	**323,711**	**195,677**	**48,800**	**203,813**

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

The tables below summarize the effective interest rate by major currencies for monetary financial instruments not carried at fair value through profit or loss:

Group

	As at 31 December 2006					
	RMB	USD	HKD	EURO	JPY	GBP
Assets						
Cash and due from banks	0.06%	1.74%	0.60%	0.11%	—	0.17%
Balances with central banks	1.68%	0.25%	0.17%	1.71%	—	—
Placements with banks and other financial institutions	2.64%	5.25%	4.06%	3.58%	0.38%	5.17%
Loans and advances to customers, net	5.92%	5.70%	5.19%	3.78%	1.10%	5.27%
Investment securities						
— available-for-sale	2.75%	5.29%	4.21%	3.23%	0.83%	4.97%
— held-to-maturity	2.75%	4.43%	4.04%	3.43%	—	5.50%
— loans and receivables	2.19%	5.40%	3.92%	—	0.28%	4.96%
Liabilities						
Due to banks and other financial institutions	1.10%	1.72%	1.43%	0.46%	0.14%	0.97%
Due to central banks	—	4.05%	2.96%	—	—	—
Certificates of deposits and placements from banks and other financial institutions	2.76%	4.92%	4.02%	3.66%	0.14%	3.66%
Due to customers	1.67%	2.97%	2.91%	1.19%	—	3.36%
Bonds issued	4.76%	8.42%	—	—	—	—
Other borrowings	—	4.66%	—	3.94%	1.90%	4.05%

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Bank

	As at 31 December 2006					
	RMB	USD	HKD	EURO	JPY	GBP
Assets						
Cash and due from banks	0.08%	1.88%	2.20%	0.03%	—	0.05%
Balances with central banks	1.68%	0.25%	0.14%	1.71%	—	—
Placements with banks and other financial institutions	2.64%	5.26%	4.03%	3.58%	0.39%	5.15%
Loans and advances to customers, net	5.92%	5.59%	4.89%	2.80%	1.08%	5.30%
Investment securities						
— available-for-sale	2.75%	5.24%	4.73%	3.19%	0.83%	4.36%
— held-to-maturity	2.74%	3.93%	3.57%	3.23%	—	5.29%
— loans and receivables	2.18%	5.41%	3.98%	—	0.28%	5.06%
Liabilities						
Due to banks and other financial institutions	1.10%	1.92%	0.96%	0.46%	0.14%	0.97%
Due to central banks	—	4.05%	2.98%	—	—	—
Certificates of deposits and placements from banks and other financial institutions	2.76%	4.90%	4.12%	3.66%	0.01%	3.66%
Due to customers	1.67%	2.47%	1.71%	1.04%	—	2.95%
Bonds issued	4.76%	8.42%	—	—	—	—
Other borrowings	—	3.81%	—	3.94%	1.90%	4.05%

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Group

	As at 31 December 2005					
	RMB	USD	HKD	EURO	JPY	GBP
Assets						
Cash and due from banks	0.04%	1.93%	0.57%	0.24%	—	0.14%
Balances with central banks	1.58%	0.09%	3.21%	2.28%	—	—
Placements with banks and other financial institutions	1.56%	4.18%	4.04%	2.29%	0.14%	4.57%
Loans and advances to customers, net	5.60%	4.79%	5.27%	2.60%	1.05%	4.64%
Investment securities						
— available-for-sale	2.53%	4.52%	3.51%	3.11%	1.20%	4.72%
— held-to-maturity	2.05%	3.90%	3.92%	2.86%	1.59%	4.79%
— loans and receivables	2.17%	4.27%	3.82%	2.30%	—	—
Liabilities						
Due to banks and other financial institutions	1.12%	1.39%	1.31%	0.32%	—	0.50%
Due to central banks	1.45%	1.15%	1.00%	2.36%	—	4.16%
Certificates of deposits and placements from banks and other financial institutions	2.52%	3.99%	3.89%	2.38%	0.19%	4.16%
Due to customers	1.59%	2.13%	2.83%	0.79%	—	2.64%
Bonds issued	4.60%	8.42%	—	—	—	—
Other borrowings	—	3.70%	—	4.13%	2.00%	4.11%

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

6 Interest rate risk (Continued)

Bank

	As at 31 December 2005					
	RMB	USD	HKD	EURO	JPY	GBP
Assets						
Cash and due from banks	0.07%	1.81%	2.65%	0.23%	—	0.07%
Balances with central banks	1.63%	0.08%	0.09%	2.28%	—	—
Placements with banks and other financial institutions	1.56%	4.15%	4.08%	2.29%	0.05%	4.54%
Loans and advances to customers, net	5.60%	4.73%	4.91%	2.52%	1.01%	4.58%
Investment securities						
— available-for-sale	2.53%	4.51%	4.27%	3.12%	1.20%	4.73%
— held-to-maturity	2.05%	3.68%	3.44%	2.64%	2.10%	4.95%
— loans and receivables	2.17%	4.30%	3.77%	2.30%	—	—
Liabilities						
Due to banks and other financial institutions	1.19%	1.33%	0.97%	0.32%	—	0.50%
Due to central banks	1.45%	1.15%	1.00%	2.36%	—	4.16%
Certificates of deposits and placements from banks and other financial institutions	2.52%	3.98%	4.09%	2.37%	0.19%	4.47%
Due to customers	1.60%	1.79%	1.63%	0.73%	—	2.23%
Bonds issued	4.60%	8.42%	—	—	—	—
Other borrowings	—	3.70%	—	4.13%	2.00%	4.11%

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk

The Group's objective in liquidity management is to ensure the availability of adequate funding at all times to meet its needs to fund deposit withdrawals and other liabilities as they fall due, as well as being able to meet its obligations to fund loan originations and commitments and to take advantage of new investment opportunities.

In developing its liquidity management strategy, the Group has considered its financing position, business development plans, market conditions and convertibility of currencies in the local market and developed a liquidity management plan in accordance with prudent principles. This plan addresses the Group's liquidity needs in multiple currencies and regions.

The Group's liquidity management policies related to assets encourage diversification and the maintenance of sufficient levels of liquid assets. The Group's policies related to liabilities focus on the stability of liabilities and the growth of the core deposit base.

In addition, the Group limits its loan to deposit ratio to 75%, as required by the PBOC. As at 31 December 2006 and 2005, the Domestic Operations of the Group are required to maintain reserves equal to 9.0%, and 7.5%, respectively, of total RMB denominated deposits and 4.0%, and 3.0%, respectively, of total foreign currency denominated deposits with the PBOC. Details are set out in Note V.13.

The tables below summarize the assets and liabilities of the Group and the Bank by relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

For purposes of these tables, loans and advances to customers are considered overdue only if principal payments are overdue. In addition, for loans and advances to customers that are repayable by installments, only the portion of the loan that is actually overdue is reported as overdue. Any part of the loan that is not due is reported according to residual maturity.

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk (Continued)

Group

	As at 31 December 2006							
	Overdue	On demand	Less than 1 month	Between 1–3 months	Between 4–12 months	Between 1–5 years	Over 5 years	Total
Assets								
Cash and due from banks	—	39,812	—	—	—	—	—	39,812
Balances with central banks	—	102,017	277,614	—	—	—	—	379,631
Placements with banks and other financial institutions	—	—	264,913	106,193	27,909	123	—	399,138
Government certificates of indebtedness for bank notes issued	—	36,626	—	—	—	—	—	36,626
Precious metals	—	42,083	—	—	—	—	—	42,083
Trading assets and other financial instruments at fair value through profit or loss	—	—	9,611	10,043	14,868	41,703	39,603	115,828
Derivative financial instruments	—	6,466	2,516	1,699	8,181	3,321	2,654	24,837
Loans and advances to customers, net	48,388	32,925	129,262	251,375	646,647	624,209	604,920	2,337,726
Investment securities								
— available-for-sale	—	—	23,457	47,972	132,998	293,914	316,837	815,178
— held-to-maturity	—	—	26,616	57,308	102,015	186,741	88,460	461,140
— loans and receivables	—	—	52,744	62,973	85,706	250,169	48,744	500,336
Investments in associates and joint ventures	—	—	—	—	—	147	5,784	5,931
Property and equipment	—	—	—	—	—	—	86,200	86,200
Investment property	—	—	—	—	—	—	8,221	8,221
Deferred income tax assets	—	—	—	—	23	21,321	52	21,396
Other assets	366	8,473	10,994	6,422	16,733	4,131	6,451	53,570
Total assets	48,754	268,402	797,727	543,985	1,035,080	1,425,779	1,207,926	5,327,653

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk (Continued)

Group

	As at 31 December 2006							
	Overdue	On demand	Less than 1 month	Between 1–3 months	Between 4–12 months	Between 1–5 years	Over 5 years	Total
Liabilities								
Due to banks and other financial institutions	—	178,777	—	—	—	—	—	178,777
Due to central banks	—	11,116	4,412	5,078	21,768	—	—	42,374
Bank notes in circulation	—	36,823	—	—	—	—	—	36,823
Certificates of deposits and placements from banks and other financial institutions	—	2,515	79,096	19,698	25,160	20,439	—	146,908
Derivative financial instruments and liabilities at fair value through profit or loss	—	2,977	22,020	16,288	40,967	18,639	12,157	113,048
Due to customers	—	1,854,295	671,453	439,215	847,843	277,401	911	4,091,118
Bonds issued	—	—	—	—	—	—	60,173	60,173
Other borrowings	—	—	947	743	5,754	22,633	33,321	63,398
Current tax liabilities	—	14	26	6	17,792	271	40	18,149
Retirement benefit obligations	—	—	82	163	713	3,087	3,399	7,444
Deferred income tax liabilities	—	—	—	—	1,808	1,201	20	3,029
Other liabilities	—	71,136	15,508	7,197	31,699	11,894	16,022	153,456
Total liabilities	—	2,157,653	793,544	488,388	993,504	355,565	126,043	4,914,697
Net liquidity gap	48,754	(1,889,251)	4,183	55,597	41,576	1,070,214	1,081,883	412,956

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk (Continued)

Bank

	As at 31 December 2006							
	Overdue	On demand	Less than 1 month	Between 1–3 months	Between 4–12 months	Between 1–5 years	Over 5 years	Total
Assets								
Cash and due from banks	—	37,842	—	—	—	—	—	37,842
Balances with central banks	—	77,810	277,071	—	—	—	—	354,881
Placements with banks and other financial institutions	—	40	214,335	59,378	21,562	7,687	—	303,002
Government certificates of indebtedness for bank notes issued	—	1,713	—	—	—	—	—	1,713
Precious metals	—	40,542	—	—	—	—	—	40,542
Trading assets and other financial instruments at fair value through profit or loss	—	—	2,967	7,254	10,311	33,203	22,846	76,581
Derivative financial instruments	—	77	1,726	1,391	7,863	2,861	2,445	16,363
Loans and advances to customers, net	46,546	2,730	118,855	233,901	605,283	481,126	483,424	1,971,865
Investment securities								
— available-for-sale	—	—	21,494	42,162	125,821	250,249	267,013	706,739
— held-to-maturity	—	—	21,077	47,967	62,063	98,480	57,811	287,398
— loans and receivables	—	—	48,966	48,310	62,417	250,169	48,744	458,606
Investment in subsidiaries	—	—	—	—	—	376	45,075	45,451
Investments in associates and joint ventures	—	—	—	—	—	10	11	21
Property and equipment	—	—	—	—	—	—	49,473	49,473
Investment property	—	—	—	—	—	—	620	620
Deferred income tax assets	—	—	—	—	—	21,791	52	21,843
Other assets	192	3,625	1,691	5,741	15,591	56	3,376	30,272
Total assets	46,738	164,379	708,182	446,104	910,911	1,146,008	980,890	4,403,212

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk (Continued)

Bank

	As at 31 December 2006							
	Overdue	On demand	Less than 1 month	Between 1–3 months	Between 4–12 months	Between 1–5 years	Over 5 years	Total
Liabilities								
Due to banks and other financial institutions	—	164,376	—	—	—	—	—	164,376
Due to central banks	—	11,091	4,412	5,078	21,768	—	—	42,349
Bank notes in circulation	—	1,909	—	—	—	—	—	1,909
Certificates of deposits and placements from banks and other financial institutions	—	830	77,969	23,610	25,614	18,573	—	146,596
Derivative financial instruments and liabilities at fair value through profit or loss	—	—	16,824	13,619	34,794	14,281	11,566	91,084
Due to customers	—	1,545,119	357,605	355,959	822,620	276,664	598	3,358,565
Bonds issued	—	—	—	—	—	—	60,173	60,173
Other borrowings	—	—	947	743	4,870	17,862	21,584	46,006
Current tax liabilities	—	14	22	6	16,404	271	40	16,757
Retirement benefit obligations	—	—	82	163	713	3,087	3,399	7,444
Deferred income tax liabilities	—	—	—	—	8	4	20	32
Other liabilities	—	58,809	7,114	5,454	30,688	10,309	153	112,527
Total liabilities	—	1,782,148	464,975	404,632	957,479	341,051	97,533	4,047,818
Net liquidity gap	46,738	(1,617,769)	243,207	41,472	(46,568)	804,957	883,357	355,394

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk (Continued)

Group

	As at 31 December 2005							
	Overdue	On demand	Less than 1 month	Between 1–3 months	Between 4–12 months	Between 1–5 years	Over 5 years	Total
Assets								
Cash and due from banks	—	41,082	—	—	—	—	—	41,082
Balances with central banks	—	113,872	202,030	1,019	20	—	—	316,941
Placements with banks and other financial institutions	—	—	220,629	92,650	18,707	113	—	332,099
Government certificates of indebtedness for bank notes issued	—	35,586	—	—	—	—	—	35,586
Precious metals	—	26,974	—	—	—	—	—	26,974
Trading assets and other financial instruments at fair value through profit or loss	—	—	6,301	3,113	15,287	56,028	31,053	111,782
Derivative financial instruments	—	3,890	2,042	753	1,583	5,347	3,193	16,808
Loans and advances to customers, net	40,150	28,363	107,549	220,426	795,450	506,258	453,916	2,152,112
Investment securities								
— available-for-sale	—	292	6,926	17,622	128,532	255,548	193,301	602,221
— held-to-maturity	—	—	31,360	70,239	160,474	247,593	97,793	607,459
— loans and receivables	—	—	29,505	16,996	11,520	260,085	43,745	361,851
Investments in associates and joint ventures	—	—	—	—	—	407	4,654	5,061
Property and equipment	—	—	—	—	—	—	62,417	62,417
Investment property	—	—	—	—	—	—	8,511	8,511
Deferred income tax assets	—	—	—	—	2	20,502	—	20,504
Other assets	302	4,418	7,823	6,743	10,145	3,812	5,397	38,640
Total assets	40,452	254,477	614,165	429,561	1,141,720	1,355,693	903,980	4,740,048

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk (Continued)

Group

	As at 31 December 2005							
	Overdue	On demand	Less than 1 month	Between 1–3 months	Between 4–12 months	Between 1–5 years	Over 5 years	Total
Liabilities								
Due to banks and other financial institutions	—	134,217	—	—	—	—	—	134,217
Due to central banks	—	29,506	529	20	—	—	—	30,055
Bank notes in circulation	—	35,731	—	—	—	—	—	35,731
Certificates of deposits and placements from banks and other financial institutions	—	640	79,584	47,363	50,464	34,575	—	212,626
Derivative financial instruments and liabilities at fair value through profit or loss	—	1,805	9,124	9,301	22,996	38,091	9,857	91,174
Due to customers	—	1,615,637	521,284	441,468	840,668	278,098	2,309	3,699,464
Bonds issued	—	—	—	—	—	—	60,179	60,179
Other borrowings	—	—	1,046	816	5,361	20,840	24,101	52,164
Current tax liabilities	—	13	—	—	23,446	—	—	23,459
Retirement benefit obligations	—	—	76	151	661	2,883	3,281	7,052
Deferred income tax liabilities	—	—	—	—	1,782	354	—	2,136
Other liabilities	—	74,494	14,906	5,585	28,384	12,170	733	136,272
Total liabilities	—	1,892,043	626,549	504,704	973,762	387,011	100,460	4,484,529
Net liquidity gap	40,452	(1,637,566)	(12,384)	(75,143)	167,958	968,682	803,520	255,519

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk (Continued)

Bank

	As at 31 December 2005							
	Overdue	On demand	Less than 1 month	Between 1–3 months	Between 4–12 months	Between 1–5 years	Over 5 years	Total
Assets								
Cash and due from banks	—	38,275	—	—	—	—	—	38,275
Balances with central banks	—	82,936	201,437	—	—	—	—	284,373
Placements with banks and other financial institutions	—	—	160,496	62,996	14,748	5,414	—	243,654
Government certificates of indebtedness for bank notes issued	—	1,641	—	—	—	—	—	1,641
Precious metals	—	25,238	—	—	—	—	—	25,238
Trading assets and other financial instruments at fair value through profit or loss	—	—	1,229	1,972	12,465	44,796	21,620	82,082
Derivative financial instruments	—	—	798	521	1,587	5,263	3,160	11,329
Loans and advances to customers, net	38,671	837	98,739	200,848	760,911	362,141	326,595	1,788,742
Investment securities								
— available-for-sale	—	—	5,132	14,716	126,386	221,832	174,076	542,142
— held-to-maturity	—	—	29,117	59,606	126,218	122,175	78,027	415,143
— loans and receivables	—	—	24,763	11,368	3,948	260,085	43,746	343,910
Investment in subsidiaries and joint ventures	—	—	—	—	—	421	44,659	45,080
Investments in associates	—	—	—	—	—	1	44	45
Property and equipment	—	—	—	—	—	—	48,061	48,061
Investment property	—	—	—	—	—	—	461	461
Deferred income tax assets	—	—	—	—	—	20,389	—	20,389
Other assets	291	2,689	1,782	6,485	9,399	558	4,633	25,837
Total assets	38,962	151,616	523,493	358,512	1,055,662	1,043,075	745,082	3,916,402

III FINANCIAL RISK MANAGEMENT (Continued)

7 Liquidity risk (Continued)

Bank

	As at 31 December 2005							
	Overdue	On demand	Less than 1 month	Between 1–3 months	Between 4–12 months	Between 1–5 years	Over 5 years	Total
Liabilities								
Due to banks and other financial institutions	—	124,948	—	—	—	—	—	124,948
Due to central banks	—	29,481	529	20	—	—	—	30,030
Bank notes in circulation	—	1,786	—	—	—	—	—	1,786
Certificates of deposits and placements from banks and other financial institutions	—	535	82,241	49,993	50,320	32,834	—	215,923
Derivative financial instruments and liabilities at fair value through profit or loss	—	—	6,937	7,460	20,048	32,766	9,112	76,323
Due to customers	—	1,323,694	301,258	292,438	815,485	274,519	1,793	3,009,187
Bonds issued	—	—	—	—	—	—	60,179	60,179
Other borrowings	—	—	1,046	816	5,361	20,840	24,101	52,164
Current tax liabilities	—	13	—	—	22,427	—	—	22,440
Retirement benefit obligations	—	—	76	151	661	2,883	3,281	7,052
Deferred income tax liabilities	—	—	—	—	—	23	—	23
Other liabilities	—	61,151	6,366	5,238	27,494	11,722	563	112,534
Total liabilities	—	1,541,608	398,453	356,116	941,796	375,587	99,029	3,712,589
Net liquidity gap	38,962	(1,389,992)	125,040	2,396	113,866	667,488	646,053	203,813

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Group's business. It is unusual for a banks' asset and liability exposures to be completely matched, as transactions vary in nature and have different settlement terms. An unmatched position potentially enhances profitability, but also increases the 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 interest rates and exchange rates.

Liquidity requirements to support calls under guarantees and standby letters of credit are considerably less than the amount of the commitment because the Group does not generally expect the third party to draw funds under the agreement. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, as many of these commitments will expire or terminate without being funded and therefore these amounts are not included in the liquidity risk tables above.

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

8 Insurance risk

Insurance contracts are mainly sold in Hong Kong and are mainly denominated in Hong Kong Dollars. The risk under any one insurance contract is the possibility that the insured event occurs and the uncertainty of the amount of the resulting claim. This risk is inherently random and, therefore, unpredictable. The Group manages its portfolio of insurance risks through its underwriting policies, portfolio management techniques, and claims processing.

For a portfolio of insurance contracts where the theory of probability is applied to pricing and provisioning, the principal risk that the Group faces under its insurance contracts is that the actual claims and benefit payments exceed the carrying amount of the insurance liabilities. This could occur because the frequency or severity of the claims and benefits are greater than estimated. Insurance events are random and the actual number and amount of claims and benefits will vary from year to year from the level established using statistical techniques.

The Group manages these risks through its underwriting strategy, adequate reinsurance arrangements and proactive claims handling. The underwriting strategy attempts to ensure that the underwritten risks are well diversified in terms of type and amount of risk and industry.

Uncertainty in the estimation of future benefit payments and premium receipts for long-term insurance contracts arises from the unpredictability of long-term changes in overall levels of mortality. In order to assess the uncertainty due to the mortality assumption and lapse assumption, the Group conducted mortality studies and lapse studies in order to determine the appropriate assumptions. These studies reflect consistent results in both assumptions with appropriate margin.

9 Fair values of financial assets and liabilities

Fair value estimates are made at a specific point in time based on relevant market information and information about the various financial instruments. The following methods and assumptions were used to estimate the fair value of each class of financial instrument which were not presented on the Group's and the Bank's balance sheet at their fair value.

Cash and due from banks, balances with central banks, placements with banks and other financial institutions, due to banks and other financial institutions and due to central banks

These financial assets and liabilities generally have a maturity or re-pricing of less than one year and their carrying value approximates fair value.

III FINANCIAL RISK MANAGEMENT (Continued)

9 Fair values of financial assets and liabilities (Continued)

Loans and advances to customers and investment securities classified as loans and receivables

Loans and advances are recorded, net of the allowance for impairment losses. The fair value of loans and advances represents the discounted amount of their estimated future cash flows discounted at current market rates (Note IV.2).

Held-to-maturity investment securities

The fair value of held-to-maturity investment securities is based on "bid" market prices or broker/dealer price quotations. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

Due to customers, certificates of deposits and placements from banks and other financial institutions

The fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand.

The fair value of fixed interest-bearing deposits and placements without a quoted market price is based on discounted cash flows using interest rates for new debt issuances with similar remaining maturities.

Bonds issued and other borrowings

The fair value of these instruments is calculated based on quoted "ask" market prices. For those instruments where quoted market prices are not available, a discounted cash flow model is used based on a current market rate appropriate for the nature of the obligation and the remaining term to maturity.

(Amount in millions of Renminbi, unless otherwise stated)

III FINANCIAL RISK MANAGEMENT (Continued)

9 Fair values of financial assets and liabilities (Continued)

The following tables summarize the carrying amounts and the approximate fair values of those financial assets and liabilities not presented on the Group's and the Bank's balance sheets at their fair value.

	As at 31 December 2006			
	Group		Bank	
	Carrying value	Fair value	Carrying value	Fair value
Financial assets				
Loans and advances to customers, net	**2,337,726**	**2,337,710**	**1,971,865**	**1,971,846**
Investment securities				
— held-to-maturity	**461,140**	**459,897**	**287,398**	**287,082**
— loans and receivables	**500,336**	**500,359**	**458,606**	**458,581**
Financial liabilities				
Certificates of deposit and placements from banks and other financial institutions	**146,908**	**146,967**	**146,596**	**146,655**
Due to customers	**4,091,118**	**4,091,513**	**3,358,565**	**3,358,960**
Bonds issued	**60,173**	**60,931**	**60,173**	**60,931**
Other borrowings	**63,398**	**57,441**	**46,006**	**40,049**

	As at 31 December 2005			
	Group		Bank	
	Carrying value	Fair value	Carrying value	Fair value
Financial assets				
Loans and advances to customers, net	2,152,112	2,152,232	1,788,742	1,788,873
Investment securities				
— held-to-maturity	607,459	605,287	415,143	414,341
— loans and receivables	361,851	361,613	343,910	343,692
Financial liabilities				
Certificates of deposit and placements from banks and other financial institutions	212,626	212,689	215,923	215,988
Due to customers	3,699,464	3,700,445	3,009,187	3,010,241
Bonds issued	60,179	62,071	60,179	62,071
Other borrowings	52,164	42,547	52,164	42,547

III FINANCIAL RISK MANAGEMENT (Continued)

10 Fiduciary activities

The Group provides custody, entrusted loan administration, trustee and investment management services to third parties. Assets that are held in a fiduciary capacity are not included in these financial statements. As at 31 December 2006 and 2005, the balances of securities and other financial instruments held in custody accounts amounted to approximately RMB707,953 million and RMB562,823 million, respectively; entrusted loans amounted to approximately RMB98,046 million and RMB51,626 million, respectively; and the balances of precious metals held in custody accounts amounted to approximately RMB3,150 million and RMB2,696 million, respectively.

IV CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Areas susceptible to changes in essential estimates and judgments, which affect the carrying value of assets and liabilities, are set out below. It is impracticable to determine the effect of changes to either the key assumptions discussed below or other estimation uncertainties. It is possible that actual results may be materially different from the estimates referred to below.

1 Impairment losses on loans and advances

The Group reviews its loan portfolios to assess impairment on a periodic 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 income statement, the Group makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and advances 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.

(Amount in millions of Renminbi, unless otherwise stated)

IV CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (Continued)

2 Fair value of financial instruments

The fair values of financial instruments that are not quoted in active markets are determined by using valuation techniques. Valuation techniques used include discounted cash flows analysis and models. To the extent practical, models use only observable data, however areas such as credit risk (both own and counterparty's), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect reported fair value of financial instruments. With respect to PRC government obligations related to large-scale policy directed financing transactions, such as the one described in Note V.18(4), fair value is determined using the stated interest rate of the related instrument. In this regard, there are no relevant market prices or yields reflecting arm's length transactions of a comparable size and tenor, available.

3 Held-to-maturity investments

The Group follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgment. In making this judgment, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to hold these investments to maturity other than for specific circumstances defined in IAS 39 such as, selling an insignificant amount close to maturity, it will be required to reclassify the entire portfolio of assets as available-for-sale.

4 Employee retirement benefit obligations

As described more fully in Notes II.22 (2) and V.31, the Bank has established liabilities in connection with benefits paid to certain retired and early retired employees. The amounts of employee benefit expense and these liabilities are dependent on assumptions used in calculating such amounts. These assumptions include discount rates, pension benefit inflation rates, medical benefit inflation rates, and other factors. Actual results that differ from the assumptions are recognized immediately and, therefore, affect recognized expense in the year in which such differences arise. While management believes that its assumptions are appropriate, differences in actual experience or changes in assumptions may affect the Bank's expense related to its employee retirement benefit obligations.

IV CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (Continued)

5 Income taxes

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

V NOTES TO THE FINANCIAL STATEMENTS

1 Segment information

The Group's businesses operate in three principal geographical areas: the Chinese Mainland, Hong Kong and Macau, and other overseas locations. Significant other overseas locations include New York, London, Singapore and Tokyo. Within Hong Kong and Macau, BOCHK Holdings and its intermediate holding companies, collectively referred to as BOC Hong Kong Group, account for the majority of the Group's overseas operating activities.

The geographical analysis of revenues, segment results, segment assets, segment liabilities and capital expenditure reflects the process through which the Group's operating activities are managed. In accordance with the Group's organizational structure and its internal financial reporting process, the Group has determined that geographical segments should be presented as its primary segment.

Interest and fee income, total assets, total liabilities, credit commitments and capital expenditure have generally been based on the country in which the branch or subsidiary is located.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 Segment information (Continued)

As at and for the year ended 31 December 2006

		Hong Kong & Macau					
	Chinese Mainland	BOC Hong Kong Group[1]	Others	Sub-total	Other overseas locations	Elimination	Total
Interest income	167,024	41,061	4,870	45,931	7,563	(5,184)	215,334
Interest expense	(65,575)	(24,668)	(3,158)	(27,826)	(5,750)	5,188	(93,963)
Net interest income	101,449	16,393	1,712	18,105	1,813	4	121,371
Fee and commission income	9,593	4,893	2,311	7,204	911	(569)	17,139
Fee and commission expense	(964)	(1,306)	(529)	(1,835)	(82)	65	(2,816)
Net fee and commission income	8,629	3,587	1,782	5,369	829	(504)	14,323
Net trading (losses)/gains	(3,927)	1,835	570	2,405	(22)	—	(1,544)
Net gains/(losses) on investment securities	664	(5)	434	429	39	—	1,132
Other operating income[1]	1,695	7,317	4,044	11,361	85	(45)	13,096
Impairment (losses)/write back on loans and advances	(15,546)	1,836	1,147	2,983	221	—	(12,342)
Operating expenses and others[1]	(50,357)	(13,431)	(3,520)	(16,951)	(1,483)	60	(68,731)
Operating profit	42,607	17,532	6,169	23,701	1,482	(485)	67,305
Share of results of associates and joint ventures	—	4	683	687	—	(55)	632
Profit before income tax	42,607	17,536	6,852	24,388	1,482	(540)	67,937
Income tax expense	(16,138)	(2,902)	(533)	(3,435)	(290)	190	(19,673)
Profit for the year	26,469	14,634	6,319	20,953	1,192	(350)	48,264

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 Segment information (Continued)

As at and for the year ended 31 December 2006 (Continued)

		Hong Kong & Macau					
	Chinese Mainland	BOC Hong Kong Group[1]	Others	Sub-total	Other overseas locations	Elimination	Total
Segment assets	4,220,394	926,023	152,125	1,078,148	214,766	(191,586)	5,321,722
Investments in associates and joint ventures	1	59	5,871	5,930	—	—	5,931
Total assets	4,220,395	926,082	157,996	1,084,078	214,766	(191,586)	5,327,653
Segment liabilities	3,921,219	844,984	135,405	980,389	204,675	(191,586)	4,914,697
Other segment items:							
Capital expenditure	5,954	740	666	1,406	52	—	7,412
Depreciation and amortization	5,193	557	188	745	88	—	6,026
Credit commitments	884,607	188,664	14,812	203,476	61,297	(61,558)	1,087,822

(1) Other operating income and operating expenses and others of BOC Hong Kong Group for 2006 included insurance premium earned and insurance benefits and claims amounting to RMB6,349 million and RMB6,820 million respectively. In 2006, BOC Hong Kong Group acquired a 51% equity interest in BOC Group Life Assurance Company Limited from Bank of China Group Insurance Company Limited, a wholly owned subsidiary of the Group. The results of BOC Group Life Assurance Company Limited were reported under "Others" of the Hong Kong & Macau segment in 2005.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 Segment information (Continued)

As at and for the year ended 31 December 2005

		Hong Kong & Macau					
	Chinese Mainland	BOC Hong Kong Group	Others	Sub-total	Other overseas locations	Elimination	Total
Interest income	134,177	27,873	3,687	31,560	5,526	(3,315)	167,948
Interest expense	(51,094)	(13,675)	(1,651)	(15,326)	(3,835)	3,315	(66,940)
Net interest income	83,083	14,198	2,036	16,234	1,691	—	101,008
Fee and commission income	7,004	4,119	715	4,834	889	(29)	12,698
Fee and commission expense	(1,797)	(1,110)	(498)	(1,608)	(75)	29	(3,451)
Net fee and commission income	5,207	3,009	217	3,226	814	—	9,247
Net trading gains	1,889	1,878	126	2,004	390	—	4,283
Net (losses)/gains on investment securities	(875)	(86)	376	290	3	—	(582)
Other operating income	2,092	2,402	6,434	8,836	222	—	11,150
Impairment (losses)/write back on loans and advances	(15,345)	2,635	641	3,276	583	—	(11,486)
Operating expenses and others	(46,375)	(5,986)	(5,845)	(11,831)	(1,778)	—	(59,984)
Operating profit	29,676	18,050	3,985	22,035	1,925	—	53,636
Share of results of associates and joint ventures	19	2	154	156	—	—	175
Profit before income tax	29,695	18,052	4,139	22,191	1,925	—	53,811
Income tax expense	(18,911)	(2,880)	(142)	(3,022)	(320)	—	(22,253)
Profit for the year	10,784	15,172	3,997	19,169	1,605	—	31,558

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 Segment information (Continued)

As at and for the year ended 31 December 2005 (Continued)

		Hong Kong & Macau					
	Chinese Mainland	BOC Hong Kong Group	Others	Sub-total	Other overseas locations	Elimination	Total
Segment assets	3,736,929	848,767	116,045	964,812	186,995	(153,749)	4,734,987
Investments in associates and joint ventures	1	64	4,996	5,060	—	—	5,061
Total assets	3,736,930	848,831	121,041	969,872	186,995	(153,749)	4,740,048
Segment liabilities	3,586,428	770,166	102,829	872,995	178,855	(153,749)	4,484,529
Other segment items:							
Capital expenditure	5,379	592	68	660	67	—	6,106
Depreciation and amortization	5,528	543	127	670	116	—	6,314
Credit commitments	699,066	168,203	14,131	182,334	52,434	(38,072)	895,762

Business segments comprise the Group's secondary segment. The Group provides services through six main business segments: corporate banking, personal banking, treasury operations, investment banking, insurance and other operations. Segment revenue, segment results, segment assets and capital expenditure presented in business segments include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Funding is provided to and from individual business segments through treasury operations as part of the asset and liability management process. The pricing of these transactions is based on management's assessment of its average cost of funding and interest bearing assets and liabilities. The transactions are eliminated on consolidation.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 Segment information (Continued)

Corporate banking — providing services to corporate customers including current accounts, deposits, overdrafts, lending, trade related products and other credit facilities, custody, foreign currency and derivative products.

Personal banking — providing services to retail customers including current accounts, savings, deposits, investment savings products, credit and debit cards, consumer loans and mortgages and wealth management.

Treasury operations — consisting of foreign exchange transactions, customer-based interest rate and foreign exchange derivative transactions, money market transactions, proprietary trading and asset-liability management. The results of this segment include the inter-segment funding income and expenses, resulting from interest bearing assets and liabilities; and foreign currency translation gains and losses.

Investment banking — consisting of debt and equity underwriting and financial advisory, sales and trading of securities, stock brokerage, investment research and asset management services, and private equity investment services.

Insurance — underwriting of general and life insurance business and insurance agency services.

Other operations of the Group comprise investment holding and other miscellaneous activities, none of which constitutes a separately reportable segment or can be allocated on a reasonable basis.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 Segment information (Continued)

As at and for the year ended 31 December 2006

	Corporate banking	Personal banking	Treasury operations	Investment banking	Insurance	Others	Elimination	Total
Interest income	96,920	88,291	84,521	679	594	536	(56,207)	215,334
Interest expenses	(41,111)	(51,877)	(54,661)	(543)	(19)	(1,963)	56,211	(93,963)
Net interest income/(expense)	55,809	36,414	29,860	136	575	(1,427)	4	121,371
Fee and commission income	7,039	7,774	930	2,039	3	385	(1,031)	17,139
Fee and commission expense	(365)	(1,537)	(171)	(396)	(546)	(270)	469	(2,816)
Net fee and commission income/ (expense)	6,674	6,237	759	1,643	(543)	115	(562)	14,323
Net trading gains/(losses)	4,105	2,264	(8,810)	310	546	40	1	(1,544)
Net gains/(losses) on investment securities	—	—	695	—	—	437	—	1,132
Other operating income*	136	396	32	149	7,968	5,700	(1,285)	13,096
Impairment losses on loans and advances	(11,542)	(794)	—	(6)	—	—	—	(12,342)
Operating expenses and others*	(22,904)	(27,121)	(8,818)	(1,177)	(7,965)	(2,096)	1,350	(68,731)
Operating profit	32,278	17,396	13,718	1,055	581	2,769	(492)	67,305
Share of results of associates and joint ventures	—	—	—	238	2	440	(48)	632
Profit before income tax	32,278	17,396	13,718	1,293	583	3,209	(540)	67,937
Income tax expense								(19,673)
Profit for the year								48,264
Segment assets	1,795,152	687,553	2,725,362	22,755	19,933	108,722	(37,755)	5,321,722
Investments in associates and joint ventures	—	—	—	911	244	4,844	(68)	5,931
Total assets	1,795,152	687,553	2,725,362	23,666	20,177	113,566	(37,823)	5,327,653
Capital expenditure	1,542	2,744	105	24	19	2,978	—	7,412

* Other operating income includes insurance premium income earned and operating expenses and others include insurance benefits and claims.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 Segment information (Continued)

As at and for the year ended 31 December 2005

	Corporate banking	Personal banking	Treasury operations	Investment banking	Insurance	Others	Elimination	Total
Interest income	83,217	68,471	56,519	478	407	359	(41,503)	167,948
Interest expenses	(31,913)	(36,169)	(38,466)	(371)	—	(1,524)	41,503	(66,940)
Net interest income/(expense)	51,304	32,302	18,053	107	407	(1,165)	—	101,008
Fee and commission income	5,447	5,876	898	573	3	131	(230)	12,698
Fee and commission expense	(314)	(2,167)	(366)	(205)	(497)	(132)	230	(3,451)
Net fee and commission income/ (expense)	5,133	3,709	532	368	(494)	(1)	—	9,247
Net trading gains/(losses)	4,278	2,067	(2,024)	262	(309)	9	—	4,283
Net (losses)/gains on investment securities	—	—	(880)	—	—	298	—	(582)
Other operating income*	153	400	9	75	5,395	6,109	(991)	11,150
Impairment (losses)/write back on loans and advances	(12,708)	1,147	—	(14)	—	89	—	(11,486)
Operating expenses and others*	(21,127)	(25,508)	(7,105)	(524)	(4,665)	(2,046)	991	(59,984)
Operating profit	27,033	14,117	8,585	274	334	3,293	—	53,636
Share of results of associates and joint ventures	—	—	—	42	—	133	—	175
Profit before income tax	27,033	14,117	8,585	316	334	3,426	—	53,811
Income tax expense								(22,253)
Profit for the year								31,558
Segment assets	1,655,351	599,263	2,397,839	14,418	12,316	74,224	(18,424)	4,734,987
Investments in associates and joint ventures	—	—	—	668	—	4,393	—	5,061
Total assets	1,655,351	599,263	2,397,839	15,086	12,316	78,617	(18,424)	4,740,048
Capital expenditure	1,296	2,628	86	—	7	2,089	—	6,106

* Other operating income includes insurance premium income earned and operating expenses and others include insurance benefits and claims.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

1 Segment information (Continued)

With effect from 1 January 2006, the internal funds transfer pricing mechanism of the Bank was revised and the above tabulation of segment information is calculated on this new basis. The new pricing mechanism is based on market deposit and lending rates, adjusted for pre-determined margins. These margins reflect differentiation based on product features and maturity. Previously, blended mid prices between the Bank's average cost of funding and average yield on interest bearing assets were used, without product or maturity differentiation. The intent of the change is to better reflect actual market conditions and the asset-liability management process.

The effect of the change in basis of pricing between business segments for the year ended 31 December 2005 is summarized below. Under the new basis , the net interest income of the Treasury operation has increased as the new basis has resulted in an increase in the inter-segment pricing margin in relation to the funding provided by Treasury operations to Corporate and Personal banking.

Year ended 31 December 2005

	Corporate banking	Personal banking	Treasury operations	Investment banking	Insurance	Others	Total
Net interest income as reported previously	52,215	37,008	12,436	107	407	(1,165)	101,008
Effect of change — (decrease)/increase	(911)	(4,706)	5,617	—	—	—	—
Net interest income as revised	51,304	32,302	18,053	107	407	(1,165)	101,008
Operating profit as reported previously	27,944	18,823	2,968	274	334	3,293	53,636
Effect of change — (decrease)/increase	(911)	(4,706)	5,617	—	—	—	—
Operating profit as revised	27,033	14,117	8,585	274	334	3,293	53,636
Profit before income tax as reported previously	27,944	18,823	2,968	316	334	3,426	53,811
Effect of change — (decrease)/increase	(911)	(4,706)	5,617	—	—	—	—
Profit before income tax as revised	27,033	14,117	8,585	316	334	3,426	53,811

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

2 Net interest income

	Year ended 31 December	
	2006	2005
Interest income		
Loans and advances to customers	**128,934**	110,313
Investment securities	**67,195**	44,938
Due from banks and other financial institutions	**19,205**	12,697
Sub-total	**215,334**	167,948
Interest expense		
Due to customers	**(79,939)**	(55,914)
Due to banks and other financial institutions	**(9,393)**	(6,512)
Other borrowed funds	**(4,631)**	(4,514)
Sub-total	**(93,963)**	(66,940)
Net interest income	**121,371**	101,008

Included in interest income is RMB628 million and RMB529 million related to the unwinding of the discount on the allowance for identified impaired loans for the years ended 31 December 2006 and 2005 respectively (Notes V.17).

3 Net fee and commission income

	Year ended 31 December	
	2006	2005
Agency commissions	**4,621**	2,735
Settlement and clearing fees	**3,848**	2,941
Credit commitment fees	**3,064**	2,693
Bank card fees	**2,937**	2,340
Custodian and other fiduciary service fees	**531**	483
Others	**2,138**	1,506
Fee and commission income	**17,139**	12,698
Fee and commission expense	**(2,816)**	(3,451)
Net fee and commission income	**14,323**	9,247

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

4 Net trading (losses)/gains

	Year ended 31 December	
	2006	2005
Net (losses)/gains from foreign exchange and foreign exchange products[1]	**(2,290)**	2,226
Net (losses)/gains from precious metal transactions	**(68)**	150
Net gains from interest rate instruments	**492**	1,753
Net gains from trading equity securities	**324**	130
Others	**(2)**	24
	(1,544)	4,283

(1) The net (losses)/gains from foreign exchange and foreign exchange products include spread income in respect of the Group's operations in foreign exchange transactions business, realised and unrealised gains/losses of foreign exchange derivatives, and exchange differences arising from the retranslation of foreign currency denominated monetary assets and liabilities.

In connection with the retranslation of its foreign currency denominated monetary assets and liabilities, the Group recognised losses of approximately RMB14.2 billion (2005: RMB8.5 billion). These foreign currency translation losses mainly resulted from an increase in the Group's on balance sheet USD exposure and further appreciation of RMB against USD during 2006. These losses were partially offset by the change in fair value gains of the Huijin option RMB1.9 billion (2005: RMB3.2 billion), the USD/RMB swaps of RMB2.2 billion (2005: RMB0.01 billion), and a gain of RMB0.3 billion (2005: RMB0.6 billion) arising from other foreign exchange related products (Note III.5). While the net changes in fair value of the USD/RMB swaps above include the swap funding costs borne by the Bank, the related interest on the higher yielding financial assets denominated in USD earned by the Bank is reported in the Interest income.

5 Net gains/(losses) on investment securities

	Year ended 31 December	
	2006	2005
Derecognition of available-for-sale securities	**1,178**	(606)
(Provision)/write back for impairment losses	**(46)**	24
	1,132	(582)

The net gains on derecognition of available-for-sale securities for the year ended 31 December 2006 include a gain of RMB1,309 million arising from the disposal of the Group's equity interest in a state owned enterprise to the parent company of this enterprise. Such interest was previously acquired by the Group through a debt restructuring.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

6 Other operating income

	Year ended 31 December	
	2006	2005
Insurance premiums		
— Long term insurance contracts	**6,349**	3,807
— General insurance contracts	**1,359**	1,430
Gains on disposal of subsidiaries and associates	**789**	320
Gains on disposal of property and equipment and other assets	**717**	870
Changes in fair value of investment properties	**595**	1,697
Dividend income	**186**	194
Others	**3,101**	2,832
Total	**13,096**	11,150

7 Operating expenses and others

	Year ended 31 December	
	2006	2005
Staff costs (Note V.8)	**30,896**	27,106
General operating and administrative expenses[1]	**14,603**	13,251
Depreciation and amortization	**6,026**	6,314
Business and other taxes	**6,462**	5,680
Insurance benefits and claims		
— Long term insurance contracts	**6,820**	3,497
— General insurance contracts	**664**	656
Operating lease rentals	**1,775**	1,550
Impairment (write back)/losses on other assets	**(171)**	433
Losses on disposal of property and equipment	**148**	205
Provision for litigation losses (Note V.34)	**897**	712
Other expenses	**611**	580
Total	**68,731**	59,984

(1) Included in the general operating and administrative expenses are auditors' remuneration paid to PricewaterhouseCoopers of RMB183 million (2005: RMB154 million) for the year ended 31 December 2006.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

8 Staff costs

	Year ended 31 December	
	2006	2005
Salaries and benefits	**23,293**	18,096
Defined contribution plans(1)(2)	**3,079**	2,753
Retirement benefits(3) (Note V.31)	**1,391**	3,358
Housing funds	**1,224**	1,000
Social security costs	**993**	464
Others	**916**	1,435
Total	**30,896**	27,106

(1) Contributions to defined contribution plans for the years ended 31 December 2006 and 2005 include the effect of deductions of forfeited contributions of approximately RMB34 million and RMB27 million, respectively.

(2) In 2005, the Group established the Annuity Plan (Note II.22), a defined contribution plan, in addition to local labour and social security bureau contribution plans. The expense recorded in the income statement for the years ended 31 December 2006 and 2005 amounted to RMB955 million and RMB1,238 million respectively. The expense for the year ended 31 December 2005 included a special contribution of RMB500 million made by Huijin to the Annuity Plan. See Note V.35 (4) and 40 (3).

(3) The retirement benefits for the year ended 31 December 2005 included an expense of RMB3,064 million, relating to the Bank's voluntary early retirement scheme which was terminated with effect from 31 December 2005.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

9 Directors', supervisors' and senior management's emoluments

The total remuneration of the directors and supervisors for the years ended 31 December 2006 and 2005 are approximately RMB11 million and RMB10 million respectively.

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

For the year ended 31 December 2006
(Amount in thousands of Renminbi)

	Fees	Basic salaries, allowances and benefits in kind	Contributions to pension schemes	Discretionary bonuses	Total
Executive directors					
Xiao Gang[4]	78[3]	640	103	703	1,524
Li Lihui	93[3]	609	97	730	1,529
Hua Qingshan	78[3]	530	87	613	1,308
Li Zaohang	78[3]	525	87	617	1,307
Independent non-executive directors					
Anthony Francis Neoh	400	—	—	—	400
William Peter Cooke	606	—	—	—	606
Patrick de Saint-Aignan	400	—	—	—	400
Alberto Togni	146	—	—	—	146
Non-executive directors					
Zhang Jinghua[1]	—	—	—	—	—
Yu Erniu[1]	—	—	—	—	—
Zhu Yan[1]	—	—	—	—	—
Zhang Xinze[1]	—	—	—	—	—
Hong Zhihua[1]	—	—	—	—	—
Huang Haibo[1]	—	—	—	—	—
Frederick Anderson Goodwin	—	—	—	—	—
Seah Lim Huat Peter	—	—	—	—	—
Supervisors					
Liu Ziqiang[4]	—	566	92	655	1,313
Wang Xueqiang	—	426	68	384	878
Liu Wanming	—	426	68	380	874
Li Chunyu	—	299	44	135	478
Liu Dun	—	226	30	167	423
	1,879	4,247	676	4,384	11,186

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

9 Directors', supervisors' and senior management's emoluments (Continued)

For the year ended 31 December 2005
(Amount in thousands of Renminbi)

	Fees	Basic salaries, allowances and benefits in kind	Contributions to pension schemes	Discretionary bonuses	Total
Executive directors					
Xiao Gang	—(3)	727	64	500	1,291
Li Lihui	—	689	31	460	1,180
Hua Qingshan	77(3)	600	61	400	1,138
Li Zaohang	77(3)	591	61	400	1,129
Independent non-executive directors					
Anthony Francis Neoh	660	—	—	—	660
William Peter Cooke	578	—	—	—	578
Suzanne Labarge	333	—	—	—	333
Non-executive directors					
Zhang Jinghua(1)	—	—	—	—	—
Yu Erniu(1)	—	—	—	—	—
Zhu Yan(1)	—	—	—	—	—
Zhang Xinze(1)	—	—	—	—	—
Hong Zhihua(1)	—	—	—	—	—
Huang Haibo(1)	—	—	—	—	—
Supervisors					
Liu Ziqiang	—	664	25	430	1,119
Wang Xueqiang	—	400	17	318	735
Liu Wanming	—	394	17	318	729
Li Chunyu	—	309	33	93	435
Liu Dun	—	149	32	169	350
	1,725	4,523	341	3,088	9,677

(1) During 2006, these full-time non-executive directors of the Bank received emoluments from Huijin for their services to the Bank.

(2) In July 2002, options to purchase shares of BOCHK Holdings were granted to several directors of the Bank under the Pre-Listing Share Option Scheme (as more fully described in Note V.32). During the years 2006 and 2005, no options were exercised, and no benefits arising from the granting of these share options were included in the directors' emoluments disclosed above or recognized in the income statement.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

9 Directors', supervisors' and senior management's emoluments (Continued)

(3) In addition to the fees disclosed, these executive directors of the Bank waived emoluments amounting to RMB0.88 million (2005: RMB1 million) for the year ended 31 December 2006.

(4) The amounts of discretionary bonuses payable to these executive director and supervisor for the year ended 31 December 2006 are subject to approval of the Bank's shareholders in the Annual General Meeting to be held on 14 June 2007.

Five highest paid individuals

Of the five individuals with the highest emoluments, none of them are directors or supervisors whose emoluments are disclosed above.

The emoluments payable to the five individuals whose emoluments were the highest in the Group for the years ended 31 December 2006 and 2005 respectively are as follows:

	Year ended 31 December	
	2006	2005
Basic salaries and allowances	**8**	20
Discretionary bonuses	**132**	20
Contributions to pension schemes	**1**	—
	141	40

Emoluments of the individuals were within the following bands:

	Year ended 31 December	
Amounts in RMB	**2006**	2005
6,000,001–6,500,000	**—**	1
6,500,001–7,000,000	**—**	1
7,000,001–7,500,000	**—**	1
9,000,001–9,500,000	**—**	1
11,500,001–12,000,000	**—**	1
19,500,001–20,000,000	**1**	—
23,500,001–24,000,000	**1**	—
25,000,001–25,500,000	**1**	—
28,500,001–29,000,000	**1**	—
44,500,001–45,000,000	**1**	—

During the years ended 31 December 2006 and 2005, the Group has not paid any emoluments to the directors, supervisors or any of the five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

10 Income tax expense

	Year ended 31 December	
	2006	2005
Current income tax		
Chinese Mainland income tax	**16,477**	18,536
Hong Kong profits tax	**2,717**	2,453
Overseas taxation	**570**	302
	19,764	21,291
Deferred income tax (Note V.33)	**(91)**	962
	19,673	22,253

The provision for Chinese Mainland 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 Chinese Mainland as determined in accordance with the relevant PRC income tax rules and regulations for the years ended 31 December 2006 and 2005. In addition, the Bank's Overseas Operations are subject to supplementary PRC tax at tax rate determined by the relevant PRC Authority.

The Group's operations in Hong Kong are subject to Hong Kong profits tax at the rate of 17.5% on the estimated assessable income for the years ended 31 December 2006 and 2005.

Taxation on overseas profits has been calculated on the estimated assessable profit at the rates of taxation prevailing in the countries or regions in which the Group operates.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

10 Income tax expense (Continued)

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the basic domestic tax rate of the Bank as follows:

	Year ended 31 December	
	2006	2005
Profit before income tax	**67,937**	53,811
Tax calculated at 33%	**22,419**	17,758
Effect of different tax rates in Overseas Operations	**(3,880)**	(3,713)
Supplementary tax on overseas income paid in the PRC	**2,510**	1,388
Prior year tax expense adjustment(1)	**(300)**	2,376
Income not subject to tax(2)	**(2,402)**	(1,862)
Expenses not deductible for tax purposes(3)	**781**	5,264
Others(4)	**545**	1,042
Income tax expense	**19,673**	22,253

(1) The prior year tax expense adjustments for the year 2005 included RMB1,921 million related to the reversal in 2004 of certain provisions recorded in prior years. The relevant domestic tax authorities determined that these reversals constituted taxable income as they related to the implementation of the Joint Stock Reform Plan.

(2) It mainly comprised the interest income from the PRC treasury bills.

(3) In 2005, non tax-deductible expenses primarily included staff salary costs in excess of the deduction limit permitted under relevant PRC tax regulations. Following the completion of the listings of the Bank's ordinary shares in June 2006 on the Hong Kong Stock Exchange and Shanghai Stock Exchange, the Bank has successfully obtained approval from the Ministry of Finance ("MOF") and the State Administration of Taxation ("SAT") for deduction of its domestic staff salary costs amounting to RMB15,669 million when determining the Bank's taxable income for the 2006 financial year.

(4) Others primarily included non-performing loans sold in 2005 and 2006. The deferred income tax assets arising from the associated loan loss provisions were subsequently derecognized.

Subsequent to the balance date on 16 March 2007, the National People's Congress approved the new PRC Enterprise Income Tax Law. The details and the Group's preliminary assessment of the impact of the relevant changes are discussed in Note V.43 (1).

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

11 Earnings per share (Basic and diluted)

Basic and diluted earnings per share for the years ended 31 December 2006 and 2005 have been computed by dividing the profit for each year by the weighted average number of ordinary shares in issue during the period.

The Group had no dilutive potential ordinary shares as at 31 December 2006 and 2005.

	Year ended 31 December	
	2006	2005
Profit attributable to equity holders of the Bank	**42,830**	25,921
Weighted average number of ordinary shares in issue (in millions)	**236,055**	186,425
Basic and diluted earnings per share (in RMB)	**0.18**	0.14

12 Cash and due from banks

Group

	As at 31 December	
	2006	2005
Cash	**31,110**	28,644
Due from banks	**8,702**	12,438
Total	**39,812**	41,082

As at 31 December 2006 and 2005, the Group's Cash and Due from banks included in Cash and cash equivalents amounted to RMB38,805 million and RMB40,087 million, respectively (Note V.39).

Bank

	As at 31 December	
	2006	2005
Cash	**27,632**	25,144
Due from banks	**10,210**	13,131
Total	**37,842**	38,275

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

13 Balances with central banks

Group

	As at 31 December	
	2006	2005
Mandatory reserves	**277,855**	202,030
Other deposits	**101,776**	114,911
Total	**379,631**	316,941

Bank

	As at 31 December	
	2006	2005
Mandatory reserves	**277,071**	201,437
Other deposits	**77,810**	82,936
Total	**354,881**	284,373

The Group places mandatory reserve funds with the PBOC and the central banks of other countries or regions where it has operations. As at 31 December 2006, mandatory reserve funds placed with the PBOC were calculated at 9% (2005: 7.5%) and 4% (2005: 3%) of eligible RMB deposits and foreign currency deposits from customers of domestic branches of the Bank respectively. The amounts of mandatory reserve funds placed with the central banks of other countries are determined by local jurisdiction.

These mandatory reserve funds are not available for use in the Group's day to day operations.

As at 31 December 2006 and 2005, the Group's balances with central banks included in cash and cash equivalents amounted to RMB101,776 million and 108,149 million, respectively (Note V.39).

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

14 Placements with banks and other financial institutions

Group

	As at 31 December	
	2006	2005
Placements with domestic banks	**33,567**	52,439
Placements with other domestic financial institutions	**21,579**	26,302
Placements with overseas banks and other financial institutions	**344,491**	253,904
	399,637	332,645
Allowance for impairment losses	**(499)**	(546)
	399,138	332,099
Impaired placements	**499**	546
Percentage of impaired placements to total placements with banks and other financial institutions	**0.12%**	0.16%

Bank

	As at 31 December	
	2006	2005
Placements with domestic banks	**29,235**	50,480
Placements with other domestic financial institutions	**21,579**	26,302
Placements with overseas banks and other financial institutions	**252,687**	167,418
	303,501	244,200
Allowance for impairment losses	**(499)**	(546)
	303,002	243,654
Impaired placements	**499**	546
Percentage of impaired placements to total placements with banks and other financial institutions	**0.16%**	0.22%

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

14 Placements with banks and other financial institutions (Continued)

As at 31 December 2006 and 2005, the Group's placements with banks and other financial institutions included in cash and cash equivalents amounted to RMB305,618 million and RMB233,301 million, respectively (Note V.39).

The movement in allowance for impairment losses on placements with banks and other financial institutions is as follows:

Group and Bank

	2006	2005
At 1 January	**546**	1,508
Addition	**—**	39
Write-off	**(47)**	(1,001)
At 31 December	**499**	546

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

15 Trading assets and other financial instruments at fair value through profit or loss

Group

	As at 31 December	
	2006	2005
Trading debt securities		
Government	**17,802**	19,116
Public sector and quasi-government	**1,032**	2,095
Financial institution	**22,644**	30,599
Corporate	**4,204**	4,179
	45,682	55,989
Other debt securities at fair value through profit or loss (designated at initial recognition)		
Government	**20,444**	10,704
Public sector and quasi-government	**8,559**	12,974
Financial institution	**30,225**	19,979
Corporate	**5,724**	7,625
	64,952	51,282
Trading equity securities	**5,194**	4,511
	115,828	111,782
Analyzed as follows:		
Listed in Hong Kong	**6,087**	7,648
Listed outside Hong Kong	**76,353**	82,895
Unlisted	**33,388**	21,239
	115,828	111,782

Included in the balances above are treasury bills held by the Group amounting to RMB11,895 million and RMB7,298 million as of 31 December 2006 and 2005, respectively.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

15 Trading assets and other financial instruments at fair value through profit or loss (Continued)

Bank

	As at 31 December	
	2006	2005
Trading debt securities		
Government	**13,571**	16,072
Public sector and quasi-government	**—**	100
Financial institution	**13,149**	14,439
Corporate	**1,031**	1,149
	27,751	31,760
Other debt securities at fair value through profit or loss (designated at initial recognition)		
Government	**20,281**	10,704
Public sector and quasi-government	**7,877**	12,974
Financial institution	**16,913**	19,666
Corporate	**3,759**	6,978
	48,830	50,322
	76,581	82,082
Analyzed as follows:		
Listed in Hong Kong	**2,441**	3,004
Listed outside Hong Kong	**63,507**	71,902
Unlisted	**10,633**	7,176
	76,581	82,082

Included in the balances above are treasury bills held by the Bank amounting to RMB8,262 million, and RMB5,621 million as of 31 December 2006 and 2005, respectively.

Included in other debt securities designated at fair value through profit or loss are certain non-trading debt securities which are economically hedged with derivative instruments. Gains and losses arising on the related derivative instruments are intended to substantially offset the gains and losses arising on these securities.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

16 Derivative financial instruments

The Group enters into the following foreign currency exchange rate or interest rate related derivative financial instruments for trading, asset and liability management and on behalf of customers:

Currency forwards represent commitments to purchase and sell foreign currency on a future date. 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 buy or sell a foreign currency or interest rate financial instrument on a future date at an agreed price in the financial market under the administration of the stock exchanges. 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 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). Except for certain currency swap contracts, no exchange of principal takes place.

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. In consideration for the assumption of foreign exchange or interest rate risk, the seller receives a premium from the purchaser. Options may be either negotiated over-the-counter ("OTC") between the Group and its counterparty or exchange-traded.

The contractual/notional amounts and fair values of derivative instruments held by the Group and the Bank are set out in the following table. The contractual/notional amounts of financial instruments provide a basis for comparison with fair value instruments recognized 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 market risks. The derivative instruments become favorable (assets) or unfavorable (liabilities) as a result of fluctuations in market interest rates or foreign exchange rates or equity/commodity prices relative to their terms. The aggregate fair values of derivative financial assets and liabilities can fluctuate significantly from time to time.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

16 Derivative financial instruments (Continued)

Group

	As at 31 December 2006			As at 31 December 2005		
	Contractual/ notional amount	Fair value Assets	Fair value Liabilities	Contractual/ notional amount	Fair value Assets	Fair value Liabilities
Exchange rate derivatives						
Currency forwards and swaps(1)	**993,008**	**11,860**	**(4,974)**	563,397	6,991	(4,813)
Currency options purchased(2)	**187,446**	**5,735**	**—**	176,643	3,781	—
Currency options written	**38,272**	**—**	**(419)**	19,369	—	(374)
		17,595	**(5,393)**		10,772	(5,187)
Interest rate derivatives						
Interest rate swaps	**369,093**	**4,236**	**(4,832)**	361,332	3,132	(5,246)
Cross-currency interest rate swaps	**34,793**	**1,532**	**(2,932)**	39,427	1,735	(4,131)
Interest rate options purchased	**41,151**	**592**	**—**	11,584	148	—
Interest rate options written	**48,939**	**—**	**(161)**	98,994	—	(215)
Interest rate futures	**14,675**	**40**	**(9)**	14,939	28	(34)
		6,400	**(7,934)**		5,043	(9,626)
Equity derivatives	**10,572**	**453**	**(390)**	15,442	14	(7)
Precious metal derivatives	**10,520**	**389**	**(606)**	21,008	979	(932)
Total derivative financial instrument assets/ (liabilities) (Note V.27)		**24,837**	**(14,323)**		16,808	(15,752)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

16 Derivative financial instruments (Continued)

Bank

	As at 31 December 2006			As at 31 December 2005		
	Contractual/ notional amount	Fair value Assets	Fair value Liabilities	Contractual/ notional amount	Fair value Assets	Fair value Liabilities
Exchange rate derivatives						
Currency forwards and swaps(1)	**694,961**	**4,651**	**(2,097)**	286,268	2,515	(2,391)
Currency options purchased(2)	**185,956**	**5,724**	**—**	173,993	3,759	—
Currency options written	**35,153**	**—**	**(403)**	17,866	—	(346)
		10,375	**(2,500)**		6,274	(2,737)
Interest rate derivatives						
Interest rate swaps	**331,111**	**3,712**	**(3,930)**	328,245	3,050	(4,559)
Cross-currency interest rate swaps	**32,313**	**1,520**	**(2,895)**	37,786	1,785	(4,062)
Interest rate options purchased	**40,293**	**586**	**—**	11,377	148	—
Interest rate options written	**48,125**	**—**	**(151)**	96,950	—	(180)
Interest rate futures	**5,180**	**1**	**(1)**	9,701	1	(4)
		5,819	**(6,977)**		4,984	(8,805)
Precious metal derivatives	**3,156**	**169**	**(166)**	2,482	71	(64)
Total derivative financial instrument assets/ (liabilities) (Note V.27)		**16,363**	**(9,643)**		11,329	(11,606)

(1) Since 2005, the Bank has entered into foreign exchange swap transactions with the PBOC to manage its assets and liabilities. Under these agreements, the PBOC sold USD to the Bank in spot transactions for RMB and agreed to buy back the USD after one year or three years at agreed exchange and swap rates, which reflect the interest rate differentials between USD and RMB at the respective inception date of the transactions. See Note III. 5(i).

(2) On 5 January 2005, the Bank entered into a foreign currency option agreement with Huijin whereby the Bank acquired options to sell to Huijin USD, totaling USD18 billion, of no more than USD1,500 million at the beginning of each calendar month during the year ending 31 December 2007 at a fixed exchange rate of USD1 to RMB8.2769. The related option premium of RMB4,469 million is payable by the Bank to Huijin in 12 equal monthly installments at the beginning of each calendar month during the year ending 31 December 2007. The fair value of the Huijin option, which has taken into consideration this option premium payable, as at 31 December 2006 amounted to RMB5,180 million (2005: RMB3,231 million). See Note III.5 (i).

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

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

16 Derivative financial instruments (Continued)

The Group and the Bank primarily undertake transactions in foreign exchange and interest rate contracts with other financial institutions. Management has established position limits of these contracts by counterparties. Actual credit exposures and limits are regularly monitored and controlled by management.

Credit risk weighted amounts

The credit risk weighted amounts are the amounts calculated with reference to the guidelines issued by the CBRC and are dependent on, among other factors, the creditworthiness of the counterparty and the maturity characteristics of each type of contract.

Group

	As at 31 December	
	2006	2005
Derivatives		
Exchange rate contracts	**4,468**	3,744
Interest rate contracts	**3,379**	3,543
Other derivative contracts	**35**	45
	7,882	7,332

Bank

	As at 31 December	
	2006	2005
Derivatives		
Exchange rate contracts	**3,880**	3,208
Interest rate contracts	**3,228**	3,469
	7,108	6,677

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

16 Derivative financial instruments (Continued)

Replacement costs

Replacement costs are the costs 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.

Group

	As at 31 December	
	2006	2005
Derivatives		
Exchange rate contracts	**17,595**	10,772
Interest rate contracts	**6,400**	5,043
Other derivative contracts	**842**	993
	24,837	16,808

Bank

	As at 31 December	
	2006	2005
Derivatives		
Exchange rate contracts	**10,375**	6,274
Interest rate contracts	**5,819**	4,984
Other derivative contracts	**169**	71
	16,363	11,329

The credit risk weighted amounts and replacement costs stated above have not taken the effects of netting arrangements into account.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

17 Loans and advances to customers, net

Group

	As at 31 December	
	2006	2005
Corporate loans and advances	**1,849,275**	1,712,262
Personal loans and advances	**582,744**	523,003
	2,432,019	2,235,265
Allowance for impairment losses	**(94,293)**	(83,153)
Loans and advances to customers, net	**2,337,726**	2,152,112

Bank

	As at 31 December	
	2006	2005
Corporate loans and advances	**1,616,052**	1,483,933
Personal loans and advances	**448,775**	384,390
	2,064,827	1,868,323
Allowance for impairment losses	**(92,962)**	(79,581)
Loans and advances to customers, net	**1,971,865**	1,788,742

As at 31 December 2006, there were no bills pledged as collateral under repurchase agreements by the Group and Bank (2005: RMB11,968 million). See Note V. 38(2).

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

17 Loans and advances to customers, net (Continued)

Group

	Loans and advances for which allowance is collectively assessed[1]	Identified impaired loans and advances[2] for which allowance is collectively assessed	Identified impaired loans and advances[2] for which allowance is individually assessed	Sub-total	Total	Identified impaired loans and advances as a % of gross total loans and advances
At 31 December 2006						
Gross loans and advances	**2,328,787**	**21,502**	**81,730**	**103,232**	**2,432,019**	**4.2%**
Allowance for impairment losses	**(27,712)**	**(12,735)**	**(53,846)**	**(66,581)**	**(94,293)**	
Net loans and advances	**2,301,075**	**8,767**	**27,884**	**36,651**	**2,337,726**	
At 31 December 2005						
Gross loans and advances	2,125,735	26,288	83,242	109,530	2,235,265	4.9%
Allowance for impairment losses	(25,406)	(12,009)	(45,738)	(57,747)	(83,153)	
Net loans and advances	2,100,329	14,279	37,504	51,783	2,152,112	

Bank

	Loans and advances for which allowance is collectively assessed[1]	Identified impaired loans and advances[2] for which allowance is collectively assessed	Identified impaired loans and advances[2] for which allowance is individually assessed	Sub-total	Total	Identified impaired loans and advances as a % of gross total loans and advances
At 31 December 2006						
Gross loans and advances	**1,963,822**	**20,342**	**80,663**	**101,005**	**2,064,827**	**4.9%**
Allowance for impairment losses	**(27,043)**	**(12,688)**	**(53,231)**	**(65,919)**	**(92,962)**	
Net loans and advances	**1,936,779**	**7,654**	**27,432**	**35,086**	**1,971,865**	
At 31 December 2005						
Gross loans and advances	1,765,174	24,116	79,033	103,149	1,868,323	5.5%
Allowance for impairment losses	(24,813)	(11,644)	(43,124)	(54,768)	(79,581)	
Net loans and advances	1,740,361	12,472	35,909	48,381	1,788,742	

(1) Loans and advances for which allowance is collectively assessed consist of loans and advances which have not been identified as impaired i.e. primarily loans graded pass and special mention.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

17 Loans and advances to customers, net (Continued)

(2) Identified impaired loans and advances include loans for which objective evidence of impairment exists and which have been identified as bearing an impairment loss and assessed either:

- individually (including mainly significant corporate loans and advances which are impaired over a certain amount); or
- collectively (i.e. portfolios of insignificant homogenous loans, which includes insignificant corporate loans and advances and all personal loans which are impaired).

Movements of allowance for impairment losses on loans and advances are as follows:

Group

	2006	2005
At 1 January	83,153	74,769
Impairment losses for the year	12,342	11,486
Loans and advances written off	(3,711)	(4,852)
Amounts recovered on loans and advances written off in previous years	3,589	2,954
Exchange differences	(452)	(675)
Unwind of discount on allowance	(628)	(529)
At 31 December	94,293	83,153

Bank

	2006	2005
At 1 January	79,581	69,109
Impairment losses for the year	14,440	14,235
Loans and advances written off	(2,864)	(3,781)
Amounts recovered on loans and advances written off in previous years	1,201	972
Transfer from overseas operations	1,524	—
Exchange differences	(381)	(558)
Unwind of discount on allowance	(539)	(396)
At 31 December	92,962	79,581

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Investment securities

Group

	As at 31 December	
	2006	2005
Debt securities available-for-sale (at fair value)		
Government	**297,129**	229,064
Public sector and quasi-government	**152,822**	106,840
Financial institution	**230,999**	170,038
Corporate	**126,358**	87,068
	807,308	593,010
Equity securities (at fair value)	**7,870**	9,211
Total securities available-for-sale	**815,178**	602,221
Debt securities held-to-maturity (at amortized cost):		
Government	**146,502**	231,156
Public sector and quasi-government	**97,025**	135,002
Financial institution	**172,666**	203,724
Corporate	**44,947**	37,577
Total securities held-to-maturity	**461,140**	607,459
Debt securities classified as loans and receivables (at amortized cost):		
China Orient Bond(1)	**160,000**	160,000
PBOC Special Bills(2)	**91,612**	91,530
PBOC Target Bills(3)	**28,702**	—
Special Purpose Treasury Bond(4)	**42,500**	42,500
Long term notes — Financial institution	**14,545**	1,545
Short term bills and notes(5)		
Public sector and quasi-government	**3,895**	6,096
Financial institution	**139,659**	49,993
Corporate	**6,623**	—
Certificate Treasury Bonds and others	**12,952**	10,343
	500,488	362,007
Allowance for impairment losses	**(152)**	(156)
Total securities classified as loans and receivables	**500,336**	361,851
Total(6), (7)	**1,776,654**	1,571,531

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Investment securities (Continued)

Group

	As at 31 December	
	2006	2005
Analyzed as follows:		
Securities available-for-sale		
Debt securities		
— Listed	**430,550**	344,872
— Unlisted	**376,758**	248,138
	807,308	593,010
Equity securities		
— Listed	**4,350**	1,757
— Unlisted	**3,520**	7,454
	7,870	9,211
	815,178	602,221
Debt securities held-to-maturity		
— Listed	**228,815**	332,841
— Unlisted	**232,325**	274,618
	461,140	607,459
Debt securities classified as loans and receivables		
— Unlisted	**500,336**	361,851
Total	**1,776,654**	1,571,531
Listed in Hong Kong	**16,561**	14,223
Listed outside Hong Kong	**647,154**	665,247
Unlisted	**1,112,939**	892,061
Total(6)	**1,776,654**	1,571,531

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Investment securities (Continued)

Bank

	As at 31 December	
	2006	2005
Debt securities available-for-sale (at fair value)		
Government	**283,860**	219,566
Public sector and quasi-government	**145,929**	102,200
Financial institution	**195,235**	146,373
Corporate	**81,002**	70,798
	706,026	538,937
Equity securities (at fair value)	**713**	3,205
Total securities available-for-sale	**706,739**	542,142
Debt securities held-to-maturity (at amortized cost)		
Government	**144,292**	227,718
Public sector and quasi-government	**75,749**	103,074
Financial institution	**62,702**	74,791
Corporate	**4,655**	9,560
Total securities held-to-maturity	**287,398**	415,143
Debt securities classified as loans and receivables (at amortized cost):		
China Orient Bond(1)	**160,000**	160,000
PBOC Special Bills(2)	**91,612**	91,530
PBOC Target Bills(3)	**28,702**	—
Special Purpose Treasury Bond(4)	**42,500**	42,500
Long term notes — Financial institution	**14,545**	1,545
Short term bills and notes		
Public sector and quasi-government	**3,895**	5,992
Financial institution	**98,006**	32,156
Corporate	**6,546**	—
Certificate Treasury Bonds and others	**12,952**	10,343
Sub-total	**458,758**	344,066
Allowance for impairment losses	**(152)**	(156)
Total securities classified as loans and receivables	**458,606**	343,910
Total(6), (7)	**1,452,743**	1,301,195

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Investment securities (Continued)

Bank

	As at 31 December	
	2006	2005
Analyzed as follows:		
Securities available-for-sale		
Debt securities		
— Listed	**411,933**	332,413
— Unlisted	**294,093**	206,524
	706,026	538,937
Equity securities		
— Listed	**81**	1
— Unlisted	**632**	3,204
	713	3,205
	706,739	542,142
Debt securities held-to-maturity		
— Listed	**199,520**	296,266
— Unlisted	**87,878**	118,877
	287,398	415,143
Debt securities classified as loans and receivables		
— Unlisted	**458,606**	343,910
Total	**1,452,743**	1,301,195
Listed in Hong Kong	**3,336**	4,110
Listed outside Hong Kong	**608,198**	624,570
Unlisted	**841,209**	672,515
Total	**1,452,743**	1,301,195

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Investment securities (Continued)

The market values of the above listed held-to-maturity securities are set out below:

Group

	As at 31 December			
	2006		2005	
	Carrying value	**Market value**	Carrying value	Market value
Investment securities held-to-maturity				
Listed in Hong Kong	**4,596**	**4,563**	5,129	5,107
Listed outside Hong Kong	**224,219**	**225,162**	327,712	329,128

Bank

	As at 31 December			
	2006		2005	
	Carrying value	**Market value**	Carrying value	Market value
Investment securities held-to-maturity				
Listed in Hong Kong	**412**	**412**	427	420
Listed outside Hong Kong	**199,108**	**200,295**	295,839	297,360

(1) The Bank transferred certain non-performing assets to China Orient Asset Management Corporation ("China Orient") in 1999 and 2000. On 1 July 2000, China Orient issued a ten-year bond with a par value of RMB160,000 million to the Bank as consideration. The interest rate of the bonds is 2.25% per annum. Pursuant to Caijin [2004] No. 87 "Notice of the MOF regarding Relevant Issues relating to the Principal and Interest of Debt Securities of Financial Asset Management Companies Held by Bank of China and China Construction Bank", from 1 January 2005, should China Orient fail to pay in full the interest on the debt securities or repay the principal in full according to the contractual terms of the bond, the MOF shall provide funding support to enable China Orient to fulfill its obligations.

(2) On 30 June 2004, the PBOC issued a Special Bill with a par value of RMB18,100 million in exchange for certain policy-related assets of the Bank. The tenor of the bill is 3 years, with an interest rate of 1.89% per annum. The Bank has also been appointed as an agent to collect the policy-related assets.

On 30 June 2004, the Bank sold a portfolio of non-performing loans to China Cinda Asset Management Corporation ("Cinda") and received consideration in the form of a Special Bill issued by the PBOC, with a par value of RMB73,430 million. The tenor of the bill is 5 years, with an interest rate of 1.89% per annum.

On 22 June 2006, the PBOC issued special PBOC Bills amounting to RMB82 million in exchange for certain non-performing loans, as previously approved by the State Council. The tenor of the bill is 5 years, with an interest rate of 1.89% per annum.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Investment securities (Continued)

Without the approval of the PBOC, the special PBOC Bills referred to above are non-transferable and may not be used as collateral for borrowings. The PBOC has the option to settle these bills in whole or in part before their maturity.

(3) On 16 May and 13 July 2006, the Bank invested in PBOC Bills for commercial banks, with a par value of RMB8,000 million and RMB21,000 million, respectively. The bills have tenor of 1 year with an interest rate of 2.11% per annum.

Without the approval of the PBOC, these PBOC bills are non-transferable and may not be used as collateral for borrowings.

(4) This represents a Special Purpose Treasury Bond issued by the MOF with a par value of RMB42,500 million maturing on 18 August 2028. This bond was originally issued with an annual coupon interest rate of 7.2% per annum. In accordance with Ren Da Chang Hui Zi [2004] No. 25 "Resolution of the Standing Committee of the National People's Congress on the Approval of the Report of the State Council on the Payment of Interest on the Special Purpose Treasury Bond of 1998", the Special Purpose Treasury Bond was restructured among other things to reduce the annual coupon interest rate to 2.25%, the rate established by the PRC Government for use in connection with large-scale policy directed financing transactions, and reinstate cash interest payments from 1 December 2004. This restructuring was accounted for as the derecognition of the original Special Purpose Treasury Bond yielding 7.2% and recognition of a restructured Special Purpose Treasury Bond yielding 2.25%, with a remaining maturity equal to that of the original Special Purpose Treasury Bond.

The transactions related to the Special Purpose Treasury Bond described above were accounted for with reference to rates determined by the PRC Government in similar transactions engaged in or directed by the PRC Government, the sole owner of the Bank's equity capital at the time of the transaction. As discussed in Note IV.2, there were no relevant market prices or yields, reflecting arm's length transactions of a comparable size and tenor available.

(5) As at 31 December 2006 and 2005, the Group's short term bills and notes included in cash and cash equivalents amounted to RMB73,745 million and RMB15,575 million, respectively (Note V.39).

(6) Included in the balance as of 31 December 2006 are treasury bills held by the Group and the Bank amounting to RMB248,292 million (2005: RMB228,154 million) and RMB235,233 million (2005: RMB222,625 million) respectively.

(7) As at 31 December 2006, the Group's and the Bank's debt securities of RMB55,212 million (2005: RMB49,658 million) and RMB51,632 million (2005: RMB45,106 million), respectively, were pledged as collateral to third parties under agreements to repurchase (Note V.38 (2)).

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Investment securities (Continued)

Movements of investment securities are as follows:

Group

	Available-for-sale	**Held-to-maturity**	**Loans and receivables**	**Total**
At 1 January 2006	**602,221**	**607,459**	**361,851**	**1,571,531**
Additions	**821,368**	**308,947**	**505,731**	**1,636,046**
Sales and redemptions	**(603,271)**	**(449,771)**	**(367,986)**	**(1,421,028)**
Accretion	**4,360**	**2,918**	**3,251**	**10,529**
Fair value changes	**20**	**—**	**—**	**20**
Exchange differences	**(9,520)**	**(8,413)**	**(2,515)**	**(20,448)**
Impairment losses	**—**	**—**	**4**	**4**
At 31 December 2006	**815,178**	**461,140**	**500,336**	**1,776,654**

	Available-for-sale	Held-to-maturity	Loans and receivables	Total
At 1 January 2005	357,587	457,994	413,941	1,229,522
Additions	927,624	515,344	133,328	1,576,296
Sales and redemptions	(662,363)	(356,715)	(184,540)	(1,203,618)
(Amortization)/accretion, net	(634)	1,412	697	1,475
Fair value changes	796	—	—	796
Exchange differences	(17,979)	(10,590)	(1,598)	(30,167)
Reclassification (Note V.21)	(2,810)	—	—	(2,810)
Impairment losses	—	14	23	37
At 31 December 2005	602,221	607,459	361,851	1,571,531

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

18 Investment securities (Continued)

Bank

	Available-for-sale	**Held-to-maturity**	**Loans and receivables**	**Total**
At 1 January 2006	**542,142**	**415,143**	**343,910**	**1,301,195**
Additions	**710,533**	**248,276**	**423,338**	**1,382,147**
Sales and redemptions	**(539,356)**	**(375,327)**	**(308,634)**	**(1,223,317)**
Accretion	**3,975**	**3,009**	**2,136**	**9,120**
Fair value changes	**(2,238)**	**—**	**—**	**(2,238)**
Exchange differences	**(8,317)**	**(3,703)**	**(2,148)**	**(14,168)**
Impairment losses	**—**	**—**	**4**	**4**
At 31 December 2006	**706,739**	**287,398**	**458,606**	**1,452,743**

	Available-for-sale	Held-to-maturity	Loans and receivables	Total
At 1 January 2005	349,453	252,254	383,680	985,387
Additions	847,842	432,940	93,543	1,374,325
Sales and redemptions	(638,541)	(267,575)	(132,561)	(1,038,677)
(Amortization)/accretion, net	(496)	2,061	226	1,791
Fair value changes	835	—	—	835
Exchange differences	(16,951)	(4,537)	(1,001)	(22,489)
Impairment losses	—	—	23	23
At 31 December 2005	542,142	415,143	343,910	1,301,195

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

19 Certificates of deposit held

Certificates of deposit held are included within the following balance sheet captions:

Group

	As at 31 December	
	2006	2005
Trading assets and other financial instruments at fair value through profit or loss	**3,813**	3,147
Investment securities		
— available-for-sale	**8,663**	4,540
— held-to-maturity	**12,681**	18,817
— loans and receivables	**388**	460
	25,545	26,964
Analyzed as follows:		
Listed in Hong Kong	**492**	163
Listed outside Hong Kong	**31**	1,008
Unlisted	**25,022**	25,793
	25,545	26,964
Market value of listed certificates of deposit held	**523**	1,169

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

19 Certificates of deposit held (Continued)

Bank

	As at 31 December	
	2006	2005
Trading assets and other financial instruments at fair value through profit or loss	**927**	154
Investment securities		
— available-for-sale	**75**	239
— held-to-maturity	**—**	405
— loans and receivables	**388**	460
	1,390	1,258
Analyzed as follows:		
Listed in Hong Kong	**—**	—
Listed outside Hong Kong	**—**	154
Unlisted	**1,390**	1,104
	1,390	1,258
Market value of listed certificates of deposit held	**—**	154

20 Investment in subsidiaries

	As at 31 December	
	2006	2005
Investments at cost:		
Unlisted shares	**45,451**	45,080

Details of the Bank's principal subsidiaries are set out below. These principal subsidiaries are private companies except otherwise stated. All holdings are in the ordinary share capital of the undertaking concerned.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

20 Investment in subsidiaries (Continued)

Name	Place of incorporation and operation	Date of incorporation/ establishment	Paid-in capital (in millions)	Equity held (%)	Principal business
Directly held					
BOC Hong Kong (Group) Limited	Hong Kong	12 September 2001	HKD34,806	100	Holding company
BOC International Holdings Limited	Hong Kong	10 July 1998	HKD3,539	100	Investment banking
Bank of China Group Insurance Company Limited	Hong Kong	23 July 1992	HKD1,269	100	Insurance services
Bank of China Group Investment Limited ("BOCGI")	Hong Kong	18 May 1993	HKD200	100	Investment holding
Tai Fung Bank Limited	Macau	1942	MOP1,000	50.31	Commercial banking
Indirectly held					
BOC Hong Kong (Holdings) Limited ("BOCHK Holdings")(1)	Hong Kong	12 September 2001	HKD52,864	65.87	Holding company
Bank of China (Hong Kong) Limited(2)	Hong Kong	16 October 1964	HKD43,043	65.87	Commercial banking
Nanyang Commercial Bank, Limited(3)	Hong Kong	2 February 1948	HKD600	65.87	Commercial banking
Chiyu Banking Corporation Limited(2), (3)	Hong Kong	24 April 1947	HKD300	46.43	Commercial banking
BOC Credit Card (International) Limited	Hong Kong	9 September 1980	HKD480	65.87	Credit card services
BOC Group Trustee Company, Limited(3)	Hong Kong	1 December 1997	HKD200	76.31	Provision of trustee services
Singapore Aircraft Leasing Enterprise Pte. Limited(4) (Note V. 42)	Singapore	25 November 1993	USD308	100.00	Aircraft leasing

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

20 Investment in subsidiaries (Continued)

(1) BOCHK Holdings is listed on the Stock Exchange of Hong Kong Limited.

(2) Bank of China (Hong Kong) Limited, in which the Group holds a 65.87% equity interest, holds 70.49% of the voting shares of Chiyu Banking Corporation Limited.

(3) Bank of China (Hong Kong) Limited, Nanyang Commercial Bank Limited, Chiyu Banking Corporation Limited and BOC International Holdings Limited, in which the Group holds 65.87%, 65.87%, 46.43% and 100% of their equity interests respectively, hold 54%, 6%, 6% and 34% shares of BOC Group Trustee Company Limited, respectively.

(4) On 15 December 2006, the Group acquired 100% of the share capital of Singapore Aircraft Leasing Enterprise Pte. Ltd ("SALE"). (See Note V.42).

(5) For the year ended 31 December 2006, the financial statements of all the principal subsidiaries as stated above, except for SALE, were audited by PricewaterhouseCoopers. For the year ended 31 December 2005, except for BOCGI, the financial statements of all the principal subsidiaries as stated above were audited by PricewaterhouseCoopers.

21 Investment in associates and joint ventures

Group

	2006	2005
At 1 January	**5,061**	1,227
Investment cost addition	**924**	1,547
Transfer from available-for-sale securities	**—**	556
Adoption of equity accounting for investment in an associate[1] (Note V. 36)	**—**	2,194
Disposal of investment in associates	**(59)**	(510)
Share of results after tax	**632**	175
(Provision)/write back of impairment losses	**(344)**	7
Dividends received	**(134)**	(116)
Foreign exchanges and others	**(149)**	(19)
At 31 December	**5,931**	5,061

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

21 Investment in associates and joint ventures (Continued)

(1) In 2005, the Group entered into a contract with an independent third party to acquire a further 5% of the equity shares of Huaneng International Power Development Corporation. The carrying value of this investment on purchase was RMB1,255 million and is included in Investment securities cost additions for 2005. As a result of this transaction, the Group holds 20% of the equity of Huaneng International Power Development Corporation and accounts for the investment using the equity method. Consequently, the then existing 15% investment in Huaneng International Power Development Corporation was reclassified from available-for-sale securities to Investment in associates, resulting in a reclassification of RMB2,810 million from Investment securities representing the original cost of RMB556 million and the reversal of the cumulative change in fair value recorded in the Reserve for fair value changes of available-for-sale securities of RMB2,254 million (Note V.37). The cumulative impact resulting from the adoption of the equity method of RMB2,194 million representing the post acquisition share of net profits, has been credited to Undistributed profits.

Bank

	As at 31 December	
	2006	2005
Investment at cost:		
Unlisted shares	**21**	45

Particulars of the principal associates and joint ventures of the Group are set out as follows:

	Place of incorporation/ establishment	Equity held (%)	Paid-in capital (in millions)	Principal business
Huaneng International Power Development Corporation	PRC	20	USD450	Power plant operations
BOC International (China) Limited	PRC	49	RMB1,500	Securities underwriting, investment advisory, and brokerage services
CJM Insurance Brokers Limited	Hong Kong	33	HKD6	Insurance broker
Joint Electronic Teller Services Limited	Hong Kong	19.96	HKD10	Private inter-bank message switching network and ATM services
Dongfeng Peugeot Citroen Auto Finance Company Limited	PRC	50	RMB500	Car loan and financing services

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

22 Property and equipment

Group

	Buildings and improvements	Equipment and motor vehicles	Construction in progress	Aircraft	Total
At 31 December 2006					
Cost	**67,660**	**32,132**	**6,973**	**20,572**	**127,337**
Accumulated depreciation	**(15,317)**	**(23,891)**	**—**	**(34)**	**(39,242)**
Allowance for impairment losses	**(1,494)**	**—**	**(401)**	**—**	**(1,895)**
Net book amount	**50,849**	**8,241**	**6,572**	**20,538**	**86,200**
At 31 December 2005					
Cost	67,216	29,739	3,861	—	100,816
Accumulated depreciation	(15,066)	(21,306)	—	—	(36,372)
Allowance for impairment losses	(1,494)	(2)	(531)	—	(2,027)
Net book amount	50,656	8,431	3,330	—	62,417

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

22 Property and equipment (Continued)

Group (Continued)

	Buildings and improvements	Equipment and Motor vehicles	Construction in progress	Aircraft	Total
Year ended 31 December 2006					
Opening net book amount	**50,656**	**8,431**	**3,330**	**—**	**62,417**
Additions	**1,134**	**2,793**	**3,771**	**211**	**7,909**
Acquisition of a subsidiary	**—**	**—**	**1,692**	**20,209**	**21,901**
Transfer from investment property, net (Note V. 23)	**180**	**—**	**—**	**—**	**180**
Reclassification	**1,964**	**124**	**(2,207)**	**119**	**—**
Disposals	**(571)**	**(44)**	**(10)**	**—**	**(625)**
(Allowance for)/write back of Impairment losses	**22**	**—**	**(4)**	**—**	**18**
Depreciation charge	**(2,195)**	**(2,980)**	**—**	**(34)**	**(5,209)**
Exchange differences	**(341)**	**(83)**	**—**	**33**	**(391)**
Closing net book amount	**50,849**	**8,241**	**6,572**	**20,538**	**86,200**
Year ended 31 December 2005					
Opening net book amount	53,512	8,798	2,702	—	65,012
Additions	1,781	2,789	1,701	—	6,271
Transfer to investment property, net (Note V. 23)	(937)	—	—	—	(937)
Reclassification	656	10	(666)	—	—
Disposals	(1,210)	(382)	(405)	—	(1,997)
Allowance for impairment losses	(100)	—	(1)	—	(101)
Depreciation charge	(2,428)	(2,758)	—	—	(5,186)
Exchange differences	(618)	(26)	(1)	—	(645)
Closing net book amount	50,656	8,431	3,330	—	62,417

As at 31 December 2006, the net book amount of aircraft owned by the Group acquired under finance lease arrangements was RMB661 million.

As at 31 December 2006, the net book amount of aircraft owned by the Group that have been pledged for loan facilities was RMB19,264 million (Note V.30).

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

22 Property and equipment (Continued)

Bank

	Buildings and improvements	Equipment and motor vehicles	Construction in process	Total
At 31 December 2006				
Cost	**52,276**	**27,076**	**5,019**	**84,371**
Accumulated depreciation	**(12,584)**	**(20,420)**	**—**	**(33,004)**
Allowance for impairment losses	**(1,493)**	**—**	**(401)**	**(1,894)**
Net book amount	**38,199**	**6,656**	**4,618**	**49,473**
At 31 December 2005				
Cost	51,885	24,922	3,842	80,649
Accumulated depreciation	(12,656)	(17,922)	—	(30,578)
Allowance for impairment losses	(1,485)	(2)	(523)	(2,010)
Net book amount	37,744	6,998	3,319	48,061
Year ended 31 December 2006				
Opening net book amount	**37,744**	**6,998**	**3,319**	**48,061**
Additions	**928**	**2,220**	**3,391**	**6,539**
Transfer to investment property, net	**(197)**	**—**	**—**	**(197)**
Reclassification	**1,964**	**124**	**(2,088)**	**—**
Disposals	**(402)**	**(104)**	**(4)**	**(510)**
Write back of impairment losses	**14**	**—**	**—**	**14**
Depreciation charge	**(1,859)**	**(2,574)**	**—**	**(4,433)**
Exchange differences	**7**	**(8)**	**—**	**(1)**
Closing net book amount	**38,199**	**6,656**	**4,618**	**49,473**
Year ended 31 December 2005				
Opening net book amount	38,581	7,386	2,666	48,633
Additions	1,697	2,346	1,700	5,743
Reclassification	657	9	(666)	—
Disposals	(691)	(377)	(381)	(1,449)
Impairment losses	(100)	—	—	(100)
Depreciation charge	(2,082)	(2,368)	—	(4,450)
Exchange differences	(318)	2	—	(316)
Closing net book amount	37,744	6,998	3,319	48,061

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

22 Property and equipment (Continued)

According to relevant PRC laws and regulations, after conversion into a joint stock limited liability company, the Bank is required to re-register its property and equipment under the name of Bank of China Limited. As at 31 December 2006, the process of re-registration has not been completed. However, this registration process does not affect the rights of Bank of China Limited to these assets.

The carrying value of buildings and improvements is analyzed based on the remaining terms of the leases as follows:

Group

	As at 31 December	
	2006	2005
Held in Hong Kong		
on long-term lease (over 50 years)	**7,330**	7,041
on medium-term lease (10–50 years)	**4,009**	4,031
	11,339	11,072
Held outside Hong Kong		
on long-term lease (over 50 years)	**3,766**	3,719
on medium-term lease (10–50 years)	**35,099**	35,338
on short-term lease (less than 10 years)	**645**	527
	39,510	39,584
	50,849	50,656

Bank

	As at 31 December	
	2006	2005
Held outside Hong Kong		
on long-term lease (over 50 years)	**3,092**	2,911
on medium-term lease (10–50 years)	**34,532**	34,384
on short-term lease (less than 10 years)	**575**	449
	38,199	37,744

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

23 Investment property

Group

	2006	2005
At 1 January	**8,511**	6,288
Additions	**10**	45
Transfer (to)/from property and equipment, net (Note V. 22)	**(180)**	937
Disposals	**(452)**	(312)
Fair value changes	**595**	1,697
Exchange differences	**(263)**	(144)
At 31 December	**8,221**	8,511

Bank

	2006	2005
At 1 January	**461**	467
Additions	**—**	45
Transfer from property and equipment, net (Note V.22)	**197**	—
Disposals	**—**	(23)
Fair value changes	**(48)**	(12)
Exchange differences	**10**	(16)
At 31 December	**620**	461

Investment properties are mainly held by BOCHK Holdings, a subsidiary of the Group and are included in the consolidated balance sheets at valuation determined on the basis of their open market value as estimated by an independent firm of chartered surveyors, Chesterton Petty Limited. The carrying value as at 31 December 2006 and 2005 amounted to RMB7,516 million, and RMB7,843 million, respectively, based on valuations performed at 31 October 2006 and 31 October 2005 respectively. Chesterton Petty Limited also confirmed that there had been no material changes in valuation at 31 December 2006 and 2005 as compared to the valuation at 31 October 2006 and 2005 respectively.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

23 Investment property (Continued)

The carrying value of investment properties is analyzed based on the remaining terms of the leases as follows:

Group

	As at 31 December	
	2006	2005
Held in Hong Kong		
on long-term lease (over 50 years)	**6,804**	7,042
on medium-term lease (10–50 years)	**548**	794
on short-term lease (less than 10 years)	**40**	41
	7,392	7,877
Held outside Hong Kong		
on long-term lease (over 50 years)	**556**	414
on medium-term lease (10–50 years)	**202**	149
on short-term lease (less than 10 years)	**71**	71
	829	634
	8,221	8,511

Bank

	As at 31 December	
	2006	2005
Held outside Hong Kong		
on long-term lease (over 50 years)	**552**	390
on medium-term lease (10–50 years)	**—**	—
on short-term lease (less than 10 years)	**68**	71
	620	461

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

24 Other assets

Group

	As at 31 December	
	2006	2005
Interest receivable	**24,414**	20,483
Accounts receivable and prepayments	**18,370**	10,397
Intangible assets[(1)]	**4,889**	1,383
Foreclosed assets	**1,967**	2,051
Land use rights[(2)]	**1,108**	1,850
Others	**2,822**	2,476
Total	**53,570**	38,640

Bank

	As at 31 December	
	2006	2005
Interest receivable	**20,035**	16,107
Accounts receivable and prepayments	**5,605**	3,380
Intangible assets[(1)]	**1,147**	1,329
Foreclosed assets	**1,736**	1,767
Land use rights[(2)]	**1,108**	1,850
Others	**641**	1,404
Total	**30,272**	25,837

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

24 Other assets (Continued)

(1) Intangible assets

Group

	Goodwill	Aircraft firm orders and options	Computer software and others	Total
Year ended 31 December 2006				
Opening net book amount	**—**	**—**	**1,383**	**1,383**
Acquisition of a subsidiary (Note V. 42)	**1,875**	**1,856**	**—**	**3,731**
Additions	**—**	**—**	**329**	**329**
Amortization	**—**	**—**	**(520)**	**(520)**
Transfer (out)/in	**—**	**(47)**	**6**	**(41)**
Exchange difference	**3**	**4**	**—**	**7**
Closing net book amount	**1,878**	**1,813**	**1,198**	**4,889**
Year ended 31 December 2005				
Opening net book amount	—	—	1,647	1,647
Additions	—	—	260	260
Amortization	—	—	(518)	(518)
Transfer out	—	—	(6)	(6)
Closing net book amount	—	—	1,383	1,383

Bank

Computer software and others

	Year ended 31 December	
	2006	2005
Opening net book amount	**1,329**	1,591
Additions	**329**	260
Amortization	**(520)**	(518)
Transfer in/(out)	**9**	(4)
Closing net book amount	**1,147**	1,329

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

24 Other assets (Continued)

(2) Land use rights

Land use rights represent the right to use land appropriated by the PRC Government. According to MLR [2004] No. 253 "Response Concerning the Disposal of Land Assets in the Restructuring of Bank of China" and MLR [2005] No. 165 "Response Concerning the Additional Disposal of Land Assets of Bank of China Limited" issued by the Ministry of Land and Resources, the rights to use 4,032 pieces of land originally appropriated by the PRC Government have been transferred to the Bank. The land must be used for the purposes originally approved by the PRC Government. Upon obtaining the rights to the use of the lands appropriated by the PRC Government for specified uses, the Bank can allocate the land in the form of capital contributions (through equity investment) or leases to direct investees of the Bank. If the use of the land is altered or the land is allocated to parties other than those mentioned above, applications for approval must be filed with the related municipal and county level land and resources authorities where the underlying pieces of land are located, and the fees for land assignments should be paid as required.

These land use rights are primarily used by the Bank for its operating activities. There were no significant alterations to the use of the land and no significant disposals to third parties during the years ended 31 December 2006 and 2005.

The carrying value of land use rights is analyzed based on the remaining terms of the leases as follows:

Group and Bank

	As at 31 December	
	2006	2005
Held outside Hong Kong		
on long-term lease (over 50 years)	**27**	21
on medium-term lease (10–50 years)	**1,068**	1,823
on short-term lease (less than 10 years)	**13**	6
	1,108	1,850

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

25 Due to central banks

Group

	As at 31 December	
	2006	2005
Special foreign exchange deposits from PRC Government agencies	**41,956**	28,873
Borrowings from central banks	**25**	520
Others	**393**	662
	42,374	30,055

Bank

	As at 31 December	
	2006	2005
Special foreign exchange deposits from PRC Government agencies	**41,956**	28,848
Borrowings from central banks	**—**	520
Others	**393**	662
	42,349	30,030

26 Government certificates of indebtedness for bank notes issued and bank notes in circulation

Bank of China (Hong Kong) Limited and Bank of China Macau Branch are note issuing banks for Hong Kong dollar and Macau Pataca notes in Hong Kong and Macau, respectively. Under local regulations, these two entities are required to place deposits of funds to the Hong Kong and Macau governments respectively to secure the currency notes in circulation.

Bank notes in circulation represent the liabilities in respect of Hong Kong Dollar notes and Macau Pataca notes in circulation, issued respectively by Bank of China (Hong Kong) Limited and Bank of China Macau branch.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

27 Derivative financial instruments and liabilities at fair value through profit or loss

Group

	As at 31 December	
	2006	2005
Derivative financial instruments liabilities (Note V.16)	**14,323**	15,752
Liabilities at fair value through profit or loss		
Structured deposits	**86,474**	70,069
Short positions in foreign currency debt securities	**8,690**	3,740
Short position in exchange fund bills	**3,561**	1,613
	98,725	75,422
	113,048	91,174

Bank

	As at 31 December	
	2006	2005
Derivative financial instruments liabilities (Note V.16)	**9,643**	11,606
Liabilities at fair value through profit or loss		
Structured deposits	**77,498**	63,507
Short positions in foreign currency debt securities	**3,943**	1,210
	81,441	64,717
	91,084	76,323

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

28 Due to customers

Group

	As at 31 December	
	2006	2005
Demand deposits		
Corporate customers	**979,653**	836,763
Individual customers	**770,583**	667,957
	1,750,236	1,504,720
Time deposits		
Corporate customers	**549,118**	511,983
Individual customers	**1,645,914**	1,554,369
	2,195,032	2,066,352
Security and margin deposits	**145,850**	128,392
Total	**4,091,118**	3,699,464

Bank

	As at 31 December	
	2006	2005
Demand deposits		
Corporate customers	**883,939**	747,059
Individual customers	**565,893**	492,876
	1,449,832	1,239,935
Time deposits		
Corporate customers	**434,924**	404,500
Individual customers	**1,334,994**	1,242,669
	1,769,918	1,647,169
Security and margin deposits	**138,815**	122,083
Total	**3,358,565**	3,009,187

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

29 Bonds issued

Group and Bank

				As at 31 December	
	Issue date	Maturity date	Interest rate	**2006**	2005
Bonds issued					
1994 US Dollar Debt Securities	10 March 1994	15 March 2014	8.25%	**173**	179
Subordinated bonds issued					
2004 RMB Debt Securities(1)					
First Tranche	7 July 2004	20 July 2014	4.87%	**14,070**	14,070
Second Tranche	22 October 2004	16 November 2014	4.94%	**12,000**	12,000
2005 RMB Debt Securities(2)					
First Tranche	18 February 2005	4 March 2015	4.83%	**15,930**	15,930
Second Tranche (fixed rate)	18 February 2005	4 March 2020	5.18%	**9,000**	9,000
Second Tranche (floating rate)	18 February 2005	4 March 2015	floating rate	**9,000**	9,000
				60,000	60,000
				60,173	60,179

(1) Pursuant to Yinfu [2004] No. 35 "Response of the PBOC on the Issuance of Subordinated Bonds by Bank of China" and Yinjianfu [2004] No. 81 "Response of the CBRC on the Issuance of Subordinated Bonds by Bank of China", the Bank issued the following subordinated bonds:

The first tranche of subordinated bonds issued on 7 July 2004 has a maturity of 10 years, with a fixed coupon rate of 4.87%, paid annually. The Bank has the option to redeem all or part of the bonds at face value on 20 July 2009. If the Bank does not exercise this option, the annual coupon rate of the bonds for the second 5-year period shall be the original coupon rate plus 2.8%, and shall remain fixed for the remaining term of the bonds.

The second tranche of subordinated bonds issued on 22 October 2004 has a maturity of 10 years, with a fixed coupon rate of 4.94%, paid annually. The holders had the option to convert, at face value, all or part of the bonds to floating rate debt of an equivalent amount on 16 November 2005 or 16 November 2006. None of the bond holders exercised these options. The Bank has the option to redeem all or part of the bonds at face value on 16 November 2009. If the Bank does not exercise this option, the coupon rate for the second 5-year period shall be the original coupon rate plus 3%, and shall be fixed for the remaining term of the bonds.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

29 Bonds issued (Continued)

(2) The first tranche of subordinated bonds issued on 18 February 2005 has a maturity of 10 years, with a fixed coupon rate of 4.83%, paid annually. The Bank has the option to redeem all or part of the bonds at face value on 4 March 2010. If the Bank does not exercise this option, the annual coupon rate of the bonds for the second 5-year period shall be the original coupon rate plus 3%, and shall remain fixed for the remaining term of the bonds.

The second tranche of subordinated bonds issued on 18 February 2005 comprises a fixed rate portion and a floating rate portion.

The second tranche of fixed rate subordinated bonds issued on 18 February 2005 has a maturity of 15 years, with a fixed coupon rate of 5.18%, paid annually. The Bank has the option to redeem all or part of the bonds at face value on 4 March 2015. If the Bank does not exercise this option, the annual coupon rate of the bonds for the third 5-year period shall be the original coupon rate plus 3%, and shall remain fixed through the maturity date.

The second tranche of floating rate subordinated bonds issued on 18 February 2005 has a maturity of 10 years, with a floating rate based on a 7-day domestic money market rate, paid semi-annually. The Bank has the option to redeem all or part of the bonds at face value on 4 March 2010. If the Bank does not exercise this option, the floating rate for the second 5-year period shall be the original floating rate plus 1%.

These RMB denominated bonds are subordinated to all other claims on the assets of the Bank, except those of the equity holders. In the calculation of the Group's capital adequacy ratio, these bonds qualify for inclusion as supplementary capital in accordance with the relevant CBRC guidelines.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

30 Other borrowings

Group

	As at 31 December	
	2006	2005
Special purpose borrowings[1]		
Export credit loans	**13,955**	17,147
Foreign government loans	**17,577**	18,414
Other subsidized loans	**14,474**	16,603
	46,006	52,164
Term loans and other borrowings[2]	**17,392**	—
	63,398	52,164

Bank

	As at 31 December	
	2006	2005
Special purpose borrowings[1]		
Export credit loans	**13,955**	17,147
Foreign government loans	**17,577**	18,414
Other subsidized loans	**14,474**	16,603
	46,006	52,164

(1) Special purpose borrowings are long-term borrowings in multiple currencies from foreign governments and/or banks in the form of export credit loans, foreign government loans and other subsidized loans. These special purpose loans are normally used to finance projects of special commercial purpose in the PRC and the Bank is obliged to repay these loans when they fall due.

As of 31 December 2006, the maturity of special purpose borrowings ranges from within 1 month to 36 years. The interest bearing special purpose borrowings bear floating and fixed interest rates ranging from 0.2% to 9.2%. These terms are consistent with those related to similar development loans from these entities.

(2) These term loans and other borrowings relate to the financing of the aircraft leasing business of SALE, a wholly owned subsidiary of the Bank.

As at 31 December 2006, these term loans and other borrowings have a maturity ranging from within 5 months to 12 years and bear floating and fixed interest rates ranging from 5.55% to 7.56%. The term loans and other borrowings of RMB16.2 billion are secured by aircraft of the Group. See Note V.22.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

31 Retirement benefit obligations

The Group recognizes a liability for the present value of the unfunded obligation relating to retirement benefits payable to certain retired and early retired employees in the consolidated balance sheet. As of 31 December 2006 and 2005, the actuarial liabilities in relation to the supplemental benefit obligation for employees who retired prior to 31 December 2003 and early retirement obligation existing at the respective year-end dates were RMB7,444 million and RMB7,052 million, which were assessed by Hewitt Associates LLC and BOC Group Life Assurance Company Limited respectively, using the projected unit credit actuarial cost method.

The amounts of retirement benefit costs recognized in the income statement comprise:

Group and Bank

	2006	2005
Interest cost	**236**	274
Net actuarial loss recognized in the year	**1,155**	3,084
Total (Note V.8)	**1,391**	3,358

The movements of the net liabilities recognized in the balance sheets are as follow:

Group and Bank

	2006	2005
At 1 January	**7,052**	4,274
Amounts recognized in the income statement as above	**1,391**	3,358
Benefits paid	**(999)**	(580)
At 31 December	**7,444**	7,052

Primary assumptions used:

	As at 31 December	
	2006	2005
Discount rate	**3.60%**	4.60%
Pension Benefit Inflation rate	**2.00%**	2.00%
Medical Benefit Inflation rate	**7.12%**	7.12%

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

32 Share option schemes

(1) *Share Appreciation Rights Plan*

In November 2005, the Bank's Board of Directors and equity holders approved and adopted a Share Appreciation Rights Plan under which eligible participants including directors, supervisors, management and other personnel designated by the Board, will be granted share appreciation rights, up to 25% of which will be exercisable each year beginning on the third anniversary date from the date of the grant. The share appreciation rights will be valid for seven years from the date of grant. Eligible participants will be entitled to receive an amount equal to the difference, if any, between the average closing market price of the Bank's H shares in the ten days prior to the date of grant and the average closing market price of the Bank's H shares in the 12 months prior to the date of exercise as adjusted for any change in the Bank's equity. The plan provides cash-settled share-based payment only and accordingly, no shares will be issued under the share appreciation rights plan.

No share appreciation rights were granted during the year ended 31 December 2006 and 2005, and no rights were outstanding under such plan as of 31 December 2006 and 2005.

(2) *Share Option Scheme and Sharesave Plan*

On 10 July 2002, the shareholders of BOCHK Holdings, approved and adopted two share option schemes, namely, the Share Option Scheme and the Sharesave Plan.

No options were granted pursuant to the Share Option Scheme or the Sharesave Plan during the period from 10 July 2002 to 31 December 2006.

(3) *BOCHK Holdings Pre-listing Share Option Scheme*

On 5 July 2002, certain of the Bank's directors, senior management personnel and employees of the Group were granted options by BOC Hong Kong (BVI) Limited ("BOCHK (BVI)"), the immediate holding company of BOCHK Holdings, pursuant to a Pre-listing Share Option Scheme to purchase from BOCHK (BVI) an aggregate of 31,132,600 previously issued and outstanding shares of BOCHK Holdings for HKD8.50 per share. These options, with a ten-year term, vest ratably over four years from 25 July 2002. No further offers to grant any options under the Pre-listing Share Option Scheme will be made. The Group has no legal or constructive obligation to repurchase or settle the options in cash. The Group has taken advantage of the transitional provision of IFRS 2 under which the required recognition and measurements have not been applied to the options granted to employees of the Group on or before 7 November 2002.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

32 Share option schemes (Continued)

(3) *BOCHK Holdings Pre-listing Share Option Scheme (Continued)*

Details of the movement of share options outstanding are as follows:

	Directors and key management of BOCHK (BVI)	Other employees	Others[1]	Total number of share options
At 1 January 2006	**6,142,500**	**10,619,250**	**1,446,000**	**18,207,750**
Transferred	**239,000**	**(239,000)**	**—**	**—**
Less: Share options exercised during the year	**—**	**(4,278,700)**	**—**	**(4,278,700)**
Less: Share options lapsed during the year	**—**	**(43,500)**	**—**	**(43,500)**
At 31 December 2006	**6,381,500**	**6,058,050**	**1,446,000**	**13,885,550**
At 1 January 2005	6,142,500	12,849,300	1,446,000	20,437,800
Less: Share options exercised during the year	—	(2,121,550)	—	(2,121,550)
Less: Share options lapsed during the year	—	(108,500)	—	(108,500)
At 31 December 2005	6,142,500	10,619,250	1,446,000	18,207,750

(1) These represent share options held by former directors or former employees of BOCHK Holdings.

Regarding the share options exercised during the years ended 31 December 2006 and 2005 the weighted average share price of BOCHK Holdings' shares at the time of exercise was HKD16.50 (equivalent to RMB16.91), and HKD15.01 (equivalent to RMB15.61) respectively.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

33 Deferred income taxes

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes related to the same fiscal authority. The table below includes the deferred income tax assets and liabilities of the Group and the Bank after offsetting qualifying amounts:

Group

	As at 31 December	
	2006	2005
Deferred income tax assets	**21,396**	20,504
Deferred income tax liabilities	**(3,029)**	(2,136)
	18,367	18,368

Bank

	As at 31 December	
	2006	2005
Deferred income tax assets	**21,843**	20,389
Deferred income tax liabilities	**(32)**	(23)
	21,811	20,366

The movements of the deferred income tax account are as follows:

Group

	2006	2005
At 1 January	**18,368**	19,215
Credited/(charged) to income statement (Note V.10)	**91**	(962)
Available-for-sale securities	**622**	94
Acquisition of a subsidiary (Note V. 42)	**(786)**	—
Exchange differences	**72**	21
At 31 December	**18,367**	18,368

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

33 Deferred income taxes (Continued)

Bank

	2006	2005
At 1 January	**20,366**	21,518
Credited/(charged) to income statement	**807**	(636)
Available-for-sale securities	**632**	(498)
Exchange differences	**6**	(18)
At 31 December	**21,811**	20,366

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

Group

	As at 31 December	
	2006	2005
Deferred income tax assets		
Asset impairment provisions	**20,205**	17,744
Fair value changes of trading assets and other financial instruments at fair value through profit or loss, available-for-sale securities and derivative financial instruments	**3,482**	3,204
Statutory asset revaluation surplus	**2,539**	2,640
Pension and other benefit costs	**821**	578
Other temporary differences	**699**	311
	27,746	24,477
Deferred income tax liabilities		
Fair value changes of trading assets and other financial instruments at fair value through profit or loss, available-for-sale securities and derivative financial instruments	**(5,124)**	(3,643)
Depreciation of property and equipment	**(1,688)**	(442)
Fair value changes of investment property	**(1,928)**	(1,978)
Other temporary differences	**(639)**	(46)
	(9,379)	(6,109)
	18,367	18,368

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

33 Deferred income taxes (Continued)

Bank

	As at 31 December	
	2006	2005
Deferred income tax assets		
Asset impairment provisions	**20,103**	17,596
Fair value changes of trading assets and other financial instruments at fair value through profit or loss, available-for-sale securities and derivative financial instruments	**3,458**	3,159
Statutory asset revaluation surplus	**2,539**	2,640
Pension and other benefit costs	**821**	578
Other temporary differences	**91**	131
	27,012	24,104
Deferred income tax liabilities		
Fair value changes of trading assets and other financial instruments at fair value through profit or loss, available-for-sale securities and derivative financial instruments	**(5,124)**	(3,643)
Depreciation of property and equipment	**(69)**	(63)
Other temporary differences	**(8)**	(32)
	(5,201)	(3,738)
	21,811	20,366

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

33 Deferred income taxes (Continued)

The deferred income tax (charge)/credit in the income statement comprises the following temporary differences:

Group

	Year ended 31 December	
	2006	2005
Asset impairment provisions	**2,461**	1,466
Fair value changes of trading assets and other financial instruments at fair value through profit or loss, available-for-sale securities and derivative financial instruments	**(1,825)**	(2,229)
Pension and other benefit costs	**243**	183
Statutory asset revaluation surplus	**(101)**	(140)
Fair value changes of investment property	**(18)**	(172)
Other temporary differences	**(669)**	(70)
	91	(962)

Subsequent to the balance date on 16 March 2007, the National People's Congress approved the new PRC Enterprise Income Tax Law. The details and the Group's preliminary assessment of the impact of the relevant changes are discussed in Note V.43 (1).

34 Other liabilities

Group

	As at 31 December	
	2006	2005
Items in the process of clearance and settlement	**65,510**	52,957
Interest payable	**33,834**	27,024
Salary and welfare payable	**9,052**	6,031
Payable to the MOF (Note V.40 (1))	**8,680**	17,362
Allowance for litigation losses[1]	**1,985**	1,516
Others[2]	**34,395**	31,382
Total	**153,456**	136,272

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

34 Other liabilities (Continued)

Bank

	As at 31 December	
	2006	2005
Items in the process of clearance and settlement	**50,877**	48,829
Interest payable	**31,747**	25,291
Salary and welfare payable	**7,652**	5,389
Payable to the MOF (Note V.40 (1))	**8,680**	17,362
Allowance for litigation losses[(1)]	**1,783**	1,516
Others	**11,788**	14,147
Total	**112,527**	112,534

(1) Movements of allowance for litigation losses are as follows:

Group

	2006	2005
At 1 January	**1,516**	1,310
Provision for the year (Note V.7)	**897**	712
Utilized during the year	**(428)**	(506)
At 31 December (Note V. 38(1))	**1,985**	1,516

Bank

	2006	2005
At 1 January	**1,516**	1,310
Provision for the year	**692**	712
Utilized during the year	**(425)**	(506)
At 31 December (Note V. 38(1))	**1,783**	1,516

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

34 Other liabilities (Continued)

(2) Included in other liabilities of the Group are insurance liabilities as of 31 December 2006 and 31 December 2005 arising from insurance contracts analyzed as follows:

Group

	As at 31 December	
	2006	2005
Long term insurance contracts	**14,625**	8,383
General insurance contracts	**2,200**	2,079
Total insurance liabilities, net	**16,825**	10,462

35 Share capital and capital reserve

Group

	Number of ordinary shares (in millions)	Ordinary shares of RMB1 each	Capital reserve	Treasury shares	Total
Balance at 1 January 2005	186,390	186,390	(10,432)	—	175,958
Issue of ordinary shares (net of issuance costs)(1)	23,037	23,037	3,964	—	27,001
Capital contribution from an equity holder(4)	—	—	500	—	500
Others	—	—	14	—	14
Balance at 31 December 2005/ 1 January 2006	**209,427**	**209,427**	**(5,954)**	**—**	**203,473**
Issue of ordinary shares (net of issuance costs)(1)	**44,412**	**44,412**	**72,567**	**—**	**116,979**
Purchase of treasury Shares(3)	**(50)**	**—**	**—**	**(216)**	**(216)**
Others	**—**	**—**	**4**	**—**	**4**
Balance at 31 December 2006	**253,789**	**253,839**	**66,617**	**(216)**	**320,240**

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

35 Share capital and capital reserve (Continued)

Bank

	Number of ordinary shares (in millions)	Ordinary shares of RMB1 each	Capital reserve	Treasury shares	Total
Balance at 1 January 2005	186,390	186,390	(10,511)	—	175,879
Issue of ordinary shares (net of issuance costs)(1)	23,037	23,037	3,964	—	27,001
Capital contribution from an equity holder(4)	—	—	500	—	500
Others	—	—	(7)	—	(7)
Balance at 31 December 2005/ 1 January 2006	**209,427**	**209,427**	**(6,054)**	**—**	**203,373**
Issue of ordinary shares (net of issuance costs)(1)	**44,412**	**44,412**	**72,219**	**—**	**116,631**
Others	**—**	**—**	**1**	**—**	**1**
Balance at 31 December 2006	**253,839**	**253,839**	**66,166**	**—**	**320,005**

As at 31 December 2006, the Bank's share capital is as follows:

Domestic listed A shares, par value RMB1.00 per share(2)	**177,818,910,740**
Overseas listed H shares, par value RMB1.00 per share(2)	**76,020,251,269**
Total	**253,839,162,009**

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

35 Share capital and capital reserve (Continued)

(1) In December 2005, the Bank issued 23,037,009,860 ordinary shares with a par value of RMB1 per share to certain strategic investors for total consideration of RMB27,057 million.

In March 2006, the Bank issued 8,514,415,652 ordinary shares to the National Council for Social Security Fund at a cash consideration of RMB10,000 million including share premium of RMB1,481 million.

In June 2006, the Bank issued 29,403,878,000 H shares with a par value of RMB1 per share, with share premium totaling RMB58,128 million (net of share issuance costs of RMB2,435 million), through a global offering to Hong Kong and overseas investors ("Global Offering"). As part of the Global Offering, 46,616,373,269 shares owned by equity holders prior to the Global Offering, except Huijin, were converted into H shares. Each of these investors, with the exception of Huijin, had previously entered into separate investor rights agreements with Huijin and the Bank. Among other things, the provisions of these investor rights agreements included net asset protection, price protection and put options where Huijin has agreed to undertake to meet the settlement of these rights and obligations. Except for the net asset protection which will expire in 2008, the related price protection and put option rights lapsed following the completion of the Global Offering by the Bank. The Bank has no obligation to Huijin with respect to the potential settlement of these rights and obligations.

In June 2006, the Bank issued 6,493,506,000 A shares with a par value of RMB1 per share with share premium totaling RMB12,958 million (net of share issuance costs of RMB549 million), through the A share initial public offering to domestic investors. Upon the completion of the A share initial public offering, 171,325,404,740 shares held by Huijin prior to the A share initial public offering were converted into A shares.

(2) All A shares and H shares rank *pari passu* with the same rights and benefits.

(3) As at 31 December 2006, a wholly owned subsidiary of the Group held certain listed shares of the Bank in relation to its derivative and arbitrage business. These shares are treated as treasury shares, a deduction from shareholders' equity. Gains and losses on sale or redemption of the treasury shares are credited or charged to reserves. The total number of treasury shares as at 31 December 2006 was 50 million (2005: Nil).

(4) In accordance with the resolution of the seventh extraordinary meeting of the shareholder in 2005, Huijin agreed to make a payment of RMB500 million, funded by a specific dividend paid by the Bank relating to 2004 undistributed profits, as initial funding for the Bank's Annuity Plan. This payment has been recorded as a capital contribution in the capital reserve and as an operating expense in the income statement in 2005 (Note V.8).

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

36 Statutory reserves, general and regulatory reserves and undistributed profits

Group

	Statutory reserves	General and regulatory reserves	Undistributed profits	Total
Balance at 1 January 2006	**5,987**	**5,109**	**10,188**	**21,284**
Net profit	**—**	**—**	**42,830**	**42,830**
Appropriation to statutory reserves(1)	**4,393**	**—**	**(4,393)**	**—**
Appropriation to general reserve and regulatory reserve(2)	**—**	**8,828**	**(8,828)**	**—**
Dividends(3)	**—**	**—**	**(1,375)**	**(1,375)**
Sale of shares in subsidiaries	**—**	**(3)**	**3**	**—**
Balance at 31 December 2006	**10,380**	**13,934**	**38,425**	**62,739**

	Statutory reserves	General and regulatory reserves	Undistributed profits	Total
Balance at 1 January 2005	3,140	419	16,547	20,106
Net profit	—	—	25,921	25,921
Appropriation to statutory reserves(1)	2,847	—	(2,847)	—
Appropriation to general reserve and regulatory reserve(2)	—	4,690	(4,690)	—
Adoption of equity accounting for investment in associates	—	—	2,194	2,194
Dividends(3)	—	—	(26,937)	(26,937)
Balance at 31 December 2005	5,987	5,109	10,188	21,284

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

36 Statutory reserves, general and regulatory reserves and undistributed profits (Continued)

Bank

	Statutory reserves	General and regulatory reserves	Undistributed profits	Total
Balance at 1 January 2006	**5,465**	**2,618**	**(8,709)**	**(626)**
Net profit	**—**	**—**	**37,493**	**37,493**
Appropriation to statutory reserves[(1)]	**4,249**	**—**	**(4,249)**	**—**
Appropriation to general reserve and regulatory reserve[(2)]	**—**	**8,775**	**(8,775)**	**—**
Dividends[(3)]	**—**	**—**	**(1,375)**	**(1,375)**
Balance at 31 December 2006	**9,714**	**11,393**	**14,385**	**35,492**

	Statutory reserves	General and regulatory reserves	Undistributed profits	Total
Balance at 1 January 2005	2,766	417	2,943	6,126
Net profit	—	—	20,185	20,185
Appropriation to statutory reserves[(1)]	2,699	—	(2,699)	—
Appropriation to general reserve and regulatory reserve[(2)]	—	2,201	(2,201)	—
Dividends[(3)]	—	—	(26,937)	(26,937)
Balance at 31 December 2005	5,465	2,618	(8,709)	(626)

(1) Statutory reserves

Under relevant PRC Laws, the Bank is required to transfer 10% of its net profit, as determined under PRC GAAP, to a non-distributable Statutory surplus reserve. Appropriation to the Statutory surplus reserve may cease when the balance of such reserves has reached 50% of the share capital. Subject to the approval of the shareholders, the Statutory surplus reserve can be used for replenishing the accumulated loss or increasing the Bank's share capital. The Statutory surplus reserve amount used to increase the share capital is limited to a level where the balance of Statutory surplus reserve after such capitalization is not less than 25% of the share capital.

In addition, some overseas branches and subsidiaries are required to transfer certain percentages of their net profit to the Statutory surplus reserve as stipulated by local banking authorities.

In accordance with a resolution of the Board of Directors dated 22 March 2007, the Bank appropriated 10% of the net profit for the year ended 31 December 2006 as reported in the PRC statutory financial statements to the Statutory surplus reserves, amounting to RMB4,249 million (2005: RMB2,749 million).

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

36 Statutory reserves, general and regulatory reserves and undistributed profits (Continued)

(2) General and regulatory reserves

Pursuant to Caijin [2005] No. 49 "Measures on General Provision for Bad and Doubtful Debts for Financial Institutions" issued by MOF on 17 May 2005, banks and certain other financial institutions in the PRC are required to maintain an adequate allowance for impairment losses against their risk assets as defined. In addition to the specific allowance for impairment losses, financial institutions are required to establish and maintain a general reserve within Shareholders' equity, through the appropriation of income to address unidentified potential impairment losses. According to Caijin [2005] No.49, the general reserve should not be less than 1% of the aggregate amount of risk assets as defined by this policy, before any allowance for impairment losses at the balance sheet date. The Bank intends to achieve the required reserve level within 3 years.

In accordance with a resolution dated 22 March 2007 and on the basis of the Bank's profit for the year ended 31 December 2006, the Board of Directors of the Bank approved the appropriation of RMB8,764 million (2005: RMB2,184 million) to the general reserves for the year ended 31 December 2006. Total amount of general reserves achieved 40% of the required level.

The Regulatory reserve mainly refers to the reserve amount set aside by BOC Hong Kong (Group) Limited, a subsidiary of the Group, for general banking risks, including future losses or other unforeseeable risks. As at 31 December 2006 and 2005, the reserve amount set aside by BOC Hong Kong (Group) Limited was RMB2,533 million and RMB2,475 million respectively.

(3) Dividends

According to the 2004 profit distribution plan approved at the second extraordinary general shareholder's meeting held on 7 September 2005, the Bank distributed a cash dividend of RMB0.076 per ordinary share totalled RMB14,200 million.

According to the profit distribution plan for the first half of 2005 approved at the seventh extraordinary general shareholders' meeting held on 31 December 2005, the Bank distributed a cash dividend of RMB0.068 per ordinary shares totalled RMB12,737 million to the equity holder of the Bank as of 29 December 2005.

According to the 2005 profit distribution plan approved at a post-adjournment session of the Annual General Meeting held on 30 April 2006, the Bank distributed a dividend of RMB0.0066 per ordinary share totalled RMB1,375 million to the equity holders of the Bank as of 31 December 2005.

A dividend in respect of 2006 of RMB0.04 per share, amounting to a total dividend of RMB10,154 million is to be proposed for approval at the Annual General Meeting to be held on 14 June 2007. These financial statements do not reflect this dividend payable, which will be accounted for in shareholders' equity as an appropriation of undistributed profits in the year ending 31 December 2007.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

37 Reserve for fair value changes of available-for-sale securities

Group

	2006	2005
At 1 January	**1,899**	2,730
Net (losses)/gains from changes in fair value	**(1)**	813
Net (gains)/losses transferred to net profit on disposal	**(508)**	525
Reversal of fair value changes of Huaneng International Power Development Corporation (Note V.21)	**—**	(2,254)
Deferred income taxes	**619**	85
At 31 December	**2,009**	1,899

Bank

	2006	2005
At 1 January	**280**	(815)
Net (losses)/gains from changes in fair value	**(2,237)**	835
Net losses transferred to net profit on disposal	**287**	758
Deferred income taxes	**632**	(498)
At 31 December	**(1,038)**	280

38 Contingent liabilities and commitments

(1) *Legal proceedings*

As at 31 December 2006, the Group was involved in certain lawsuits as defendants arising from its normal business operations. As at 31 December 2006 and 2005, provisions of RMB1,985 million and RMB1,516 million were made based on court judgments or the advice of counsel. After consulting legal professionals, management of the Group believes that the ultimate outcome of these lawsuits will not have a material impact on the financial position or operations of the Group. Allowances for litigation losses based on the opinions of the Group's internal and external legal counsel are set forth in Note V.34.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

38 Contingent liabilities and commitments (Continued)

(2) *Assets pledged*

Assets pledged as collateral for repurchase and short positions with other banks and financial institutions are set forth in the tables below. As at 31 December 2006, the Group and the Bank had such Repo agreements and short positions amounting to RMB54,806 million (2005: RMB62,108 million) and RMB51,245 million (2005: RMB59,340 million) respectively. All such agreements mature within twelve months from inception.

Group

	As at 31 December	
	2006	2005
Precious metals	—	2,617
Bills (Note V.17)	—	11,968
Debt securities (Note V.18(7))	**55,212**	49,658
Total	**55,212**	64,243

Bank

	As at 31 December	
	2006	2005
Precious metals	—	2,617
Bills (Note V.17)	—	11,968
Debt securities (Note V.18(7))	**51,632**	45,106
Total	**51,632**	59,691

The Group has accepted cash collateral and security collateral that it is permitted to sell or re-pledge in connection with its Reverse repo agreements and securities lending transactions. The fair value of the collateral accepted by the Group and the Bank was RMB77,657 million (2005: RMB69,789 million) as of 31 December 2006. Both the Group and the Bank had an obligation to return collateral that it has sold with a fair value of RMB3,728 million (2005: RMB1,130 million) as of 31 December 2006.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

38 Contingent liabilities and commitments (Continued)

(3) *Capital commitments*

Group

	As at 31 December	
	2006	2005
Contracted but not provided for	**38,741**	1,893
Authorized but not contracted for	**1,536**	2,687
	40,277	4,580

Bank

	As at 31 December	
	2006	2005
Contracted but not provided for	**3,210**	1,731
Authorized but not contracted for	**1,531**	2,671
	4,741	4,402

(4) *Operating leases*

According to the irrevocable operating lease contracts, the minimum rental payments that should be paid by the Group and the Bank in the future are summarized as follows:

Group

	As at 31 December	
	2006	2005
Within one year	**1,604**	1,371
One to two years	**1,281**	1,085
Two to three years	**969**	807
Above three years	**2,832**	2,546
	6,686	5,809

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

38 Contingent liabilities and commitments (Continued)

(4) *Operating leases (Continued)*

Bank

	As at 31 December	
	2006	2005
Within one year	**1,286**	1,157
One to two years	**1,069**	949
Two to three years	**863**	756
Above three years	**2,808**	2,532
	6,026	5,394

(5) *Certificate Treasury Bond redemption commitments*

The Bank is entrusted by the MOF to underwrite certain Certificate Treasury Bonds. The investors of Certificate Treasury Bonds 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 Certificate Treasury Bonds plus unpaid interest in accordance with the early redemption arrangement.

As at 31 December 2006, the principal value of the bonds amounts to RMB84,500 million (2005: RMB80,965 million). The original maturities of these bonds vary from 1 to 5 years. As the deposits base rate established by PBOC is currently lower than the yields on all issue of Certificate Treasury Bonds, management expects the amount of redemption before the maturity dates of those bonds through the Bank will not be material.

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

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

38 Contingent liabilities and commitments (Continued)

(6) *Credit commitments*

Group

	As at 31 December	
	2006	2005
Credit commitments[(i)]		
with an original maturity of under one year	**212,179**	182,965
with an original maturity of one year or over	**258,392**	201,745
Acceptances	**217,093**	195,234
Letters of guarantee issued	**290,205**	212,987
Letters of credit issued	**109,083**	101,195
Others	**870**	1,636
Total	**1,087,822**	895,762

Bank

	As at 31 December	
	2006	2005
Credit commitments[(i)]		
with an original maturity of under one year	**98,392**	72,359
with an original maturity of one year or over	**211,520**	169,322
Acceptances	**212,163**	191,034
Letters of guarantee issued	**286,050**	202,994
Letters of credit issued	**93,613**	86,824
Others	**490**	1,431
Total	**902,228**	723,964

(i) Credit commitments represent general credit facility limits for our corporate customers. These credit facilities may be drawn in the form of cash advances or the issuance of letters of credit, acceptances or letters of guarantee.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

38 Contingent liabilities and commitments (Continued)

(7) *Credit risk weighted amounts of off balance sheet exposures*

Group

	As at 31 December	
	2006	2005
Contingent liabilities and commitments	**413,678**	329,697

The credit risk weighted amounts are the amounts calculated in accordance with the guidelines issued by the CBRC and are dependent on, among other factors, the creditworthiness of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% for contingent liabilities and commitments.

The credit risk weighted amounts stated above have not taken into account the effects of netting arrangements.

39 Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances with an original maturity of less than three months:

Group

	As at 31 December	
	2006	2005
Cash and due from banks (Note V.12)	**38,805**	40,087
Balances with central banks (Note V.13)	**101,776**	108,149
Placements with banks and other financial institutions (Note V.14)	**305,618**	233,301
Short term bills and notes (Note V.18(5))	**73,745**	15,575
Total	**519,944**	397,112

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions

Related parties are those parties that have the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. Parties are also considered to be related if they are subject to common control. Related parties may be individuals or other entities. The Group is subject to the control of the State Council of the PRC Government through Huijin.

(1) *Financial restructuring arrangements with the MOF*

As at 31 December 2006, the Group had a liability of RMB8,680 million (2005: RMB17,362 million) to the MOF in respect of the excess of the appraised value of the net assets of the Bank as at 31 December 2003 over the amount of the share capital of the Bank as at the date of the government directed financial restructuring which involved the sales of non performing loans and policy related assets and various capital injections by the government through Huijin in the conversion of the Bank into a joint stock limited company during 2003 and 2004. This liability included in "other liabilities" is non-interest bearing and is to be paid in four annual installments before 31 December 2008 (Note V.34).

(2) *Transactions with the MOF and the PBOC*

The Group enters into banking transactions with the MOF and the PBOC in the normal course of business. These include purchase and redemption of investment securities issued by the MOF and the PBOC; maintenance of mandatory reserves; other deposits and amounts due to the PBOC; underwriting and distribution of Certificate Treasury Bonds issued by the MOF through the Group's branch network and earning commission income based on such bonds sold. Details of mandatory reserves and other deposits with and investments in securities issued by the PBOC are set out in Note V.13 and Note V.18 respectively. Details of foreign currency spot and swap transactions with the PBOC are set out in Note III.5 and Note V.16. Details of balances due to the PBOC are set out in Note V.25. Details of other transactions and balances are set forth below.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

(2) *Transactions with the MOF and the PBOC (Continued)*

(i) *Treasury bonds and PBOC bonds*

The Group purchases and redeems bonds issued by the MOF and the PBOC. The volume of such transactions and related interest rate range for the years ended 31 December 2006 and 2005 and the outstanding balances as of the respective year end dates are set out below:

	Year ended 31 December	
	2006	2005
Purchases during the year	**574,169**	642,574
Redemption/sales during the year	**570,554**	384,559
Interest rate range (Note V.40(7))	**1.22%–9.00%**	0.41%–9.00%
	2006	2005
Outstanding balance at 1 January	**533,625**	271,120
Outstanding balance at 31 December	**539,828**	533,625

(ii) *Transactions with the MOF in relation to the underwriting and distribution of Certificate Treasury Bonds*

The Group underwrites Certificate Treasury Bonds issued by the MOF and undertakes the role of a distributor of these bonds through its branch network and earns commission income based on the amount of such bonds sold (Note V.38(5)).

	Year ended 31 December	
	2006	2005
Total distribution of Certificate Treasury Bonds in the year	**25,350**	26,000
Commission income earned in the year	**269**	252
	2006	2005
Outstanding balance at 1 January	**10,185**	8,717
Outstanding balance at 31 December	**12,800**	10,185

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

(3) *Transactions with Huijin*

Huijin became the equity holder of the Bank from 30 December 2003. As of December 31 2006, Huijin owned a 67.49% equity interest in the Bank following the completion of the Bank's Global Offering and A share initial public offering.

In 2005, the Bank entered into a foreign currency option agreement with Huijin (as discussed in detail in Note V.16 (2)) to reduce its foreign currency exposure and as at 31 December 2006 and 2005, the outstanding notional amount of the foreign currency option agreement was USD18 billion.

On 15 May 2006, a dividend of RMB1,375 million, relating to the year ended 31 December 2005 was paid to Huijin, in accordance with the approval by the equity holders at a post-adjournment session of the Annual General Meeting on 30 April 2006.

In accordance with the resolution of the seventh Extraordinary Meeting of the Shareholder in 2005, Huijin agreed to the appropriation of RMB500 million of distributed dividends in 2004, as start-up funding for the Bank's new annuity plan, as discussed in Note II.22. This payment has been recorded as a capital contribution in the Capital Reserve and as an operating expense in the income statement for the year ended December 31, 2005. See Note V.8.

Deposit

	2006	2005
At 1 January	**38,869**	—
Deposits received during the year	**288,128**	42,972
Deposits repaid during the year	**(304,937)**	(4,103)
At 31 December	**22,060**	38,869

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

(4) *Transactions with other companies controlled by Huijin*

Huijin also has controlling equity interests in certain other bank and non-bank entities in the PRC. The Group enters into banking transactions with these companies in the normal course of its business. These include trading assets, investment securities and money market transactions.

The volume of such transactions and related interest rate range for the years ended 31 December 2006 and 2005 and the outstanding balances with these companies as of 31 December 2006 and 2005 are as follows:

(i) *Trading assets and investment securities*

	Year ended 31 December	
	2006	2005
Purchases during the year	**1,207**	1,499
Redemptions/sales during the year	**1,804**	1,218
Interest rate range (Note V.40 (7))	**3.15%–6.54%**	0.26%–5.90%
	2006	2005
Outstanding balance at 1 January	**2,400**	2,183
Outstanding balance at 31 December	**1,762**	2,400

(ii) *Due from banks*

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.00%–5.40%**	0.00%–3.74%
	2006	2005
Outstanding balance at 1 January	**88**	94
Outstanding balance at 31 December	**121**	88

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

(4) *Transactions with other companies controlled by Huijin (Continued)*

(iii) *Placements with banks and other financial institutions*

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**2.40%–6.05%**	0.37%–5.50%
	2006	2005
Outstanding balance at 1 January	**2,318**	3,537
Outstanding balance at 31 December	**1,662**	2,318

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

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.00%–3.00%**	0.00%–2.50%
	2006	2005
Outstanding balance at 1 January	**2,076**	1,895
Outstanding balance at 31 December	**1,971**	2,076

(v) *Placements from banks and other financial institutions*

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.99%–4.25%**	0.09%–4.50%
	2006	2005
Outstanding balance at 1 January	**243**	—
Outstanding balance at 31 December	**106**	243

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

(5) *Transactions with other state controlled entities*

The Bank is subject to the control of the State Council of the PRC Government through Huijin, which also directly and indirectly controls a significant number of entities through its government authorities, agencies and affiliates. Accordingly, the Group has extensive transactions with other state controlled entities. The nature of these transactions for the year ended 31 December 2006 and 2005, conducted in the ordinary course of business, includes, but is not limited to, the following:

— Lending, provision of credit and guarantees and deposit taking;

— Inter-bank balance taking and placing;

— Sale, purchase, underwriting and redemption of bonds issued by other state controlled entities;

— Rendering of foreign exchange, remittance, investment related services;

— Entrusted lending and provision of other custody services; and

— Purchasing of utilities, telecommunication and postal services.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

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

(i) *Due from banks*

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.00%–11.00%**	0.00%–4.67%
	2006	2005
Outstanding balance at 1 January	**3,547**	2,085
Outstanding balance at 31 December	**3,499**	3,547

No allowance for impairment losses on amounts due from banks has been recognized during the years ended 31 December 2006 and 2005.

(ii) *Placements with banks and other financial institutions*

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.07%–7.40%**	0.00%–6.09%
	2006	2005
Outstanding balance at 1 January	**68,794**	55,747
Outstanding balance at 31 December	**42,963**	68,794
Allowance for impairment losses	**(499)**	(546)

Impairment losses on placements with banks and other financial institutions recognized at 31 December 2006 and 2005 are immaterial.

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

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

(iii) *Loans and advances to customers*

As at 31 December 2006 and 2005, corporate loans accounted for 76% and 77%, respectively of the total loans and advances to customers. The remaining balances comprise personal loans primarily to individuals which are not individually significant. The Group's 3,000 largest outstanding corporate loans to single customers as at 31 December 2006 and 2005 (those with balances exceeding RMB100 million) accounted for 57.3% and 58.6%, respectively of the total outstanding corporate loans, amounting to RMB1,060,326 million and RMB1,003,638 million. Given that these large loans accounted for the majority of the Group's total corporate loan balances, the management is of the opinion that disclosure of related party transactions of these large borrowers as identified by management set forth below demonstrates the potential effect of the Group's lending to other state controlled entities.

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.20%–18.24%**	0.72%–16.99%
Impairment losses on individually assessed loans and advances for the year	**5,169**	4,741
	2006	2005
Outstanding balance at 1 January[1]	**471,500**	547,416
Outstanding balance at 31 December	**576,653**	638,460
Allowance for impairment losses on individually assessed loans and advances at 31 December	**(11,988)**	(14,308)

(1) For the years ended 31 December 2006 and 2005, the population of accounts was based on balances as of 31 December in the respective year.

The maturity analysis set out in Note III.7 gives an overview of the average turnover of the loan portfolio which provides a basis for assessing the average turnover of the loans and advances to related parties.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

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

(iv) *Trading assets and investment securities*

	Year ended 31 December	
	2006	2005
Purchases during the year	**276,278**	192,532
Redemptions/sales during the year	**245,303**	95,920
Interest rate range (Note V.40 (7))	**0.48%–8.25%**	0.39%–9.20%
	2006	2005
Outstanding balance at 1 January	**319,039**	222,084
Outstanding balance at 31 December	**349,173**	319,039
Allowance for impairment losses at 31 December	**(152)**	(156)

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

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.00%–4.82%**	0.00%–3.75%
	2006	2005
Outstanding balance at 1 January	**87,033**	54,802
Outstanding balance at 31 December	**124,466**	87,033

(vi) *Placements from banks and other financial institutions*

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.01%–7.60%**	0.00%–7.08%
	2006	2005
Outstanding balance at 1 January	**152,409**	84,813
Outstanding balance at 31 December	**104,486**	152,409

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

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

(vii) *Due to customers*

As at 31 December 2006 and 2005, approximately 59% and 60%, respectively of the balances due to customers are represented by balances due to personal customers which are not individually significant. Of the remaining 41% and 40%, of the balances due to customers as at 31 December 2006 and 2005, respectively, 47% and 50%, are represented by the Group's 4,000 largest corporate deposits amounting to RMB793,519 million and RMB728,475 million, respectively. Given that these deposits accounted for a significant portion of the Group's total corporate deposit balances, the management is of the opinion that disclosure of related party transactions of these large deposits as identified by the Group's management as set forth below demonstrates the potential effect of the Group's deposits from other state controlled entities.

	Year ended 31 December	
	2006	2005
Interest rate range (Note V.40 (7))	**0.00%–8.40%**	0.00%–6.40%
	2006	2005
Outstanding balance at 1 January[1]	**343,169**	299,827
Outstanding balance at 31 December	**464,088**	463,980

(1) For the years ended 31 December 2006 and 2005, the population of accounts was based on balances as of 31 December in the respective year.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

(6) *Transactions with associates and joint ventures*

The Group enters into banking transactions with associates and joint ventures in the normal course of business at commercial terms. These include loans and advances, deposit taking and such other normal banking businesses. The outstanding balances with associates and joint ventures and related allowance for impairment losses as of the respective year end dates, and the volume of transactions for the years ended 31 December 2006 and 2005 are stated below. The related interest income and expense amounts are not considered significant.

(i) *Loans and advances*

	2006	2005
Outstanding balance as of 1 January	**7,240**	1,246
Granted during the year	**381**	8,128
Repaid during the year	**(6,616)**	(989)
Write-off and other changes during the year	**(191)**	(1,145)
Outstanding balance as of 31 December	**814**	7,240
Allowance for impairment losses	**(18)**	(119)

(ii) *Deposits*

	2006	2005
Outstanding balance as of 1 January	**856**	1,227
Received during the year	**6,498**	3,879
Repaid and other changes during the year	**(4,065)**	(4,250)
Outstanding balance as of 31 December	**3,289**	856

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

40 Related party transactions (Continued)

(6) *Transactions with associates and joint ventures (Continued)*

(iii) *Trading assets and investment securities*

	2006	2005
Purchases during the year	—	1,307
Redemptions/sales during the year	188	1,123
Interest rate range (Note V.40 (7))	2.70–2.92%	1.61–2.92%

	2006	2005
Outstanding balance at 1 January	188	—
Outstanding balance at 31 December	—	188

(7) *Interest rate*

Interest rate disclosed in Note V.40(2) to (6) varies across product groups and transactions depending on maturity, credit risk of the counterparty and currency. In particular, given local market conditions, the spread of certain significant or long dated transactions can vary across the market.

(8) *Transactions with key management personnel*

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including Directors and Executive officers.

The Group enters into banking transactions with key management personnel in the normal course of business. During 2006 and 2005, there were no material transactions and balances with key management personnel on an individual basis.

The key management compensation for the year ended 31 December 2006 and 2005 is detailed as follows:

	Year ended 31 December	
	2006	2005
Short-term employment benefits	32	30
Post-employment benefits	1	1
Total	33	31

Included in the above key management compensation are RMB3.90 million and RMB3.34 million paid by Huijin in 2006 and 2005, respectively.

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

41 Balances with subsidiaries

Included in the following captions of the Bank's Balance sheets are balances with subsidiaries:

	As at 31 December	
	2006	2005
Due from banks	**3,234**	5,154
Placements with other banks and financial institutions	**36,673**	27,128
Due to other banks	**(4,111)**	(6,787)
Placements from other banks and financial institutions	**(11,647)**	(13,441)

42 Acquisition of subsidiaries

On 15 December 2006, Bank of China Group Investment Limited, a wholly owned subsidiary of the Bank, acquired 100% of the share capital of SALE for cash consideration of USD978 million (RMB7,627 million equivalent). See Note V.20.

The operating income of the acquired company was not significant to the Group for the year ended 31 December 2006.

The details of the fair value of the assets and liabilities acquired and goodwill arising as at 15 December 2006 are as follows:

	Fair value	**Acquiree's carrying amount**
Cash and cash equivalents	**2,254**	**2,254**
Property and equipment	**21,901**	**21,693**
Intangible assets	**1,856**	**—**
Other assets	**428**	**428**
Deferred income tax liabilities	**(777)**	**(260)**
Other liabilities	**(19,910)**	**(19,910)**
Net assets acquired	**5,752**	**4,205**
Goodwill (Note V.24)	**1,875**	
Total purchase consideration paid by cash	**7,627**	
Less: Cash and cash equivalents in subsidiary acquired	**(2,254)**	
Net cash outflow on acquisition	**5,373**	

(Amount in millions of Renminbi, unless otherwise stated)

V NOTES TO THE FINANCIAL STATEMENTS (Continued)

42 Acquisition of subsidiaries (Continued)

The goodwill is attributable to the high profitability of the acquired business and the significant synergies expected to arise. Fair value of assets and liabilities acquired were based on discounted cash flow models.

There was no provision required in connection with this acquisition.

43 Events after the balance sheet date

(1) On 16 March 2007, the National People's Congress approved the new PRC Enterprise Income Tax Law. This legislation reduces the enterprise income tax rate for domestic enterprises from 33% to 25% with effect from 2008. This reduction in enterprise income tax rate will directly reduce the Group's effective tax rate, and the Group will benefit from this prospectively from 2008. The tax rate reduction will also affect the carrying value of the net deferred tax assets of the Group's domestic operations as IAS 12 requires deferred tax items to be written down to reflect future realization at the newly enacted tax rate of 25% upon approval by the National People's Congress. The Group has performed a preliminary assessment based on the relevant net deferred tax asset balance as at 31 December 2006 and estimated that the amount of write-down will be approximately RMB4.4 billion.

(2) Subsequent to the balance sheet date, the Bank exercised three tranches of the Huijin option, having a notional amount of USD4.5 billion and also entered into certain foreign exchange spot transactions of USD6.8 billion to further reduce its net foreign currency exposure. See Note III.5 (i).

Concurrently the Bank entered into a series of CIRS, having a notional amount of USD11.3 billion. See Note III.5 (i).