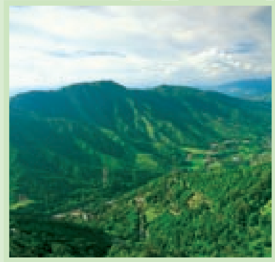
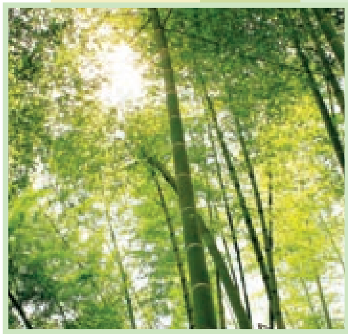
中銀香港(控股)有限公司
BOC HONG KONG (HOLDINGS) LIMITED

Stock Code: 2388

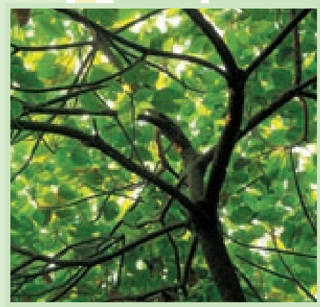


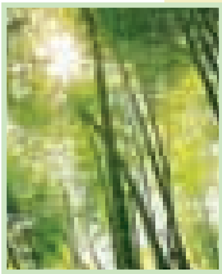


# FORTIFYING OUR FOUNDATIONS

## in a challenging environment

Annual Report 2008



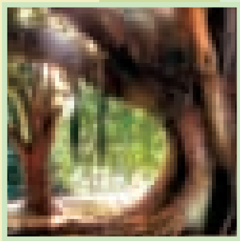


### Theme

2008 was a highly challenging year for both the Group and Hong Kong. Our major focus has been to safeguard the Group's financial strength and competitiveness.

The Group, just like our great mother nature, has the regenerative strength to face the challenges ahead of us. This provides the theme for our annual report – "Fortifying our Foundations in a Challenging Environment".

By riding on our solid foundation and strong franchise, the Group is able to proactively realign our development strategy to capture growing opportunities from the changing industry landscape, creating brighter prospects for our stakeholders.



## OUR VISION

# TO BE YOUR PREMIER BANK

Combining the initials of mission and core values, we have

## BOC SPIRIT

## OUR MISSION

**Build**
customer satisfaction and provide quality and professional service

**Offer**
rewarding career opportunities and cultivate staff commitment

**Create**
values and deliver superior returns to shareholders

## OUR CORE VALUES

**Social Responsibility**
We care for and contribute to our communities

**Performance**
We measure results and reward achievement

**Integrity**
We uphold trustworthiness and business ethics

**Respect**
We cherish every individual

**Innovation**
We encourage creativity

**Teamwork**
We work together to succeed

# Contents



中國銀行(香港) BANK OF CHINA (HONG KONG)

香港2009東亞運動會鑽石伙伴 Diamond Partner

HONG KONG 2009 EAST ASIAN GAMES

**BOC Hong Kong (Holdings) Limited** ("the Company") was incorporated in Hong Kong on 12 September 2001 to hold the entire equity interest in Bank of China (Hong Kong) Limited ("BOCHK"), its principal operating subsidiary. Bank of China Limited holds a substantial part of its interests in the shares of the Company through BOC Hong Kong (BVI) Limited, an indirect wholly owned subsidiary of Bank of China Limited.

BOCHK is a leading commercial banking group in Hong Kong. With over 280 branches and 470 ATMs and other delivery channels in Hong Kong, BOCHK and its subsidiaries offer a comprehensive range of financial products and services to retail and corporate customers. BOCHK is one of the three note issuing banks in Hong Kong. In addition, BOCHK and its subsidiaries have 19 branches and sub-branches in the Mainland of China to provide cross-border banking services to customers in Hong Kong and the Mainland. BOCHK is appointed by the People's Bank of China as the Clearing Bank for Renminbi (RMB) business in Hong Kong.

The Company began trading on the main board of the Stock Exchange of Hong Kong on 25 July 2002, with stock code "2388", ADR OTC Symbol: "BHKLY".

# FINANCIAL HIGHLIGHTS

| For the year | **2008 HK$'m** | 2007 HK$'m | Change +/(-)% |
|---|---|---|---|
| Net operating income before impairment allowances | **25,526** | 27,254 | (6.34) |
| Operating profit | **4,182** | 18,033 | (76.81) |
| Profit before taxation | **4,078** | 19,126 | (78.68) |
| Profit for the year | **3,007** | 15,817 | (80.99) |
| Profit attributable to the equity holders of the Company | **3,343** | 15,446 | (78.36) |
| **Per share** | **HK$** | HK$ | +/(-)% |
| Earnings per share | **0.3162** | 1.4609 | (78.36) |
| Dividend per share | **0.4380** | 0.9150 | (52.13) |
| **At year-end** | **HK$m** | HK$m | +/(-)% |
| Capital and reserves attributable to the equity holders of the Company | **82,719** | 92,842 | (10.90) |
| Issued and fully paid share capital | **52,864** | 52,864 | – |
| Total assets | **1,147,244** | 1,067,637 | 7.46 |
| **Financial ratios** | **%** | % | |
| Return on average total assets[1] | **0.27** | 1.53 | |
| Return on average capital and reserves attributable to the equity holders of the Company[2] | **3.81** | 17.40 | |
| Cost to income ratio | **34.36** | 28.52 | |
| Loan to deposit ratio[3] | **56.74** | 51.66 | |
| Average liquidity ratio[4] | **41.74** | 50.92 | |
| Capital adequacy ratio[5] | **16.17** | 13.08 | |

1. Return on average total assets = $\dfrac{\text{Profit for the year}}{\text{Daily average balance of total assets}}$

2. Return on average capital and reserves attributable to the equity holders of the Company

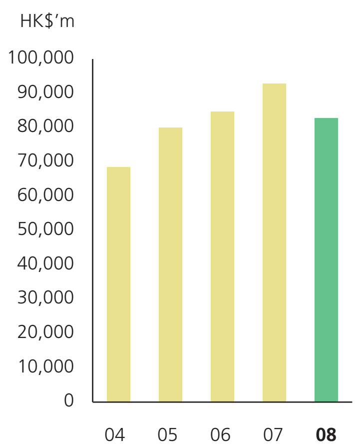
$$= \frac{\text{Profit attributable to the equity holders of the Company}}{\text{Average of the beginning and ending balance of capital and reserves attributable to the equity holders of the Company}}$$

3. Loan to deposit ratio is calculated as at year end. Loan represents gross advances to customers. Deposit also includes structured deposits reported as "Financial liabilities at fair value through profit or loss".

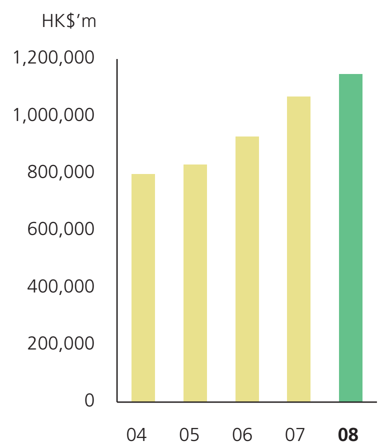
4. Average liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio of BOCHK for the year.

5. Capital adequacy ratio is computed on the consolidated basis that comprises the positions of BOCHK and certain subsidiaries specified by the HKMA for its regulatory purposes and in accordance with the Banking (Capital) Rules.

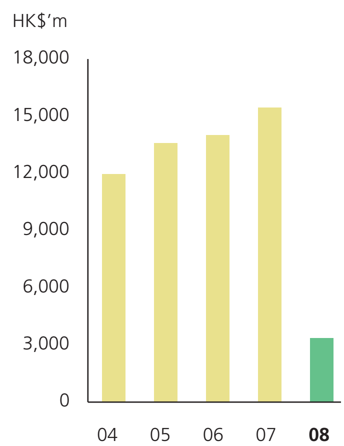
### Capital and reserves attributable to the equity holders of the Company




### Total assets




### Profit attributable to the equity holders of the Company



# FIVE-YEAR FINANCIAL SUMMARY

The financial information of the Group for the last five years commencing from 1 January 2004 is summarised below:

| For the year | **2008** **HK$'m** | 2007 HK$'m | 2006 HK$'m | 2005[3] HK$'m | 2004[2,4] HK$'m |
|---|---|---|---|---|---|
| Net operating income before impairment allowances | **25,526** | 27,254 | 21,309 | 18,158 | 15,909 |
| Operating profit | **4,182** | 18,033 | 16,545 | 15,052 | 12,184 |
| Profit before taxation | **4,078** | 19,126 | 17,139 | 16,502 | 14,252 |
| Profit for the year | **3,007** | 15,817 | 14,284 | 13,856 | 12,121 |
| Profit attributable to the equity holders of the Company | **3,343** | 15,446 | 14,007 | 13,596 | 11,963 |
| **Per share** | **HK$** | HK$ | HK$ | HK$ | HK$ |
| Earnings per share | **0.3162** | 1.4609 | 1.3248 | 1.2859 | 1.1315 |
| **At year-end** | **HK$'m** | HK$'m | HK$'m | HK$'m | HK$'m |
| Advances and other accounts | **469,493** | 420,234 | 352,858 | 338,403 | 309,211 |
| Total assets | **1,147,244** | 1,067,637 | 928,953 | 831,002 | 796,776 |
| Daily average balance of total assets | **1,099,198** | 1,032,577 | 915,900 | 831,789 | 776,792 |
| Deposits from customers[1] | **811,516** | 799,565 | 703,776 | 639,031 | 631,330 |
| Total liabilities | **1,062,712** | 972,579 | 842,313 | 749,289 | 727,016 |
| Issued and fully paid share capital | **52,864** | 52,864 | 52,864 | 52,864 | 52,864 |
| Capital and reserves attributable to the equity holders of the Company | **82,719** | 92,842 | 84,655 | 79,935 | 68,521 |
| **Financial ratios** | **%** | % | % | % | % |
| Return on average total assets | **0.27** | 1.53 | 1.56 | 1.67 | 1.56 |
| Cost to income ratio | **34.36** | 28.52 | 30.78 | 31.75 | 34.72 |
| Loan to deposit ratio[1] | **56.74** | 51.66 | 49.32 | 52.27 | 49.61 |

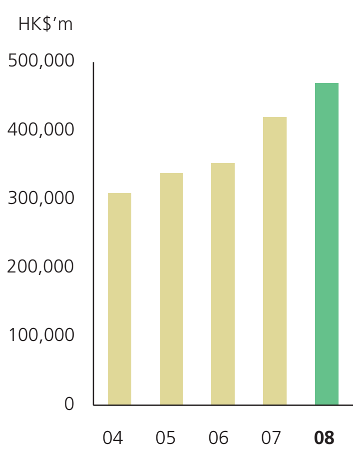
1. Since 2005, deposits from customers also include structured deposits reported as "Financial liabilities at fair value through profit or loss".

2. On 1 January 2005, a number of new and revised HKFRSs and HKASs came into effect. The resulting changes in accounting treatment and presentation of various income statement and balance sheet items may render certain comparative figures for the year 2004 not strictly comparable.

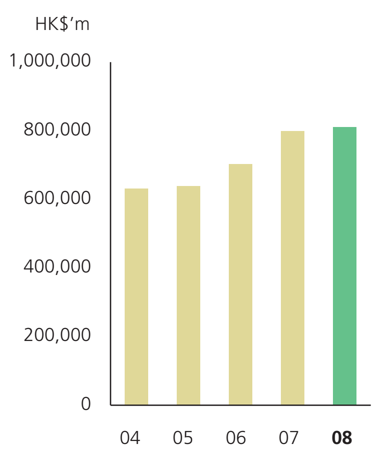
3. In June 2006, the Company acquired a 51% shareholding of an under common control entity, BOC Life. The financial statements have been prepared in accordance with the principles of merger accounting as set out in Accounting Guideline 5 "Merger accounting for common control combinations" issued by the HKICPA. The comparative amounts for the year 2005 have been restated in accordance with the principles for merger accounting to present the result and assets of the Group as if such combination had occurred from the date when the Company and BOC Life first came under common control.

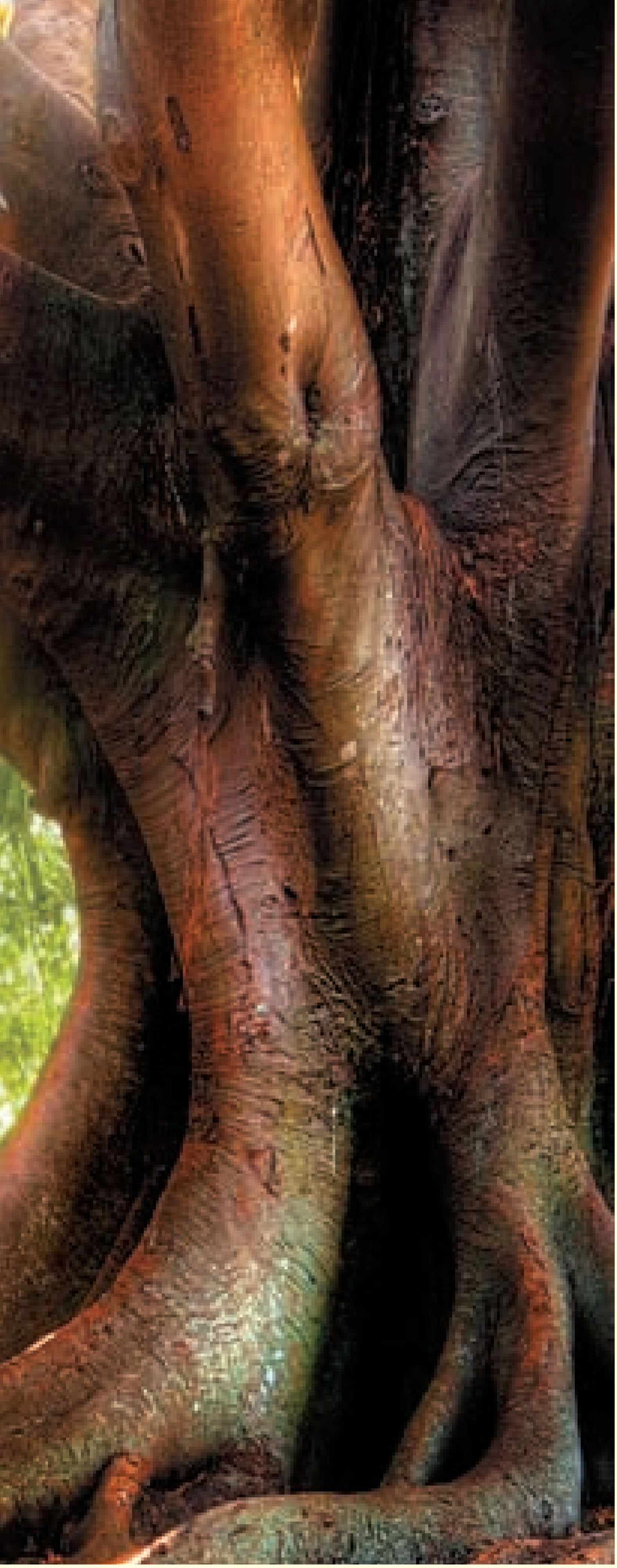
4. The financial information of 2004 had not been restated to reflect the adoption of merger accounting upon the acquisition of BOC Life as the difference before and after restatement is insignificant.

### Advances and other accounts




### Deposits from customers





# 根深

# Solid Foundation

# CHAIRMAN'S STATEMENT

2008 was a highly challenging year with an unusual combination of exceptionally difficult events. We were faced with the extreme volatilities in major financial markets, particularly in the second half of the year, triggered by the collapse of Lehman Brothers. The impact of the global financial turmoil on Hong Kong also became more noticeable in the latter half of the year. While the Group's traditional banking businesses continued to deliver solid performance, its investment-related businesses were negatively affected by the fallout of the financial crisis. The Group's net operating income before impairment allowances was HK$25,526 million, down 6.3% while operating profit before impairment allowances was HK$16,755 million, down 14.0%. The Group's profit attributable to shareholders decreased by 78.4% year-on-year to HK$3,343 million or HK$0.3162 per share. The substantial drop in our profit was largely due to the continued markdowns on the Group's securities investments, which resulted in total provisions of HK$11,900 million for the period. The Board recommends no final dividend payment for 2008 (2008 interim dividend: HK$0.4380 per share) in view of the earnings hit in the second half and the need to preserve capital strength in a turbulent market.

Throughout the year, our over-riding focus has been, and remains to be, the safeguard of the Group's financial strength and competitiveness amid this unparalleled crisis. A number of proactive initiatives have been taken, focusing on the management of our capital, liquidity and risks. We have reinforced our capital base through the subordinated loans granted by our parent bank, Bank of China Limited ("BOC"). A strong capital position provides the Group with greater operating flexibility to meet its business development needs and to weather the economic uncertainties arising from the global financial turmoil. Our consolidated capital adequacy ratio stood comfortably at 16.17% as at the end of 2008. In addition, we continued to exercise rigorous risk control and focus on liquidity management. As at the end of 2008, our financial position remained solid with total assets reaching HK$1,147.2 billion, up 7.5% from the end of 2007. Our liquidity position remained strong at 41.74%. Loan quality was healthy with the classified or impaired loan ratio at a low level of 0.46%, edging up slightly from 0.44% a year ago.

In response to the market changes and uncertainties, we swiftly adjusted our business strategies based on a more prudent approach and streamlined our expenses. We continued to grow our franchise in a tough market. Our individual and corporate customer base continued to expand, especially with good progress in new focus areas such as custody and cash management. We maintained a strong deposit base which increased compared to the end of 2007 with improved deposit mix. We continued to focus on prudent lending business and maintained our leading market positions in residential mortgage and loan syndication businesses. Our net interest income reached a new record level despite the pressure from falling interest rates. Fee income from our traditional banking services, including fee income from loans, credit cards and RMB business also posted solid growth. We continued to solidify our leadership in RMB banking business in Hong Kong.

I would also like to say a few words about the Lehman Brothers Mini-bonds issue. The consequences of the collapse of Lehman Brothers have been more profound than the market expected, which unfortunately also affected our customers who had invested in Lehman related structured products. As a responsible banking group that cares for the interests of customers, we have been deeply concerned about the distress and anxiety of those affected customers. Each customer is important to us. We have been proactively addressing their concerns and I sincerely hope that the issue would be resolved as quickly and satisfactorily as possible.

For 2009, we expect the market environment to remain highly challenging and volatile while global economies will remain under stress. The global economic crisis may continue to affect us in the near term. It is extremely important for us to stay flexible, alert and proactive in managing our risks, capital, liquidity and expenses. While business activities may slow down amid the global economic downturn, we will focus on enhancing our business capabilities and operating efficiency to better position ourselves for the market recovery. In response to the changing industry landscape, we will adjust our business strategies accordingly by capitalising on our core strength areas. We will also continue to invest judiciously in accordance with our strategic priorities for our long-term growth.

Despite the market uncertainties ahead, we see considerable business opportunities for BOCHK, especially by fostering closer collaboration with our parent bank, BOC. The setup of BOC Group's Asia-Pacific Syndicated Loan Centre last year proved to be a great success by leveraging BOCHK's expertise, BOC's network in the Asia-Pacific Region and the BOC Group's franchise. With close cooperation with BOC, BOCHK is well positioned to provide comprehensive offshore financial services to the Chinese enterprises going global. We will continue to strengthen this unique collaborative platform between BOCHK and BOC in various business areas to extend our presence in the region and to better serve the needs of our customers. I am confident that these collaborative opportunities will create value for the customers and shareholders of both BOCHK and BOC.

Last year was a particularly busy year for our Board Members as we managed our way through the challenging environment. I would like to thank them for their dedication and wise counsel. I would also like to extend my heartfelt thanks to our Management team and all associates for their wholehearted commitments and efforts during the year. On behalf of the Board, I would like to take this opportunity to thank Mr. Lee Raymond Wing Hung, who will retire as the Group's Chief Financial Officer and Executive Director of the Company effective from 1 June 2009, for his service and contributions to the Company. We have already started the search for a suitably qualified candidate to fill the position of the Chief Financial Officer of the Company and the Bank. Announcement on the progress of the recruitment will be made in due course. Last but not least, I would like to thank the continued support of our shareholders and customers, which is important to the long-term success of the Group.

**XIAO Gang**
*Chairman*

24 March 2009

# CHIEF EXECUTIVE'S REPORT

The operating environment in the past year was as challenging as any we had seen in decades. The negative impact of the global financial turmoil was felt in virtually all sectors of the global economy, particularly in the latter half of the year. We witnessed a widespread credit crunch and the liquidity problems encountered by a large number of major players in the financial, commercial and industrial sectors. Back home, the financial sector did not escape the crisis while the manufacturing and export sectors suffered from diminished external demand. This in turn affected the job market and income level, with the retailing sector hard hit. Pessimistic sentiment prevailed in most investment markets.

## Key Initiatives

During this unprecedented crisis, our overall focus has been to safeguard the Group's financial strength and enhance its competitiveness. Throughout the year, we took various initiatives in the areas of capital preservation, liquidity management, risk control and cost containment, in order to fortify our foundation.

- We adopted decisive measures to enhance our capital base and optimise our capital structure with the support of our parent bank, BOC, from which we obtained two subordinated loans.
- We minimised the risk exposure of our balance sheet by proactively adjusting our asset allocation.
- We exercised rigorous control in liquidity management amid extremely volatile market conditions.
- We continuously reassessed the risk exposure of our loan portfolio and adjusted our lending strategies in a swift and prudent manner.
- We took prompt action to contain our costs in view of the weakening operating environment.

## Business Highlights

In response to rapid market changes and amid economic uncertainties, we refined our business strategy, capitalising on our core strengths and continuing to grow our franchise under tough environment. This geared us towards the steady performance of our traditional business segments in what was a turbulent year during 2008.

- Net interest income – a key part of the Group's core operating income – continued to rise despite pressure from falling interest rates.
- Our lending business scored higher growth than the market in 2008. Total loans and advances registered double-digit growth.
- Our loan-to-deposit ratio rose steadily while loan quality remained satisfactory. The Group's deposit mix also improved on a strong deposit base.
- Fee income from traditional banking services grew by a healthy margin, reflecting our strength in these core business areas.
- We maintained our market leadership in residential mortgage lending, loan syndication and RMB-related banking in Hong Kong respectively.
- The Group's Mainland business registered growth in operating income. Our loan quality in the Mainland also remained good.
- Good progress was made in deepening our collaboration with BOC in various business fields.

## Financial Performance

The Group's financial performance in 2008 was hurt by the increasingly difficult market conditions.

Operating income decreased by 6.3% to HK$25,526 million. While there was an increase of 3.9% in net interest income, it was more than offset by the 17.5% reduction in fees and commission income as well as the operating loss incurred by the Group's insurance business. With the 12.8% rise in operating expenses, operating profit before impairment allowances was down by 14.0% to HK$16,755 million. The Group's profit attributable to shareholders decreased by 78.4% year-on-year to HK$3,343 million. This was caused mainly by the increase in impairment charges on securities investments amounting to HK$11,900 million. Earnings per share were HK$0.3162, representing a drop of 78.4%.

Return on total average assets (ROA) and return on average shareholders' funds (ROE) were 0.27% and 3.81%

respectively, versus 1.53% and 17.40% respectively for 2007. ROA and ROE before impairment allowances were 1.52% and 19.09% respectively.

Net interest income increased to HK$20,157 million as the Group's average interest-earning assets grew by 7.3% to HK$1,006,440 million. This growth was achieved by the expansion of our lending business and the increase in average deposits from customers, banks and financial institutions. We witnessed further growth in higher yielding loans. At the same time, we were able to adjust the pricing of new loan facilities to reflect the tightening of credit in the market. Net interest margin (NIM) was down by 0.07 percentage point to 2.0% in 2008, due mainly to decline in the contribution from net free fund as market interest rates dropped significantly. The substantial increase in RMB deposits from the participating banks also contributed to 0.04 percentage point decline in NIM given the Group's role as the RMB Clearing Bank in Hong Kong. Should this factor be excluded, the adjusted NIM would have been 2.07%, down by 0.03 percentage point.

The performance of our core lending business remained sound in 2008. Its growth slowed down somewhat in the second half as we opted for a more prudent lending policy in view of the increasing uncertainty in the credit market. Total loans and advances to customers rose by a healthy 11.5% to HK$460,447 million. This was due to the across-the-board growth of loans, of which corporate loans grew by 13.7%, residential property mortgage by 9.1% and card advances by 13.7%. Loans for use outside Hong Kong registered a growth of 19.5% with Mainland lending up by 5.6%. The Group's loan-to-deposit ratio at end-2008 was up 5.08 percentage points to 56.74% as the growth of loans outpaced that of deposits.

The Group's net fees and commission income declined by 17.5% to HK$5,179 million largely attributable to the fall in investment-related fee income. The investment environment turned sluggish in the aftermath of the global financial crisis. As customers mostly steered clear of investment products, the investment and insurance fee income decreased by 34.3% to HK$2,964 million.

On the positive side, we recorded a growth of 16% in the fee income from our traditional banking business. Loan commission grew markedly by 47.8% to HK$513 million, benefiting from our expanded loan portfolio and the successful launch of BOC Group's Asia Pacific Loan Syndicated Centre. RMB-related business performed exceptionally well by recording an income growth of 62.8%. Our credit card business, bills service and currency exchange business also posted encouraging performance, growing their fee income by 18.8%, 16.2% and 10.9% respectively. Concurrently, we witnessed good progress in new business areas such as custody services and cash management, which have made new contribution to the Group's fee income.

Thanks to the strong performance in the first half of 2008, we achieved a year-on-year growth in net trading income of 88.9% to HK$1,914 million. This remarkable growth was driven by the 126.1% surge in the trading income from currency exchange and foreign exchange products. We captured the opportunity by launching those products to meet the higher demand from customers for currency-related products in the volatile market and the anticipated appreciation of the RMB. We also saw a significant improvement in the net trading income from mark-to-market on foreign exchange swap contracts.

As for BOC Life, its insurance and investment income declined by HK$1,497 million due to the weak performance of its investment assets and the lower business volume in the second half of the year.

In view of the unstable market conditions, we reassessed our impairment charges and increased our provisions accordingly. For the Group's US mortgage-backed securities and other debt securities, an amount of HK$9,170 million was provided. A total of HK$2,730 million was provided for the Group's investment in the shares of Bank of East Asia.

Amid the aggravating economic conditions, the Group was highly prudent in managing its operating expenses. In the second half of 2008, we even managed to trim down our core operating expenses by 4.3% as compared with the first half. For the whole year, we outperformed the market by containing the increase of our core operating expenses to 2.9% and the corresponding cost-to-income ratio by 2.83 percentage points to 31.35%. However, it was only due to the extraordinary expenses mainly in connection with the Lehman Brothers Mini-bonds issue totaling HK$769 million that our total operating expenses rose by 12.8% while our cost-to-income ratio rose by 5.84 percentage points to 34.36%.

The Group's financial position remained stable. At the end of 2008, our total assets stood at HK$1,147,244 million, representing an increase of 7.5% versus end-2007, which was mainly because of the expansion of our loan portfolio. The Group's classified or impaired loan ratio increased by a negligible margin of 0.02 percentage point to 0.46% – far below the market average of 1.24%.

To better prepare ourselves for the uncertainty in the financial market, we further strengthened our capital position by two subordinated loans from BOC. The first loan of 660 million Euros was made in June while the second loan of US$2,500 million, in December. The Group's consolidated capital adequacy ratio was therefore up 3.09 percentage points to 16.17% at the end of 2008, with tier-one ratio at 10.86%. Reflecting our healthy liquidity position, the Group's average liquidity ratio stood at 41.74%, versus 50.92% in 2007.

## Business Review

### *Personal Banking*

The Group's Personal Banking business was subject to declining interest rates and the adverse change in market conditions in the second half of the year. Its operating income was HK$10,690 million, down 24%. Net interest income and other operating income fell by 20.1% and 29.5% respectively. Profit before taxation was HK$4,892 million, down 39.8%.

Over the year, we maintained growth in our traditionally strong segments. We also took various initiatives to reinforce our capabilities and strengthen our competitiveness.

We succeeded in driving the growth of the residential property mortgage business while consistently maintaining our market leadership. Through marketing promotion schemes and service enhancement, we outperformed the market by growing our mortgage loans by 9.1% year-on-year, higher than the market average of 5.1%. Towards the latter half of the year, we strengthened our risk assessment and control on the mortgage business. The quality of mortgage loans remained excellent with the delinquency and rescheduled loan ratio falling further to 0.05%, versus a market average of 0.19%.

We sustained the growth momentum of our credit card business. Card advances and card issuance increased by 13.7% and 2.8% respectively whereas cardholder spending and merchant acquiring volume rose by 12.7% and 19.9% respectively. We took advantage of new business opportunities, such as the Beijing Olympics, to launch a series of new cards and expand our card-related service. In collaboration with China UnionPay (CUP), the "BOC CUP Dual Currency Credit Card" was issued in December 2008. The asset quality of our card business remained good with the charge-off ratio standing well below the market average at 2.22%.

We maintained our market leadership in the RMB-related banking business in Hong Kong. We commanded the largest share of RMB deposits, which surged by 58.5% in 2008. We led the market in the RMB credit card business, growing our card issuance, cardholder spending and merchant acquiring volume by 24.6%, 49.8% and 60.5% respectively. To better serve our customers, our RMB cash withdrawal service has been extended to all of our ATMs located at MTR stations. During the year, we acted as the joint lead manager and bookrunner as well as placing bank for RMB bonds issued in Hong Kong by three major Mainland banks to a total value of 9 billion yuan.

Capitalising on our strong franchise, we continued to expand our high net-worth customer base and reinforce our status as a professional wealth management service provider. We have been working closely with BOC in preparation for the offering of cross-border wealth management services in the Mainland. This service will be offered through designated branches of BOC in the Mainland in the first half of 2009. As at the end of 2008, the number of wealth management customers increased by a very encouraging 21.5% from a year ago.

To enhance operational efficiency, we continued to consolidate our service platforms for investment, insurance and wealth management services. We also optimised our distribution channels. To provide more efficient and professional service to different customers, we added new wealth management centres and mortgage advice centres to our network in Hong Kong. Our e-banking channels have also been further upgraded to facilitate transactions with customers.

### *Corporate Banking*

Throughout 2008, Corporate Banking basically maintained steady growth. It attained an increase of 7.1% in operating income to HK$8,211 million with the rise in both net interest income and other operating income. Its profit before taxation was HK$5,524 million, down 15.4% mainly due to the increase in net charge of loan impairment allowance.

Corporate Banking made considerable progress in growing both its core and new business segments as well as in reinforcing its service platform for corporate clients.

We strengthened our leading position and enlarged our shares in two syndicated loan markets, namely, the "Hong Kong-Macau" and the "Mainland-Hong Kong-Macau" regions. As reported in our Interim Report, the Group was appointed in January 2008 as BOC Group's Asia-Pacific Syndicated Loan Centre. After this appointment, we immediately proceeded to extend our reach to the Asia-Pacific region and succeeded in becoming the sole arranger for two major Australian enterprises, which helped to enhance our market status.

We continued to upgrade our business platform. Through the enhancement of product offerings, services and channels, we recorded a steady year-on-year rise in SME loans and received awards for supporting the development of SMEs in Hong Kong. Our trade finance business expanded through product innovation and the streamlining of credit approval. Strong upsurge was recorded in the first half of the year but it slowed down in the fourth quarter as the performance of Hong Kong's external trade weakened. The outstanding balance of trade finance showed a slight increase of 1.2% against end-2007 but there was still a strong increase of 32.0% in the volume of trade bills settlement.

We forged ahead with the development of new businesses with encouraging results. Our cross-border cash management business expanded as we continued to enhance our service for major Mainland enterprises. Locally we broadened our cash management customer base through product innovation and refinement. Meanwhile, our custody business advanced with the expansion of the number of customers. In 2008, we became the custodian for a number of locally-listed or offshore-incorporated investment funds. The Group was appointed by a joint-venture investment bank in the Mainland as the foreign custodian for its first QDII product, which was also the first broker-type QDII product approved in the Mainland. By end-2008, total assets under the Group's custody was HK$200 billion.

During the year we enhanced the Group's financial services for corporate customers by setting up a commercial wealth management team. This team of professionals is responsible for customising financial management strategy and conducting regular reviews to help customers in maximising their wealth potential and managing risks.

As the economic downturn lingered on, the Group took a number of proactive measures to contain its risk exposure to corporates. A special working group was established and tasked with evaluating the risk exposure of the Group's loan portfolio. Comprehensive and frequent re-assessment of credit risk and stress tests on customers from key business segments were conducted. In accordance with the market conditions, we adjusted our loan pricing strategy after taking into full account the liquidity and risk factors.

### *Mainland Business*

The Group's Mainland business continued to make advances and attained satisfactory growth in 2008. Total advances to customers grew by 5.6%, of which RMB loans surged by 12.6%. Customer deposits up by 72.5%. Total operating income increased by 15.9% to HK$990 million, which was driven primarily by the growth of net interest income as well as net fees and commission income. It was, however, partially offset by the foreign exchange loss resulting from the revaluation of NCB (China)'s HKD capital against the appreciated RMB. Operating profit before impairment allowances fell by 3.1% year-on-year. Should the revaluation factor be excluded, operating profit before impairment allowances would have increased by 23.3%. Our asset quality in the Mainland remained good, with the classified loan ratio standing at 0.88%, increasing by 0.20 percentage point mainly due to the downgrade of certain large accounts.

In 2008, we stepped up our effort in extending cross-border financial services to both personal and corporate customers. New deposits, mortgage and other lending products were rolled out with good response. New branches and sub-branches were opened in targeted locations, as a result of which our network in the Mainland comprised 18 branches and sub-branches by the end of 2008. The opening of more branches is underway.

### *Treasury*

The Treasury segment registered a 32.6% growth in operating income in 2008. This was driven by the rise in both net interest income and other operating income. Operating profit before impairment allowances grew by 32.6% to HK$7,226 million. However, the segment recorded a loss before taxation of HK$1,944 million mainly due to the substantial increase in net charge of impairment allowance on securities investments.

As the global financial crisis unfolded during the year, we worked with relentless efforts on portfolio management so as to safeguard our investment portfolio and minimise potential loss. Fund safety and liquidity are our primary considerations in formulating investment strategies. As a result, the Group's exposure to US non-agency RMBS dropped by 51.3% to HK$19.3 billion at end-2008, of which sub-prime-related investments decreased to HK$1.05 billion. Despite the market volatility, there was no default in the RMBS portfolio and we continued to receive interest and repayments on those mortgage-backed securities. Our exposure was also reduced through disposal. We refined our investment strategy to give more weight to high-quality debt securities, including sovereign-related securities. By end-2008, the proportion of such investments in the Group's portfolio grew to 25%, versus 6% a year ago.

The Group succeeded in growing its traditional businesses and further improving its product manufacturing capability. Through the effective promotion of commodity and currency-related treasury products, we recorded robust growth in related income. At the same time, we expanded our product offerings by launching new investment products under our own brand. In view of the global financial turmoil, we promptly conducted a comprehensive evaluation of all products under distribution and reviewed our internal regulations, risk control measures and compliance procedures.

### *Insurance*

The Group's Insurance segment recorded a fall of 32.5% to HK$6,625 million in operating income. Net interest income was up 42.4% to HK$1,122 million and other operating income was down 39.1% to HK$5,503 million, caused by the weak performance of investment assets and the decline in premium income. A loss before taxation of HK$1,231 million was registered.

We moved forward with our business strategy by introducing a broader range of products to serve customers' needs. Large-scale promotion and marketing campaigns were staged during the year to boost sales, reinforce our brand image and grow our market share. At the same time, we continued to develop a multi-channel platform and expand our sales force.

### Outlook

Given the external-oriented nature of the Hong Kong economy, the economic outlook in Hong Kong for 2009 crucially hinges on the development in the global economy. As a high degree of uncertainty still hovers over the global financial market, the operating environment is expected to remain tough in the coming year and perhaps well beyond. We have seen contractions in our GDP growth, rising unemployment and negative wealth effects. However, we in Hong Kong are in a better position as we are blessed with the unswerving support of the Mainland, which maintains relatively stable economic conditions and financial strength. The RMB 4 trillion-yuan stimulus plan announced by the PRC Central Government in November 2008 and subsequent policies and measures to protect and stimulate the Chinese economy are expected to give rise to new opportunities for the Hong Kong economy and its financial services sector.

On the management side, to fend off any existing and unseen difficulties, we will continue to strengthen risk management and internal control. We will stay highly alert and proactive in responding to market changes and in anticipating the development of the situation. Underpinned by a solid capital base and liquidity position, we are now better equipped to weather the current financial turmoil and provided with greater flexibility in meeting our development needs. However, in driving growth and developing new business, we will remain stringent in managing our costs.

On the business front, we should leverage our fundamental strengths to enhance the competitiveness of our core business. We will build on our strong franchise in traditional banking businesses. By attaining a more balanced loan portfolio, a better deposit mix and a stronger customer base, we seek to improve the overall business structure. We will also strive to boost our operational efficiency. To cater to the diverse needs of customers, we will align our strategy with the changing environment and provide quality banking and financial services that can also address customers' prime concerns such as stability, safety and liquidity.

While ensuring our market leadership in Hong Kong's existing RMB banking business, we expect the imminent launch of the RMB trade settlement pilot scheme that allows the use of RMB as a currency for trade settlement between Guangdong Province, Yangtze River Delta and HKSAR will open a major window of opportunities for expanding the Group's RMB banking business. Meanwhile, having launched the first dual currency (HKD-RMB) credit card jointly with China UnionPay in Hong Kong, we are now in an advantageous position to expand our credit card business in both Hong Kong and the Mainland. Furthermore, we will continue to expand our cross-border financial services to serve both corporate and personal customers.

We will continue to collaborate with BOC to capture emerging business opportunities in China and provide more wide-ranging cross-border banking services to Mainland enterprises intending to expand outside China. As BOC Group's Asia-Pacific Syndicated Loan Centre, we will explore new business in the region so as to expand the territorial coverage of our loan syndication business. Riding on our experience and capabilities, we will act as an effective product manufacturing agent and a service support centre for BOC in the Asia-Pacific region. In anticipation of growing demand in the Mainland, we have already established a joint venture with BOC to provide bank card related services and support in this huge market.

In concluding, it is apparent that the current economic slowdown is unlikely to end soon. However, backed by the strong foundations we have systematically built for the Group in recent years and with the continued guidance of the Board as well as the support of shareholders, customers and colleagues, I truly believe that we will come through in better shape in the days ahead.

**HE Guangbei**
*Vice Chairman & Chief Executive*

Hong Kong, 24 March 2009

# 葉茂

# Extensive Network

# MANAGEMENT'S DISCUSSION AND ANALYSIS

The following sections provide metrics and analytics of the Group's performance, financial position, and risk management. These should be read in conjunction with the financial statements included in this Annual Report.

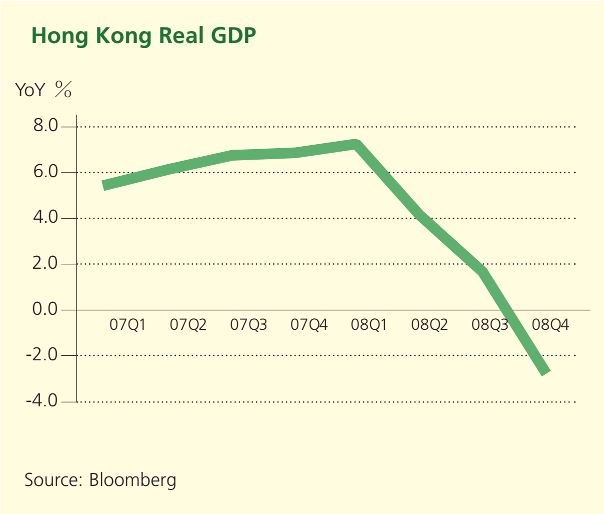
## PERFORMANCE MEASUREMENT

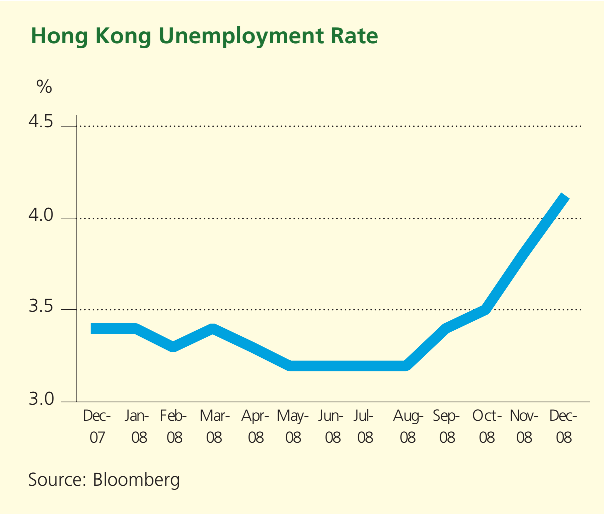
The following table highlights the Group's financial performance in terms of earnings, dividend payout, cost efficiency, asset growth, loan quality, and capital strength in 2008.

| Financial Indicators | Performance | Result Highlights |
|---|---|---|
| Earnings | Profitability declined as a result of the global economic slowdown and increased volatility in financial markets.<br>• Operating profit before impairment allowances decreased by 14.0% to HK$16,755 million.<br>• Profit attributable to shareholders decreased by 78.4% to HK$3,343 million. | • **Operating profit before impairment allowances: down 14.0%**<br>• **Profit attributable to shareholders: down 78.4%** |
| ROE[1] and ROA[2] | • ROE and ROA were 3.81% and 0.27% respectively.<br>• ROE and ROA before impairment allowances were 19.09% and 1.52% respectively. | • **ROE: 3.81%**<br>• **ROA: 0.27%** |
| Dividend payout ratio | An interim dividend of HK$0.438 per share was paid to the shareholders. The Board proposes not to pay a final dividend for 2008. | • **Total dividend per share for 2008: HK$0.438** |
| Net interest income and net interest margin | • Net interest income increased by 3.9% to HK$20,157 million.<br>• Net interest margin was 2.00% in 2008. Net interest spread rose but was offset by the decline in contribution from net free fund because of falling market interest rates. The pricing of new corporate loan facilities also improved with the tightened credit environment. | • **Net interest income: up 3.9%**<br>• **Net interest margin: 2.00%** |
| Non-interest income[3] | Non-interest income to operating income[4] ratio was 21.03%, a drop of 7.81 percentage points primarily due to the decrease in investment-related agency fee income as well as the operating loss of the life insurance business. | • **Non-interest income to operating income ratio: 21.03%** |
| Cost efficiency | Cost-to-income ratio rose by 5.84 percentage points to 34.36% as operating expenses increased by 12.8% while operating income decreased by 6.3%. | • **Cost-to-income ratio: 34.36%, maintained well below the market average** |
| Total assets | • Total assets grew by 7.5% to HK$1,147.2 billion. Loans and deposits[5] rose by 11.5% and 1.5% respectively. | • **Total assets: up 7.5%** |
| Loan quality | • Formation of new classified loans[6] remained at a low level of less than 0.4% of total loans.<br>• Classified or impaired loan[7] ratio was slightly up 0.02 percentage point from 0.44% at end-2007 to 0.46% at end-2008. | • **Classified or impaired loan ratio: 0.46%, well below the market average** |
| Capital strength and liquidity | • Capital adequacy ratio was up 3.09 percentage points to 16.17% with improved capital structure. Tier one ratio stood at 10.86%.<br>• Liquidity remained abundant. | • **Capital adequacy ratio: 16.17%**<br>• **Liquidity ratio: 41.74%** |

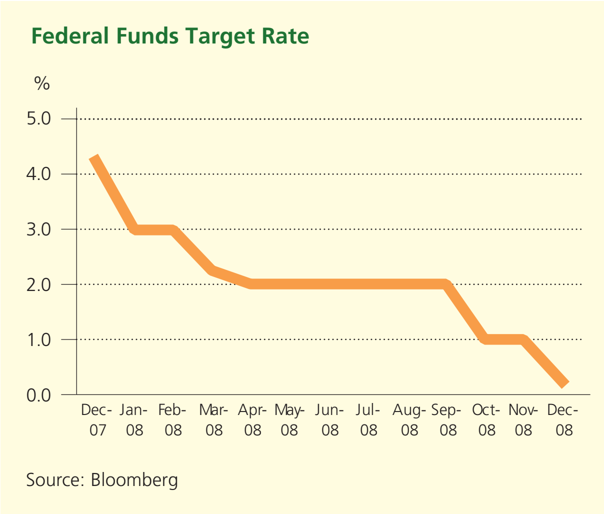
(1) ROE represents return on average capital and reserves attributable to the equity holders of the Company.
(2) ROA represents return on average total assets and is defined in "Financial Highlights".
(3) Non-interest income represents net fees and commission income, net trading income, net gain/(loss) on financial instruments designated at fair value through profit or loss, net gain/(loss) on investments in securities, net insurance premium income, other operating income and net insurance benefits and claims.
(4) Operating income comprises net interest income and non-interest income as defined in (3) above.
(5) Including structured deposits.
(6) Classified loans are advances to customers which have been classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality.
(7) Classified or impaired loans represent advances which have been classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired. Repossessed assets are initially recognised at the lower of their fair value less costs to sell or the amortised cost of the related outstanding loans on the date of repossession. The related loans and advances are deducted from loans and advances.

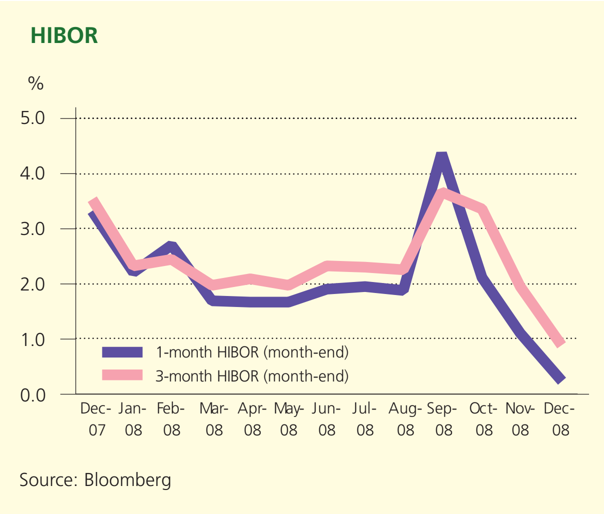
## BUSINESS ENVIRONMENT



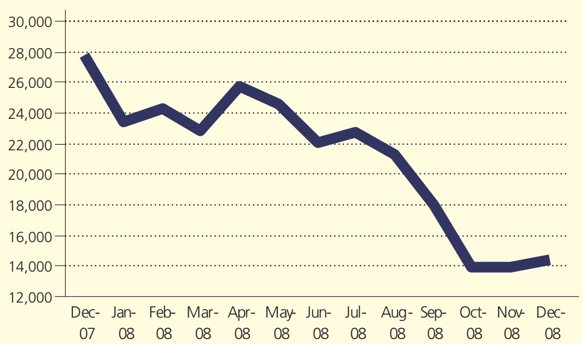

The economic environment deteriorated drastically in 2008 and made it unusually challenging for the operation of the banking industry. In the first half of the year, there were already signs of a global economic slowdown subsequent to the US subprime mortgage crisis. In the second half of the year, the US subprime crisis deepened and spread to other credit markets. The global financial landscape turned gloomy and the financial system came under severe strain. The need for rescuing the two US mortgage agencies, Fannie Mae and Freddie Mac, by the US government, the bankruptcy of the investment bank Lehman Brothers Holdings Inc. ("Lehman Brothers"), and the possible collapse of the insurance giant AIG sparked widespread concerns about the stability of financial institutions and the global interbank market was severely affected as counterparty risk surged. The global financial crisis and economic downturn inevitably had an adverse impact on Hong Kong. The Hong Kong economy recorded quarter-on-quarter contraction starting from the second quarter of 2008 following an extended period of expansion for four years. The slowing down of economic activity was primarily caused by weak private consumption, diminished merchandise exports and rising unemployment rate which reached 4.1% at the end of 2008. Inflationary pressure in Hong Kong was unabated in the first half of the year with the composite consumer price index ("CCPI") rising by 3.3% in July compared with end-2007. The pressure was somewhat relieved in the second half as commodity and oil prices as well as wages began to fall, causing the CCPI to rise by a more modest 2.1% by end-2008.



Central governments around the world have taken drastic measures to rescue their respective financial systems and economies. The US Federal Reserve continued with the interest rate cut cycle since September 2007 and slashed the US Federal Funds Target Rate by an aggregate of 400 basis points in 2008 to 0.25% by the end of 2008. Meanwhile, banks in Hong Kong also lowered their Prime rates. Average 1-month HIBOR and 1-month LIBOR declined substantially from 4.97% and 5.49% respectively in September 2007 to 1.46% and 2.51% respectively in May 2008 but then rose in September to 2.75% and 2.93% respectively because of the higher counterparty risk and surging demand for liquidity after the bankruptcy of Lehman Brothers. Interest rate volatility rose and the HIBOR-LIBOR spread fluctuated sharply. To ease the money market stress, the Hong Kong Monetary Authority ("HKMA") injected liquidity into the banking system and at the same time took other pre-emptive measures such as providing liquidity assistance and lowering the borrowing costs to banks. As a result, HIBORs declined substantially along with LIBORs.

**Hang Seng Index**




Source: Bloomberg

The downward trend of local stock market continued in 2008, with the Hang Seng Index ("HSI") falling further still. Local share prices rebounded in April after the announcements by major corporations of strong earnings. However, equity prices fell sharply during the second half of the year as the global financial crisis intensified. HSI closed at 14,387 points at end-2008, versus 27,813 points at end-2007, shedding almost half of the total market value.

In the local residential property market, prices declined notably in the third quarter of 2008 after the sharp increases recorded in late 2007 and early 2008. The transaction volume plunged as tightened credit sentiment and weakened economic prospects put a brake on housing demand and speculative activities. With a high degree of uncertainty still looming over the economy and labour market conditions, housing demand remained sluggish in the second half of 2008. Transaction volume, in terms of the number of agreements for sale and purchase of all building units, contracted by 22.2% compared to 2007.

The financial crisis and economic downturn posed a number of formidable challenges to the local banking sector in 2008 and banks' profitability was severely eroded. Asset quality worsened, leading to a rise in the provisions for loans and investment portfolios. The classified loan ratio of retail banks rose to an average of 1.24% at end-2008.

## CONSOLIDATED FINANCIAL REVIEW

The financial crisis took its toll on the global economy, including Hong Kong, in 2008, particularly in the second half of the year. The intensification of the financial crisis and increased volatility in financial markets led to the rapid deterioration of both the market sentiments and the operating environment. Against this background, the banking sector as a whole suffered. After registering satisfactory financial results with strong growth in core earnings in the first six months of the year, the Group's financial performance for the whole year of 2008 was severely tarnished by the drastic change in the market environment in the second half of the year. As a result, the Group's operating profit before impairment allowances decreased by HK$2,726 million, or 14.0%, to HK$16,755 million. There was growth in both net interest income and net trading income of the banking operation. However, these increases were more than offset by the operating loss recorded by the Group's insurance segment, lower net fees and commission income as well as higher operating expenses. The Group's profit attributable to shareholders decreased by HK$12,103 million, or 78.4%, to HK$3,343 million, due to the significant increase in impairment charge on securities investments, a net charge of loan impairment allowances as well as the deficit arising from the revaluation of properties. Earnings per share were HK$0.3162. Return on average total assets ("ROA") and return on average shareholders' funds ("ROE") were 0.27% and 3.81% respectively. ROA and ROE before impairment allowances were 1.52% and 19.09% respectively.

### Financial Highlights

| HK$'m, except percentage amounts | **2008** | 2007 |
|---|---|---|
| Operating income | **25,526** | 27,254 |
| Operating expenses | **(8,771)** | (7,773) |
| Operating profit before impairment allowances | **16,755** | 19,481 |
| Net (charge)/reversal of impairment allowances | **(12,573)** | (1,448) |
| Others | **(104)** | 1,093 |
| Profit before taxation | **4,078** | 19,126 |
| Profit attributable to equity holders of the Company | **3,343** | 15,446 |
| Earnings per share (HK$) | **0.3162** | 1.4609 |
| Return on average total assets | **0.27%** | 1.53% |
| Return on average shareholders' funds* | **3.81%** | 17.40% |
| Return on average total assets before impairment allowances | **1.52%** | 1.89% |
| Return on average shareholders' funds before impairment allowances* | **19.09%** | 21.95% |
| Net interest margin (NIM) | **2.00%** | 2.07% |
| Adjusted NIM** | **2.07%** | 2.10% |
| Non-interest income to operating income ratio | **21.03%** | 28.84% |
| Cost-to-income ratio | **34.36%** | 28.52% |

* Shareholders' funds represent capital and reserves attributable to the equity holders of the Company.

** Adjusted for the estimated impact of BOCHK's RMB clearing function. Since December 2003, the Bank has been the clearing bank to provide RMB clearing services for banks in Hong Kong that operate RMB business. Acting as the clearing bank, the Bank deposits those RMB deposits taken in Hong Kong by the participating banks with the People's Bank of China ("PBOC"). At the same time, the Bank earns an interest spread between the RMB funds taken from participating banks and those placed with the PBOC. As RMB deposits grow, the impact on the Group's average interest-earning assets and net interest margin ("NIM") becomes more material. It is, therefore, considered necessary to also provide information on NIM before incorporating the estimated impact of RMB clearing services (hereafter called "Adjusted net interest margin").

Analyses of the Group's financial performance and business operations are set out in the following sections.

**Net Interest Income and Margin**

| HK$'m, except percentage amounts | 2008 | 2007 |
|---|---|---|
| Interest income | **35,281** | 46,056 |
| Interest expense | **(15,124)** | (26,661) |
| Net interest income | **20,157** | 19,395 |
| Average interest-earning assets | **1,006,440** | 938,377 |
| Net interest spread | **1.78%** | 1.65% |
| Net interest margin | **2.00%** | 2.07% |
| Adjusted net interest margin* | **2.07%** | 2.10% |

* Excluding the estimated impact of BOCHK's RMB clearing function

Net interest income increased by HK$762 million, or 3.9%, to HK$20,157 million in 2008. Average interest-earning assets grew by HK$68,063 million, or 7.3%, to HK$1,006,440 million. Although net interest spread rose by 13 basis points, net interest margin fell by 7 basis points to 2.00% mainly due to a decline of 20 basis points in the contribution from net free fund. The significant increase in RMB deposits from participating banks in 2008 also led to the decrease in the net interest margin. Should the estimated impact of BOCHK's RMB clearing function in Hong Kong be excluded, the adjusted net interest margin would have been 2.07%, showing a fall of 3 basis points only.

Market interest rates fluctuated widely in 2008. Following the interest rate cut cycle kicked off by the US Federal Reserve in September 2007, market interest rates declined substantially and stayed at low levels in the first half of 2008. However, as the financial crisis continued to unfold and Lehman Brothers filed bankruptcy in mid-September 2008, the money market was under severe stress. One-month LIBOR once climbed to the peak of 4.59% in early October 2008. Further cuts in the Federal Funds Target Rate and the US government's US$700 billion financial bailout package helped ease the interbank credit market tension. One-month LIBOR then dropped to 0.44% at end-2008. Meanwhile, HKD interest rates followed broadly the same direction as their USD counterparts. Average one-month HIBOR in 2008 fell by 228 basis points to 2.00% while average one-month LIBOR fell by 257 basis points to 2.68% compared to 2007. The Group's average HKD Prime rate decreased by 219 basis points to 5.40%, thus widening the HKD Prime-to-one month HIBOR spread (hereafter called "Prime-HIBOR spread") by 9 basis points to 3.40%.

The increase in net interest income was mainly attributable to the growth in average interest earning assets, driven by the increase in average customer deposits as well as average deposits of banks and other financial institutions. Net interest spread increased with the widened securities spread in the falling interest rate environment. Average higher yielding loans, such as Mainland lending and trade finance, continued to grow. At the same time, the pricing of new corporate loan facilities had improved under the tightening credit environment. Loan spread, however, was compressed by the lower average pricing on the mortgage portfolio. The Group also took extra care in managing funding costs and its deposit mix continued to improve with an increase in the proportion of average demand deposits and current accounts* as well as savings deposits in its average total deposits. Deposit spread decreased with lower market rates as deposits rates were already at a very low level. Contribution from net free fund decreased as market interest rates dropped significantly.

* excluding IPO-related funds

The summary below shows the average balances and average interest rates of individual assets and liabilities:

| ASSETS | Year ended 31 December 2008 Average balance HK$'m | Year ended 31 December 2008 Average yield % | Year ended 31 December 2007 Average balance HK$'m | Year ended 31 December 2007 Average yield % |
|---|---|---|---|---|
| Loans to banks | **261,660** | **2.11%** | 207,454 | 4.01 |
| Debt securities investments | **306,807** | **4.27%** | 331,422 | 4.92 |
| Loans and advances to customers | **424,187** | **3.83%** | 382,040 | 5.45 |
| Other interest-earning assets | **13,786** | **2.92%** | 17,461 | 3.73 |
| Total interest-earning assets | **1,006,440** | **3.51%** | 938,377 | 4.91 |
| Non interest-earning assets | **92,758** | **–** | 94,200 | – |
| Total assets | **1,099,198** | **3.21%** | 1,032,577 | 4.46 |

| LIABILITIES | Year ended 31 December 2008 Average balance HK$'m | Year ended 31 December 2008 Average rate % | Year ended 31 December 2007 Average balance HK$'m | Year ended 31 December 2007 Average rate % |
|---|---|---|---|---|
| Deposits and balances of banks and other financial institutions | **79,969** | **1.91%** | 45,819 | 3.38% |
| Current, savings and fixed deposits | **767,006** | **1.65%** | 742,152 | 3.27% |
| Certificate of deposits issued | **1,474** | **3.73%** | 2,266 | 3.58% |
| Other interest-bearing liabilities | **27,597** | **3.08%** | 27,189 | 2.92% |
| Total interest-bearing liabilities | **876,046** | **1.73%** | 817,426 | 3.26% |
| Non interest-bearing deposits | **37,053** | **–** | 36,866 | – |
| Shareholders' funds* and non interest-bearing liabilities | **186,099** | **–** | 178,285 | – |
| Total liabilities | **1,099,198** | **1.38%** | 1,032,577 | 2.58% |

* Shareholders' funds represent capital and reserves attributable to the equity holders of the Company.

*Second Half Performance*

Compared to the first half of 2008, net interest income increased by HK$99 million, or 1.0%. Average interest-earning assets grew by HK$35,292 million, or 3.6%. Net interest margin and net interest spread fell by 6 basis points and 2 basis points respectively. Contribution from net free funds fell by 4 basis points.

The increase in net interest income was mainly attributable to the growth in average interest earning assets, driven by the increase in average customer deposits as well as average deposits and balances of banks and other financial institutions. The increase was partially offset by the decline in contribution from net free funds with lower market interest rates. Gross rate of debt securities declined due to repricing and increase in lower yielding liquefiable securities in the intensifying financial crisis. Average pricing of new corporate loan facilities continued to improve, however, loan spread was compressed as Prime-HIBOR spread was narrowed by 48 basis points compared to the first half of 2008. Deposit mix improved with an increase in the proportion of average demand deposits and current accounts* as well as savings deposits in the Group's average total deposits. Deposit spread increased as the Group managed its funding costs more prudently.

* excluding IPO-related funds

**Net Fees and Commission Income**

| HK$'m | **2008** | 2007 |
|---|---|---|
| Investment and insurance fee income | **2,964** | 4,511 |
| Securities brokerage (Stockbroking) | **2,380** | 3,560 |
| Securities brokerage (Bonds) | **259** | 211 |
| Sale of funds | **218** | 683 |
| Life insurance* | **107** | 57 |
| Credit cards | **1,220** | 1,027 |
| Bills commissions | **683** | 588 |
| Loan commissions | **513** | 347 |
| Payment services | **486** | 464 |
| Account services | **261** | 290 |
| RMB business | **223** | 137 |
| Currency exchange | **204** | 184 |
| Trust services | **173** | 153 |
| General insurance | **102** | 96 |
| Correspondent banking | **44** | 37 |
| Guarantees | **37** | 32 |
| Custody | **45** | 4 |
| IPO-related business | **30** | 105 |
| Others | **229** | 202 |
| Fees and commission income | **7,214** | 8,177 |
| Fees and commission expenses | **(2,035)** | (1,903) |
| Net fees and commission income | **5,179** | 6,274 |

* Fee income from life insurance only included that from the Group's insurance business partner after group consolidation elimination.

Net fees and commission income decreased by HK$1,095 million, or 17.5%, to HK$5,179 million, mainly due to the decline in investment-related fee income, which will be discussed in the next section "Investment and Insurance Business". Fee income from the Group's traditional banking businesses improved. Loan commission grew strongly by HK$166 million or 47.8%. This was mainly attributed to the successful implementation of the Group's new business model as well as the increase in syndicated loans following the Group's appointment as the "Asia-Pacific Syndicated Loan Centre" of the BOC Group in early 2008. Fees from the credit card business showed a satisfactory growth of HK$193 million or 18.8% as cardholder spending and merchant acquiring volume were up 12.7% and 19.9% respectively. Fee income from bills, RMB-related business and currency exchange recorded double-digit growths of 16.2%, 62.8% and 10.9% respectively. Following the introduction of custody business in 2007, its contribution to the Group's fee income was encouraging in 2008. However, fee income from IPO-related business decreased markedly by 71.4% as IPO activities reduced significantly. Meanwhile, fees and commission expenses increased by HK$132 million or 6.9%, mainly due to increase in credit card, currency exchange service and RMB-related business expenses.

*Second Half Performance*

Compared to the first half of 2008, net fees and commission income decreased by HK$619 million or 21.4%, largely because of the decline in investment-related fee income, which will be discussed in the next section. Meanwhile, fees and commission income from RMB-related business and card business increased by 25.3% and 11.1% respectively. Fees and commission expenses were up 15.1%, mainly because of higher credit card, currency exchange service and RMB-related business expenses.

**Investment and Insurance Business**

| HK$'m | **2008** | 2007 |
|---|---|---|
| Investment and insurance fee income | | |
| Securities brokerage (Stockbroking) | **2,380** | 3,560 |
| Securities brokerage (Bonds) | **259** | 211 |
| Sale of funds | **218** | 683 |
| Life insurance* | **107** | 57 |
| | **2,964** | 4,511 |
| Insurance and investment income of BOC Life | | |
| Net insurance premium income | **5,891** | 8,426 |
| Interest income | **1,122** | 788 |
| Net (loss)/gain on financial instruments designated at fair value through profit or loss | **(136)** | 893 |
| Others | **17** | 15 |
| Gross insurance and investment income of BOC Life# | **6,894** | 10,122 |
| Less: net insurance benefits and claims | **(7,709)** | (9,440) |
| | **(815)** | 682 |
| Total investment and insurance income | **2,149** | 5,193 |
| Of which: Life insurance fee income* | **107** | 57 |
| Insurance income of BOC Life# | **(815)** | 682 |
| Total life insurance income | **(708)** | 739 |
| Investment fee income | **2,857** | 4,454 |
| Total investment and insurance income | **2,149** | 5,193 |

* Fee income from life insurance only included that from the Group's insurance business partner after group consolidation elimination.

\# Before commission expenses.

In 2008, particularly in the second half, as the financial crisis intensified, investors' appetite for investment and wealth management products weakened further. This had a negative impact on the Group's investment and insurance related business which declined significantly following an exceptionally strong 2007. The Group's total investment and insurance income decreased by HK$3,044 million, or 58.6% to HK$2,149 million, mainly due to the decrease in both the income from stock broking and sale of funds coupled with the loss incurred by its insurance segment. Income from stock broking declined by HK$1,180 million or 33.1% due to lower business volume along with the fall in market transactions. Income from the sale of funds decreased by HK$465 million or 68.1% as the sales of open-end funds fell with diminished demand. Meanwhile, commission from the sales of bonds rose by HK$48 million, or 22.7% as sales of structured notes rose by 15.8% resulting from the successful private placement service introduced by the Group in the first half of the year. Fee income from the Group's insurance business partner also increased by HK$50 million, or 87.7% on the back of the 56.9% increase in sales volume. As for BOC Life, insurance income decreased by HK$1,497 million, which was mainly attributable to the weak performance of its investment assets with a loss of HK$136 million compared to a gain of HK$893 million in 2007. Net insurance premium income declined by HK$2,535 million, or 30.1%, as sales slowed down. During the first half of the year, the Group launched several large-scale promotional and marketing activities to reinforce the Group's brand image and boost the sales of regular pay products. Product mix continued to improve with net insurance premium income from regular premium products increasing by 39.6% year-on-year.

*Second Half Performance*

Compared to the first half of 2008, total investment and insurance income decreased by HK$1,443 million, or 80.3%. There was a broad-based decrease in investment and insurance fee income of HK$522 million or 29.9% as market demand further weakened in the second half of the year. The insurance income of BOC Life was down HK$921 million mainly due to the weak performance of its investment assets, lower net insurance premium income coupled with the increase in net insurance benefits and claims amid a falling interest rate environment.

**Net Trading Income**

| HK$'m | **2008** | 2007 |
|---|---|---|
| Foreign exchange and foreign exchange products | **1,809** | 800 |
| Interest rate instruments | **(127)** | 30 |
| Equity instruments | **119** | 181 |
| Commodities | **113** | 2 |
| Net trading income | **1,914** | 1,013 |

Net trading income was HK$1,914 million, up HK$901 million or 88.9% year-on-year mainly due to the surge in net trading income from foreign exchange and foreign exchange products by HK$1,009 million or 126.1%. During 2008, the currency market became volatile and the anticipated appreciation of the RMB boosted customers' appetite for currency-related products. Taking advantage of higher demand, the Group successfully grew its income from foreign exchange activities by HK$482 million or 42.1%. Meanwhile, net trading income from mark-to-market on foreign exchange swap contracts* significantly improved by HK$662 million. The increase was partially offset by a foreign exchange loss arising from the revaluation of Nanyang Commercial Bank (China), Limited's ("Nanyang (China)") Hong Kong Dollar capital funds against the appreciated RMB during the course of approval for conversion into RMB. Net trading income from interest rate instruments declined by HK$157 million, which was caused by the mark-to-market loss on interest rate swap contracts. Net trading income of equity instruments decreased by HK$62 million or 34.3%, mainly due to decline in the fair value of certain equity instruments. The decline was partly offset by the option premium income from the newly launched "Equity-Linked Investments". Net trading income from commodities increased by HK$111 million because of higher customer demand for bullion products in a volatile commodity market.

* Foreign exchange swap contracts are usually used for the Group's liquidity management and funding activities. Under foreign exchange swap contracts, the Group exchanges one currency (original currency) for another (swapped currency) at the spot exchange rate (spot transaction) and commits to reverse the spot transaction by exchanging the same currency pair at a future maturity at a predetermined rate (forward transaction). In this way, surplus funds in original currency are swapped into another currency for liquidity and funding purposes without any foreign exchange risk. Under HKAS 39, the exchange difference between the spot and forward contracts is recognised as foreign exchange gain or loss (as included in "net trading income"), while the corresponding interest differential between the surplus funds in original currency and swapped currency is reflected in net interest income.

*Second Half Performance*

Compared to the first half of 2008, net trading income declined by HK$560 million or 45.3% in the second half of the year. The decrease was mainly attributable to the decreased fair value of interest rate swap contracts. Income from foreign exchange transactions and structured deposits also dropped with lower customer demand when market sentiments deteriorated drastically and the US Dollar turned strong in the second half of 2008. This decline was offset by the mark-to-market gain on foreign exchange swap contracts.

**Net (Loss)/Gain on Financial Instruments Designated at Fair Value through Profit or Loss (FVTPL)**

| HK$'m | **2008** | 2007 |
|---|---|---|
| Net (loss)/gain on financial instruments designated at FVTPL of the banking business | **(316)** | (25) |
| Net (loss)/gain on financial instruments designated at FVTPL of BOC Life | **(136)** | 893 |
| Net (loss)/gain on financial instruments designated at FVTPL | **(452)** | 868 |

Compared to the net gain of HK$868 million recorded in 2007, a net loss on financial instruments designated at fair value through profit or loss of HK$452 million was recorded in 2008. This was mainly due to the net loss on equity investments held by BOC Life against the net gain recorded in 2007. In addition, the Group's banking business and BOC Life registered mark-to-market loss on their certain debt securities designated at fair value through profit and loss as their market values were adversely affected by the financial crisis. This included a net loss of HK$130 million with respect to the bonds issued by Lehman Brothers.

*Second Half Performance*

Compared to the net loss of HK$1,484 million recorded in the first half of 2008, net gain on financial instruments designated at fair value through profit or loss in the second half of 2008 was HK$1,032 million. This was mainly caused by the mark-to-market gain of certain debt securities investments of BOC Life recorded in the second half of 2008 under a low interest rate environment.

**Operating Expenses**

| HK$'m, except percentage amounts | **2008** | 2007 |
|---|---|---|
| Staff costs | **4,554** | 4,656 |
| Premises and equipment expenses (excluding depreciation) | **1,076** | 958 |
| Depreciation on owned fixed assets | **992** | 787 |
| Other operating expenses | **2,149** | 1,372 |
| Operating expenses | **8,771** | 7,773 |
| Cost-to-income ratio | **34.36%** | 28.52% |

In view of the weakening local economy and intensifying global financial crisis, the Group took pre-emptive measures by launching various cost containment programmes in the second half of the year. As a result, performance-related remuneration, promotional expenses and other business-related expenses had been well contained. These programmes proved to be effective as the growth in operating expenses in the second half of the year significantly slowed down versus the first half of the year.

Total operating expenses were up HK$998 million, or 12.8%, to HK$8,771 million which included the expenses* mainly related to the Lehman Brothers Mini-bonds issue ("Mini-bonds issue") totalling HK$769 million. Cost-to-income ratio rose by 5.84 percentage points over 2007 to 34.36%. Should the said expenses mainly related to the Mini-bonds issue be excluded, the Group's operating expenses would have increased by HK$229 million or 2.9% while the cost-to-income ratio would have risen by 2.83 percentage points to 31.35%.

Staff costs fell by HK$102 million, or 2.2%, primarily due to lower performance-related remuneration. Compared to end-2007, headcount measured in full-time equivalents rose slightly by 36 to 13,463 at end-2008.

Premises and equipment expenses increased by HK$118 million or 12.3% mainly because of higher IT costs and rental in 2008 and as inflationary pressure mounted in the first half of the year.

Depreciation on owned fixed assets rose by HK$205 million, or 26.0%, to HK$992 million due to the increase in computer equipment as the Group continued its infrastructure improvement as well as the effect of the appreciation of the value of bank premises in the first half of the year.

Other operating expenses were up HK$777 million, or 56.6%, mainly due to the additional expenses in relation to the Mini-bonds issue. Higher business taxes due to increased business in the Mainland as well as a larger amount of donations also contributed to the rise. Promotional expenses, however, were lower. Should the expenses* mainly related to the Mini-bonds issue be excluded, other operating expenses would have increased slightly by HK$8 million or 0.6%.

*Second Half Performance*

Compared to the first half of 2008, total operating expenses rose by HK$595 million, or 14.6%, mainly due to additional expenses incurred in relation to the Mini-bonds issue. If the expenses* mainly related to the Mini-bonds issue were excluded, operating expenses would have decreased by HK$174 million or 4.3%.

* including the related legal expenses

**Net (Charge)/Reversal of Loan Impairment Allowances**

| HK$'m | **2008** | 2007 |
|---|---|---|
| Net (charge)/reversal of loan impairment allowances | | |
| Individual assessment | | |
| – new allowances | **(813)** | (330) |
| – releases | **83** | 299 |
| – recoveries | **722** | 1,311 |
| Collective assessment | | |
| – new allowances | **(691)** | (625) |
| – releases | **10** | – |
| – recoveries | **28** | 30 |
| Net (charge)/reversal to Income Statement | **(661)** | 685 |

In 2008, the Group recorded a net charge of loan impairment allowances of HK$661 million. Compared to a net reversal of HK$685 million in 2007, this change in net charge of loan impairment allowances was mainly due to the increase in the net charge of allowances (before recoveries) from individual assessment and the decline in loan recoveries.

Net charge of individual impairment allowances (before recoveries) was HK$730 million, up HK$699 million from HK$31 million recorded in 2007. The increase in net impairment charge (before recoveries) was caused by the increase in new allowances made to cover the formation of new impaired loans and further deterioration of existing impaired accounts as the repayment capability of borrowers deteriorated in the economic downturn. The reduction in the release of allowances, due to the repayment made by certain large accounts in 2007, also contributed to the increase in net impairment charge.

Net charge of collective impairment allowances (before recoveries) was HK$681 million. The new allowances were mainly attributable to the expanded loan portfolio and the deterioration in asset quality of loans and advances amid the financial crisis.

The Group continued to make recoveries of loans that were previously written off. Total recoveries in individual and collective assessment amounted to HK$750 million, down HK$591 million compared to 2007 during which certain large accounts were recovered.

*Second Half Performance*

Net charge of loan impairment allowances increased by HK$519 million in the second half of 2008, mainly because of the increase in new allowances from individual assessment as the formation of new impaired loans occurred mainly in the second half of the year when the economy began to slow down. Impairment charge from collective assessment increased as asset quality of loans and advances deteriorated in the second half of the year. The increase in impairment charge from individual and collective assessment was partially offset by the increase in recoveries.

**Net Charge of Impairment Allowances on Securities Investments**

| HK$'m | **2008** | 2007 |
|---|---|---|
| Held-to-maturity securities | **(4,061)** | (1,844) |
| Available-for-sale securities | **(7,839)** | (289) |
| Net charge of impairment allowances on securities investments | **(11,900)** | (2,133) |

As the global financial crisis intensified in the second half of the year, the Group's investments in securities were negatively affected. In view of the increased volatility in major capital markets, the Group carried out a comprehensive assessment on its impairment charges, taking into account the relevant criteria and specific features of the investments, and increased its provisions accordingly. As a result, the Group recorded a total of HK$9,170 million of net charge of impairment allowances for its portfolio of US non-agency residential mortgage-backed securities ("RMBS") and other debt securities. The Group also recorded a charge of impairment allowance of HK$2,730 million against its investments in The Bank of East Asia, Limited, the share price of which fell sharply in the financial turmoil. The table below illustrates the breakdown of the Group's net charge of impairment allowances against its investments in securities in 2008 and 2007.

| HK$'m | 2008 | 2007 |
|---|---|---|
| US non-agency residential mortgage-backed securities | | |
| Subprime | **522** | (1,513) |
| Alt-A | **(1,734)** | (574) |
| Prime | **(7,041)** | (46) |
| | **(8,253)** | (2,133) |
| Other debt securities | **(917)** | – |
| Sub-total | **(9,170)** | (2,133) |
| Investment in Bank of East Asia, Limited | **(2,730)** | – |
| Total net (charge)/reversal of impairment allowances on securities investments | **(11,900)** | (2,133) |

For details about the composition of the Group's investment securities portfolio, and the impairment and provisioning policies on investments, please refer to Note 28, Note 2 and Note 3 to the Financial Statements.

*Second Half Performance*

Compared to the first half of 2008, the net charge of impairment allowances rose significantly by HK$7,602 million in the second half of the year.

As at 31 December 2008, the carrying value of the Group's exposure to bonds issued by Lehman Brothers was HK$39 million, comprising solely senior unsecured bonds. In 2008, the Group recorded HK$352 million net charge of impairment allowances and HK$130 million of net loss on financial instruments designated at fair value through profit or loss with respect to the aforesaid bonds.

**Property Revaluation**

| HK$'m | 2008 | 2007 |
|---|---|---|
| Net (loss)/gain on revaluation of premises | **(24)** | 19 |
| Net (loss)/gain on fair value adjustments on investment properties | **(132)** | 1,056 |
| Deferred tax | **93** | (143) |
| Net (loss)/gain on fair value adjustments on investment properties, after tax | **(39)** | 913 |

The aggregate impact of property revaluation before tax on the income statement in 2008 was a loss of HK$156 million, of which HK$132 million came from the revaluation of investment properties and HK$24 million from the revaluation of premises. This was a reversal to the aggregate gain recorded in the first half of the year as property prices in Hong Kong suffered a slump since the third quarter after the sharp increase recorded in late 2007 and early 2008. The related deferred tax credit on revaluation of investment properties amounted to HK$93 million. As a result, the net impact of fair value adjustments on investment properties on the Group's profit attributable to equity holders in 2008 was a loss of HK$39 million.

*Second Half Performance*

A net loss of HK$687 million from revaluation of investment properties after tax was recorded in the second half of 2008, against the net gain of HK$648 million in the first half of 2008. This was broadly in line with the decline in property prices since the third quarter of the year.

**Financial Position**

| HK$'m, except percentage amounts | At 31 December 2008 | At 31 December 2007 |
|---|---|---|
| Cash and balances with banks and other financial institutions | **153,269** | 159,065 |
| Placements with banks and other financial institutions maturing between one and twelve months | **89,718** | 53,154 |
| Hong Kong SAR Government certificates of indebtedness | **34,200** | 32,770 |
| Securities investments[1] | **335,493** | 335,623 |
| Advances and other accounts | **469,493** | 420,234 |
| Fixed assets and investment properties | **30,522** | 31,351 |
| Other assets[2] | **34,549** | 35,440 |
| Total assets | **1,147,244** | 1,067,637 |
| Hong Kong SAR currency notes in circulation | **34,200** | 32,770 |
| Deposits and balances of banks and other financial institutions | **88,779** | 60,599 |
| Deposits from customers | **802,577** | 793,606 |
| Debt securities in issue at amortised cost[3] | **1,042** | 2,089 |
| Insurance contract liabilities | **28,274** | 22,497 |
| Other accounts and provisions | **80,501** | 61,018 |
| Subordinated liabilities[4] | **27,339** | – |
| Total liabilities | **1,062,712** | 972,579 |
| Minority interests | **1,813** | 2,216 |
| Capital and reserves attributable to the equity holders of the Company | **82,719** | 92,842 |
| Total liabilities and equity | **1,147,244** | 1,067,637 |
| Loan-to-deposit ratio | **56.74%** | 51.66% |

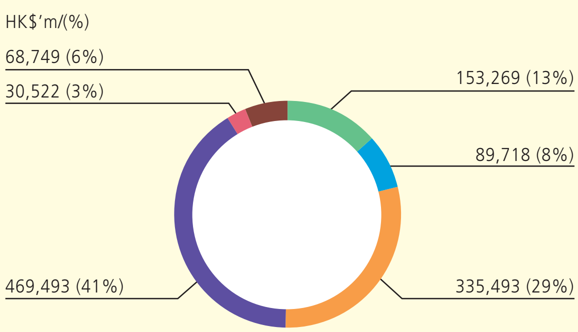
1 Securities investments comprise investment in securities and financial assets at fair value through profit or loss.

2 Interests in associates, deferred tax assets and derivative financial instruments are included in other assets.

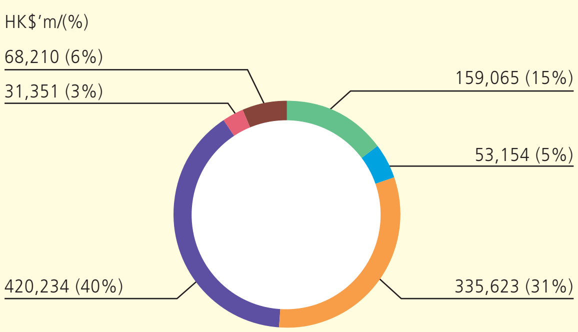
3 Debt securities in issue at amortised cost represents the notes issued under the Group's notes programme.

4 Subordinated liabilities represent the subordinated loans granted by the Group's parent bank, Bank of China Limited.

**Balance Sheet Mix as at 31 December 2008**




**Balance Sheet Mix as at 31 December 2007**




- Cash and balances with banks and other financial institutions
- Placements with banks and other financial institutions maturing between one and twelve months
- Securities investments
- Advances and other accounts
- Fixed assets and investment properties
- Other assets

The Group's total assets were HK$1,147,244 million as at 31 December 2008, up HK$79,607 million or 7.5% from the end of 2007. Key changes include:

- Cash and balances with banks and other financial institutions decreased by HK$5,796 million or 3.6% mainly due to the decrease in placements with banks and other financial institutions maturing within one month. This was partially offset by the increase in RMB deposits from participating banks placed with the PBOC.

- Placements with banks and other financial institutions maturing between one and twelve months increased by HK$36,564 million, or 68.8%, as the Group lengthened its interbank placements in the low interest rate environment.

- Advances and other accounts increased by HK$49,259 million, or 11.7%, mainly due to the growth of advances to customers by HK$47,385 million or 11.5%.

- Securities investments decreased slightly by HK$130 million. To ensure liquidity and safeguard its surplus funds, the Group increased investments in short-term government bills and expanded its investments in debt securities of governments and government guaranteed agencies. As of 31 December 2008, the carrying value of the Group's total exposure to US non-agency RMBS dropped to HK$19.3 billion from HK$39.7 billion as of end-2007. The Group had exposures to structured investment vehicles ("SIV"s) held by its 51% owned subsidiary, BOC Life. The carrying value of total exposure to the SIV's amounted to HK$57 million at end-2008 (At end-2007: approximately HK$100 million). The Group did not have exposure to collateralised debt obligations at end-2008 (At end-2007: nil).

**Advances to Customers**

| HK$'m, except percentage amounts | **At 31 December 2008** | **%** | At 31 December 2007 | % |
|---|---|---|---|---|
| Loans for use in Hong Kong | **336,597** | **73.1** | 305,677 | 74.0 |
| Industrial, commercial and financial | **188,774** | **41.0** | 168,656 | 40.8 |
| Individuals | **147,823** | **32.1** | 137,021 | 33.2 |
| Trade finance | **24,555** | **5.3** | 24,275 | 5.9 |
| Loans for use outside Hong Kong | **99,295** | **21.6** | 83,110 | 20.1 |
| Total advances to customers | **460,447** | **100.0** | 413,062 | 100.0 |

Total advances to customers rose by HK$47,385 million or 11.5% to HK$460,447 million, due to the growth in both corporate and individual loans as well as loans for use outside Hong Kong. This was attributable to the successful implementation of the Group's business strategies under its new business model, effective marketing, together with the Bank's appointment as the "Asia-Pacific Syndicated Loan Centre" of the BOC Group in early 2008.

Loans for use in Hong Kong grew by 10.1%.

- Lending to the industrial, commercial and financial sectors increased by HK$20,118 million, or 11.9%, to HK$188,774 million, driven by the growth in loans for property investment, wholesale and retail trade, information technology, property development, as well as manufacturing.

- Residential mortgage loans (excluding those under the Government-sponsored Home Ownership Scheme) was up HK$9,720 million, or 9.1%, to HK$116,303 million. This was a result of the Group's effective marketing efforts and product innovation.

- Card advances surged by HK$792 million, or 13.7%, to HK$6,553 million, which was in line with the increase in cardholder spending.

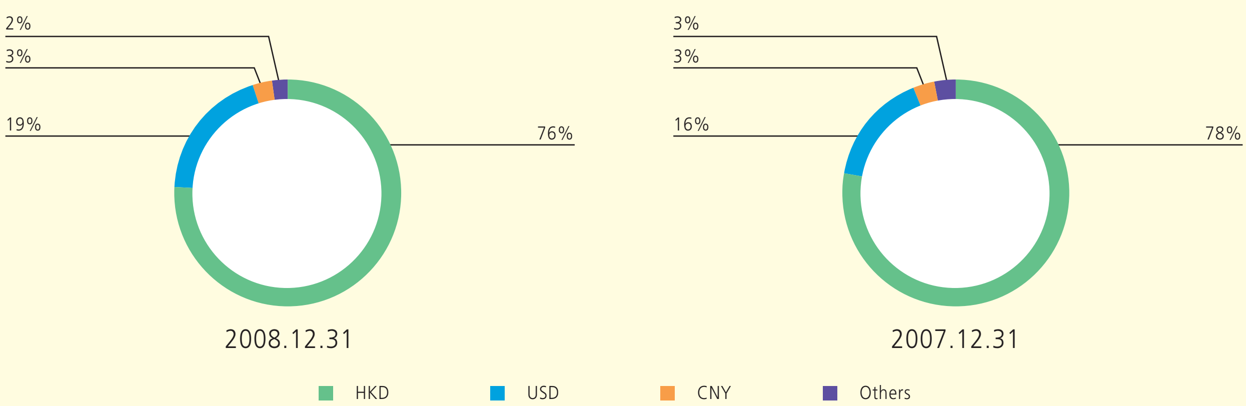
- Other individual lending increased by HK$782 million, or 7.3%, to HK$11,490 million mainly due to the growth in personal loans.

Trade finance recorded a mild increase of HK$280 million, or 1.2% against the decline in the import and export trade in Hong Kong in 2008. Meanwhile, loans for use outside Hong Kong grew strongly by HK$16,185 million or 19.5%.

*Second Half Performance*

Compared to the strong first half, the economic environment significantly deteriorated in the second half of the year and hence hindered further growth in advances to customers. At the same time, the Group took various strategic measures to contain its risk exposure amidst the global economic downturn. As a result, the Group's total advances to customers decreased by HK$15,140 million, or 3.2%, in the second half of the year.

**Total Advances to Customers by Currency Mix (%)**




In terms of currency mix, advances to customers in HKD and USD accounted for 75.5% and 19.0% respectively of the total at the end of 2008 while advances to customers in RMB and other currencies accounted for 3.3% and 2.2% respectively. The proportion of advances to customers in USD rose by 3.4% while advances to customers in HKD declined by 2.9%.

**Deposits from Customers**

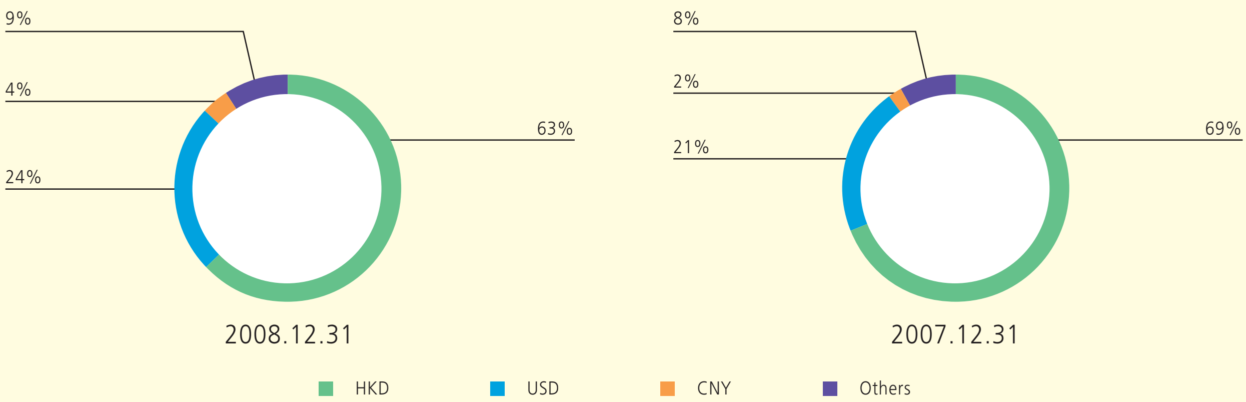
| HK$'m, except percentage amounts | **At 31 December 2008** | **%** | At 31 December 2007 | % |
|---|---|---|---|---|
| Demand deposits and current accounts | **46,042** | **5.7** | 40,499 | 5.1 |
| Savings deposits | **377,273** | **46.5** | 286,653 | 35.9 |
| Time, call and notice deposits | **379,262** | **46.7** | 466,454 | 58.3 |
| Total deposits from customers | **802,577** | **98.9** | 793,606 | 99.3 |
| Structured deposits | **8,939** | **1.1** | 5,959 | 0.7 |
| Adjusted total deposits from customers | **811,516** | **100.0** | 799,565 | 100.0 |

Total deposits from customers increased by HK$8,971 million, or 1.1%, to HK$802,577 million, with improved deposit mix. Demand deposits and current accounts increased by HK$5,543 million or 13.7%. Savings deposits rose by HK$90,620 million or 31.6%. Time, call and notice deposits were down HK$87,192 million or 18.7% as customers sought liquidity under the low interest rate environment and switched their funds to savings deposits. Structured deposits, a hybrid of retail deposit and derivatives offering a higher nominal interest rate, increased by HK$2,980 million, or 50.0%. The Group's loan-to-deposit ratio was up 5.08 percentage points to 56.74% at the end of 2008 as total loan growth outpaced deposits growth.

*Second Half Performance*

Total deposits from customers dropped by HK$16,533 million, or 2.0% in the second half of 2008. Demand deposits and current accounts increased by HK$5,135 million or 12.6% while savings deposits rose by HK$81,771 million or 27.7%. However, time, call and notice deposits dropped by HK$103,439 million or 21.4%. Structured deposits, on the other hand, rose significantly by HK$5,338 million or 148.2% in the low interest rate environment.

**Adjusted Total Deposits from Customers by Currency Mix (%)**




In terms of currency mix, HKD and USD deposits accounted for 62.8% and 24.1% respectively at the end of 2008, while deposits in RMB and other currencies accounted for 3.7% and 9.4% respectively. The proportion of HKD deposits dropped by 6.3 percentage points while that of RMB and other currencies rose by 1.5 percentage points and 1.7 percentage points respectively from the end of 2007, reflecting customers' preference for shifting their funds into RMB deposits in anticipation of the appreciation of RMB and into other foreign currency deposits for higher returns. The proportion of USD deposits also rose by 3.1%. The Group's HKD loan-to-deposit ratio was 68.3%, up from 58.7% at end-2007 as HKD loans increased while HKD deposits decreased.

**Loan Quality**

| HK$'m, except percentage amounts | **At 31 December 2008** | At 31 December 2007 |
|---|---|---|
| Advances to customers | **460,447** | 413,062 |
| Classified or impaired loan ratio[1] | **0.46%** | 0.44% |
| Impairment allowances | **2,301** | 1,385 |
| Regulatory reserve for general banking risks | **4,503** | 4,130 |
| Total allowances and regulatory reserve | **6,804** | 5,515 |
| Total allowances as a percentage of advances to customers | **0.50%** | 0.34% |
| Total allowances and regulatory reserve as a percentage of advances to customers | **1.48%** | 1.34% |
| Impairment allowances on classified or impaired loan ratio[2] | **38.96%** | 22.52% |
| Residential mortgage loans[3] – delinquency and rescheduled loan ratio[4] | **0.05%** | 0.15% |
| Card advances – delinquency ratio[4,5] | **0.29%** | 0.28% |

| | **2008** | 2007 |
|---|---|---|
| Card advances – charge-off ratio[5] | **2.22%** | 2.40% |

(1) Classified or impaired loans represent advances which have been classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired. Repossessed assets are initially recognised at the lower of their fair value less costs to sell or the amortised cost of the related outstanding loans on the date of repossession. The related loans and advances are deducted from loans and advances.

(2) Including impairment allowances on loans classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

(3) Residential mortgage loans exclude those under the Home Ownership Scheme and other government-sponsored home purchasing schemes.

(4) Delinquency ratio is measured by a ratio of total amount of overdue loans (more than three months) to total outstanding loans.

(5) Excluding Great Wall cards and computed according to the HKMA's definition.

The Group's loan quality remained sound with its classified or impaired loan ratio increasing slightly by 0.02 percentage point to 0.46%, well below the market average. Classified loans increased by approximately HK$0.3 billion or 18.6% to HK$2.1 billion. New classified loans in 2008 represented approximately 0.4% of total loans outstanding.

Total impairment allowances, including both individual assessment and collective assessment, amounted to HK$2,301 million. Impairment allowances on classified or impaired loan ratio was 38.96%. The Group's regulatory reserve rose by HK$373 million to HK$4,503 million as advances to customers increased.

The quality of the Group's residential mortgage loans continued to improve with the combined delinquency and rescheduled loan ratio having fallen by 0.10 percentage point to 0.05% at end-2008. The quality of card advances remained strong, with the charge-off ratio declining from 2.40% in 2007 to 2.22% in 2008. Both ratios were well below the market average.

**Capital and Liquidity Ratios**

| HK$'m, except percentage amounts | At 31 December 2008 | At 31 December 2007 |
|---|---|---|
| Core capital | **65,172** | 67,145 |
| Deductions | **(1,536)** | (483) |
| Core capital after deductions | **63,636** | 66,662 |
| Supplementary capital | **32,675** | 5,161 |
| Deductions | **(1,536)** | (483) |
| Supplementary capital after deductions | **31,139** | 4,678 |
| Total capital base after deductions | **94,775** | 71,340 |
| Risk-weighted assets | | |
| Credit risk | **545,107** | 510,970 |
| Market risk | **9,097** | 7,998 |
| Operational risk | **44,144** | 39,139 |
| Deductions | **(12,273)** | (12,875) |
| Total risk-weighted assets | **586,075** | 545,232 |
| Capital adequacy ratios (consolidated basis) | | |
| Core capital ratio | **10.86%** | 12.23% |
| Capital adequacy ratio | **16.17%** | 13.08% |

| | 2008 | 2007 |
|---|---|---|
| Average liquidity ratio | **41.74%** | 50.92% |

Consolidated capital adequacy ratio of the banking group at 31 December 2008 was 16.17%, up 3.09 percentage points from end-2007 due to the increase in total capital base. Total capital base rose by 32.8% to HK$94,775 million mainly due to two subordinated loans of EURO 660 million and USD2,500 million respectively from its parent bank, Bank of China Limited, on 27 June 2008 and 23 December 2008 respectively. These subordinated loans meet the conditions laid down in the Banking (Capital) Rules and have been included as supplementary capital for the purpose of determining the capital base of the banking group. The Group's capital structure was therefore further improved with a higher proportion of supplementary capital to total capital base at end-2008. Meanwhile, risk-weighted assets rose by 7.5% to HK$586,075 million, mainly due to the growth in advances to customers.

Average liquidity ratio remained strong at 41.74% in 2008.

## BUSINESS REVIEW

This section covers the performance of the Group's business lines together with their respective financial results.

### PERSONAL BANKING

| HK$'m, except percentage amounts | **Full-year ended 31 December 2008** | Full-year ended 31 December 2007 | Increase/ (decrease) |
|---|---|---|---|
| Net interest income | **6,511** | 8,144 | -20.1% |
| Other operating income | **4,179** | 5,931 | -29.5% |
| Operating income | **10,690** | 14,075 | -24.0% |
| Operating expenses | **(5,669)** | (5,829) | -2.7% |
| Operating profit before impairment allowances | **5,021** | 8,246 | -39.1% |
| Net charge of loan impairment allowances | **(120)** | (112) | +7.1% |
| Others | **(9)** | (5) | +80.0% |
| Profit before taxation | **4,892** | 8,129 | -39.8% |

| | **At 31 December 2008** | At 31 December 2007 | Increase/ (decrease) |
|---|---|---|---|
| Segment assets | **165,148** | 162,634 | +1.5% |
| Segment liabilities | **523,682** | 545,397 | -4.0% |

Note: For additional segmental information, see Note 49 to the Financial Statements.

#### Results

Personal Banking recorded a profit before taxation of HK$4,892 million in 2008. Low interest rates and a sluggish investment market had an adverse impact on both its net interest income and fees and commission income from investment-related agency businesses. As a result, operating profit before impairment allowances decreased by 39.1% to HK$5,021 million year-on year.

Net interest income decreased by 20.1% to HK$6,511 million primarily due to narrower deposits spread. Other operating income fell by 29.5% to HK$4,179 million, mainly caused by the decline in fees and commission income from stock broking and sales of open-end funds. A non-recurring gain arising from the initial recognition of shares received from Visa Inc. in 2007 also caused the decline in other operating income in 2008 on a comparable basis.

Operating expenses were down by 2.7% to HK$5,669 million, mainly due to the fall in staff costs as performance-related remuneration decreased. Lower promotional expenses also contributed to savings in operating expenses.

Net charge of loan impairment allowances rose by 7.1% to HK$120 million, mainly due to the deterioration of borrowers' debt servicing capability and lower collateral values as well as the reduction in recoveries.

Advances and other accounts, including mortgage loans and card advances, increased by 7.1% to HK$152,285 million. Customer deposits fell by 2.5% to HK$500,391 million.

### Maintaining market leadership in residential property mortgage

The local property market turned sluggish in the second half of 2008 after recording a revival in late 2007. Both housing prices and transaction volume have declined notably since the third quarter of 2008. Nevertheless, the Group managed to achieve good results in its residential mortgage business through effective marketing and the introduction of a wider range of mortgage products. By the end of 2008, outstanding residential mortgage loans grew by 9.1%, outperforming the market growth of 5.1%. To commemorate the 2008 Beijing Olympics, a series of new mortgage plans were rolled out, such as the "8 Privilege Offers for the 2008 Olympics Mortgage Scheme" and "Olympic Decathlon Mortgage Scheme". In order to enhance its marketing capacity, the Group strengthened its strategic partnership and participated in joint promotion campaigns with major property developers. In March 2008, the Group also set up four Mortgage Advice Centres in selected areas to provide convenient and professional consultancy services to customers. All these initiatives sustained the Group's competitive edge in the residential mortgage market and ensured its leading position in the underwriting of new mortgages. In view of the economic downturn and turbulence in the financial market, the Group further strengthened its risk assessment and control on its mortgage business. Meanwhile, the credit quality of residential mortgages remained strong with the delinquency and rescheduled loan ratio falling further to 0.05%. For its outstanding service, the Group was awarded the "Sing Tao Excellent Services Brand Award 2008 – Mortgage and Loan Services" by *Sing Tao Daily* and the "Capital Weekly Service Awards 2008 – Mortgage" by *Capital Weekly*.

### Maintaining competitive edge in investment and insurance business

In 2008, in the wake of the global financial crisis, stock markets throughout the world experienced a slump. The local equity market also plummeted and the collapse of Lehman Brothers further weakened investors' appetite for investment and wealth management products. This had an adverse impact on the Group's investment-related distribution business. Nevertheless, the Group strove to maintain its competitiveness and enhance its trading platforms to meet the diverse needs of customers. The "Online Securities Margin Trading" and "Closing Auction Session for Securities Trading" services were introduced during the year. The Group also launched the "Automated Stock Trading Hotline" service exclusively for its wealth management customers. At the same time, the Group continued its support for environmental protection by introducing the "Securities e-Statement" service. In anticipation of a volatile market in 2008, the Group launched the "Balanced Investment Fund Series" (the "Series") at the end of 2007 to raise customers' awareness of portfolio risk management while offering a wide array of investment products.

In respect of its Bancassurance business, the Group continued to improve its product offerings, strengthen its brand and develop its sales force.

During the year, a series of new insurance products were launched to satisfy both personal and corporate customers' needs in the area of protection and wealth accumulation. For wealth accumulation side, the "Fortuitous Saving Protection Plan" was launched in the first quarter of 2008, and the "5-Year Joyful Life Insurance Plan" in the fourth quarter of 2008, providing customers with guaranteed cash value and guaranteed cash coupon. For protection, the "BOC Family Comprehensive Protection Plan", a first-of-its-kind bundled insurance product in the market, was launched in May 2008 to offer extensive protection covering home content, annual travel, personal accident, golfers and domestic helpers. In September 2008, the "BOC Business Comprehensive Insurance Plan", a professional all-in-one insurance package, was introduced to corporate customers. The Group's insurance product suite was also substantially enriched after the introduction of the "Pleasure 5-year Saving Protection Plan", "Harvest Joy Protection Plan", and "China Express Accidental Emergency Medical Plan", thus enabling customers to decide their financial and protection needs at different stages of their lives.

In addition to product innovation, different promotional and marketing campaigns were rolled out in major media during the year to help reinforce the Group's brand image and to reward the Group's customers for their support for the Group's Bancassurance Services. Extensive training and reinforcement were provided to frontline sales teams to upgrade their product and service proficiency.

### Expanding high net worth customer base and service foothold

Despite the general slowdown in the local economy in the second half of 2008, the Group made good progress in expanding its high net worth customer base and in reinforcing its strong position as a professional wealth management service provider. During the year, the Group launched the "Olympic Five Rings Rewards" which offered its customers exclusive privileges in foreign currency fixed deposits, RMB services, investment funds subscription and securities trading. To promote its expertise in wealth management services, the Group staged a number of wealth management expositions and investment seminars and sponsored market information and forecast in local newspapers. The Group also seized increasing opportunities in the Mainland China by working closely with BOC in launching the cross-border wealth management service. This service will be offered through designated branches of BOC in the Mainland and will further simplify the operation flow in the first half of 2009. Meanwhile, the Group enhanced the procedures and provided additional channels for account opening through call centre and internet banking for potential customers to access the wealth management services. At the end of 2008, the total number of wealth management customers* grew by 21.5% while assets of wealth management customers maintained with the Group declined by 12.7% because of the negative market conditions.

### Developing the mass retail customer base

The Group continued to exploit the growth potential of mass retail customers for expanding its personal banking business. In 2008, the Group re-packaged the i-Free Integrated Account service ("i-Free") which provides customers with a hassle-free and multi-dimensional banking service covering different banking areas. The service was re-positioned to appeal to the younger clientele with a healthy and dynamic life style. Various acquisition campaigns bundled with MPF, RMB deposits, payroll and investment services were launched. Meanwhile, the Group rolled out the "Operational Customer Relationship Management" system to provide front-line staff with an integrated customer contact platform to conduct sale and service, thus enhancing customer experience and reinforcing the Group's marketing capabilities. As a result, the total number of i-Free customers and related assets maintained with the Group surged by 322.4% and 197.3% respectively in 2008.

### Continuing to grow credit card business

The Group's card business sustained its growth momentum in card advances and customer base. Card advances and the number of cards in issue increased by 13.7% and 2.8% respectively from the end of last year. Cardholder spending volume and merchant acquiring volume grew by 12.7% and 19.9% respectively. At the same time, the Group continued its product innovation by offering a wide range of new products. To promote the Beijing 2008 Olympic Games, the Group introduced the "VISA BOC Olympic Games Platinum Card" in May 2008. In August 2008, the Group also launched the "BOC Elite Platinum Commercial Card" as a flexible financing solution for corporate customers. Two co-branded cards namely "BOC Esso MasterCard" and "SOGO VISA Platinum Card" were introduced in May and September respectively to provide customers with unsurpassed shopping experience and lifestyle privileges. In partnership with China UnionPay, the "BOC CUP Dual Currency Credit Card" was launched in December 2008. Acting as the event partner bank, the Group was authorized to provide acquiring services to merchants located at the Olympic Village, equestrian game venue and media hotels in Hong Kong. Meanwhile, the Group's card business in the Mainland continued to grow and the "EMV Titanium Card" was introduced during the year. Following the establishment of BOC Services Company, Limited, a joint venture between BOC Credit Card (International) Ltd. and BOC in late 2007, the Group has been benefiting from the strengthening of its bank card-related service and support in the rapidly growing market in the Mainland. Meanwhile, the charge-off ratio stood at 2.22%, well below the market average.

### Leading RMB banking business in Hong Kong

The Group continued to lead the RMB banking business in Hong Kong. The Group secured the largest market share in the RMB deposits-taking business in Hong Kong with the amount of RMB deposits increasing by 58.5% in 2008. At the same time, the Group maintained its leading position in the RMB credit card business as the number of RMB credit cards issued increased by 24.6% while the RMB card acquiring volume and RMB cardholder spending volume increased by 60.5% and 49.8% respectively. To meet the huge demand for RMB deposits, the Group launched the "RMB Exchange Express" to provide customers with a more convenient RMB exchange service. At the same time, the Group also introduced the "RMB Remittance Express", providing customers with RMB remittance service to bank accounts of the Group's branches in the Mainland with preferential handling charges. During the year, the Group acted as the joint lead manager, bookrunner and placing bank for RMB bonds valued at a total of 9 billion yuan issued in Hong Kong by major Mainland banks.

* Including wealth management VIP and wealth management Prime customers

### Channel rationalisation and e-channel development

The Group continued to optimise its distribution channels. During 2008, the Group added 14 wealth management centres and 4 Mortgage Advice Centres to its network in Hong Kong. At the end of 2008, the Group's service network in Hong Kong included a total of 286 branches (versus 288 at end-2007). Within this network, to provide exclusive financial services to selected customers, 108 Wealth Management Prime centres and 21 Wealth Management VIP centres have been in operation.

To strengthen its leading position in providing RMB services in Hong Kong, the Group extended its RMB ATM withdrawal services to all of its ATMs located in MTR stations. The number of ATMs with RMB withdrawal service reached 429 at the end of 2008 while the number of RMB withdrawals from the Group's ATM network in 2008 registered a significant increase against that of 2007. In view of the increasing demand of customers for RMB withdrawal and payment services, the Group collaborated with China UnionPay to enable the Group's new cardholders to enjoy RMB ATM services at China UnionPay's extensive ATM network and Point of Sale services in over one million shops all over China and around the world. Moreover, money exchange services were expanded to all branches.

The Group continued to enhance its internet banking platform to provide more efficient internet banking services to its customers. The number of personal e-banking customers increased by 12.2% while stock trading transactions through all e-channels accounted for 76.2% of total transactions. The Group also enhanced the Interactive Voice Response System to provide more user-friendly phone banking services and strengthened the telemarketing capability of call centres.

The staff of the Group won the "Outbound Contact Centre Agent of the Year" Silver Award and the "Inbound Contact Centre Agent of the Year" Bronze Award in the 9th Annual Contact Centre Awards 2008 competition organised by the Hong Kong Call Centre Association.

### Launch of Beijing 2008 Olympic Games Hong Kong Dollar Commemorative Banknotes

In celebration of the Beijing 2008 Olympic Games, the Group as the sole banking sponsor launched the Beijing 2008 Olympic Games Hong Kong Dollar Commemorative Banknotes for public sale in July 2008 and received overwhelming response. This was the first time ever in the history of modern Olympic Games that commemorative banknotes were issued. Proceeds generated from the sale of the HKD Olympic Banknote were donated to charity.

## CORPORATE BANKING

| HK$'m, except percentage amounts | **Full-year ended 31 December 2008** | Full-year ended 31 December 2007 | Increase/ (decrease) |
|---|---|---|---|
| Net interest income | **5,949** | 5,739 | +3.7% |
| Other operating income | **2,262** | 1,930 | +17.2% |
| Operating income | **8,211** | 7,669 | +7.1% |
| Operating expenses | **(2,143)** | (1,940) | +10.5% |
| Operating profit before impairment allowances | **6,068** | 5,729 | +5.9% |
| Net (charge)/release of loan impairment allowances | **(541)** | 797 | -167.9% |
| Others | **(3)** | – | N/A |
| Profit before taxation | **5,524** | 6,526 | -15.4% |

| | **At 31 December 2008** | At 31 December 2007 | Increase/ (decrease) |
|---|---|---|---|
| Segment assets | **324,606** | 281,680 | +15.2% |
| Segment liabilities | **309,254** | 284,353 | +8.8% |

Note: For additional segmental information, see Note 49 to the Financial Statements.

### Results

Corporate Banking achieved good results in pre-provision profit and business development. Operating profit before impairment allowances rose by 5.9% to HK$6,068 million year-on-year. The increase was mainly driven by the growth of net interest income and other operating income. However, after accounting for the net charge of loan impairment allowances, profit before taxation declined by 15.4%.

Net interest income rose by 3.7% to HK$5,949 million, mainly due to the increase in average loans and advances, which was partly offset by narrowed deposit spread as market interest rates declined. Other operating income was up by 17.2%, primarily attributable to the growth in both fees income from loan and bills services.

Operating expenses increased by 10.5% to HK$2,143 million mainly because of higher staff cost after the headcount increase in the Mainland branches, higher business tax for Mainland business as well as increased depreciation charges on computer equipment.

Net charge of loan impairment allowances was HK$541 million, compared to the net release of loan impairment allowances of HK$797 million in 2007. The net charge reflected the reduction of loan recoveries and the increase in the loan impairment allowances made to cover the formation of new impaired loans and further deterioration of existing impaired accounts as the repayment capability of certain accounts deteriorated amid the economic downturn.

Advances and other accounts increased by 15.2% to HK$323,268 million. Customer deposits rose by 8.5% to HK$305,546 million.

### Maintaining market leadership in loan syndication

The Group maintained its leading position in loan syndication. Not only did the Group remain the top mandated arranger in both the Hong Kong-Macau and the Mainland-Hong Kong-Macau syndicated loan markets in 2008, its market shares also rose significantly. Following its appointment as the "Asia-Pacific Syndicated Loan Centre" of the BOC Group in January 2008, the Group extended its strength in loan syndication business to the wider Asia-Pacific region. During the year, the Group successfully won the bid to become the sole arranger for the syndicated loan for two well-established enterprises in Australia, thus enhancing its market status in the region. As a result, the ranking of BOC Group in the Asia-Pacific region was considerably elevated in the year. The Group established the first phase of its "Loan Syndication Information Management System" in the first half of 2008. This new system links up similar networks of the BOC Group's major branches, thus optimising the sharing of supporting information among group members and enhancing overall operational efficiency.

### Market recognition of SME business

The Group continued to expand and refine its product offerings to meet changing market needs. In early 2008, the Group and the Hong Kong Productivity Council jointly introduced the "Green Equipment Financing Scheme", a preferential lending package for corporate customers to acquire environment-friendly equipment. The Group also introduced the "Corporate Privilege" services at 74 selected branches to provide tailor-made services to targeted customers. At the same time, two Commercial Centres and an SME Centre were established to strengthen its service support to the SME business. In response to the HKSAR Government's initiatives of supporting SME businesses in the global financial crisis, the Group devoted more resources to promote the "SME Loan Guarantee Scheme", which helps enterprises secure loans from participating banks for meeting general business needs with the Government acting as the guarantor. In recognition of its success and innovative services provided to the SME business, the Group was given the "SME's Best Partner Award 2008" by the Hong Kong Chamber of Small and Medium Business Limited as well as the "*Capital Weekly* Service Awards 2008 – SME Banking" by *Capital Weekly*. In 2008, the Group recorded a steady year-on-year growth of SME loans.

### Trade finance business adversely affected by contraction in global trade

During the year, the Group continued to actively develop its trade finance business by introducing a number of new factoring products with enhanced product features in order to enhance its competitiveness and market penetration. The "Trade Facilities Reform Programme" was launched to streamline the credit approval process and improve the credit utilisation rate. As a result, the trade finance business attained a strong growth in the first half of the year. However, it decelerated in the fourth quarter as the external economic environment deteriorated. Coupled with the risk management measures taken by the Group, the outstanding balance of trade finance slowed to a 1.2% increase over end-2007. The Group recorded a 32.0% increase in the volume of trade bills settlement compared to 2007, primarily driven by the strong import and export trade in the first three quarters of 2008.

### Robust expansion of cash management

The Group made good progress in developing its cash management business. During the year, the Group continued to design and consolidate cross-border cash management projects for top-tier Mainland enterprises. Agreements on cash management services were concluded with several large Mainland corporates seeking overseas expansion. At the same time, the Group strove to enhance its competitive edge in the local cash management business. Refinement of existing products such as "Integrated Receivables and Payment Solutions" and continuous development of new products have been underway to meet the diverse needs of customers. In July 2008, the Group introduced the "Enterprise Resource Planning Integration" to make it easier for customers to handle various cash management transactions through their own financial systems. The remittance points of BOC Remittance Plus increased to over 2900. At the end of 2008, the number of CBS Online customers increased by 60.5% while that of BOC Wealth Master customers rose by 32.7%.

### Forging ahead with the development of custody services

Following the establishment of a custody team in 2007, the Group's custody business continued to grow in 2008 with the number of clients recording satisfactory increase from end-2007. The Group has been the safe harbour for parking investment assets by institutional clients in the volatile market. During the year, the Group succeeded in becoming the custodian for a number of investment funds listed locally or incorporated offshore. In January 2008, the Group was appointed by a joint venture investment bank in the Mainland as the foreign custodian for its first QDII product, which was also the first broker-type QDII product ever approved in the Mainland. Through close collaboration with its parent, BOC, the Group successfully implemented several QDII mandates during the year. At the same time, the Group worked closely with BOC to conduct business reviews and explore new business opportunities. At end-2008, total assets under the Group's custody were valued at HK$200 billion.

### Expansion of financial services to corporate customers

The Group is committed to offering a comprehensive range of financial services to meet customers' needs. In 2008, the Group established a specialised team for commercial wealth management to provide professional wealth management services for its corporate customers. The team formulates tailor-made financial management strategy and provides regular reviews to help customers in maximising their wealth potential while managing risks with the professional tools.

### Proactive measures in risk management against global economic downturn

In response to the global economic downturn, the Group formulated a series of strategic measures to contain its risk exposure. These measures included stepping up the scrutiny of corporate risk and setting up a specialised working group on "crisis and risk management" for a full evaluation of the Group's risk exposure in its loan portfolio. Meanwhile, the Group conducted comprehensive re-assessments of credit risks and stress tests on customers from key business segments, especially those more adversely affected by the global economic downturn. Those customers identified with higher risk were closely monitored. Moreover, the Group lifted the average pricing of new corporate loan facilities granted during the year, in view of higher risk premium amidst the general tightening in liquidity.

## MAINLAND BUSINESS

### Making good progress in expanding Mainland business

Mainland business remains one of the Group's strategic focuses and continued to record satisfactory growth. With the local incorporation of NCB (China) since December 2007, the Group's Mainland operation has been making good progress in business development. In 2008, total advances to customers grew by 5.6%, with RMB loans surging by 12.6%. Customer deposits increased strongly by 72.5%. Total operating income recorded a growth of 15.9%, driven by the growth of both net interest income and net fees and commission income which was, however, partially offset by the foreign exchange loss arising from the revaluation of NCB (China)'s Hong Kong Dollar capital funds against the appreciated RMB. Operating profit before impairment allowances dropped by 3.1% year-on-year. Should the estimated impact of the exchange revaluation of the Mainland operation's capital funds be excluded**, operating profit before impairment allowances would have increased by 23.3%. Loan quality remained sound. The classified loan ratio stood at 0.88%, representing an increase of 0.20 percentage point from end-2007mainly due to the downgrade of several large accounts.

** The estimated impact of the exchange revaluation of the Mainland operation's capital funds included the exchange revaluation loss of NCB (China)'s HKD capital funds and the revaluation gain of the RMB operating funds of the Group's other mainland branches.

The Group continued to make good progress in expanding its cross-border financial services to better serve both personal and corporate customers. With the opening of its Guangzhou Panyu sub-branch and Hangzhou and Nanning branches, the Group's total number of branches and sub-branches in the Mainland increased to 18 by the end of 2008. Of these 18 branches and sub-branches, 6 had been approved to conduct full RMB businesses while 10 had been permitted to conduct RMB businesses except for Mainland residents. In addition, NCB (China)'s Shanghai Xuhui sub-branch already commenced business in January 2009 while the preparation for the opening of its Chengdu branch and Beijing Jianguomen sub-branch is underway following the approval granted by the China Banking Regulatory Commission ("CBRC"). The Group actively promoted its cross-border services, including RMB remittance and account opening services for non-domestic customers. With the expansion of domestic RMB businesses in the Mainland, the Group launched a wide range of deposits products such as "call deposits" and the "Smart Banking Account" as well as various mortgage products including the "All-You-Want Mortgage Scheme". In addition, new lending products had been introduced with good response from corporate customers.

**TREASURY**

| HK$'m, except percentage amounts | **Full-year ended 31 December 2008** | Full-year ended 31 December 2007 | Increase/ (decrease) |
|---|---|---|---|
| Net interest income | **7,178** | 5,869 | +22.3% |
| Other operating income | **879** | 206 | +326.7% |
| Operating income | **8,057** | 6,075 | +32.6% |
| Operating expenses | **(831)** | (627) | +32.5% |
| Operating profit before impairment allowances | **7,226** | 5,448 | +32.6% |
| Net charge of impairment allowances on securities investments | **(9,170)** | (2,133) | +329.9% |
| (Loss)/Profit before taxation | **(1,944)** | 3,315 | -158.6% |

| | **At 31 December 2008** | At 31 December 2007 | Increase/ (decrease) |
|---|---|---|---|
| Segment assets | **603,965** | 566,661 | +6.6% |
| Segment liabilities | **203,481** | 116,095 | +75.3% |

Note: For additional segmental information, see Note 49 to the Financial Statements.

**Results**

The Treasury segment registered a 32.6% growth in operating income in 2008, mainly driven by the increase in net interest income and other operating income. The increase was partially offset by the rise in operating expenses. Operating profit before impairment allowances grew by 32.6% to HK$7,226 million. However, the segment recorded a loss before taxation of HK$1,944 million mainly due to a net charge of impairment allowance of HK$9,170 million on the Group's portfolio of US non-agency RMBS and other debt securities.

Net interest income rose by 22.3% mainly due to higher interest spread on the debt securities portfolio with lower funding cost as market rates declined.

Other operating income surged by 326.7% mainly because of the improvement of net trading income from mark-to-market on foreign exchange swap contracts as well as higher income from other foreign exchange activities. During the year, the currency market was volatile and the anticipated appreciation of the RMB boosted the demand for currency-related products. As a result, the business volume of the foreign exchange businesses rose. Growth in income from commodities also contributed to the increase in operating income due to higher demand for bullion products amid the volatile commodity market.

Operating expenses increased by 32.5% to HK$831 million mainly due to the increase in depreciation charges on computer equipment and higher staff costs.

### Safeguarding investment assets and enhancing portfolio management

The crash of the global stock markets, the virtual halt of inter-bank lending and diminished risk appetite of investors created a very challenging environment for the Group's investment portfolio management in the latter half of 2008. To ensure the liquidity and safety of surplus funds, the Group adjusted its asset allocation and increased its investments in short-term government bills. Meanwhile, by expanding its investments in high-quality fixed rate debt securities of high quality governments and government guaranteed agencies, the Group was able to generate a stable income stream despite a low interest rate environment. Moreover, the Group's investment decision-making process and portfolio risk management have been enhanced through the operation of three specialised investment teams focusing on different markets and with the Asset Liability Management System which was launched last year. Communication on the latest market developments between investment teams and the Group's subsidiaries was further strengthened.

In response to the financial crisis, the Group closely monitored the market movement, conducted detailed analysis of the underlying risks of its portfolio and managed its banking book investments proactively. The Group has established disposal and watch lists and has taken appropriate actions to safeguard its investments based on dynamic assessment of the market environment. The carrying value of the Group's exposure to US non-agency RMBS dropped by 51.3% to HK$19.3 billion at end-2008. In addition to the impairment allowances provided for the portfolio, the reduction in exposure was also attributable to repayment and disposal. Of the Group's total exposure to US non-agency RMBS, about 39.5% was originated* prior to 2006, 53.3% in 2006 and 7.2% in 2007 (Further analysis of the Group's US non-agency RMBS is available in Note 4.1 to the Financial Statements).

* The vintage analysis of US non-agency RMBS was based on their year of first issue.

In respect of the Group's total exposure in debt securities issued by banks and other financial institutions, the Group maintained a diversified portfolio in terms of names and geography. The following table presents an analysis of these securities as at 31 December 2008 by related issuers' country of residence and by credit rating and credit risk characteristic, based on Moody's ratings or their equivalent to the respective issues of the debt securities, in terms of the proportion to the total exposure:

| % | United States | Australia | United Kingdom | European Union | Mainland China | Canada | Others | Total | Total** |
|---|---|---|---|---|---|---|---|---|---|
| Aaa | 0.7 | 1.6 | 1.8 | 6.6 | – | 2.1 | 3.8 | 16.6 | 18.9 |
| Aa1 to Aa3 | 6.9 | 12.0 | 7.3 | 11.1 | – | 3.0 | 8.2 | 48.5 | 60.1 |
| A1 to A3 | 5.3 | 0.4 | 0.5 | 1.6 | 3.9 | 0.1 | 2.7 | 14.5 | 17.6 |
| Lower than A3 | – | – | 0.2 | 0.5 | 0.3 | – | 0.1 | 1.1 | 1.1 |
| Unrated | – | 1.1 | 4.2 | 6.2 | 3.3 | 0.5 | 4.0 | 19.3 | 2.3 |
| Total | 12.9 | 15.1 | 14.0 | 26.0 | 7.5 | 5.7 | 18.8 | 100.0 | 100.0 |

** Including issuer rating distribution for debt securities with no issue rating.

### Growing traditional businesses while improving product manufacturing capabilities

The fluctuation of the currency and precious metal markets and the anticipated appreciation of the RMB created business opportunities for traditional treasury products in 2008. The Group grasped the opportunities to promote its traditional products and recorded robust growth in foreign exchange as well as commodity-related income. Meanwhile, the Group continued to improve its product manufacturing capabilities and introduce new treasury products to meet the diverse needs of customers. During the year, the Group further expanded its product offerings by launching its first equity-linked investment products under its own brand and introducing a number of new equity-linked notes and equity warrants. In view of the global financial turmoil, the Group acted promptly by conducting a comprehensive evaluation of all products under distribution and reviewed its internal regulations, risk control measures and compliance procedures. The Group also provided customers with up-to-date market information in order to safeguard their investments and at the same time delivered thematic training and services to front-line staff to respond to customers' enquiries.

**INSURANCE**

| HK$'m, except percentage amounts | **Full-year ended 31 December 2008** | Full-year ended 31 December 2007 | Increase/ (decrease) |
|---|---|---|---|
| Net interest income | **1,122** | 788 | +42.4% |
| Other operating income | **5,503** | 9,030 | -39.1% |
| Operating income | **6,625** | 9,818 | -32.5% |
| Net insurance benefits and claims | **(7,709)** | (9,440) | -18.3% |
| Net operating income | **(1,084)** | 378 | -386.8% |
| Operating expenses | **(147)** | (117) | +25.6% |
| (Loss)/Profit before taxation | **(1,231)** | 261 | -571.6% |

| | **At 31 December 2008** | At 31 December 2007 | Increase/ (decrease) |
|---|---|---|---|
| Segment assets | **31,703** | 24,545 | +29.2% |
| Segment liabilities | **30,977** | 23,182 | +33.6% |

Note: For additional segmental information, see Note 49 to the Financial Statements.

### Results

The Group's Insurance segment recorded a loss before taxation of HK$1,231 million in 2008 mainly due to the decline in other operating income caused by the weak performance of its investment assets and decrease in premium income. The decline was partly offset by the increase in net interest income and the fall in net insurance benefits and claims.

Net interest income rose by 42.4% mainly due to the growth of the investment in debt securities made by the premium income in 2008. Other operating income fell by 39.1% primarily due to the decline in net insurance premium income as sales contracted substantially and a net loss on its investment assets compared to a gain recorded in 2007. Net insurance benefits and claims were down 18.3% mainly due to the decline in net insurance premium income.

Operating expenses increased by 25.6% mainly because of higher staff costs after headcount increase.

Assets in the insurance segment grew by 29.2% because of the growth of debt securities investments and deposits with banks. Liabilities rose by 33.6% with increases in insurance contract liabilities and subordinated liabilities.

### Expanding product offerings and enhancing brand awareness

The Group continued to broaden its product range and create new products to meet the emerging needs of customers. New single-premium products such as the "Fortuitous Saving Protection Plan", "Pleasure 5-year Saving Protection Plan" and "5-Year Joyful Life Insurance Plan" were launched with good response. To keep up with the ever-changing market, a new life product targeting the SME segment was launched in the first half of the year. In July, the Group introduced the "Harvest Joy Protection Plan", a unique back-end charged investment-linked insurance plan. In addition to product innovation, large-scale promotional and marketing activities were rolled out during the first half of the year to help reinforce the brand's image and boost the sales of various regular-pay products. The premium income of regular-pay products was up 40.1% year-on-year while the Group's market share and market ranking in terms of total individual new business standard premium in 2008 went up over the same period last year.

### Focusing on further development of multi-channel platform

The development of a multi-channel platform remained the Group's focus in 2008. Following the establishment of BOC Life's telemarketing call centre in late 2007, a branch-based direct insurance specialist team was set up in the first half of 2008. The team specialised in analyzing the financial need of customers and in cross-selling life insurance products. A mobile sales team was launched in the fourth quarter to further expand the sales network. Contribution to new business sales from non-branch channels rose significantly in 2008.

## REGULATORY DEVELOPMENT

### Basel II Capital Accord

Basel II is an international capital adequacy framework introduced by the Basel Committee on Banking Supervision in 2004 to replace the 1988 Basel Accord. The new framework comprises 3 pillars which align regulatory capital requirements more closely with inherent risks and introduce new capital charge on operational risk. It also stipulates a framework for the supervisory review of capital adequacy by the regulatory authority and a greater scope of disclosure on capital adequacy and risk management. Since the introduction of Basel II by Hong Kong banks in 2007, the Group has adopted the Standardised Approach to calculate statutory minimum capital requirement on credit risk, market risk and operational risk under Pillar One. The Group intends to gradually adopt the Foundation Internal Ratings-Based ("FIRB") approach which is a more risk-sensitive approach on the calculation of the regulatory capital requirements. During 2008, the Group continues to devote substantial resources to the preparation for the implementation of Basel II. With the implementation of the Borrower Rating models and Facility Grading system for the Group's corporate banking business and Probability of Default, Exposure at Default and Loss Given Default models for the Group's personal banking business, together with their supporting system platforms, an electronic workflow system to support the automated credit application and approval process, and the Capital Adequacy Ratio calculation engine, the Group has established a solid foundation for the adoption of the FIRB approach. The core infrastructure required for the FIRB approach, including the related key models, system platforms, procedures and policies are all close to completion while the user acceptance test for the calculation of the regulatory capital requirement is in progress.

Under Pillar Two, the Group has implemented its internal capital adequacy assessment process ("ICAAP"). Using the statutory minimum capital adequacy ratio ("CAR") as a starting point, requirement for extra capital (capital add-on) needed to cover the risks not captured under Pillar One was assessed. Scorecard methodology has been used to evaluate the Group's risk profile in order to assess the capital add-on and determine the Group's minimum CAR. An Operating CAR Range has also been established which also considers the need for future business growth and efficiency of capital utilisation.

To comply with Pillar Three on the disclosure requirements prescribed by the Banking (Disclosure) Rules ("Disclosure Rules"), the Group has formulated its Financial Disclosure Policy, and the relevant disclosures made in 2008 were in accordance with the Disclosure Rules.

## RELATIONSHIP-PRODUCT-CHANNEL ("RPC") MODEL

Following the implementation of the Relationship-Product-Channel ("RPC") Model in March 2007, the Group has continued to reinforce its capabilities in customer relationship management, product management and channel management by adopting a more focused customer segmentation model, putting in place professional product management and servicing teams, and optimising channels and workflows. During the year, the Group made further progress in strengthening the model and ensure its effectiveness. This includes the filling of some vacant key positions or hiring of senior executives from other market-leading institutions and realignment of product management teams, formulating new sales programmes to target on the Group's corporate customers, enhancing internal management information system and business intelligence capabilities for Relationship Managers or frontline sales staff to better understand customers' needs and identify cross-selling opportunities, and further streamlining operation and procedures in branches to improve sales and servicing ratios and to reinforce marketing efforts.

## CORPORATE DEVELOPMENT, TECHNOLOGY AND OPERATIONS

### Human Resources

Despite the difficult business environment brought about by the financial crisis, the Group has continued to invest in human resources development for long-term business growth and the realisation of its vision and strategic goals. During the year, the Group reviewed and put forward its mid-term human resources strategies for 2008-2012 which will form the blueprint for the Group's human resources development to improve manpower structure and staff quality in the next few years. At the same time, the Group also refined its staff performance management system. Taken as a whole, these measures were meant to enhance the Group's manpower structure, staff quality and productivity.

In 2008, the Group continued to provide comprehensive training programmes for all levels of staff. EMBA programmes and executive development programmes conducted jointly with reputable universities such as Harvard University and Oxford University were organised for the senior management and selected staff. During the year, 2,400 internal training courses were organised with over 134,000 attendees. Training programmes were offered to frontline staff to help them acquire professional qualifications. Meanwhile, an e-learning platform is available as a supplementary channel to provide an easy and convenient way of staff training. Moreover, a three-year Management Trainee Programme and a one-year Officer Trainee Programme have also been in place since 2006.

### Technology and operations

In 2008, the Group continued to strengthen its information technology infrastructure under its 5-year IT development strategy. Several projects were completed during the year. The second phase of the new treasury platform revamp programme was implemented to support limit monitoring and strengthen position management. The Continuous Linked Settlement platform was established to enhance liquidity and risk management for foreign exchange transactions. The Credit and Facility Rating platform, an electronic credit workflow process, was launched to improve the credit approval efficiency. Both the cash management and custody platforms were enhanced to ensure higher operational efficiency and better service quality. Meanwhile, Phase 2 of the Operational Customer Relationship Management platform was launched to enhance overall customer relationship management. The new teller platform has been rolled out in most of the Group's local branches.

As part of the Group's long-term IT strategy, the Group initiated the Financial and Financial Risk Management System ("FRMS") in 2006 to revamp the existing computer systems for different finance functions, including financial accounting, management reporting, multi-dimension profitability analysis, capital management, and asset and liability management. Subsequent to the launch of the Asset Liability Management System in 2007, both the General Ledger and the Fund Transfer Pricing systems were successfully implemented in the fourth quarter of 2008.

## CREDIT RATINGS

| As at 31 December 2008 | Long-term | Short-term |
|---|---|---|
| Fitch | A | F1 |
| Moody's | Aa3 | P-1 |
| Standard & Poor's | A- | A-2 |

There has been no change in BOCHK's credit ratings since end-2007.

As at 31 December 2008, BOCHK's long-term and short-term foreign currency issuer default ratings assigned by Fitch Ratings were A and F1 respectively while the support rating was 2.

In respect of the ratings assigned by Moody's Investors Service, BOCHK's long-term and short-term local and foreign currency bank deposit ratings remained Aa3 and P-1 respectively. Financial Strength Rating was C+.

BOCHK's long-term and short-term counterparty credit ratings assigned by Standard & Poor's were A- and A-2 respectively. The Bank Fundamental Strength Rating was B.

## RISK MANAGEMENT

### *Banking Group*

#### Overview

The Group believes that sound risk management is crucial to the success of any organisation. In its daily operation, the Group attaches a high degree of importance to risk management and emphasises that a balance must be struck between risk control and business growth and development. The principal types of risk inherent in the Group's businesses are reputation risk, legal and compliance risk, strategic risk, credit risk, market risk, interest rate risk, liquidity risk and operational risk. The Group's risk management objective is to enhance shareholder value by maintaining risk exposures within acceptable limits.

#### Risk Management Governance Structure

The Group's risk management governance structure is designed to cover the whole process of all businesses and ensure that various risks are properly managed and controlled in the course of conducting business. The Group has a sound risk management organisational structure for implementing a comprehensive set of policies and procedures to identify, measure, monitor and control various risks that may arise. These risk management policies and procedures are regularly reviewed and modified to reflect changes in markets and business strategies. Various groups of risk takers assume their respective responsibilities for risk management.

The Board of Directors, representing the interests of shareholders, is the highest decision-making authority of the Group and has the ultimate responsibility for risk management. The Board, with the assistance of its committees, has the primary responsibility for formulating risk management strategies and ensuring that the Group has an effective risk management system to implement these strategies. The Risk Committee (RC), a standing committee established by the Board of Directors, is responsible for overseeing the Group's various types of risks, reviewing and approving high-level risk-related policies and overseeing their implementation, reviewing significant or high risk exposures or transactions and exercising its power of veto if it considers that any transaction should not proceed. The Audit Committee (AC) assists the Board in fulfilling its role in overseeing the internal control system.

The Chief Executive (CE) is responsible for managing the Group's various types of risks, approving detailed risk management policies, and approving material risk exposures or transactions within his authority delegated by the Board of Directors. The Chief Risk Officer (CRO) assists the CE in fulfilling his responsibilities in the day-to-day management of risks. The CRO is responsible for initiating new risk management strategies, projects and measures that will enable the Group to better monitor and manage new risk issues or areas that may arise from time to time from new businesses, products and changes in the operating environment. He may also take appropriate initiatives in response to regulatory changes. The CRO is also responsible for reviewing material risk exposures or transactions within his delegated authority and exercising his power of veto if he believes that any transaction should not proceed.

Various units of the Group have their respective risk management responsibilities. Business units act as the first line of defence while risk management units, which are independent from the business units, are responsible for the day-to-day management of different kinds of risks. Risk management units have the primary responsibilities for drafting, reviewing and updating various risk management policies and procedures.

The Group's principal banking subsidiaries, Nanyang, Nanyang (China) and Chiyu, are subject to risk policies that are consistent with those of the Group. These subsidiaries execute their risk management strategies independently and report to the Group's management on a regular basis.

#### Credit Risk Management

Credit risk is the risk that a customer or counterparty will be unable to or unwilling to meet its obligations under a contract. It arises principally from the lending, trade finance and treasury businesses, and covers inter-bank transactions as well as investments in bonds and securities. For details of the Group's Credit Risk Management, please refer to Note 4 to the Financial Statements in this Annual Report.

### Interest Rate Risk Management

The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are repricing risk, basis risk, yield curve risk and option risk. For details of the Group's Interest Rate Risk Management, please refer to Note 4 to the Financial Statements in this Annual Report.

### Market Risk Management

Market risk is the risk of loss that results from movements in market rates and prices. The Group's market risk in the trading book arises from customer-related business and proprietary trading. Trading positions are subject to daily mark-to-market valuation. The risk includes potential losses arising from a change in foreign exchange and interest rates as well as the prices of equities and commodities. The major market risk in the banking book arises from the Group's investment portfolio. The risk includes potential losses arising from changes in market parameters such as credit, liquidity, and interest rate risk. These positions are subject to monthly mark-to-market valuation.

Market risk management framework

Market risk is managed within various major risk limits approved by the RC, including risk positions and/or risk factor sensitivities. Since April 2007, BOCHK has also formally applied Value-at-Risk (VAR) limit as a daily risk management tool. These overall risk limits are divided into sub-limits by reference to different risk products, including interest rates, foreign exchange rates, commodities and equities. Transactions are classified into different risk product categories according to the prominent type of risk inherent in the transactions.

Market risk arising from the banking book is managed within various risk limits such as P/L Management Alert Limit (P/L MAL) and P/L Management Alert Trigger (P/L MAT) which are approved by Asset and Liability Management Committee (ALCO). The mark-to-market result is reported to ALCO on a monthly basis.

As aforesaid, the Group's risk management objective is to enhance shareholder value by maintaining risk exposures within acceptable limits. The Group's market risk management framework comprises three levels. The Board of Directors and its Risk Committee are the ultimate decision-making authorities. The formulation of risk management procedures and the implementation mechanism, and the monitoring of compliance are mainly the responsibility of the Group's senior management (including CE and CRO). The Risk Management Department (RMD) is responsible for overseeing the Group's market risk to ensure that overall and individual market risks are within the Group's risk tolerance. Risk exposures are monitored on a day-to-day basis to ensure that they are within the established risk limits and are regularly reported to the senior management. Nanyang and Chiyu have their own independent risk monitoring units to monitor limit compliance on a daily basis.

The Group controls market risk by restricting individual operations to trade only a list of permissible instruments authorised by senior management and within various market risk limits approved by RC. The individual operations are also required to enforce rigorous new product approval procedures to ensure that all risks that may arise are thoroughly identified, properly measured and adequately controlled.

The Group also uses the VAR technique to measure potential losses and market risks of its trading book for reporting to the RC and senior management on a periodic basis. VAR is a statistical technique which estimates the potential losses that could occur on risk positions taken over a specified time horizon within a given level of confidence. BOCHK, being the banking entity within the Group with the major trading positions, which are mainly foreign currency positions in major currencies, uses VAR technique to monitor and control market risk on a daily basis.

The Group has changed its VAR calculation from a variance/co-variance basis to a historical simulation basis with effect from April 2007. The Group uses historical movements in market rates and prices, a 99% confidence level and a 1-day holding period to calculate portfolio and individual VAR. Movements in market prices are calculated by reference to market data from the last two years.

**VAR**

The following table sets out the VAR for all trading market risk exposure[1] of BOCHK.

| HK$'m | | At 31 December | Minimum for the year | Maximum for the year | Average for the year |
|---|---|---|---|---|---|
| VAR for all market risk | – 2008 | 12.6 | 3.0 | 13.5 | 6.5 |
| | – 2007 | 3.2 | 1.4 | 10.4 | 4.1 |
| VAR for foreign exchange risk products | – 2008 | 13.1 | 2.5 | 14.2 | 6.0 |
| | – 2007 | 2.7 | 1.0 | 9.4 | 4.0 |
| VAR for interest rate risk products | – 2008 | 4.2 | 1.0 | 5.9 | 2.9 |
| | – 2007 | 1.5 | 0.5 | 3.9 | 1.6 |
| VAR for equity risk products | – 2008 | 0.2 | 0.1 | 2.8 | 0.5 |
| | – 2007 | 0.4 | 0.1 | 1.1 | 0.4 |
| VAR for commodity risk products | – 2008 | 0.0 | 0.0 | 0.5 | 0.0 |
| | – 2007 | 0.0 | 0.0 | 0.4 | 0.1 |

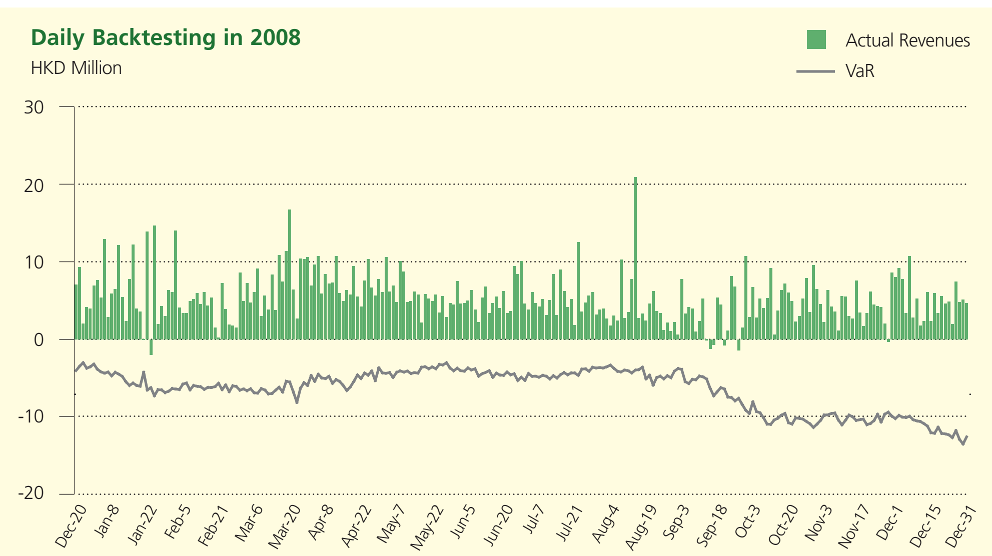
In 2008, the average daily revenue[2] of BOCHK earned from market risk-related trading activities was HK$5.35 million (2007: HK$3.06 million).

1 Structural FX positions have been excluded.

2 Revenues from structural FX positions and back-to-back transactions have been excluded.

The predictive power of the VAR measure is monitored by backtesting, which compares the calculated VAR figure of those trading positions of each business day with the actual revenues arising on those positions on the next business day. These actual revenues exclude non-trading income, including fees and commissions. If backtesting revenues are negative and exceeding the VAR, a "backtesting exception" is noted. Backtesting results are reported to the Group's senior management, including CE and CRO.

Generally speaking, the number of backtesting exceptions in a rolling 12-month period will not exceed four times, given a 99% confidence level. BOCHK conducts backtesting on a monthly basis and the graph below shows the backtesting result of the trading VAR of BOCHK.




There is no actual loss exceeding the VAR estimate for BOCHK in 2008.

Although a valuable guide to risk, VAR should always be viewed in the context of its limitations. For example:

- the use of historical data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;
- the use of a one-day holding period assumes that all positions can be liquidated or hedged in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day holding period may be insufficient to liquidate or hedge all positions fully;
- the use of a 99 per cent confidence level, by definition, does not take into account losses that might occur beyond this level of confidence; and
- VAR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

The Group recognises these limitations by augmenting its VAR limits with other position and sensitivity limit structures. Additionally, the Group applies a wide range of stress testing, both on individual portfolios and on the Group's consolidated positions. The stress testing programme of the trading book includes sensitivity testing on changes in risk factors with various degrees of severity, as well as scenario analysis on historical events including the 1987 Equity Market Crash, 1994 Bond Market Crash, the 1997 Asian Financial Crisis and the 11 September event in the United States in 2001. The Group also reassesses the stress testing programme to ensure its adequacy in view of the financial market crisis in 2008. The Group's stress-testing regime provides the senior management with an assessment of the financial impact of identified extreme events on the market risk exposures of the Group.

### Liquidity Risk Management

The aim of liquidity management is to enable the Group to meet, even under adverse market conditions, all its maturing repayment obligations on time, and to fund all its asset growth and strategic opportunities without forced liquidation of its assets at short notice.

The Group funds its operations principally by accepting deposits from retail and corporate depositors. In addition, the Group may issue certificates of deposit to secure long-term funds. Funding may also be secured through adjusting the asset mix in the Group's investment portfolio. The Group uses the majority of funds raised to extend loans, to purchase debt securities or to conduct interbank placements.

The Group monitors the liquidity risks using cash flow analysis (under normal condition and stress conditions respectively) and by examining deposit stability, concentration risk, mismatch ratios, loan-to-deposit ratio and liquidity profile of the investment portfolio. The primary objective of the Group's asset and liability management strategy is to achieve optimal returns while ensuring adequate levels of liquidity and capital within an effective risk control framework and ALCO is responsible for establishing these policy directives (including the liquidity contingency plan), and RC sanctions the liquidity management policies. The Treasury Department (TD) manages the liquidity risk according to the established policies. The Finance Department (FD) monitors the Group's liquidity risks and reports to ALCO regularly. RMD reviews the policies, guidelines and limits proposed by TD.

In 2008, the Group further enhanced its liquidity risk management process by putting in place more stringent stress testing requirements in view of the then prevailing market situation.

### Operational Risk Management

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events.

The Group has put in place an effective internal control process which requires the establishment of detailed policies and control procedures for all the key activities. Proper segregation of duties and authorisation is the fundamental principle followed by the Group. RMD formulates corporate-level policies and procedures concerning operational risk management which are approved by RC. The management of respective business lines is responsible for managing and reporting operational risks specific to their business units by applying the respective tools such as key risk indicators, self assessment and operational risk events reporting mechanism to identify, assess and control the risks inherent in their business processes, activities and products. These are followed by periodic monitoring and ongoing review of changes by RMD. Besides the current operational risk status, trends derived from historical data are served as alert on potential risks. RMD evaluates the operational risk profile, records operational risk data and reports operational risk issues to RC and the senior management. The Group also takes out insurance to mitigate unforeseeable operational risks.

Business continuity plans are in place to support business operations in the event of emergency or disaster. Adequate backup facilities are maintained and periodic drills are conducted.

### Reputation Risk Management

Reputation risk is the risk that negative publicity regarding the Group's business practices, whether genuine or not, will cause a potential decline in the customer base or lead to costly litigation or revenue erosion. Reputation risk is inherent in every aspect of business operation and covers a wide spectrum of issues.

In order to mitigate reputation risk, the Group has formulated and duly followed its Reputation Risk Management Policy. The policy aims to prevent and manage reputation risk proactively at an early stage when an incident occurs. The system entails continuous monitoring of external reputation risk incidents and published failures of risk incidents in the financial industry.

The recent Lehman Minibonds incident has had an adverse impact on the Group's reputation as there have been alleged cases of mis-selling. The Group is handling customer's complaints cautiously so as to minimise the reputation risk.

### Legal and Compliance Risk Management

Legal risk is the risk that unenforceable contracts, lawsuits or adverse judgments may disrupt or otherwise negatively affect the operation or financial condition of the Group. Compliance risk is the risk of legal or regulatory sanctions, financial loss, or loss to reputation a bank may suffer as a result of its failure to comply with all applicable laws and regulations. Legal and compliance risks are managed by the Legal and Compliance Department headed by a General Manager who reports to the Chief Risk Officer.

### Strategic Risk Management

Strategic risk generally refers to the risks that may induce immediate or future negative impact on the financial and market positions of the Group because of poor strategic decisions, improper implementation of strategies and lack of response to the market. The Board of Directors reviews and approves the policy for the management of strategic risks. Key strategic issues have to be fully evaluated and properly endorsed by the senior management and the Board.

The Group will regularly review its business strategies to cope with the latest market situation and developments.

### Capital Management

The major objective of capital management is to maximise shareholders' total return while maintaining a capital adequacy position commensurate with the Group's overall risk profile. The Group periodically reviews its capital structure and adjusts the capital mix where appropriate to achieve the targeted weighted average cost of capital. ALCO monitors the Group's capital adequacy. The Group complied with all the statutory capital standards for all the periods in 2008.

To comply with HKMA's requirements as stated in the Supervisory Policy Manual "Supervisory Review Process", the Group has implemented its internal capital adequacy assessment process (ICAAP). Using the statutory minimum capital adequacy ratio (CAR), 8%, as a starting point, extra capital (capital add-on) needed to cover the risks not captured under Pillar I was assessed. Scorecard methodology has been used to evaluate the Group's risk profile in order to assess the capital add-on and determine the minimum CAR. An Operating CAR Range has also been established which incorporates the need for future business growth and efficiency of capital utilisation.

In 2008, the Group took further measures to strengthen its capital position, including the borrowing of subordinated loans from the parent bank.

### Stress Testing

The Group supplements the analysis of various types of risks with stress testing. Stress testing is a risk management tool for estimating the Group's risk exposures under stressed conditions arising from extreme but plausible market or macroeconomic movements. These tests are conducted on a regular basis and ALCO monitors the results against limits approved by RC. Stress test results are also reported to the Board and RC regularly.

### *BOC Life Insurance*

The principal activity of BOC Life's business is the underwriting of long-term insurance business in life and annuity, linked long-term business and retirement scheme management in Hong Kong. Major types of risks arising from the BOC Life's insurance business are insurance risk and market risk. BOC Life manages these risks independently and reports to RC on a regular basis. The key risks of its insurance business and related risk control process are as follows:

### Insurance Risk Management

BOC Life is in the business of insuring against the risk of mortality, morbidity, disability, critical illness, accidents and related risks. BOC Life manages these risks through the application of its underwriting policies and reinsurance arrangement.

The underwriting strategy is intended to set premium pricing at an appropriate level that corresponds with the underlying exposure of the risks underwritten. Screening processes, such as the review of health condition and family medical history, are also included in BOC Life's underwriting procedures.

Within the insurance process, concentrations of risk may arise where a particular event or series of events could impact heavily upon BOC Life's liabilities. Such concentrations may arise from a single insurance contract or through a small number of related contracts, and relate to circumstances where significant liabilities could arise.

For the in-force insurance contracts, most of the underlying insurance liabilities are related to endowment and unit-linked insurance products. For most of the insurance policies issued by it, BOC Life has a retention limit on any single life insured. BOC Life reinsures the excess of the insured benefit over the limit for standard risks (from a medical point of view) under an excess of loss reinsurance arrangement. BOC Life does not have in place any reinsurance for contracts that insure against survival risk.

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 and persistency. In order to assess the uncertainty due to the mortality assumption and lapse assumption, BOC Life conducts mortality study and lapse study in order to determine the appropriate assumptions. In these studies, consistent results are reflected in both assumptions with appropriate margins.

### Market Risk Management

**(i) Interest Rate Risk Management**

An increase in interest rates may result in the depreciation of the value of the bond portfolio. It may also result in customers accelerating surrenders. A decrease in interest rates may result in an inability to adequately match guarantees or lower returns leading to customer dissatisfaction. BOC Life manages the asset liability matching of its portfolios within an asset liability management (ALM) framework, that has been developed to achieve investment returns that match its obligations under insurance contracts.

**(ii) Liquidity Risk Management**

Liquidity risk is the risk of not being able to meet obligations as they fall due without incurring unacceptable loss. BOC Life's asset liability matching framework includes cashflow management in a bid to preserve liquidity to match policy payout from time to time. In the normal course of BOC Life's business, new business premiums generate constant cash inflows and as a result, the portfolios also grow gradually to meet future liquidity requirement.

**(iii) Credit Risk Management**

BOC Life has exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Key areas to which BOC Life's insurance business is exposed include:

- Default risk of bond issuers or the counterparties of structured products
- Credit spread widening as a result of credit migration (downgrade)
- reinsurers' share of insurance unpaid liabilities
- amounts due from re-insurers in respect of claims already paid
- amount due from insurance contract holders
- amount due from insurance intermediaries

BOC Life manages credit risk by placing limits on its exposure to each investment counterparty or group of counterparties. Such limits are subject to annual or more frequent review by the management.

In order to enhance the credit risk management, BOC Life has strengthened its communication with the Treasury Department of the Group and closely monitors and updates the established Disposal and Watch Lists to ensure consistency with the Group's credit risk management and investment strategy.

# 茁長

# Growth

# CORPORATE INFORMATION

## BOARD OF DIRECTORS

*Chairman*
**XIAO Gang**#

*Vice Chairmen*
**SUN Changji**#
**HE Guangbei**

*Directors*
**LI Zaohang**#
**ZHOU Zaiqun**#
**ZHANG Yanling**#
**LEE Raymond Wing Hung**
**GAO Yingxin**
**FUNG Victor Kwok King***
**KOH Beng Seng***
**SHAN Weijian***
**TUNG Chee Chen***
**TUNG Savio Wai-Hok***
**YANG Linda Tsao***

# Non-executive Directors
* Independent Non-executive Directors

## SENIOR MANAGEMENT

*Chief Executive*
**HE Guangbei**

*Deputy Chief Executive*
**LAM Yim Nam**

*Chief Financial Officer*
**LEE Raymond Wing Hung**

*Deputy Chief Executive*
**GAO Yingxin**

*Chief Risk Officer*
**CHEUNG Yau Shing**

*Deputy Chief Executive*
**WONG David See Hong**

*Company Secretary*
**YEUNG Jason Chi Wai**

## REGISTERED OFFICE

52nd Floor
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Hong Kong

## AUDITORS

PricewaterhouseCoopers

## SHARE REGISTRAR

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Hopewell Centre
183 Queen's Road East
Hong Kong

## ADS DEPOSITARY BANK

Citibank, N.A.
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14th Floor
New York, NY 10013
United States of America

## WEBSITE

www.bochk.com

# BOARD OF DIRECTORS AND SENIOR MANAGEMENT

*Mr. XIAO Gang*

*Mr. SUN Changji*

*Mr. HE Guangbei*

*Mr. LI Zaohang*

*Mr. ZHOU Zaiqun*

## Directors

**Mr. XIAO Gang**
*Chairman*

Aged 50, is Chairman of the Board of Directors and prior to March 2006, was Chairman of the Risk Committee of the Company and BOCHK. He is also a director of BOC (BVI) and BOCHKG. Mr. Xiao was Chairman and President of BOC from March 2003 to August 2004 and has been Chairman of BOC since its restructuring in August 2004. Prior to joining BOC, Mr. Xiao joined People's Bank of China ("PBOC") in 1981 and had served various positions in PBOC, including Director of the Research Bureau, Head of the China Foreign Exchange Trading Center, Director of the Planning and Treasury Department, Assistant Governor and Director of the Monetary Policy Department, Assistant Governor and President of Guangdong Branch of PBOC and Director of the Guangdong Branch of the State Administration of Foreign Exchange. Mr. Xiao served as Deputy Governor of PBOC from 1998 to 2003. He was also Chairman of China Association of Banks from June 2003 to December 2004. Mr. Xiao graduated from Renmin University of China with a master's degree in Law.

**Mr. SUN Changji**
*Vice Chairman*

Aged 66, is Vice Chairman of the Board of Directors and Chairman of the Nomination and Remuneration Committee of the Company and BOCHK. He is also a director of BOC (BVI) and BOCHKG. Mr. Sun was Vice Chairman of BOC from 2000 to 2004 and Executive Vice President of BOC from 1999 to 2004. He was concurrently the President of China Orient Asset Management Corporation from 1999 to 2001. In 2003, Mr. Sun was elected as a member of the Tenth National Committee of the Chinese People's Political Consultative Conference. Mr. Sun is a senior engineer (professor). He was the First Deputy Director-General of the State Administration of Machinery Industry of the PRC from 1998 to 1999 and Vice Minister of the Ministry of Machinery Industry of the PRC from 1993 to 1998. Prior to that, he was a Deputy Director-General of the Production Department of the Ministry of Machinery Industry from 1991 to 1993. Mr. Sun graduated from Tsinghua University in 1966 with a bachelor's degree.

**Mr. HE Guangbei**
*Vice Chairman and Chief Executive*

Aged 54, is Vice Chairman and Chief Executive with overall responsibility for the business and operations of BOCHK and a member of the Strategy and Budget Committee of the Company and BOCHK. He is also Chairman of Nanyang, Nanyang (China), Chiyu and BOC Life, Vice Chairman of Hong Kong General Chamber of Commerce, and director of Hong Kong Interbank Clearing Limited, HKICL Services Limited and Hong Kong Note Printing Limited. He is the designated representative of BOCHK to the Hong Kong Association of Banks where he served as the presiding Chairman in 2008. He holds various public positions which include member of the HKMA Exchange Fund Advisory Committee and Banking Advisory Committee, member of the Hong Kong Government Commission on Strategic Development, Board member of Hong Kong Airport Authority, Honorary President of the Hong Kong Chinese Enterprises Association and general committee member of the Hong Kong General Chamber of Commerce. Mr. He joined BOC in 1980 and since then, he had assumed various positions at BOC and had been posted to its New York Branch and Paris Branch. He was Managing Director of BOC from 1999 to 2004 and Executive Vice President from 2000 to 2003. Mr. He graduated from the Beijing Second Foreign Languages Institute in 1979 with a bachelor's degree and obtained a master's degree in international management studies from the University of Texas at Dallas in 1985.

**Mr. LI Zaohang**
*Non-executive Director*

Aged 53, is a Non-executive Director and a member of the Nomination and Remuneration Committee of the Company and BOCHK. He joined China Construction Bank ("CCB") in 1980 and had held various positions including Manager, Branch Manager, General Managers of various departments at CCB's Head Office and Executive Vice President. In 2000, Mr. Li joined BOC as Executive Vice President and has served as Managing Director and Executive Director successively. Mr. Li graduated from Nanjing University of Information Science and Technology.

**Mr. ZHOU Zaiqun**
*Non-executive Director*

Aged 56, is a Non-executive Director and a member of the Audit Committee and Strategy and Budget Committee of the Company and BOCHK. He is also Chairman of BOC-CC. Mr. Zhou is currently an Executive Director and Executive Vice President of BOC. He was a Managing Director of BOC from 2000 to 2004. He has over 20 years' experience in the banking industry. He was General Manager of the Industrial and Commercial Bank of China ("ICBC"), Beijing Branch from 1999 to 2000 and General Manager of the Planning and Financial Department of ICBC from 1997 to 1999. Mr. Zhou obtained a master's degree from Dongbei University of Finance and Economics in 1997.

Mdm. ZHANG Yanling

Mr. LEE Raymond Wing Hung

Mr. GAO Yingxin

Dr. FUNG Victor Kwok King

## Directors

**Mdm. ZHANG Yanling**
*Non-executive Director*

Aged 57, is a Non-executive Director and a member of the Risk Committee of the Company and BOCHK. She is also Executive Vice President of BOC, Chairman of Bank of China (UK) Limited and Vice Chairman of BOCI. Mdm. Zhang has been Vice Chairman of ICC Commission on Banking Technique and Practice since 2003. Mdm. Zhang joined BOC in 1977. She was Executive Assistant President of BOC from 2000 to 2002. Mdm. Zhang was General Manager of BOC, Milan Branch from 2000 to 2001 and General Manager of the Legal Department of BOC from 2001 to 2002. She was Deputy General Manager of the Training Department of BOC from 1992 to 1997, General Manager of the Banking Department from 1997 to 2000 and Managing Director of BOC from 2000 to 2004. She graduated from Liaoning University in 1977 with a bachelor's degree and obtained a master's degree from Wuhan University in 1999.

**Mr. LEE Raymond Wing Hung**
*Executive Director and*
*Chief Financial Officer*

Aged 59, is an Executive Director of the Company and the Bank as well as the Chief Financial Officer of the Group. He is also a director of Nanyang, Nanyang (China), BOC-CC and BOC Life. Mr. Lee is a fellow of the Association of Chartered Certified Accountants and an associate of the Hong Kong Institute of Certified Public Accountants. He has over 30 years' of extensive international banking experience acquired both locally and overseas. Prior to joining the Group, Mr. Lee was a Director, Alternate Chief Executive and Managing Director of CITIC International Financial Holdings Limited from 2002 to 2003, and was a Director and Chief Executive of the Hong Kong Chinese Bank from 1999 to 2002. He was seconded by the Bank of New York in 1992 to serve as a Director and Alternate Chief Executive of Wing Hang Bank and had remained in that capacity until 1999. While serving in Wing Hang, Mr. Lee was concurrently a Senior Vice President and Managing Director of the Bank of New York, where he had served in different capacities in New York and Toronto since 1982. Prior to 1982, he had worked for Bank of America for 8 years in various positions in different Asian and North American cities.

**Mr. GAO Yingxin**
*Executive Director and*
*Deputy Chief Executive*

Aged 46, is an Executive Director of the Company and the Bank as well as the Deputy Chief Executive in charge of Corporate Banking and Financial Institutions. He is also Vice Chairman of Nanyang (China) and director of Nanyang and BOC Insurance. Before joining BOCHK, he was President and Chief Operating Officer of BOCI. Mr. Gao joined the BOC Group in 1986 where he began working on financing projects for various industries at BOC's Head Office in Beijing. In 1999, he became General Manager of Corporate Banking at BOC Head Office where he was responsible for managing and building BOC Group's customer relationships with and global financing for multinational corporations and premium domestic clients in the mainland of China. He was also in charge of BOC's major financing projects. From 1995 to 1996, he worked for the Finance Department of Northern Telecom (Nortel) Head Office in Canada. Mr. Gao graduated from the East China University of Science and Technology in Shanghai with a master's degree in engineering in 1986.

**Dr. FUNG Victor Kwok King**
*Independent Non-executive Director*

Aged 63, is an Independent Non-executive Director and a member of the Audit Committee and Nomination and Remuneration Committee of the Company and BOCHK. Dr. Fung holds Bachelor and Master Degrees in Electrical Engineering from the Massachusetts Institute of Technology and a Doctorate in Business Economics from Harvard University. He is Group Chairman of Li & Fung (1937) Limited and publicly listed Li & Fung group companies including Li & Fung Limited, Integrated Distribution Services Group Limited and Convenience Retail Asia Limited. He is also an Independent Non-executive Director of Orient Overseas (International) Limited, CapitaLand Limited in Singapore and Baosteel Group Corporation in the PRC, and a Non-executive Director of Hup Soon Global Corporation Limited in Singapore. In public service, Dr. Fung is Chairman of International Chamber of Commerce. He is a member of the Chinese People's Political Consultative Conference and a member of the Executive Committee of the Commission on Strategic Development of the Hong Kong Government. Dr. Fung is also Chairman of the Hong Kong University Council, the Greater Pearl River Delta Business Council and the Hong Kong – Japan Business Cooperation Committee. From 1991 to 2000, he was Chairman of the Hong Kong Trade Development Council and from 1996 to 2003, he was the Hong Kong representative on the APEC Business Advisory Council. He was also Chairman of the Hong Kong Airport Authority from June 1999 to May 2008. In 2003, the Government awarded Dr. Fung the Gold Bauhinia Star for distinguished services to the community.

*Mr. KOH Beng Seng*

*Mr. SHAN Weijian*

*Mr. TUNG Chee Chen*

*Mr. TUNG Savio Wai-Hok*

## Directors

**Mr. KOH Beng Seng**
*Independent Non-executive Director*

Aged 58, is an Independent Non-executive Director, Chairman of Risk Committee and a member of the Audit Committee of the Company and BOCHK. Mr. Koh is currently the Chief Executive Officer of Octagon Advisors Pte Ltd, a business and management consulting company based in Singapore. He is also an independent non-executive director of three Singaporean listed companies, namely, Singapore Technologies Engineering Ltd and Fraser and Neave Limited and Great Eastern Holdings Limited, director of Sing-Han International Financial Services Limited and director of Japan Wealth Management Securities Company Limited. Mr. Koh was deputy president of United Overseas Bank ("UOB") and a member of UOB's Executive Committee from 2000 to 2004. During this period, he was in charge of UOB's operations, delivery channels, information technology, corporate services, and risk management and compliance functions and played a key role in driving the successful integration of Overseas Union Bank and UOB in 2001. Prior to that, Mr. Koh has spent over 24 years at the Monetary Authority of Singapore where he made significant contributions to the development and supervision of the Singapore financial sector in his capacity as Deputy Managing Director, Banking & Financial Institutions Group. He has also served as a director of Chartered Semiconductor Manufacturing and as a part-time adviser to the International Monetary Fund. Mr. Koh holds a Bachelor of Commerce degree from Nanyang University in Singapore and a Master of Business Administration degree from Columbia University of the USA.

**Mr. SHAN Weijian**
*Independent Non-executive Director*

Aged 55, is an Independent Non-executive Director, Chairman of the Audit Committee and a member of the Nomination and Remuneration Committee of the Company and BOCHK. Mr. Shan is currently a Partner of TPG Capital and director of a number of companies, including Shenzhen Development Bank Co., Ltd., TCC International Holdings Limited, Changhwa Commercial Bank, Ltd., Taiwan Cement Corporation and Taishin Financial Holdings Co., Ltd. He was a Managing Director of JP Morgan, a director of Korea First Bank, an assistant professor at the Wharton School of the University of Pennsylvania and an Investment Officer at the World Bank in Washington DC. Mr. Shan graduated from the Beijing Institute of Foreign Trade with a major in English in 1979. He obtained a master's degree in business administration from the University of San Francisco in 1981, and received a Master of Arts degree in economics and a PhD degree in business administration from the University of California at Berkeley in 1984 and 1987 respectively.

**Mr. TUNG Chee Chen**
*Independent Non-executive Director*

Aged 66, is an Independent Non-executive Director and a member of the Audit Committee and Nomination and Remuneration Committee of the Company and BOCHK. Mr. Tung is also the Chairman and Chief Executive Officer of Orient Overseas (International) Limited. He is an Independent Non-executive Director of a number of listed companies, including Zhejiang Expressway Company Limited, PetroChina Company Limited, Wing Hang Bank Limited, U-Ming Marine Transport Corp., Sing Tao News Corporation Limited and Cathay Pacific Airways Limited. Mr. Tung was educated at the University of Liverpool, United Kingdom, where he obtained a bachelor's degree in science in 1964. He later obtained a master's degree in mechanical engineering from the Massachusetts Institute of Technology in 1966.

**Mr. TUNG Savio Wai-Hok**
*Independent Non-executive Director*

Aged 57, is an Independent Non-executive Director and a member of the Audit Committee, Risk Committee and Strategy and Budget Committee of the Company and BOCHK. Mr. Tung is one of the founding partners of Investcorp, where he was a Managing Director and Head of the Technology Investment Group until February 2009. He remains an advisor and Chairman of the Technology Investment Committee. Before joining Investcorp in 1984, he worked for Chase Manhattan Bank for about 11 years, holding various positions in its front, middle and back offices and served in its offices in New York, Bahrain, Abu Dhabi and London. Mr. Tung had served on the boards of many of Investcorp portfolio companies, including Club Car, Circle K, Saks Fifth Avenue, Simmons Mattresses, Star Market, and Stratus Computer. He is currently the Chairman of Wireless Telecom Group. He is also a board member and treasurer of the Aaron Diamond AIDS Research Center, an affiliate of Rockefeller University and a board member of the Committee of 100. Mr. Tung holds a BSc in Chemical Engineering from Columbia University of New York. He is a trustee of Columbia University. He is also on the board of the Columbia Investment Management Company and chairs the Finance Committee of Columbia University and is a member of the Columbia University Medical Center ("Health Science") Committee.


Mdm. YANG Linda Tsao


Mr. LAM Yim Nam


Mr. CHEUNG Yau Shing


Mr. WONG David See Hong


Mr. YEUNG Jason Chi Wai

## Directors

**Mdm. YANG Linda Tsao**
*Independent Non-executive Director*

Aged 82, is an Independent Non-executive Director of the Company and BOCHK. She is the founding chair of the Strategy and Budget Committee and a member of the Audit Committee and Nomination and Remuneration Committee of the Company and BOCHK. Since 2000, Mdm. Yang has chaired the Asian Corporate Governance Association (ACGA), a non-profit, member-supported organization based in Hong Kong. ACGA is committed to promoting sound corporate governance practices among Asian business enterprises through education, research, and advocacy. She serves on the Advisory Board of The Pacific Pension Institute and trustee of The Asia Foundation in San Francisco. The foundation has 17 field offices in Asia. Appointed by President Clinton as Ambassador and Executive Director to the Asian Development Bank (ADB) in 1993, Mdm. Yang was the first Asian and first woman appointed by the U.S. Government to serve on the board of multilateral financial institution. At her retirement in December 1999, the then U.S. Secretary of the Treasury Dr. Larry Summers presented her with the Distinguished Service Award of the Treasury Department for her contribution in shaping assistance program to affected countries during the Asian Financial Crisis 1997 – 1998 and to improving the bank's operations and private sector development strategy. Before that, she was California's Savings and Loan Commissioner and Vice President of the Board of Administration of the Public Employees' Retirement System of the State of California (CalPERS) and Vice Chairman of its Investment Committee. Mdm. Yang graduated from St. John's University in Shanghai and earned her Master of Philosophy degree (Economics) from Columbia University in New York.

## Senior Management

**Mr. LAM Yim Nam**
*Deputy Chief Executive*

Aged 56, is the Deputy Chief Executive in charge of Personal Banking and Product Management, Channel Management and BOC-CC. He is also a Director of BOC-CC and BOC Life. Mr. Lam has over 25 years' experience in the banking industry. From 1989 to 1998, he was Deputy General Manager of the Kwangtung Provincial Bank, Hong Kong Branch. Mr. Lam was Deputy General Manager of BOC, Hong Kong Branch from 1998 to 1999, and Acting General Manager of the National Commercial Bank, Hong Kong Branch from 2000 to 2001. Mr. Lam graduated from the Chinese University of Hong Kong with a bachelor's degree and a master's degree in business administration.

**Mr. CHEUNG Yau Shing**
*Chief Risk Officer*

Aged 47, is the Chief Risk Officer of the Group in charge of the Group's overall risk management function, overseeing BOCHK's Risk Management Department and Legal and Compliance Department. He is also a Director of Nanyang and Nanyang (China). Mr. Cheung has more than 20 years of experience in banking and accounting. Before joining BOCHK, he had worked for Hang Seng Bank for more than 9 years, during which he had assumed various positions including Assistant General Manager and Chief Credit Officer, Head of Credit Risk Management Department and Head of Audit Department. Before joining Hang Seng Bank, he was Vice President and Audit Manager of Chase Manhattan Bank. He had also served the Hong Kong Government and KPMG as Audit Examiner and Accountant respectively. Mr. Cheung graduated from the University of Hong Kong in 1984 with a Bachelor of Social Sciences Degree in Economics and Management Studies. He is a fellow of the Chartered Association of Certified Accountants and a Certified Public Accountant of the Hong Kong Institute of Certified Public Accountants.

**Mr. WONG David See Hong**
*Deputy Chief Executive*

Aged 55, is the Deputy Chief Executive of the Group with the overall responsibility for the financial market businesses which include Global Markets, Cash Management, Custody, Investment and Insurance, and other capital market related business lines. Prior to joining the Group, Mr. Wong was Corporate Executive Vice President and Country Executive of ABN AMRO Bank and was responsible for ABN AMRO Bank's operations in South East Asia. He joined ABN AMRO Bank in 1995 and has held various senior positions within ABN AMRO Bank including Regional Head of Financial Markets, Country Executive in Singapore, and Managing Director of the Hong Kong Branch. Mr. Wong has spent the last 25 years in the banking sector and has extensive knowledge and experience in treasury and financial products. Mr. Wong currently serves as the Board Members of Energy Market Authority and Civil Service College in Singapore. Mr. Wong graduated from the University of Singapore with a Bachelor's Degree in Business Administration and was awarded a Master's Degree in Science in Investment Management by the Hong Kong University of Science and Technology.

**Mr. YEUNG Jason Chi Wai**
*Board Secretary and Company Secretary*

Aged 54, is the Board Secretary and Company Secretary of the Company and BOCHK. Mr. Yeung has over 10 years' experience practising corporate and commercial law. Prior to joining the BOC Group in 2001, Mr. Yeung was General Counsel and director of China Everbright Limited and a partner of Woo, Kwan, Lee & Lo. He has also served at the Securities and Futures Commission in Hong Kong. Mr. Yeung was educated at the University of Hong Kong where he obtained a bachelor's degree in social sciences. Mr. Yeung later graduated from The College of Law, United Kingdom and further obtained a bachelor's degree in law from the University of Western Ontario, Canada and a master's degree in business administration from the Richard Ivey School of Business of the University of Western Ontario, Canada.

# REPORT OF THE DIRECTORS

The Directors are pleased to present their report together with the audited consolidated financial statements of the Company and its subsidiaries for the year ended 31 December 2008.

### Principal Activities

The principal activities of the Group are the provision of banking and related financial services. An analysis of the Group's performance for the year by business segments is set out in Note 49 to the financial statements.

### Results and Appropriations

The results of the Group for the year are set out in the consolidated income statement on page 94.

The Board has recommended keeping sufficient funds for operation in the future and does not propose any final dividend for the year ended 31 December 2008. With the interim dividend per share of HK$0.438 paid during 2008, the total dividend per share amounted to HK$0.438 for the whole year.

### Closure of Register of Members

The Register of Members of the Company will be closed from Friday, 15 May 2009 to Thursday, 21 May 2009 (both days inclusive), during which period no transfer of shares will be registered. In order to qualify for attending the forthcoming annual general meeting, all transfer documents, accompanied by the relevant share certificates, must be lodged with the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong, not later than 4:30 p.m. on Thursday, 14 May 2009.

### Reserves

Details of movements in the reserves of the Group are set out in the consolidated statement of changes in equity on pages 97 to 98.

### Donations

Charitable and other donations made by the Group during the year amounted to approximately HK$21 million.

### Properties, Plant and Equipment

Details of movements in properties, plant and equipment of the Group are set out in Note 32 to the financial statements.

### Share Capital

Details of the share capital of the Company are set out in Note 42 to the financial statements.

As at the latest practicable date prior to the issue of this Annual Report and based on publicly available information, the public float of the Company was approximately 34%. The Directors consider that there is sufficient public float in the shares of the Company.

### Distributable Reserves

Distributable reserves of the Company as at 31 December 2008, calculated under section 79B of the Hong Kong Companies Ordinance, amounted to approximately HK$2,747 million.

### Five-year Financial Summary

A summary of the results, assets and liabilities of the Group for the last five years is set out on page 3.

### Directors

The present Directors of the Company are set out on page 54. The biographical details of the Directors and senior management are set out on pages 55 to 58 of this Annual Report. The term of office for each Non-executive Director is approximately three years.

Mr. Lee Raymond Wing Hung will retire as an Executive Director and the Chief Financial Officer of the Group with effect from 1 June 2009 as announced by the Company on 6 February 2009.

In accordance with Article 98 of the Company's Articles of Association, at each annual general meeting, one-third of the Directors or the nearest number to but not less than one-third of the Directors shall retire from office by rotation and be eligible for re-election. Accordingly, Messrs. Xiao Gang, Li Zaohang, Zhou Zaiqun, Koh Beng Seng and Tung Savio Wai-Hok will retire by rotation at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

Each of the retiring Independent Non-executive Directors, namely, Mr. Koh Beng Seng and Mr. Tung Savio Wai-Hok, has given an annual confirmation of his independence to the Company. Based on such confirmation and the information available to the Board, and by reference to the "Policy on Independence of Directors" adopted by the Board which sets out more stringent independence criteria than those contained in the Listing Rules, the Board considers that Mr. Koh and Mr. Tung are independent. Further, in view of their extensive knowledge and experience, the Board believes that their re-election is in the best interests of the Company and the shareholders as a whole.

## Directors' Service Contracts

No Director offering for re-election at the forthcoming annual general meeting has a service contract with the Company or any of its subsidiaries which is not determinable by the employing company within one year without payment of compensation other than the normal statutory compensation.

## Directors' Interests in Contracts of Significance

No contracts of significance, in relation to the Group's business to which the Company, its holding companies, or any of its subsidiaries or fellow subsidiaries was a party and in which a Director had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

## Directors' Interests in Competing Business

Messrs. Xiao Gang, Li Zaohang and Zhou Zaiqun are executive directors of BOC. Mdm. Zhang Yanling is a member of the senior management of BOC.

BOC is a joint stock limited liability commercial bank in the Mainland of China providing a full range of commercial banking and other financial services through its associates throughout the world. Certain of the Group's operations overlap with and/or are complementary to those of BOC and its associates. To the extent that BOC or its associates compete with the Group, the Directors believe that the Group's interests are adequately protected by good corporate governance practices and the involvement of the Independent Non-executive Directors.

Further, the Board's mandate also expressly provides that unless permissible under applicable laws or regulations, if a substantial shareholder or a Director has a conflict of interest in the matter to be considered by the Board, the matter shall not be dealt with by way of written resolutions, but a Board meeting attended by Independent Non-executive Directors who have no material interest in the matter shall be held to deliberate on the same.

Save as disclosed above, none of the Directors is interested in any business apart from the Group's business, which competes or is likely to compete, either directly or indirectly, with the Group's business.

## Directors' Rights to Acquire Shares

On 5 July 2002, the following Directors were granted options by BOC (BVI), the immediate holding company of the Company, pursuant to a Pre-Listing Share Option Scheme to purchase from BOC (BVI) existing issued shares of the Company at a price of HK$8.50 per share. These options have a vesting period of four years from 25 July 2002 with a valid exercise period of ten years.

Particulars of the outstanding options granted to the Directors under the Pre-Listing Share Option Scheme as at 31 December 2008 are set out below:

| | | | | Number of share options | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Name of Director | Date of grant | Exercise price (HK$) | Exercisable period | Granted on 5 July 2002 | Balances as at 1 January 2008 | Exercised during the year | Surrendered during the year | Lapsed during the year | Balances as at 31 December 2008 |
| SUN Changji | 5 July 2002 | 8.50 | 25 July 2003 to 4 July 2012 | 1,590,600 | 1,590,600 | – | – | – | 1,590,600 |
| HE Guangbei | 5 July 2002 | 8.50 | 25 July 2003 to 4 July 2012 | 1,446,000 | 723,000 | – | – | – | 723,000 |
| LI Zaohang | 5 July 2002 | 8.50 | 25 July 2003 to 4 July 2012 | 1,446,000 | 1,446,000 | – | – | – | 1,446,000 |
| ZHOU Zaiqun | 5 July 2002 | 8.50 | 25 July 2003 to 4 July 2012 | 1,446,000 | 1,446,000 | 361,500 | – | – | 1,084,500 |
| ZHANG Yanling | 5 July 2002 | 8.50 | 25 July 2003 to 4 July 2012 | 1,446,000 | 1,446,000 | – | – | – | 1,446,000 |
| Total | | | | 7,374,600 | 6,651,600 | 361,500 | – | – | 6,290,100 |

Save as disclosed above, at no time during the year was the Company, its holding companies, or any of its subsidiaries or fellow subsidiaries a party to any arrangements to enable the Directors to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate.

## Directors' and Chief Executive's Interests in Shares, Underlying Shares and Debentures

As at 31 December 2008, the Directors, the Chief Executive and their respective associates had the following interests in the shares and underlying shares of the Company, as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers:

| | Number of shares/underlying shares held | | | | | |
|---|---|---|---|---|---|---|
| Name of Director | Personal interests | Family interests | Corporate interests | Other interests | Total | % of the issued share capital |
| SUN Changji | 1,590,600[1] | – | – | – | 1,590,600 | 0.015% |
| HE Guangbei | 723,000[1] | – | – | – | 723,000 | 0.007% |
| LI Zaohang | 1,446,000[1] | – | – | – | 1,446,000 | 0.014% |
| ZHOU Zaiqun | 1,085,000[2] | – | – | – | 1,085,000 | 0.010% |
| ZHANG Yanling | 1,446,000[1] | – | – | – | 1,446,000 | 0.014% |
| Total | 6,290,600 | – | – | – | 6,290,600 | 0.060% |

Notes:

1. Such interests represented the respective Directors' interests in underlying shares in respect of the share options granted to him/her pursuant to the Pre-Listing Share Option Scheme, details of which are set out in the section titled "Directors' Rights to Acquire Shares" above.

2. Such interests included Mr. Zhou's interests in 500 shares and interests in 1,084,500 underlying shares in respect of the share options granted to him pursuant to the Pre-Listing Share Option Scheme, details of which are set out in the section titled "Directors' Rights to Acquire Shares" above.

Save as disclosed above, as at 31 December 2008, none of the Directors or the Chief Executive of the Company or their respective associates had any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

## Substantial Interests in Share Capital

The register maintained by the Company pursuant to section 336 of the SFO recorded that, as at 31 December 2008, the following parties had the following interests (as defined in the SFO) in the Company set opposite their respective names:

| Name of Corporation | No. of shares of HK$5 each in the Company (% of total issued shares) | |
|---|---|---|
| Central SAFE | 6,953,617,435 | (65.77%) |
| BOC | 6,953,617,435 | (65.77%) |
| BOCHKG | 6,949,330,256 | (65.73%) |
| BOC (BVI) | 6,949,330,256 | (65.73%) |

Notes:

1. Following the reorganisation of BOC in August 2004, Central SAFE holds the controlling equity capital of BOC on behalf of the State. Accordingly, for the purpose of the SFO, Central SAFE is deemed to have the same interests in the Company as BOC.

2. BOC holds the entire issued share capital of BOCHKG, which in turn holds the entire issued share capital of BOC (BVI). Accordingly, BOC and BOCHKG are deemed to have the same interests in the Company as BOC (BVI) for the purpose of the SFO. BOC (BVI) beneficially held 6,949,330,256 shares of the Company.

3. The interest in the Company held by BOC included 4,000,000 shares held by BOC Insurance, a wholly-owned subsidiary of BOC, which had been disposed of by BOC Insurance during the reporting period.

4. BOC holds the entire issued share capital of BOCI, which in turn holds the entire issued share capital of BOCI Asia Limited and BOCI Financial Products Limited. Accordingly, BOC is deemed to have the same interests in the Company as BOCI Asia Limited and BOCI Financial Products Limited for the purpose of the SFO. BOCI Asia Limited had an interest in 91,500 shares of the Company and an interest in 117,000 shares held under physically settled equity derivatives while BOCI Financial Products Limited had an interest in 78,679 shares of the Company.

All the interests stated above represented long positions. Save as disclosed above, as at 31 December 2008, no other interests or short positions were recorded in the register maintained by the Company under section 336 of the SFO.

## Management Contracts

No contracts concerning the management or administration of the whole or any substantial part of the business of the Company were entered into or existed during the year.

## Share Options

Pursuant to written resolutions of all the Company's shareholders passed on 10 July 2002, the Company has approved and adopted two share option schemes, namely, the Share Option Scheme and the Sharesave Plan. No options have been granted by the Company pursuant to the Share Option Scheme or the Sharesave Plan during the year.

The following is a summary of the Share Option Scheme and the Sharesave Plan disclosed in accordance with the Listing Rules:

| | Share Option Scheme | Sharesave Plan |
|---|---|---|
| Purpose | To provide the participants with the opportunity to acquire proprietary interests in the Company, to attract and retain the best available personnel, to encourage and motivate the participants to work towards enhancing the value of the Company and its shares, to allow the participants to participate in the growth of the Company and to align the interests of the Company's shareholders with those of the participants. | To encourage broad-based employee ownership of the Company's shares, to increase employee awareness and participation in the Company's share price performance, to provide employees with an additional vehicle for asset accumulation and to align the interests of all employees with those of the Company's shareholders. |
| Participants | Subject to compliance with applicable laws, any full-time or part-time employee, executive or officer of the Group, executive or non-executive director of the Group, or full-time or part-time employee, executive, officer or director of BOC or any of its subsidiaries serving as a member of any committee of the Group. | Any employee, executive, officer or director of the Group, having such qualifying period of service (if any) as the Board may determine from time to time and not having been granted any options under the Share Option Scheme. |
| Total number of shares available for issue and percentage of issued share capital as at 31 December 2008 | The maximum number of shares in respect of which options may be granted under the Share Option Scheme, the Sharesave Plan and any other share option schemes and savings-based share option plans of any company in the Group (the "Other Schemes and Plans") shall not in aggregate exceed 10% of the shares in issue on 10 July 2002, that is, 1,057,278,026 shares. | Same as Share Option Scheme. |

| | Share Option Scheme | Sharesave Plan |
|---|---|---|
| Maximum entitlement of each participant | The total number of shares issued and to be issued upon the exercise of the options granted and to be granted to any one participant under the Share Option Scheme and the Other Schemes and Plans (including exercised, cancelled and outstanding options) in any twelve-month period up to and including the date of grant shall not exceed 1% of the shares in issue from time to time. | The maximum number of shares (rounded down to the next whole number) which can be paid for at the exercise price with monies equal to the aggregate of the savings contributions the participant has undertaken to make by the Maturity Date (defined as below) and interest which may be accrued thereon. Provided that the total number of shares issued and to be issued upon the exercise of the options granted and to be granted to any one participant under the Sharesave Plan and the Other Schemes and Plans (including exercised, cancelled and outstanding options) in any twelve-month period up to and including the date of grant shall not exceed 1% of the shares in issue from time to time. The amount of the monthly contribution to be made by a participant shall not be less than 1% and not more than 10% of the participant's monthly salary or such other maximum or minimum amounts as permitted by the Board. |
| Period within which the shares must be taken up under an option | Such period as shall be prescribed by the directors and specified in the letter of offer. | The thirty-day period (excluding the anniversary days) immediately after the first and second anniversary days from the date of grant or such other date as determined by the Board, or the thirty-day period immediately after the third anniversary of the date of grant or such other date as determined by the Board (the "Maturity Date"), or such other period(s) as may be determined by the Board. |

| | Share Option Scheme | Sharesave Plan |
|---|---|---|
| Minimum period for which an option must be held before it can be exercised | Such minimum period as shall be prescribed by the directors and specified in the letter of offer. | One year. |
| (a) Amount payable on acceptance of the option | (a) HK$1.00 | (a) HK$1.00 |
| (b) Period within which payments or calls must or may be made | (b) Payment or an undertaking to make payment on demand of the Company must be received by the Company within the period open for acceptance as set out in the letter of offer which shall not be less than 7 days after the offer date. | (b) Payment or an undertaking to make payment on demand of the Company must be received by the Company not later than the date specified in the letter of invitation as the directors may determine. |
| (c) The period within which loans for such purposes must be repaid | (c) Not applicable. | (c) Not applicable. |
| Basis of determining the exercise price | The exercise price is determined on the date of grant by the directors and shall not be less than the highest of:<br>(a) the nominal value of the Company's shares;<br>(b) the closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheet on the date of grant, which must be a business day; and<br>(c) the average closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheets for the five business days immediately preceding the date of grant. | Same as Share Option Scheme. |
| Remaining life | The Share Option Scheme shall remain in force for a period of ten years commencing on the first day of dealings in the Company's shares on the Stock Exchange which was 25 July 2002. | The Sharesave Plan shall remain in force for a period of ten years after the date of approval and adoption of the Sharesave Plan by the Company's shareholders which was 10 July 2002. |

Please refer to the section "Directors' Rights to Acquire Shares" for details of the options granted by BOC (BVI) over shares of the Company pursuant to the Pre-Listing Share Option Scheme.

## Purchase, Sale or Redemption of the Company's Shares

During the year, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares.

## Compliance with "Code on Corporate Governance Practices"

The Company is in full compliance with all the code provisions set out in the "Code on Corporate Governance Practices" contained in Appendix 14 of the Listing Rules and also complies with nearly all the recommended best practices set out in the said Code. For further details, please refer to the "Corporate Governance Report" contained in this Annual Report.

## Major Customers

During the year, the five largest customers of the group accounted for less than 30% of the total of interest income and other operating income of the Group.

## Connected Transactions

The Independent Non-executive Directors have reviewed the transactions which the Company disclosed in a public announcement on 2 January 2008 and confirmed that these transactions were:

(i) entered into in the ordinary and usual course of business of the Group;

(ii) conducted either on normal commercial terms or, if there were not sufficient comparable transactions to judge whether they were on normal commercial terms, were on terms that were fair and reasonable so far as the Company's shareholders are concerned;

(iii) entered into either in accordance with the terms of the agreements governing such transactions or (where there were no such agreements) on terms no less favourable than those available to or from independent third parties, as applicable; and

(iv) in each case where an annual cap had been set, that such cap was not exceeded.

In accordance with paragraph 14A.38 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, the Board of Directors engaged the auditors of the Company to perform certain factual finding procedures on the above continuing connected transactions on a sample basis in accordance with Hong Kong Standard on Related Services 4400 "Engagements to Perform Agreed-Upon Procedures Regarding Financial Information" issued by the Hong Kong Institute of Certified Public Accountants. The auditors have reported their factual findings on the selected samples based on the agreed procedures to the Board of Directors.

## Budgetary Discipline and Reporting

The annual budget of the Group is reviewed and approved by the Board of Directors prior to its implementation by the Management. Financial and business targets are allocated to business units and subsidiaries. There are defined procedures for the appraisal, review and approval of major capital and recurring expenditures. Proposed significant expenditures outside the approved budget will be referred to the Board or the relevant Board committee for decision. Financial performance against targets is reported to the Board regularly.

## Compliance with the Banking (Disclosure) Rules and the Listing Rules

The financial statements for the year ended 31 December 2008 comply with the requirements set out in the Banking (Disclosure) Rules under the Banking Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

## Auditors

The financial statements have been audited by PricewaterhouseCoopers. A resolution for their re-appointment as auditors for the ensuing year will be proposed at the forthcoming annual general meeting.

On behalf of the Board

**XIAO Gang**
*Chairman*

Hong Kong, 24 March 2009

# CORPORATE GOVERNANCE

The Company is **committed to maintaining and upholding good corporate governance** in order to protect the interests of shareholders, customers and staff. The Company abides strictly by the laws and regulations of the jurisdiction where it operates, and observes the guidelines and rules issued by regulatory authorities such as the Hong Kong Monetary Authority, the Hong Kong Securities and Futures Commission and the Stock Exchange of Hong Kong. The Company also keeps its corporate governance system under constant review to ensure that it is in line with international and local best practices.

The Company is **in full compliance with all the provisions of the Code on Corporate Governance Practices** (the Code) as appended to the Listing Rules of Hong Kong. It also **complies with nearly all the recommended best practices** set out in the Code. In particular, the Company **publishes quarterly financial and business reviews** so that shareholders can be better updated of the performance, financial position and prospects of the Company. BOCHK, the Company's wholly-owned and principal operating subsidiary, is in full compliance with the guideline in the Supervisory Policy Manual module CG-1 issued by the Hong Kong Monetary Authority and entitled "Corporate Governance of Locally Incorporated Authorised Institutions".

## Corporate Governance Framework

The **Board is at the core of the Company's corporate governance framework**, and there is **clear division of responsibilities between the Board and the Management**. The Board is responsible for providing high-level guidance and effective oversight of the Management. Generally, the Board is responsible for:

- formulating the Group's long-term strategy and monitoring the implementation thereof;
- reviewing and approving the annual business plan and financial budget;
- approving the annual, interim and quarterly reports;
- reviewing and monitoring risk management and internal control;
- ensuring good corporate governance and effective compliance; and
- monitoring the performance of the Management.

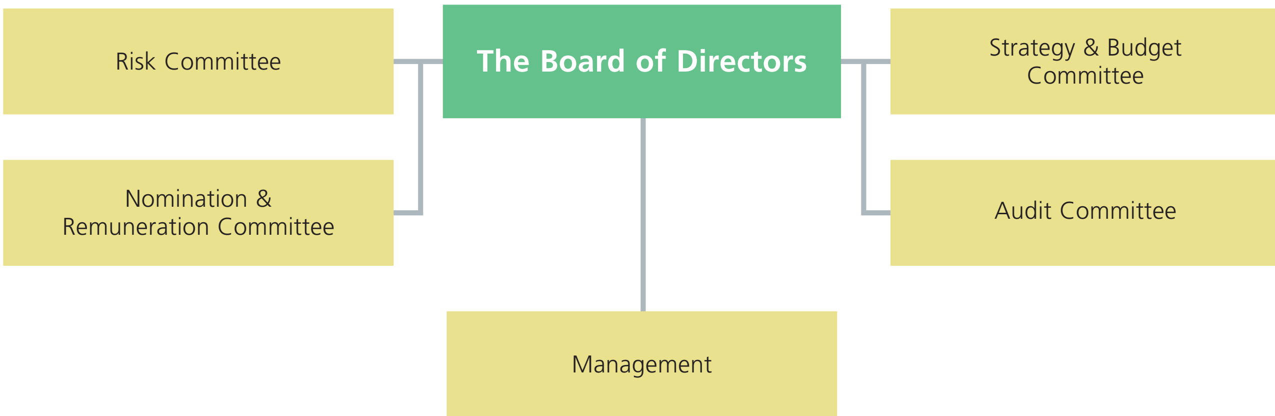
The Board authorises the Management to execute strategies that have been approved. The Management reports to the Board and is responsible for the day-to-day operation of the Group. **The Board has formulated clear written guidelines, which stipulate the circumstances under which the Management should report to and obtain prior approval from the Board** before making decisions or entering into any commitments on behalf of the Group. The Board will regularly review these guidelines.

To avoid the concentration of power in any single individual, the **positions of the Chairman and the Chief Executive are held by two different individuals. Their roles are distinct and are clearly established and stipulated in the Board's Mandate**. In short, the Chairman is responsible for ensuring that the Board properly discharges its responsibilities and conforms to good corporate governance practices and procedures. As the Chairman of the Board, he is also responsible for making sure that all Directors are properly briefed on issues arising at the board meetings, and that all Directors receive accurate, timely and clear information. The Chief Executive is responsible for providing leadership for the whole Management and implementing the important policies and development strategies approved by the Board.

Taking into consideration market practices and international best practices in corporate governance, **the Board has established four standing Board Committees** to assist it in carrying out its responsibilities. They are the Audit Committee, Nomination and Remuneration Committee, Risk Committee, and Strategy and Budget Committee. Should the need arise, the Board will authorise an independent board committee comprising all the independent non-executive Directors to review, approve and monitor connected transactions (including the continuing connected transactions) that should be approved by the Board.

**Each of the Board Committees has a well-defined mandate**. They make recommendations to the Board on relevant matters within their terms of reference, or make decisions under appropriate circumstances in accordance with the power delegated by the Board. **A secretarial department is assigned to provide support services to each Board Committee so that it can discharge its responsibilities properly and effectively**. The Board and Board Committees will participate in the annual performance appraisal of the secretarial departments to ensure the support services provided by these departments are adequate and of good quality. According to their mandates, **the Board and the Board Committees will review and evaluate their respective work process and effectiveness annually, with a view to identifying areas for improvement**.

The following chart sets out the Company's corporate governance framework.




The Company's corporate website (www.bochk.com) contains detailed information on the Company's corporate governance principles and framework, the compositions of the Board and Board Committees and a summary of their respective terms of reference, shareholders' rights and the Company's Fair Disclosure Policy.

## Board of Directors

**Non-executive Directors and independent non-executive Directors form the majority of the Board**. This structure ensures the independence and objectivity of the Board's decision-making process as well as the thoroughness and impartiality of the Board's oversight of the Management. The Board acts honestly and in good faith in order to maximise long-term shareholder value and fulfill its corporate responsibility to other stakeholders of the Group. Its decisions are made objectively and in the best interests of the Group.

The Board currently has 14 members, comprising six independent non-executive Directors, five non-executive Directors and three executive Directors. There was no change to the composition of the Board in 2008 and up to the date of this report.

**All Directors possess extensive experience in banking and management, and over one third of them are independent non-executive Directors, of whom several are experts in financial and/or risk management**. The Board has adopted the "Policy on Independence of Directors", some provisions of which are even more stringent than Rule 3.13 of the Listing Rules. The Company has received from each of the independent non-executive Directors an annual confirmation of his/her independence by reference to the Policy. On the basis of these confirmations and information available to it, the Company considers all of them to be independent. Biographical details of the Directors are set out in the "Board of Directors and Senior Management" section of this Annual Report and the Company's website at www.bochk.com.

All the existing **non-executive Directors and independent non-executive Directors** of the Company have been **appointed for a fixed term, with formal letters of appointment** setting out the key terms and conditions of their appointment. Pursuant to the Articles of Association, all Directors, including the Chairman, Vice Chairmen and Chief Executive, shall retire by rotation at least once every three years at annual general meetings and be eligible for re-election. All Directors appointed by the Board are subject to election by shareholders at the first general meeting following their appointment. The Nomination and Remuneration Committee has established a **written and formal process for the appointment of independent non-executive Directors to ensure that the appointment procedures are standardised, thorough and transparent**.

There is **no relationship (including financial, business, family or other material/relevant relationship(s)) among the Board members**. Messrs. Xiao Gang, Li Zaohang and Zhou Zaiqun are executive directors of BOC. Mdm. Zhang Yanling is a member of the senior management of BOC. It is expressly provided in the Board's Mandate that, unless permissible under applicable laws or regulations, if a substantial shareholder or Director has a conflict of interest in the matter to be considered by the Board, a Board meeting attended by independent non-executive Directors who have no material interest in the matter shall be held to deliberate on the same.

The Company has arranged for **appropriate Directors' Liability Insurance Policy to indemnify the Directors for liabilities arising out of corporate activities**. The coverage and the sum insured under the policy are reviewed annually.

To ensure that newly appointed Directors have adequate understanding of the Company's business and operation, and to enable current Directors to constantly update their skills and knowledge so that they can continue to offer informed advice and contribute to the Board, the Board enforces a **formal system for the initial induction and ongoing professional development of the Directors**. In 2008, the Board invited two honorable speakers with extensive knowledge in public policy and economics to share with the Board members on the impact of the global financial turmoil on the PRC and the Hong Kong economies respectively.

**Ten Board meetings were held during the year with an average attendance rate of 89%**. The meeting schedule was prepared and approved by the Board in the preceding year. In general, Board agenda and meeting materials are despatched to all Board members for review at least seven days before the meetings. Board agenda is approved by the Chairman following consultation with other Board members and the Management. As a general practice, the Chairman will meet all non-executive Directors (including independent non-executive Directors) in the absence of executive Directors and the Management at the beginning of each Board meeting, in order to facilitate an open and frank discussion among the non-executive Directors. This practice has been incorporated in the Working Rules of the Board. Individual attendance records of the Directors in 2008 are set out as follows:

| Director | Number of Board meetings attended | Attendance rate |
|---|---|---|
| *Non-executive Directors* | | |
| Mr. XIAO Gang *(Chairman)* | 7 out of 10 | 70% |
| Mr. SUN Changji *(Vice Chairman)* | 10 out of 10 | 100% |
| Mr. LI Zaohang | 10 out of 10 | 100% |
| Mr. ZHOU Zaiqun | 9 out of 10 | 90% |
| Mdm. ZHANG Yanling | 8 out of 10 | 80% |
| *Independent Non-executive Directors* | | |
| Dr. FUNG Victor Kwok King | 8 out of 10 | 80% |
| Mr. KOH Beng Seng | 10 out of 10 | 100% |
| Mr. SHAN Weijian | 8 out of 10 | 80% |
| Mr. TUNG Chee Chen | 9 out of 10 | 90% |
| Mr. TUNG Savio Wai-Hok | 10 out of 10 | 100% |
| Mdm. YANG Linda Tsao | 10 out of 10 | 100% |
| *Executive Directors* | | |
| Mr. HE Guangbei *(Vice Chairman and Chief Executive)* | 10 out of 10 | 100% |
| Mr. LEE Raymond Wing Hung | 10 out of 10 | 100% |
| Mr. GAO Yingxin | 6 out of 10 | 60% |

Apart from formal Board meetings and general meetings, there are opportunities for the Board and the Management to interact and communicate on relatively less formal occasions. For example, **Board members have been invited to give a talk to the Company's middle to senior management on diverse subjects leveraging on their respective background and expertise**. Further, **off-site events have been held to enhance communication among Board members, and between the Board and the Management**.

## Audit Committee

The Audit Committee currently has seven members comprising one non-executive Director and all the six independent non-executive Directors. Independent non-executive Directors make up 86% of the Committee members. The Committee is chaired by Mr. Shan Weijian, an independent non-executive Director.

The Committee assists the Board in fulfilling its oversight role over the Company and its subsidiaries in, among others, the following areas:

- integrity of financial statements and financial reporting process;
- internal control systems;
- effectiveness of internal audit function and performance appraisal of the Head of Internal Audit;
- appointment of external auditors and assessment of their qualifications, independence and performance and, with authorisation of the Board, determination of their remuneration;
- periodic review and annual audit of the Company's and the Group's financial statements, and financial and business review;
- compliance with applicable accounting standards as well as legal and regulatory requirements on financial disclosures; and
- corporate governance framework of the Group and implementation thereof.

The work performed by the Audit Committee in 2008 included the review and, where applicable, approval of:

- the Company's Directors' Report and financial statements for the year ended 31 December 2007 and the annual results announcement that were recommended to the Board for approval;
- the Company's interim financial statements for the six months ended 30 June 2008 and the interim results announcement that were recommended to the Board for approval;
- the Company's announcement on quarterly financial and business review for the period ended 31 March 2008 and 30 September 2008 that were recommended to the Board for approval;
- the audit reports and report on internal control recommendations submitted by the external auditors, and the on-site examination reports issued by regulators;
- the re-appointment of external auditors, the fees payable to external auditors for the annual audit, interim review and other non-audit services;
- the Group's internal audit plan for 2008 and key issues identified;
- the deployment of human resources and pay level of the Internal Audit, and the department's budget for 2008; and
- the 2008 key performance indicators for and 2007 performance appraisal of the Head of Internal Audit and the Internal Audit Department.

The "**Policy on Staff Reporting of Irregularities**" adopted by the Board has **proved to be effective**. Last year, reports on a number of cases were received and handled satisfactorily through the channels and procedures set out in the said Policy.

Pursuant to paragraph C.2 of the Code, the Audit Committee conducted an annual review of the effectiveness of the internal control systems of the Group in 2008. This review covered all material controls, including financial, operational and compliance controls as well as risk management. For detailed information on this topic, please refer to the "Internal Control" section below.

**Six Audit Committee meetings were held during the year with an average attendance rate of 93%**. Individual attendance records of the relevant Directors are set out as follows:

| Director | Number of committee meetings attended | Attendance rate |
|---|---|---|
| Mr. SHAN Weijian *(Chairman)* | 6 out of 6 | 100% |
| Mr. ZHOU Zaiqun | 6 out of 6 | 100% |
| Dr. FUNG Victor Kwok King | 5 out of 6 | 83% |
| Mr. KOH Beng Seng | 6 out of 6 | 100% |
| Mr. TUNG Chee Chen | 4 out of 6 | 67% |
| Mr. TUNG Savio Wai-Hok | 6 out of 6 | 100% |
| Mdm. YANG Linda Tsao | 6 out of 6 | 100% |

## Nomination and Remuneration Committee

The Nomination and Remuneration Committee currently has six members comprising two non-executive Directors and four independent non-executive Directors. The independent non-executive Directors represent two-thirds of the Committee members. The Committee is chaired by Mr. Sun Changji, Vice-chairman of the Board.

The Committee assists the Board in fulfilling its oversight role over the Company and its subsidiaries in, among others, the following areas:

- overall human resources and remuneration strategies of the Group;
- selection and nomination of Directors, Board Committee members and certain senior executives as designated by the Board from time to time;
- structure, size and composition (including skills, experience and knowledge) of Directors and Board Committee members;
- remuneration of Directors, Board Committee members and designated senior management; and
- effectiveness of the Board and Board Committees.

The work performed by the Committee in 2008 included the review and where applicable, approval of:

- performance appraisal of the executive Directors and designated senior executives for year 2007;
- proposal on staff bonus for year 2007 and salary adjustment for year 2008 for the Group, including the designated senior executives;
- key performance indicators of the Group and the designated senior executives for year 2008;
- implementation progress of the Group's medium-term human resources strategies and other major human resources policies;
- reports on self-evaluation of the Board and Board Committees, which were analyzed by the Committee. The Committee also made recommendations to the Board regarding the results of the self-evaluation, with a view to further enhancing the role and effectiveness of the Board and Board Committees;
- recruitment of the Group's designated senior executives;
- formulation, review and amendment on major HR and compensation policies; and
- matters relating to the appointment of directors to the boards of certain major subsidiaries of the Group.

Pursuant to the "**Policy on Directors' Remuneration**" adopted by the Company, in recommending the remuneration of Directors, the Committee makes reference to companies of comparable business type or scale, and the nature and quantity of work at both Board and Board Committee levels (including frequency of meetings and nature of agenda items) in order to compensate Directors reasonably for their time and efforts spent. **No individual Director is allowed to participate in the procedures for deciding his/her individual remuneration package**. Information relating to the remuneration of each Director for 2008 is set out in Note 22 of this Annual Report. The present scale of Director's fees, including additional fees for membership of Board Committees, is given below:

| | |
|---|---|
| Board of Directors: | |
| All Directors | HK$200,000 p.a. |
| Board Committees: | |
| Chairman | HK$100,000 p.a. |
| Other Committee members | HK$50,000 p.a. |

The **Nomination and Remuneration Committee** also has the delegated responsibility to **determine the specific remuneration packages of the executive Directors and designated senior executives**, including share options, benefits in kind, pension rights, etc. Currently the principal components of the Company's remuneration packages for the executive Directors and designated senior executives include basic salary, discretionary bonus and other benefits in kind. A significant portion of the executive Directors' or designated senior executives' discretionary bonus is based on the Group's and the individual's performance during the year. The Committee reviews and recommends to the Board the annual performance targets for the executive Directors and designated senior executives by reference to the corporate goals and objectives approved by the Board from time to time. The Committee also reviews the performance of the executive Directors and designated senior executives against the targets set on an ongoing basis, and reviews and approves their specific performance-based remuneration.

**Eight Nomination and Remuneration Committee meetings were held during the year with an average attendance rate of 92%**. Individual attendance records of the relevant Directors are set out as follows:

| Director | Number of committee meetings attended | Attendance rate |
|---|---|---|
| Mr. SUN Changji *(Chairman)* | 8 out of 8 | 100% |
| Mr. LI Zaohang | 8 out of 8 | 100% |
| Dr. FUNG Victor Kwok King | 7 out of 8 | 87.5% |
| Mr. SHAN Weijian | 7 out of 8 | 87.5% |
| Mr. TUNG Chee Chen | 6 out of 8 | 75% |
| Mdm. YANG Linda Tsao | 8 out of 8 | 100% |

### Risk Committee

The Risk Committee has three members in 2008. Two of them are independent non-executive Directors and one is a non-executive Director. The Committee is chaired by Mr. Koh Beng Seng, an independent non-executive Director. Mdm. Yang Linda Tsao, an independent non-executive director and the Chairlady of the Strategy and Budget Committee, attended the Risk Committee meetings from time to time as an observer.

The Committee assists the Board in fulfilling its oversight role over the Company and its subsidiaries in, among others, the following areas:

- formulation of the risk appetite and risk management strategy of the Group, and determination of the Group's risk profile;
- identification, assessment and management of material risks faced by the various business units of the Group;
- review and assessment of the adequacy and effectiveness of the Group's risk management process, system and internal control;
- review and monitoring of the Group's capital management;
- review and monitoring of the Group's compliance with the risk management process, system and internal control, including the Group's compliance with prudential, legal and regulatory requirements governing the business of the Group;
- review and approval of high-level risk-related policies of the Group; and
- review of significant or high risk exposures and transactions.

The work performed by the Committee in 2008 included the following:

- review of risk management limits;
- review of Group Operational Principles, Risk Management Policy Statement and a range of risk management policies covering strategic risk, reputation risk, credit risk, market risk, interest rate risk, liquidity risk, operational risk, legal and compliance risk and stress testing;
- review and monitoring of Basel II implementation especially the implementation progress of FIRB and ICAAP; as well as approval of FIRB models;
- approval of the Bank's Capital Management Policy, capital optimisation plans, ICAAP Framework and Minimum CAR, as well as BOCHK Group's Operating CAR Range;
- review of the fixed income investment strategy;
- review of significant high risk exposures and transactions; and
- review of various periodic risk management reports.

**Nine Risk Committee meetings were held during the year with an average attendance rate of 100%**. Individual attendance records of the relevant Directors are set out as follows:

| Director | Number of committee meetings attended | Attendance rate |
|---|---|---|
| Mr. KOH Beng Seng *(Chairman)* | 9 out of 9 | 100% |
| Mdm. ZHANG Yanling | 9 out of 9 | 100% |
| Mr. TUNG Savio Wai-Hok | 9 out of 9 | 100% |

### Strategy and Budget Committee

The Strategy and Budget Committee comprises four members: two independent non-executive directors, one non-executive director, and the Chief Executive, an executive Director. The Committee is chaired by Mdm. Yang Linda Tsao, an independent non-executive Director.

The Committee assists the Board in fulfilling its oversight role over the Company and its subsidiaries in, among others, the following areas:

- draft, review, motion, and monitor the Group's medium to long-term strategy;
- review and monitor the Group's regular/periodic (including annual) business plan and financial budget;
- draft and review the process for formulating the Group's medium to long-term strategy to ensure that they are sufficiently robust to take into account a range of alternatives;
- monitor implementation of the Group's medium to long-term strategy through pre-determined metrics and provide guidance to Management; and
- make recommendations to the Board on major capital expenditures and strategic commitments of the Group and monitor implementation of the same.

During the year, the Strategy and Budget Committee monitored Management's implementation of the Group's medium to long-term strategy as approved by the Board. The Committee also played a prominent role in driving the formulation and implementation of the Group's key business strategies, including those for the development of the bank's China business and bank card's cooperation with China UnionPay. In early 2008, the Committee reviewed the 2008-2012 rolling strategic plan for the Group and the Group's 2008 financial budget and business plan, and recommended the same to the Board for approval. In late 2008, the Committee reviewed the Group's preliminary financial budget and business plan for 2009.

**Eight Strategy and Budget Committee meetings were held during the year with an average attendance rate of 97%**. Individual attendance records of the relevant Directors are set out as follows:

| Director | Number of committee meetings attended | Attendance rate |
|---|---|---|
| Mdm. YANG Linda Tsao *(Chairlady)* | 8 out of 8 | 100% |
| Mr. HE Guangbei | 8 out of 8 | 100% |
| Mr. ZHOU Zaiqun | 7 out of 8 | 87.5% |
| Mr. TUNG Savio Wai-Hok | 8 out of 8 | 100% |

### Ad Hoc Committees

The Board established an ad hoc Independent Board Committee and an ad hoc Search Committee during the year.

### Search Committee

Following the resignation of Mr. Chan Tze Ching, Deputy Chief Executive (Financial Markets) in March 2008, the Search Committee was convened to conduct a global and open recruitment to search for a suitably qualified replacement. The Committee was chaired by Dr. Fung Victor Kwok King, independent non-executive Director. Its members included Mr. Sun Changji, Mr. He Guangbei, and independent non-executive Directors Mr. Koh Beng Seng, Mr. Shan Weijian, Mr. Tung Chee Chen, Mr. Tung Savio Wai-Hok and Mdm. Yang Linda Tsao. The Committee has engaged an independent professional search firm to assist the Committee in conducting a global and open recruitment. After several rounds of selection and with the recommendation of the Nomination and Remuneration Committee, the Board resolved to appoint Mr. Wong David See Hong as the Deputy Chief Executive of the Group with effect from 1 July 2008 to provide overall leadership for the financial market business lines covering Investment, Global Markets, Cash Management, Custody, Investment and Insurance products, and other capital market related business lines.

In August 2008, the Board resolved to recruit a Chief Operating Officer of the Group to provide overall leadership and oversight to the Group's IT, bank-wide operations, business optimisation and corporate services. With the assistance of a professional search firm, the Committee, comprising all the above-mentioned members together with Mr. Li Zaohang, a non-executive Director, was convened to conduct an open recruitment and has made substantive progress to date. As a result of the forthcoming retirement of Mr. Lee Raymond Wing Hung, executive Director and Chief Financial Officer, from 1 June 2009, the Committee has been convened in February 2009 to conduct an open and global recruitment to search for a suitably qualified candidate to fill the position of the Chief Financial Officer of the Group.

### Independent Board Committee

Pursuant to the Board's resolutions, an Independent Board Committee was set up in May and November 2008 respectively to review and approve the respective proposals for borrowing subordinated loan from BOC to enhance the Bank's supplementary capital. The Committee comprised all the independent non-executive Directors of the Company and was chaired by Mr. Tung Chee Chen. The Committee has engaged an independent financial adviser for the purpose of assisting the Committee to review the proposed subordinated loans from BOC and the terms thereof. On the basis of the independent financial adviser's affirmative advice and its own review, the Committee is satisfied that the terms of the subordinated loans are fair and reasonable, on normal commercial terms and arm's length basis, and are in the interests of the Company and its shareholders taken as a whole.

### Directors' Securities Transactions

The Company has adopted the "Code for Securities Transactions by Directors" to govern securities transactions by Directors. The terms of the said Code are more stringent than the mandatory standards set out in the "Model Code for Securities Transactions by Directors of Listed Issuers" contained in Appendix 10 of the Listing Rules. Apart from the securities of the Company, the Code applies equally to the Director's dealings in the securities of BOC which was listed on the Stock Exchange of Hong Kong in June 2006. In this connection, the Company had made specific enquiry of all Directors, who confirmed that they had complied with the standards set out in both the Company's Code and the said Model Code throughout year 2008. The Code has been revised in January and March 2009 to reflect changes made to the Model Code, including the extended "black out" period for Directors' dealing in the Company's securities.

### External Auditors

Pursuant to the "Policy on External Auditors" adopted by the Board, the **Audit Committee** reviewed and monitored and **was satisfied with the independence and objectivity of PricewaterhouseCoopers**, the Group's external auditors, **and the effectiveness of their audit procedures**, based on the principles and standards set out in the policy that were in line with international best practices. Upon the recommendation of the Audit Committee, the Board will propose that PricewaterhouseCoopers be re-appointed as auditors of the Group at the Company's 2009 annual general meeting. Subject to authorisation by the shareholders, the Board will authorise the Audit Committee to determine the remuneration of PricewaterhouseCoopers. For 2008, the fee charged by PricewaterhouseCoopers was HK$38 million, of which HK$33 million was for audit services and HK$5 million related to other services. For 2007, the fee charged by PricewaterhouseCoopers was HK$37 million, of which HK$32 million was for audit services and HK$5 million related to other services.

The Audit Committee was satisfied that the non-audit services did not affect the independence of PricewaterhouseCoopers. The non-audit service fees paid to PricewaterhouseCoopers in 2008 comprised mainly the tax-related services fee of HK$3 million, fee in relation to advisory service on New Accounting Standard, Cut-off Date Audit and Capital Injection Verification for Nanyang Commercial Bank (China) Limited of HK$1 million and miscellaneous non-audit services fee of HK$1 million.

### Internal Control

The Board has the responsibility to ensure that the Group maintains sound and effective internal controls to safeguard the Group's assets. According to the Board's delegation, the Management is responsible for the day-to-day operations and risk management.

The internal control system is designed to maximise assurance against material misstatement or loss; to manage the risk of system failure; and to assist in the achievement of the Group's objectives. In addition to safeguarding the Group's assets, it also ensures the maintenance of proper accounting records and compliance with relevant laws and regulations.

The Group conducts an annual review of the effectiveness of its internal control systems covering all material controls, including financial, operational and compliance controls as well as risk management. The review is conducted by making reference to the guidelines and definitions given by the regulatory and professional bodies for the purpose of assessing five different internal control elements, namely, the control environment, risk assessment, control activities, information and communication, and monitoring. The assessment covers all the major internal controls and measures, including financial, operational and compliance controls as well as risk management functions. The annual review is coordinated by the Group's Internal Audit, which, after the Management and various business departments have performed their self-assessment, will carry out an independent examination and other post-assessment work on the review process and results. The results of the 2008 review have been reported to the Audit Committee and the Board.

The key procedures that the Group has essentially established and implemented to provide internal controls are summarised as follows:

- with a Management that functions under a rational organisational structure and whose authority and responsibility are clearly delineated, the Group has formulated policies and procedures to ensure reasonable checks and balances for all the operating units, reasonable safeguard for the Group's assets, the implementation of internal controls and adherence to relevant laws and regulations and risk management in its operations;

- the Management draws up and continuously monitors the implementation of the Group's strategies, business plans and financial budgets. The accounting and management systems that are in place provide the basis for evaluating financial and operational performance;

- the Group has various risk management and human resources policies. There are specific units and personnel that are responsible for identifying, assessing and managing all the major risks. These include reputation, strategic, legal, compliance, credit, market, operational, liquidity and interest rate risks; (The Group's risk management governance structure is given on page 46 to page 51 in this Annual Report.)

- the Group has established an information technology governance structure that produces a range of reports on information systems and management, including information on the monitoring of various business units, financial information and operating performance. Such information facilitates the Management, business units and the regulatory bodies in assessing and monitoring the Group's operation and performance. Proper communication channels and reporting mechanisms are in place at various business units and levels to facilitate exchange of information;

- pursuant to a risk-based approach and in accordance with the internal audit plan approved by the Audit Committee, the Group's Internal Audit conducts independent reviews on such aspects as financial activities, various business units, various kinds of risks, operations and activities. Audit reports are submitted directly to the Audit Committee. Internal Audit will closely follow up on the items that require attention in a systematic way and will report to the Audit Committee and the Management in a timely manner; and

- the Audit Committee reviews the reports submitted by external auditors to the Group's Management in connection with the annual audit as well as the recommendations made by regulatory bodies on internal control. Internal Audit will follow up on the same to ensure timely implementation of the recommendations, and will also periodically report the status of the implementation to the Management and the Audit Committee.

The Group is committed to maintaining and upholding good corporate governance practices and internal control system of all subsidiaries and foreign operations are reviewed regularly. During the year of 2008, continuous improvement on the organization structure and segregation of duty, the risk management policy and procedure, and the enhancement of disclosure transparency have been undertaken. In response to the dramatic changes in the economic environment resulting from the global economic crisis, the Group has implemented a series of measures and undertaken an on-going review on the effectiveness and efficiency of the internal control mechanism. In 2008, areas for improvement have been identified and appropriate measures have been implemented.

## Communication with Shareholders and Shareholders' Rights

**The Board attaches a high degree of importance to continuous communication with shareholders**, especially direct dialogue with them at the Company's annual general meetings. Shareholders are therefore encouraged to actively participate at such meetings.

The Chairman of the Board, the Chairmen and members of Board Committees, and representatives of PricewaterhouseCoopers were present at the Company's 2008 annual general meeting held on 20 May 2008 at the Bank of China Tower to respond to questions and comments raised by shareholders. Resolutions passed at the Company's 2008 annual general meeting included: adoption of the Company's and the Group's 2007 financial statements, declaration of 2007 final dividend, re-election of Directors, re-appointment of auditors and grant of a general mandate to the Board to issue and repurchase shares of the Company.

The Board is aware of investors' concern regarding the potential dilution of the shareholders' value arising from the exercise of power pursuant to the grant of a general mandate to issue shares to the Board. To alleviate those concerns, the Board has voluntarily reduced the general mandate to issue shares to 5% of the issued share capital as compared to the 20% permitted under the Listing Rules in the event that the issue of shares is for cash and not related to any acquisition of assets for approval by the shareholders at the 2009 annual general meeting. Further, given its commitment to high standards of corporate governance, the Board announced at the 2008 annual general meeting certain **internal policies for the exercise of the powers granted to the Board under the general mandates to issue shares solely for cash and repurchase shares** as follows:

- the Board will not exercise the mandate at a discount that will result in significant dilution of shareholders' value. In the exercise of such power to issue shares for cash, the Board will have regard to factors such as the Group's capital adequacy ratio, and in particular, its Tier 1 capital, cost and benefit of raising Tier 2 capital, need for cash for the Group's business development, the principle that shareholders should be treated equally and the alternative of conducting a rights issue;

- the Board has set the triggering events for the exercise of the power to repurchase shares, which include: market price of the Company's shares is lower than the fair value of the shares; the Group has surplus funds which is in excess of its short to mid term development requirements; and the Board considers it proper and appropriate to exercise the general mandate for enhancing the return on equity or net assets or earnings per share of the Company. In general, such purchases will be made on the Stock Exchange. However, if it is expected that the size of the purchases may lead to a disorderly market for the Company's shares, then the Board will consider making the purchases through a general offer, i.e. offer to all existing shareholders in proportion to their respective shareholdings. The price at which shares are repurchased will not be higher than the fair value of the shares of the Company.

The Board has resolved to adopt the above policies if it is granted by the shareholders the general mandates to issue and repurchase shares at the 2009 annual general meeting.

**All the resolutions proposed at the Company's 2009 annual general meeting will be voted on by poll**. The Company has engaged Computershare Hong Kong Investor Services Limited, the Company's Share Registrar, to act as the scrutineer for such purpose. The results of the poll voting will be posted on the Company's website at www.bochk.com and the Stock Exchange's website at www.hkexnews.hk as soon as practicable following conclusion of the vote-counting.

In order that shareholders can have a better understanding of the agenda items to be discussed at the 2009 annual general meeting and to encourage their active participation so that exchange of views and communication can be further enhanced, **the Company has provided detailed information on the 2009 annual general meeting in a circular** which is despatched together with this Annual Report to the shareholders. This includes background information to the proposed resolutions, information on the retiring Directors and information on voting and other issues relating to the 2009 annual general meeting in the form of "Frequently Asked Questions" (including how to convene an extraordinary general meeting and how to put forward a proposal for consideration by shareholders at a general meeting).

Further shareholder information is set out in the "Investor Relations" section of this Annual Report. Shareholders who wish to raise any queries with the Board may write to the Company Secretary at 52nd Floor, Bank of China Tower, 1 Garden Road, Central, Hong Kong.

## Directors' Responsibility Statement in relation to Financial Statements

The following statement should be read in conjunction with the auditors' statement of their responsibilities as set out in the auditors' report contained in this Annual Report. The statement is made with a view to distinguishing for shareholders the respective responsibilities of the Directors and of the auditors in relation to the financial statements.

The Directors are required by the Hong Kong Companies Ordinance to prepare financial statements, which give a true and fair view of the state of affairs of the Company. The financial statements should be prepared on a going concern basis unless it is not appropriate to do so. The Directors have responsibility for ensuring that the Company keeps accounting records which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the requirements of the Hong Kong Companies Ordinance. The Directors also have general responsibilities for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The Directors consider that in preparing the financial statements contained in this Annual Report, the Company has adopted appropriate accounting policies which have been consistently applied with the support of reasonable and prudent judgements and estimates, and that all accounting standards which they consider to be applicable have been followed.

## Investor Relations Policy and Guidelines

The Company is committed to providing shareholders, the investment community and the general public access to key information that is reasonably required to make an investment decision on a fair and timely basis. Such information includes the Company's corporate strategies, business performance and prospects as well as updates of major corporate developments.

To attain a high standard of investor relations practice, the Company adopts the Fair Disclosure Policy, which is available in the Company's website for public reference. The Policy contains clear guidelines to ensure that:

1. The Listing Rules and other regulatory requirements in relation to the disclosure of price-sensitive information are complied with.
2. All communications with the public, including the investment community and the media, are fair.
3. Material non-public information is not disseminated on a selective basis.

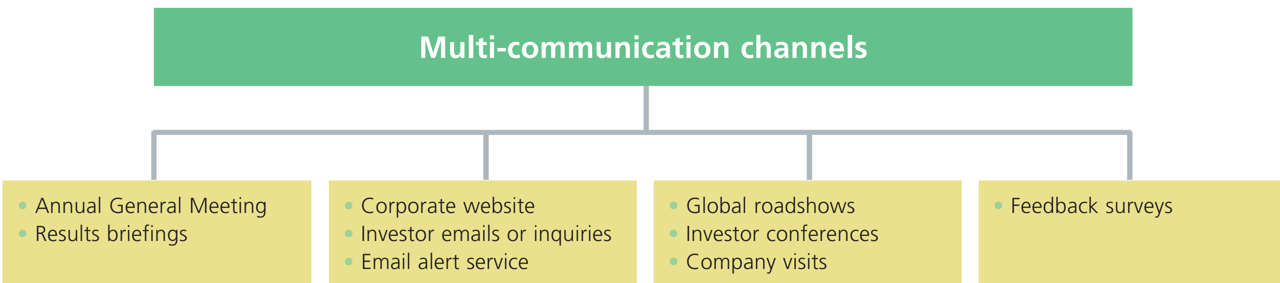
## Investor Relations Programme

Chaired by the Company's Chief Executive and comprising other senior executives, the Investor Relations Committee formulates the Company's investor relation strategies and oversees the investor relations programme. Both the Board and the Committee evaluate the effectiveness of the investor relations programme on a regular basis.

Through various channels, the Company is committed to timely and effective communication with the investment community to enhance their knowledge and understanding of the Company. The Company's investor relations activities are conducted on a global basis to enhance its profile among international investors.

### *Access to Corporate Information*

To ensure investors to have access to important corporate information on a fair and timely basis, the Investor Relations section of the Company's website (http://www.bochk.com/ir) contains all relevant information to keep investors informed of its latest development. In support of the Company's commitment in enhancing social awareness on environmental issues, the Company has taken initiatives to encourage shareholders and investors to receive corporate communication materials electronically. The IR website also includes an e-mail alert service which allows interested parties to sign up for corporate updates.



## Overview of Investor Relations Activities in 2008

In 2008, the Company continued to provide effective channels for proactive communication with investors.

### *Annual General Meeting*

At the AGM held in May 2008, the Chairmen of the Board, the Audit Committee, the Nomination and Remuneration Committee, the Risk Committee, and the Strategy and Budget Committee respectively, as well as the Company's external auditors were present to respond to questions and comments from shareholders.

### *Results Announcement*

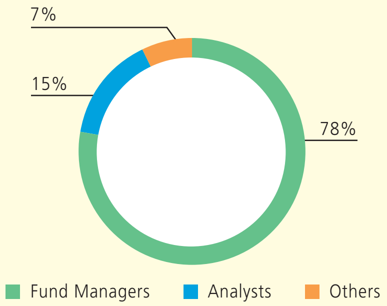
At the Group's 2007 annual results announcement and 2008 interim results announcement, the senior management led by the Chief Executive conducted briefings with analysts and the press to apprise them of the Company's operating results, business strategies and outlook, and to respond to their questions. These events, including the relevant presentation materials and announcements, were all available to the public through the Group's website, both live and as a recording.

In addition to the interim and annual results announcements, the Company also published quarterly financial and business reviews to keep shareholders updated of the Company's latest performance and financial position.

### *Communication with Investors*

In 2008, the Company had over 230 meetings with investors across the world. These meetings were held during global road-shows, international investor conferences and company visits. The Company is widely covered by more than 20 securities research institutions.

**Investor Meetings by Category**




Through continuous dialogue with investors and investor feedback surveys, the Company continued to promote two-way communication. The responses received from these initiatives enabled the Company to better understand the market's concerns and to formulate the Company's investor relations plan going forward.

## Market Recognition

The Company's commitment to transparency and dedication to maintain high standards in disclosure continued to win public recognition in 2008. The Company's 2007 annual report is granted a Silver Prize under the "General Category" in the 2008 Best Annual Reports Awards competition organized by the Hong Kong Management Association. This marked the second consecutive year that the Company's report has been awarded by the organizer.

## Going Forward

Under the principles of timeliness, fairness and transparency, the Company will continue to pursue a proactive and effective investor communication programme to keep the investors adequately informed about the Company's present and future development.

## Investor Relations Contact

Enquiries may be directed to:

Investor Relations Division
BOC Hong Kong (Holdings) Limited
52nd Floor
Bank of China Tower
1 Garden Road
Hong Kong
Telephone: (852) 2903 6602/
(852) 2826 6314
Facsimile: (852) 2810 5830
E-mail: investor_relations@bochk.com

## Shareholder Information

### Financial Calendar 2009

| | |
|---|---|
| Announcement of 2008 annual results | 24 March (Tuesday) |
| Last day in Hong Kong of dealings in the Company's shares with entitlement to attend the 2009 annual general meeting | 12 May (Tuesday) |
| Latest time in Hong Kong for lodging transfers for entitlement to attend the 2009 annual general meeting | 14 May (Thursday) 4:30 p.m. |
| Book closure period (both days inclusive) | 15 May (Friday) to 21 May (Thursday) |
| Record date for the 2009 annual general meeting | 21 May (Thursday) |
| Latest time for lodging proxy forms for 2009 Annual General Meeting | 19 May (Tuesday) 3:00 p.m. |
| 2009 Annual General Meeting | 21 May (Thursday) 3:00 p.m. |
| Announcement of 2009 interim results | Mid to late August |

## Annual General Meeting

The 2009 Annual General Meeting will be held at 3:00 p.m. on Thursday, 21 May 2009 at Meeting Room S421, Hong Kong Convention and Exhibition Centre, 1 Expo Drive, Wanchai, Hong Kong (please use Harbour Road Entrance).

## Share Information

### *Listing and Stock Codes*

| Ordinary Shares | | Level 1 ADR Programme | |
|---|---|---|---|
| The Company's ordinary shares are listed and traded on the Stock Exchange of Hong Kong Limited (HKEX). | | The Company maintains a Level 1 ADR facility for its ADSs. Each ADS represents 20 ordinary shares of the Company. | |
| ***Stock codes*** | | ***Stock codes*** | |
| HKEX | 2388 | CUSIP No.: | 096813209 |
| Reuters | 2388.HK | OTC Symbol: | BHKLY |
| Bloomberg | 2388 HK | | |

### *Market Capitalization and Index Recognition*

As at 31 December 2008, the Company's market capitalization was HK$92.8 billion, among the top 20 leading stocks on the Main Board of Hong Kong Stock Exchange in terms of market capitalization. Given the Company's sizable market capitalization and high liquidity, its shares are a constituent of the Hang Seng Index, MSCI Index and FTSE Index series.

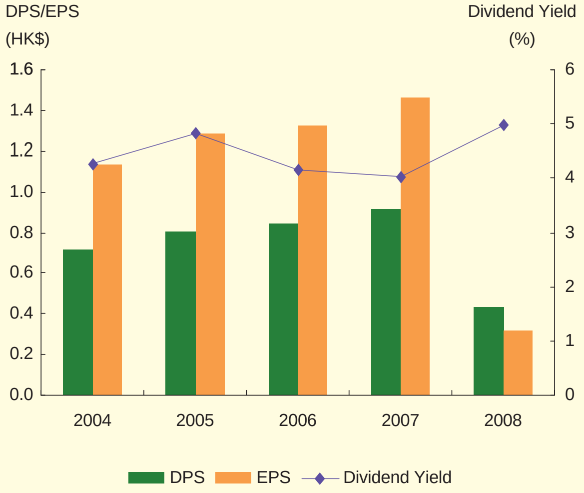
### Share Price and Trading Information

| Share price (HK$) | 2008 | 2007 | 2006 |
|---|---|---|---|
| Highest trading price during the year | 24.10 | 22.70 | 22.10 |
| Lowest trading price during the year | 7.33 | 16.78 | 14.45 |
| Closing price at year end | 8.78 | 21.85 | 21.10 |
| Average trading volume/trading day (m shares) | 23.47 | 26.20 | 28.56 |
| Number of ordinary shares issued (shares) | | 10,572,780,266 | |
| Public float | | Approximately 34% | |
| Nominal value per share | | HK$5.0 | |

### Dividends

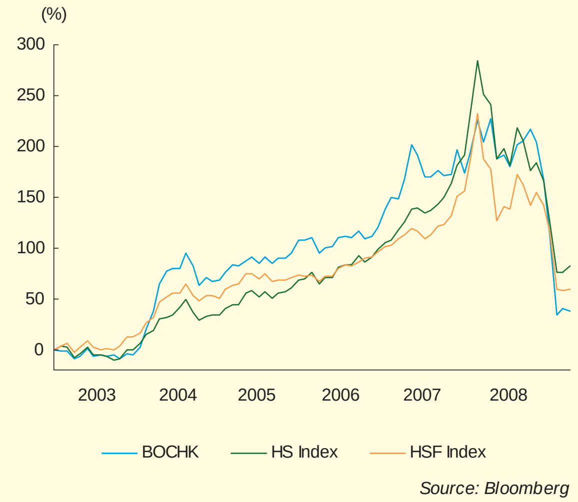
The Directors recommend no final dividend for 2008. With the interim dividend per share of HK$0.438 paid during 2008, the total dividend per share amounted to HK$0.438 for the whole year.

#### Dividend Income and Earnings




Annual dividend yield is calculated based on actual dividends paid to shareholder during that year (final dividend of previous year and interim dividend of the year) and year-end closing share price.

#### Total Shareholder Return




Total shareholder return is measured by share price appreciation and reinvested dividends.

### Credit Ratings (long-term)

| | |
|---|---|
| Standard & Poor's: | A- |
| Moody's Investors Service: | Aa3 |
| Fitch Ratings: | A |

## Shareholding Structure and Shareholder Base

As at 31 December 2008, the Company had 10,572,780,266 shares in issue of which approximately 34% was held by the public and 0.2% was held in the form of ADSs. The Company's 96,686 registered shareholders were distributed in various parts of the world, including Asia, Europe and North America. Apart from BOC, the Company is not aware of any major shareholders with a shareholding of more than 5% which has to be reported under the Securities and Futures Ordinance of Hong Kong.

During the year, our shareholder structure remained stable and the following table shows the distribution of ownership according to the register of members and the participant shareholding report generated from the Central Clearing and Settlement System as of 31 December 2008:

| Category | Number of registered shareholders | % of total | Number of issued shares | % of total |
|---|---|---|---|---|
| Individuals | 96,544 | 99.9 | 224,222,870 | 2.1 |
| Institutions, corporates and nominees | 141 | 0.1 | 3,403,804,840 | 32.2 |
| Bank of China Group | 1 | 0.0 | 6,944,752,556 | 65.7 |
| Total | 96,686 | 100.0 | 10,572,780,266 | 100.0 |

## Shareholder Enquiries

Any matters relating to your shareholding, e.g. transfer of shares, change of name or address, lost share certificates and dividend warrants, should be sent in writing to:

| | |
|---|---|
| Hong Kong | Computershare Hong Kong Investor Services Limited<br>Rooms 1806-1807<br>18th Floor, Hopewell Centre<br>183 Queen's Road East, Hong Kong<br>Telephone: (852) 2862 8555<br>Facsimile: (852) 2865 0990/(852) 2529 6087<br>E-mail: bochk.ecom@computershare.com.hk |
| USA | Citibank Shareholder Services<br>250 Royall Street<br>Canton, MA 02021, USA<br>Telephone: 1-877-248-4237 (toll free)<br>1-781-575-4555 (outside USA)<br>E-mail: Citibank@shareholders-online.com |

## Other Information

This Annual Report is available in both English and Chinese. A copy prepared in the language different from that in which you have received is available by writing to the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at Rooms 1806 - 1807, 18th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong or email to bochk.ecom@computershare.com.hk. This Annual Report is also available (in both English and Chinese) on the Company's website at www.bochk.com and the Stock Exchange's website at www.hkexnews.hk. You are encouraged to access the corporate communications of the Company through these websites in lieu of receiving printed copies to help protect the environment. We believe that it is also the most efficient and convenient method of communication with our shareholders.

If you have any queries about how to obtain copies of this Annual Report or how to access those documents on the Company's website, please call the Company's hotline at (852) 2846 2700.

# 綠遍

# Prospects

# CORPORATE SOCIAL RESPONSIBILITY

As we adhere to our motto of "Taking Root in Hong Kong and Serving Hong Kong", the Group fully understands that undertaking corporate social responsibility underpins the success of a corporation. We are committed to reciprocating to the community by supporting a wide spectrum of activities, and our dedication has won us the honour of being named a Caring Company by the Hong Kong Council of Social Service for six consecutive years.

Meanwhile, BOCHK Charitable Foundation ("the Foundation") has participated in a diverse range of charitable activities, covering education and culture, sports and health, environmental protection, social welfare and assistance to the needy in Hong Kong, Macau and the Mainland of China.

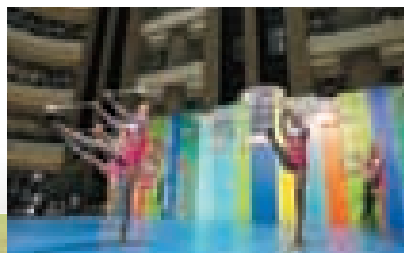
## Promoting Sports Development

The 2008 Olympics and Paralympics in Beijing and the co-hosting of the Equestrian Events in Hong Kong created a golden opportunity for fostering sports development in Hong Kong. Bank of China was the official banking partner of the Beijing 2008 Olympic Games. To commemorate the Games, BOCHK launched the Beijing Olympic Games Commemorative Banknote denominated in HK$20 for public sale as well as Charity Sets of Olympic Banknotes for public bidding. The response was overwhelming. All the net proceeds generated will be donated to charitable causes.

To capitalise on the opportunity of the Olympics, the Group has supported and pioneered a number of sports and cultural activities highlighting the themes of "People's Olympics" and "Green Olympics" to share the joy of the Beijing Olympics with the public. The series of activities leading to the Olympic climax included *BOCHK People's Olympics Carnival at Lan Kwai Fong*, *BOCHK Olympic Carnival at New Town Plaza*, *Bank of China (Hong Kong),Olympian City: Flights of Fantasy*, *Heavenly Horse – The Horse in Chinese Art and Culture Exhibition* jointly presented by the State Administration of Cultural Heritage and the Leisure and Cultural Services Department, and the *Olympic Piazza* organised by the Hong Kong Tourism Board. A diverse range of activities themed with the "Olympics" organised by the Group was granted the Gold Prize by the 2008 US Mercury Awards.

To extend its support to local elite athletes and contribute to the athletic training and sustainable development of sports in Hong Kong, the Foundation took the lead in donating HK$1 million to the *Hong Kong Athletes Career and Education Programme* launched by the Sports Federation and Olympic Committee of Hong Kong, China (SF&OC). The Foundation also gave high recognition to the excellent achievements of these sports elites by supporting the *Bank of China Hong Kong Sports Stars Awards* organised by the SF&OC and setting up in 2006 the *Best of the Best Bank of China Hong Kong Sports Stars Award*.

The Foundation advocated a sporting lifestyle and the Sport for All message



We have sponsored an array of Olympic-related programs like the *Bank of China (Hong Kong) Festival of Sport*, with an aim to promote the message of "Sport for all"

to the public by sponsoring the *Bank of China (Hong Kong) Festival of Sport* for the third consecutive year. More than 80 events were organised throughout the 18 districts by national sports associations. The opening ceremony, characterised by the People's Olympics element, was held at a shopping mall with high pedestrian flow attracting more than 10,000 participants and audiences.

Badminton is the key focus of our sports initiatives. The Foundation has allocated over HK$9.55 million for development of badminton in the past 10 years, benefiting nearly 620,000 participants. To continue our long-standing support for badminton in Hong Kong, the Foundation committed to contributing HK$3.6 million to the *2008-2011 Hong Kong Badminton Development & Training Scheme*.

For seven consecutive years, the Foundation sponsored the *Hong Kong Island & Kowloon Regional Inter-school Sports Competition* – the largest school sports competition of its kind in Hong Kong with the longest history, and the competition's top-honour award – the *BOCHK Bauhinia Bowls Award*. A total of 74,000 athletes from 275 schools participated in 8,400 events in this competition during 2008. Tickets of the Beijing Olympics and the Olympic Equestrian Events, as well as the Paralympics Equestrian Events were offered to various school sports organisations and the Hong Kong Council of Social Service by the Group, providing them with valuable opportunities to witness and experience these international sports events.

## Enriching Cultural Life

During the year, we supported a number of international arts and cultural performances manifesting the theme of People's Olympics. *Zingaro*, a world-renowned creative entertainment spectacle blending equestrian with opera and dancing, and staged in Hong Kong for the first time, was sponsored by the Foundation and presented by the Hong Kong Arts Festival. This French equestrian performance echoed the 2008 Olympics Equestrian Events held in Hong Kong and won 39,500 spectators' applause at 32 exhilarating shows. In November, the Foundation also sponsored *Yo-Yo Ma and HKPO* presented by the Hong Kong Philharmonic Orchestra and donated 120 complimentary tickets to the Community Chest and the Hong Kong Academy for Performing Arts, enabling more people to appreciate the inspiring performances of Maestro Yo-Yo Ma.

Other major cultural events which we lent support to were the Hong Kong Philharmonic's *Yundi Li's Prokofiev* and the *Appointment of Yundi Li as Visiting Fellow of the Hong Kong Academy for Performing Arts* in which Yundi Li coached young pianists in Hong Kong in four master classes.

## Building a Green Hong Kong

To promote environmental protection, the Group and the Hong Kong Productivity Council jointly launched the Green Equipment Financing Scheme.


The innovative Charity Green Walk put the elements of the Olympic Games, environmental protection and charity under one roof


The sponsorship of Yo-Yo Ma and Hong Kong Philharmonic Orchestra by the Foundation enabled the audience to appreciate the inspiring performances of Yo-Yo Ma

This is a preferential lending package for small and medium-sized enterprises to purchase environmentally-friendly equipment to enhance their productivity and operating efficiency while helping reduce environmental pollution.

We encouraged our customers to manage their finances via Internet Banking and switch to e-Statements to reduce paper use. In addition, our annual reports are printed on environmentally-friendly and elemental chlorine-free papers, and shareholders are urged to use online channels for corporate communications, including browsing annual reports and notices of meetings. We are working towards a paperless office by promoting the use of electronic correspondence and documents. For the same purpose, training materials are available on our electronic learning platform. Paper recycling bins are placed at Bank of China Tower, Bank of China Centre and Bank of China Building for recycling books, newspapers and magazines.

During the year, the environmental management systems of Bank of China Tower and Bank of China Centre attained ISO 14001 accreditation. Bank of China Tower was also awarded the Indoor Air Quality Certificate (Excellent Class) from the Environmental Protection Department and complied with the requirements of the Fresh Water Plumbing Quality Maintenance Recognition Scheme of the Water Supplies Department. We continued with our efforts to reduce carbon dioxide emissions by installing energy-saving light bulbs and replacing more efficient chillers with environment protection refrigerants in Bank of China Tower and Bank of China Centre. Water conserving devices have also been installed. In June, we participated in the "Dim it – lights out event" organised by Friends of the Earth which raised the community's awareness of energy conservation and pollution reduction.

To further echo the theme of Green Olympics, the Group launched the *Green Olympics – Charity Green Walk* at Victoria Peak that put the elements of the Olympic Games, environmental protection and charity under one roof. A total of 2,008 participants, including 800 staff and their family members, over 1,000 citizens, teachers and students of the *Green School Award*, participated in the event. They learned about the ecological attractions of the Peak with an introduction by professional eco-guides. Through this charity walk, the Foundation made a donation to the Polar Museum Foundation. Furthermore, the Foundation has been sponsoring the *Green School Award* to promote environmental awareness among teachers, parents and students.

### Nurturing the Younger Generation

Educating and nurturing the younger generation remains one of the principal areas of support of the Foundation. During the year, the Foundation awarded scholarships and bursaries to all the universities and tertiary education institutions in Hong Kong, bringing the total number of benefited students to 1,194, and the gross contribution to HK$11.38 million since 1990.

We actively support youth sports development by sponsoring "The Inter-school Sports Competition HK & Kln Secondary School Region"

The Group gave timely assistance to the earthquake victims of the afflicted areas in Sichuan

In view of the increasing economic integration between Hong Kong and the Mainland of China, the Foundation organised for the fourth year the *Internship Programme for Financial Professionals in the Mainland of China*, together with the *Summer Internship Programme for Tertiary Institution Students* for the first time. Students from universities and tertiary institutions were therefore able to have a better understanding of the economic and financial developments in our motherland and equip themselves for future challenges by undertaking an internship at branches of Bank of China in the Mainland.

### Help for the Needy

In order to give timely assistance to the victims of the Mainland's snowstorms in February 2008, the Foundation took the lead in donating HK$3 million to the afflicted areas. It also leveraged the extensive branch network of the Group and set up designated accounts to collect donations from the community. The donations collected from staff, customers and the general public reached HK$1.88 million, which has been transferred to the Mainland.

A massive earthquake jolted Sichuan on 12 May 2008. The Foundation became the first institution to make a donation of HK$3 million to the afflicted areas through the Hong Kong Red Cross. With this donation inclusive, the Group has donated a total amount of HK$10 million to the Sichuan earthquake victims. The aggregate sum of donations collected from customers and the public stood at HK$24.91 million, helping rescue work and reconstruction of the afflicted areas.

The Foundation also fully supported the *Community Chest New Territories Walk – Route 8*. There were over 32,000 participants, including some 1,000 of our staff and their family members, all contributing to this record-breaking number for the Territories Walk.

What is more, the Foundation offered donations in a wide variety of charitable activities, such as being the Diamond Sponsor of Po Leung Kuk for 11 consecutive years, and sponsoring the *Charity Golf Tournament* of Po Leung Kuk as well as the *Tung Wah Charity Gala* of Tung Wah Group of Hospitals. We were also the sponsor of the Christmas parties for special schools under the Hong Kong Red Cross and *Corporate Challenge 2008* of Outward Bound Hong Kong. The Foundation supported the *Better Health for a Better Hong Kong campaign* through our staff participation in the *MTR Hong Kong Race Walking 2008* in both sports and cheering teams.

Riding on the Group's branch network, we have helped seven charitable organisations to send out 2.8 million inserts with bank statements.

Going forward, we will continue to undertake corporate social responsibility and contribute our part in fostering a harmonious society.

The sponsorship of "Exhibition of Securities Certificates in Modern China" helped enrich the knowledge of the public about securities development in China

The world-renowned *Zingaro*, blending equestrian with opera and dancing, was well-received by the audience

**Photo by Antoine Poupel**

# OUR PEOPLE

People are the most valuable assets of any company. During the year, we enhanced our human resources management, recruitment procedures and staff training programmes in order to echo our core value of "Respect" to staff. To celebrate the Beijing 2008 Olympics and Paralympics that all Chinese people in the world are proud of, we have actively initiated a diverse range of related activities.

## Reforming our Human Resources Mechanism

To keep abreast of the latest market developments and realise the core value of "Respect" to staff, the Group has been continually enhancing its human resources and compensation policies. With competitive remuneration and benefit packages, we aim to retain, attract and motivate talents.

To ensure that the job-based mechanism is in line with the Group's business development, we have accelerated the rationalisation of our staff structure in accordance with the changing market. By rationalising job establishment and developing professional job teams, the Group offered employees a platform to fully utilise their competencies while driving the Group's business growth.

## Recruiting Top Talent

To support our business growth and strengthen our human capital, we are committed to recruiting high quality management and business professionals locally as well as from the Mainland of China and overseas. Through the application of a series of systematic and scientific assessment instruments, the quality of our professional staff has been further strengthened.

Meanwhile, we continued to introduce our Management Trainee Programme and Officer Trainee Programme to attract and nurture high-potential university graduates to become the future management talent and backbone of the Group.

## Strengthening Staff Training

In 2008, we provided 2,400 courses for about 134,000 attendees. Our training programmes were designed with three objectives: 1) to meet the Group's overall development and human resources plans to accomplish the business objectives of each unit; 2) to further promote the staff's self-enhancement as well as career development, and for the establishment of a learning organisation; 3) to optimise the input and utilisation of training resources, strengthen the cooperation with our parent bank, and enhance the overall training effectiveness.

Major training activities came in a series of workshops and seminars covering risk management, legal and compliance, corporate governance, corporate culture, sales and services skills, and leadership programmes for senior management. In addition, CUHK's Executive MBA programme and executive development programmes of Oxford University, Harvard Business School and Hong Kong University of Science & Technology were arranged for our senior management and talent pool members. Our relationship managers were required to undertake credit risk management courses and

tests by Moody's to increase their professional capability. We provided continuous training for intermediaries, professional qualification certificate courses and training on professional sales techniques, and training on new products and new systems for our frontline staff before implementation. In addition, the Wealth Management Academy of BOCHK continued to offer training in customer relationship management and sales techniques to our Wealth Management staff. What is more, the establishment of an e-learning platform, a supplementary training channel, offered added flexibility and convenience in our staff training.

### Fostering a Corporate Culture

During the year, we continued to encourage our staff to help those in need by participating in various voluntary projects organised by external organisations, including the *ATM education campaign* organised by the Hong Kong Association of Banks, the *Elderly Service Scheme* by Po Leung Kuk, the family programmes held in new towns by Yan Oi Tong, the *Community Chest Walk and Race Walking*. To further demonstrate our commitment to social responsibility, we made generous donations and appealed to our staff to participate in the donation campaign for those affected by the Sichuan Earthquake.

To highlight our core value of Respect, we organised different types of activities to express our care for staff. These included management visits to retired staff, cultural and recreational programmes and a free body check-up service.

Moreover, in view of the financial crisis, with staff under heavy pressure and considerable workloads, we have created a greetings card and prepared a healthy breakfast as well as electronic health tips leaflet for each member of our staff.

### Promoting Staff Communications

We realised the importance of strengthening effective two-way communications between staff and management. An Awards Presentation Ceremony was held in 2008 in recognition of staff members who delivered exceptional performance. A total of 10 BOC Stars were selected, and 412 staff and 43 teams were granted outstanding performance awards. To demonstrate our "Teamwork" spirit, we continued to hold the *Teamwork Activities Rewards Scheme* which encouraged our staff to participate in inter-departmental activities.

In welcoming the Beijing 2008 Olympic Games, the Group also held a number of athletic competitions and activities themed on the Olympics, covering badminton, tennis and bowling. By including parent-child activities, our staff and their family members were able to enjoy a fun-filled day in celebration of the Olympics, while cultivating team spirit and sportsmanship. In addition, some of our staff members were selected as torchbearers in the Olympic Torch Relay. The Group also fully supported 25 staff and their family members to take part in the voluntary work of the Olympic financial service.

Awards Presentation Ceremony was held in recognition of the excellent performance of our staff

We organised diverse recreational and sports activities for staff and their relatives

# SWIFTER, HIGHER, STRONGER



We launched the first-ever Beijing 2008 Olympic Games HK Dollar Commemorative Banknote in the history of the modern Olympic Games




We rolled out a series of Olympic count-down advertising campaigns

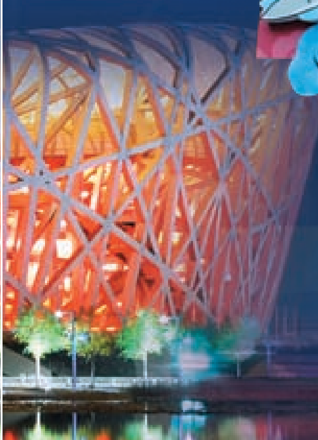
VISA BOC Olympic Games Prepaid Card featuring the Beijing Olympic mascots of "Fuwa"


VISA BOC Olympic Games Card five-ring-five-color series

Specially-designed ATM of BOCHK was installed at the Olympic Equestrian venue

Quality on-site banking services were provided to athletes, audiences, judges and the International Olympic Committee members at the Olympic Equestrian venues

The Beijing 2008 Olympic Flagship Store (Hong Kong) in BOC Tower, the largest of its kind in Hong Kong offering the most comprehensive range of Olympic souvenirs, was well-received by the public

Our staff in smart uniform and high spirit were well prepared to welcome the Beijing Olympics

# INDEPENDENT AUDITOR'S REPORT

**To the shareholders of BOC Hong Kong (Holdings) Limited**
(incorporated in Hong Kong with limited liability)

We have audited the consolidated financial statements of BOC Hong Kong (Holdings) Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 94 to 223, which comprise the consolidated and company balance sheets as at 31 December 2008, and the consolidated income statement, the consolidated and company statements of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

## Directors' responsibility for the financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, and the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

## Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

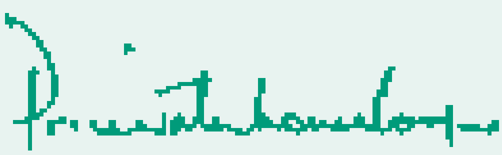
We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2008 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.



**PricewaterhouseCoopers**
*Certified Public Accountants*
Hong Kong, 24 March 2009

# CONSOLIDATED INCOME STATEMENT

| For the year ended 31 December | Notes | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|---|
| Interest income | | **35,281** | 46,056 |
| Interest expense | | **(15,124)** | (26,661) |
| **Net interest income** | 5 | **20,157** | 19,395 |
| Fees and commission income | | **7,214** | 8,177 |
| Fees and commission expenses | | **(2,035)** | (1,903) |
| **Net fees and commission income** | 6 | **5,179** | 6,274 |
| Net trading income | 7 | **1,914** | 1,013 |
| Net (loss)/gain on financial instruments designated at fair value through profit or loss | | **(452)** | 868 |
| Net loss on investment in securities | 8 | **(15)** | (53) |
| Net insurance premium income | 9 | **5,891** | 8,426 |
| Other operating income | 10 | **561** | 771 |
| **Total operating income** | | **33,235** | 36,694 |
| Net insurance benefits and claims | 11 | **(7,709)** | (9,440) |
| **Net operating income before impairment allowances** | | **25,526** | 27,254 |
| Net charge of impairment allowances | 12 | **(12,573)** | (1,448) |
| **Net operating income** | | **12,953** | 25,806 |
| Operating expenses | 13 | **(8,771)** | (7,773) |
| **Operating profit** | | **4,182** | 18,033 |
| Net (loss)/gain from disposal of/fair value adjustments on investment properties | 14 | **(118)** | 1,064 |
| Net gain from disposal/revaluation of properties, plant and equipment | 15 | **7** | 26 |
| Share of profits less losses of associates | 30 | **7** | 3 |
| **Profit before taxation** | | **4,078** | 19,126 |
| Taxation | 16 | **(1,071)** | (3,309) |
| **Profit for the year** | | **3,007** | 15,817 |
| **Attributable to:** | | | |
| Equity holders of the Company | | **3,343** | 15,446 |
| Minority interests | | **(336)** | 371 |
| | | **3,007** | 15,817 |
| **Dividends** | 18 | **4,631** | 9,674 |
| | | **HK$** | HK$ |
| **Earnings per share for profit attributable to the equity holders of the Company** | 19 | **0.3162** | 1.4609 |

The notes on pages 101 to 223 are an integral part of these financial statements.

# CONSOLIDATED BALANCE SHEET

| As at 31 December | Notes | 2008 HK$'m | 2007 HK$'m |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances with banks and other financial institutions | 23 | **153,269** | 159,065 |
| Placements with banks and other financial institutions maturing between one and twelve months | | **89,718** | 53,154 |
| Financial assets at fair value through profit or loss | 24 | **43,812** | 34,440 |
| Derivative financial instruments | 25 | **19,628** | 14,477 |
| Hong Kong SAR Government certificates of indebtedness | | **34,200** | 32,770 |
| Advances and other accounts | 26 | **469,493** | 420,234 |
| Investment in securities | 28 | **291,681** | 301,183 |
| Interests in associates | 30 | **88** | 83 |
| Investment properties | 31 | **7,727** | 8,058 |
| Properties, plant and equipment | 32 | **22,795** | 23,293 |
| Deferred tax assets | 39 | **154** | 23 |
| Other assets | 33 | **14,679** | 20,857 |
| Total assets | | **1,147,244** | 1,067,637 |
| **LIABILITIES** | | | |
| Hong Kong SAR currency notes in circulation | 34 | **34,200** | 32,770 |
| Deposits and balances of banks and other financial institutions | | **88,779** | 60,599 |
| Financial liabilities at fair value through profit or loss | 35 | **21,938** | 11,405 |
| Derivative financial instruments | 25 | **20,450** | 11,092 |
| Deposits from customers | 36 | **802,577** | 793,606 |
| Debt securities in issue at amortised cost | | **1,042** | 2,089 |
| Other accounts and provisions | 37 | **34,873** | 33,344 |
| Current tax liabilities | | **441** | 1,210 |
| Deferred tax liabilities | 39 | **2,799** | 3,967 |
| Insurance contract liabilities | 40 | **28,274** | 22,497 |
| Subordinated liabilities | 41 | **27,339** | – |
| Total liabilities | | **1,062,712** | 972,579 |
| **EQUITY** | | | |
| Share capital | 42 | **52,864** | 52,864 |
| Reserves | 43 | **29,855** | 39,978 |
| Capital and reserves attributable to the equity holders of the Company | | **82,719** | 92,842 |
| Minority interests | | **1,813** | 2,216 |
| Total equity | | **84,532** | 95,058 |
| Total liabilities and equity | | **1,147,244** | 1,067,637 |

The notes on pages 101 to 223 are an integral part of these financial statements.

Approved by the Board of Directors on 24 March 2009 and signed on behalf of the Board by:

**XIAO Gang**
Director

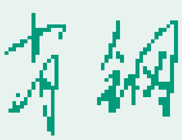
**HE Guangbei**
Director

# BALANCE SHEET

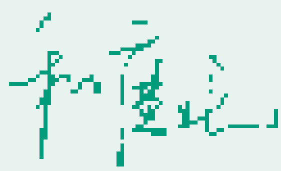
| As at 31 December | Notes | 2008 HK$'m | 2007 HK$'m |
|---|---|---|---|
| **ASSETS** | | | |
| Bank balances | | **337** | 376 |
| Investment in securities | 28 | **1,256** | 4,135 |
| Investment in subsidiaries | 29 | **54,019** | 53,764 |
| Other assets | | **–** | 5,896 |
| | | **55,612** | 64,171 |
| **LIABILITIES** | | | |
| Other accounts and provisions | | **1** | 3 |
| **EQUITY** | | | |
| Share capital | 42 | **52,864** | 52,864 |
| Reserves | 43 | **2,747** | 11,304 |
| Capital and reserve attributable to the equity holders of the Company | | **55,611** | 64,168 |
| Total liabilities and equity | | **55,612** | 64,171 |

The notes on pages 101 to 223 are an integral part of these financial statements.

Approved by the Board of Directors on 24 March 2009 and signed on behalf of the Board by:



**XIAO Gang**
Director



**HE Guangbei**
Director

# CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| | Attributable to equity holders of the Company | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share capital HK$'m | Premises revaluation reserve HK$'m | Reserve for fair value changes of available-for-sale securities HK$'m | Regulatory reserve* HK$'m | Translation reserve HK$'m | Retained earnings HK$'m | Total HK$'m | Minority interests HK$'m | Total equity HK$'m |
| At 1 January 2007 | 52,864 | 6,040 | (115) | 3,621 | – | 22,245 | 84,655 | 1,985 | 86,640 |
| Net profit for the year | – | – | – | – | – | 15,446 | 15,446 | 371 | 15,817 |
| Currency translation difference | – | – | – | – | 14 | – | 14 | – | 14 |
| 2006 final dividend paid | – | – | – | – | – | (4,726) | (4,726) | (79) | (4,805) |
| 2007 interim dividend paid | – | – | – | – | – | (4,525) | (4,525) | (78) | (4,603) |
| Revaluation of premises | – | 2,910 | – | – | – | – | 2,910 | 17 | 2,927 |
| Release upon disposal of premises | – | (23) | – | – | – | 23 | – | – | – |
| Change in fair value of available-for-sale securities taken to equity | – | – | (768) | – | – | – | (768) | 3 | (765) |
| Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities | – | – | 12 | – | – | (115) | (103) | – | (103) |
| Net impairment charges transferred to income statement | – | – | 289 | – | – | – | 289 | – | 289 |
| Release of reserve upon disposal of available-for-sale securities | – | – | 17 | – | – | – | 17 | – | 17 |
| Release of deferred tax | – | (476) | 109 | – | – | – | (367) | (3) | (370) |
| Transfer from retained earnings | – | – | – | 509 | – | (509) | – | – | – |
| At 31 December 2007 | 52,864 | 8,451 | (456) | 4,130 | 14 | 27,839 | 92,842 | 2,216 | 95,058 |
| Company and subsidiaries | 52,864 | 8,451 | (456) | 4,130 | 14 | 27,794 | 92,797 | | |
| Associates | – | – | – | – | – | 45 | 45 | | |
| | 52,864 | 8,451 | (456) | 4,130 | 14 | 27,839 | 92,842 | | |

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| | Attributable to equity holders of the Company | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Share capital HK$'m | Premises revaluation reserve HK$'m | Reserve for fair value changes of available-for-sale securities HK$'m | Regulatory reserve* HK$'m | Translation reserve HK$'m | Retained earnings HK$'m | Total HK$'m | Minority interests HK$'m | Total equity HK$'m |
| At 1 January 2008 | 52,864 | 8,451 | (456) | 4,130 | 14 | 27,839 | 92,842 | 2,216 | 95,058 |
| Net profit for the year | – | – | – | – | – | 3,343 | 3,343 | (336) | 3,007 |
| Currency translation difference | – | – | – | – | 212 | – | 212 | – | 212 |
| 2007 final dividend paid | – | – | – | – | – | (5,149) | (5,149) | (107) | (5,256) |
| 2008 interim dividend paid | – | – | – | – | – | (4,631) | (4,631) | (217) | (4,848) |
| Revaluation of premises | – | (250) | – | – | – | – | (250) | 9 | (241) |
| Release upon disposal of premises | – | (96) | – | – | – | 96 | – | – | – |
| Change in fair value of available-for-sale securities taken to equity | – | – | (12,251) | – | – | – | (12,251) | 4 | (12,247) |
| Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities | – | – | 1 | – | – | (88) | (87) | – | (87) |
| Net impairment charges transferred to income statement | – | – | 7,839 | – | – | – | 7,839 | – | 7,839 |
| Release of reserve upon disposal of available-for-sale securities | – | – | 15 | – | – | – | 15 | – | 15 |
| Release of deferred tax | – | 109 | 727 | – | – | – | 836 | (1) | 835 |
| Transfer from retained earnings | – | – | – | 373 | – | (373) | – | – | – |
| Increase in minority interest arising from capital issuance of a subsidiary | – | – | – | – | – | – | – | 245 | 245 |
| At 31 December 2008 | 52,864 | 8,214 | (4,125) | 4,503 | 226 | 21,037 | 82,719 | 1,813 | 84,532 |
| Company and subsidiaries | 52,864 | 8,214 | (4,125) | 4,503 | 226 | 20,987 | 82,669 | | |
| Associates | – | – | – | – | – | 50 | 50 | | |
| | 52,864 | 8,214 | (4,125) | 4,503 | 226 | 21,037 | 82,719 | | |

* In accordance with the requirements of the HKMA, the amounts are set aside for general banking risks, including future losses or other unforeseeable risks, in addition to the loan impairment allowances recognised under HKAS 39.

The notes on pages 101 to 223 are an integral part of these financial statements.

# STATEMENT OF CHANGES IN EQUITY

| | Attributable to equity holders of the Company | | | |
|---|---|---|---|---|
| | Share capital HK$'m | Reserve for fair value changes of available-for-sale securities HK$'m | Retained earnings HK$'m | Total equity HK$'m |
| At 1 January 2007 | 52,864 | – | 5,965 | 58,829 |
| Net profit for the year (Note 17) | – | – | 14,441 | 14,441 |
| 2006 final dividend paid | – | – | (4,726) | (4,726) |
| 2007 interim dividend paid | – | – | (4,525) | (4,525) |
| Change in fair value of available-for-sale securities taken to equity | – | 149 | – | 149 |
| At 31 December 2007 | 52,864 | 149 | 11,155 | 64,168 |
| At 1 January 2008 | **52,864** | **149** | **11,155** | **64,168** |
| Net profit for the year (Note 17) | **–** | **–** | **1,372** | **1,372** |
| 2007 final dividend paid | **–** | **–** | **(5,149)** | **(5,149)** |
| 2008 interim dividend paid | **–** | **–** | **(4,631)** | **(4,631)** |
| Change in fair value of available-for-sale securities taken to equity | **–** | **(2,879)** | **–** | **(2,879)** |
| Impairment charges transferred to income statement | **–** | **2,730** | **–** | **2,730** |
| At 31 December 2008 | **52,864** | **–** | **2,747** | **55,611** |

The notes on pages 101 to 223 are an integral part of these financial statements.

# CONSOLIDATED CASH FLOW STATEMENT

| For the year ended 31 December | Notes | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating cash inflow before taxation | 44(a) | **7,503** | 37,047 |
| Hong Kong profits tax paid | | **(2,173)** | (2,822) |
| Overseas profits tax paid | | **(131)** | (85) |
| **Net cash inflow from operating activities** | | **5,199** | 34,140 |
| **Cash flows from investing activities** | | | |
| Purchase of properties, plant and equipment | 32 | **(818)** | (1,147) |
| Acquisition of an associate | 30 | **–** | (24) |
| Proceeds from disposal of properties, plant and equipment | | **104** | 40 |
| Proceeds from disposal of investment properties | | **200** | 208 |
| Proceeds from dissolution of an associate | 30 | **–** | 1 |
| Dividends received from associates | 30 | **2** | 3 |
| **Net cash outflow from investing activities** | | **(512)** | (919) |
| **Cash flows from financing activities** | | | |
| Dividends paid to equity holders of the Company | | **(9,780)** | (9,251) |
| Dividends paid to minority shareholders | | **(324)** | (157) |
| Proceeds from capital issuance of a subsidiary | | **245** | – |
| Proceeds from subordinated liabilities | | **28,254** | – |
| Interest paid for subordinated loans | | **(226)** | – |
| **Net cash inflow/(outflow) from financing activities** | | **18,169** | (9,408) |
| Increase in cash and cash equivalents | | **22,856** | 23,813 |
| Cash and cash equivalents at 1 January | | **152,070** | 128,257 |
| **Cash and cash equivalents at 31 December** | 44(b) | **174,926** | 152,070 |

The notes on pages 101 to 223 are an integral part of these financial statements.

# NOTES TO THE FINANCIAL STATEMENTS

## 1. Principal activities

The Company is an investment holding company and its subsidiaries are principally engaged in the provision of banking and related financial services in Hong Kong.

The Company is a limited liability company incorporated and listed in Hong Kong. The address of its registered office is 52/F, Bank of China Tower, 1 Garden Road, Hong Kong.

## 2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below.

These policies have been consistently applied to all the years presented, unless otherwise stated.

### *2.1 Basis of preparation*

The consolidated financial statements of the Group have been prepared in accordance with Hong Kong Financial Reporting Standards (HKFRSs is a collective term which includes all applicable individual Hong Kong Financial Reporting Standards, HKASs and Interpretations) issued by the HKICPA, HK GAAP and the requirements of the Hong Kong Companies Ordinance.

The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale securities, financial assets and financial liabilities (including derivative financial instruments) at fair value through profit or loss, investment properties which are carried at fair value and premises which are carried at fair value or revalued amount less accumulated depreciation and accumulated impairment losses.

The preparation of financial statements in conformity with HKFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 3.

**Newly adopted HKFRSs**

The HKAS 39, 'Financial instruments: Recognition and measurement', amendment on reclassification of financial assets permits reclassification of certain financial assets out of the held-for-trading and available-for-sale categories if specified conditions are met. The related amendment to HKFRS 7, 'Financial instruments: Disclosures', introduces disclosure requirements with respect to financial assets reclassified out of the held-for-trading and available-for-sale categories. The amendment is effective prospectively from 1 July 2008. This amendment does not have any impact on the Group's financial statements as the Group has not reclassified any financial assets.

**Interpretations to existing standards already effective in 2008 but not relevant to the Group's operations**

The following Interpretations to existing standards have already been effective for accounting periods beginning on 1 January 2008 but are not relevant to the Group's operations:

- HK(IFRIC)-Int 11, 'HKFRS 2 Group and Treasury Share Transactions' (effective for annual periods beginning on or after 1 March 2007).

- HK(IFRIC)-Int 12, 'Service Concession Arrangements' (effective for annual periods beginning on or after 1 January 2008).

- HK(IFRIC)-Int 14, 'HKAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction' (effective for annual periods beginning on or after 1 January 2008).

## 2. Summary of significant accounting policies (continued)

### *2.1 Basis of preparation (continued)*

**Standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Group**

The Group has chosen not to early adopt the following standards and an interpretation to an existing standard that were issued but not yet effective for accounting periods beginning on 1 January 2008:

- HKAS 1 (Revised), 'Presentation of financial statements' (effective from 1 January 2009). The revised standard will prohibit the presentation of items of income and expenses (that is, 'non-owner changes in equity') in the statement of changes in equity, requiring 'non-owner changes in equity' to be presented separately from owner changes in equity. All non-owner changes in equity will be required to be shown in a performance statement. Where entities restate or reclassify comparative information, they will be required to present a restated balance sheet as at the beginning comparative period in addition to the current requirement to present balance sheets at the end of the current period and comparative period. The adoption of this revised standard will affect the presentation of the Group's financial statements.

- HKAS 27 (Revised), 'Consolidated and separate financial statements' (effective from 1 July 2009). The revised standard requires changes in a parent's ownership interest in a subsidiary that do not result in the loss of control are accounted for within equity. The standard also specifies the accounting when control is lost. Any remaining interest in the entity is re-measured to fair value and a gain or loss is recognised in income statement. The Group will apply HKAS 27 (Revised) prospectively from 1 January 2010.

- HKFRS 3 (Revised), 'Business combinations' (effective from 1 July 2009). The revised standard continues to apply the acquisition method to business combinations, with some significant changes. For example, all payments to purchase a business are to be recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently re-measured through the consolidated income statement. All acquisition-related costs should be expensed. The Group will apply HKFRS 3 (Revised) to all business combinations (other than common control combination) acquired on or after 1 January 2010.

- HKFRS 8 'Operating Segments' (effective from 1 January 2009). HKFRS 8 will supersede HKAS 14 Segment Reporting, under which segments were identified and reported on risk and return analysis. Items were reported on the accounting policies used for external reporting. Under HKFRS 8, which adopts the 'management approach', segments are components of an entity regularly reviewed by the entity's management. Items are presented based on internal reporting. The Group will adopt HKFRS 8 with effect from 1 January 2009 and will accordingly present segmental information which reflects the operating segments used to make operating decisions at that time.

- HK(IFRIC)-Int 13 'Customer Loyalty Programmes' (effective from 1 July 2008). HK(IFRIC)-Int 13 clarifies that when an entity provides customers with incentives to buy goods or services under a customer loyalty programme (for example, customers accumulate loyalty points to redeem free or discounted products or service), the fair value of the consideration received or receivable in respect of the initial sale shall be allocated between the award credits and the other components of the sale or service. The Group will apply the interpretation from 1 January 2009. It is not expected to have significant impact on the Group's results of operations and financial position.

- There are a number of improvements and amendments to HKFRS published in October 2008 by HKICPA which are not addressed above. The following amendments are unlikely to have a significant impact on the Group's financial statements and have therefore not been analysed in details.

    - HKAS 1 (Amendment), 'Presentation of financial statements' (effective from 1 January 2009)

## 2. Summary of significant accounting policies (continued)

### *2.1 Basis of preparation (continued)*

**Standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Group (continued)**

- HKAS 8, 'Accounting Policies, Changes in Accounting Estimates and Errors' (effective from 1 January 2009)
- HKAS 10, 'Events after the Balance Sheet Date' (effective from 1 July 2009)
- HKAS 18, 'Revenue' (effective from 1 January 2009)
- HKAS 34, 'Interim Financial Reporting' (effective from 1 January 2009)
- HKAS 39 (Amendment), 'Financial instruments: Recognition and measurement' (effective from 1 July 2009)
- HKFRS 5 (Amendment), 'Non-current assets held for sale and discontinued operations' (effective from 1 July 2009)
- HKFRS 7, 'Financial instruments: Disclosures' (effective from 1 January 2009)

**Standards, amendments and interpretations to existing standards that are not yet effective and have been assessed to be not relevant to the Group's operations**

- HKAS 16 (Amendment), 'Property, plant and equipment' (and consequential amendment to HKAS 7, 'Statement of cash flows') (effective from 1 January 2009)
- HKAS 19 (Amendment), 'Employee benefits' (effective from 1 January 2009)
- HKAS 20 (Amendment), 'Accounting for government grants and disclosure of government assistance' (effective from 1 January 2009)
- HKAS 23 (Revised) 'Borrowing costs' (effective from 1 January 2009)
- HKAS 23 (Amendment), 'Borrowing costs' (effective from 1 January 2009)
- HKAS 27 (Amendment), 'Consolidated and separate financial statements' (effective from 1 January 2009)
- HKAS 28 (Amendment), 'Investment in associates' (and consequential amendments to HKAS 32, 'Financial instruments: Presentation' and HKFRS 7, 'Financial instruments: Disclosures') (effective from 1 January 2009)
- HKAS 29 (Amendment), 'Financial reporting in hyperinflationary economies' (effective from 1 January 2009)
- HKAS 31 (Amendment), 'Interests in joint ventures' (and consequential amendments to HKAS 32 and HKFRS 7) (effective from 1 January 2009)
- HKAS 32 (Amendment), 'Financial instruments: Presentation', and HKAS 1 (Amendment), 'Presentation of financial statements', 'Puttable financial instruments and obligations arising on liquidation' (effective from 1 January 2009)

## 2. Summary of significant accounting policies (continued)

### *2.1 Basis of preparation (continued)*

**Standards, amendments and interpretations to existing standards that are not yet effective and have been assessed to be not relevant to the Group's operations (continued)**

- HKAS 38 (Amendment), 'Intangible assets' (effective from 1 January 2009)
- HKAS 40 (Amendment), 'Investment property' (and consequential amendments to HKAS 16) (effective from 1 January 2009)
- HKAS 41 (Amendment), 'Agriculture' (effective from 1 January 2009)
- HKFRS 1 (Amendment), 'First time adoption of HKFRS' and HKAS 27 'Consolidated and separate financial statements' (effective from 1 January 2009)
- HKFRS 2 (Amendment), 'Share-based payment' (effective from 1 January 2009)
- HK(IFRIC)-Int 15, 'Agreements for construction of real estates' (effective from 1 January 2009 and supercedes HK Int-3, 'Revenue – Pre-completion contracts for the sale of development properties)
- HK(IFRIC)-Int 16, 'Hedges of a net investment in a foreign operation' (effective from 1 October 2008)
- HK(IFRIC)-Int 17, 'Distributions of non-cash assets to owners' (effective from 1 July 2009)
- HK(IFRIC)-Int 18, 'Transfers of assets from customers' (effective from 1 July 2009)

### *2.2 Consolidation*

The consolidated financial statements include the financial statements of the Company and all of its subsidiaries made up to 31 December.

#### (1) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group controls the composition of the Board of Directors, controls more than half of the voting power, holds more than half of the issued capital or by any other means that entitle the Group to govern the financial and operating policies of the entities. 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.

For acquisition of a company under common control, the merger accounting method will be applied. The principle of merger accounting is a way to combine companies under common control as though the business of the acquired company had always been carried out by the acquirer. The Group's consolidated financial statements represent the consolidated results, consolidated cash flows and consolidated financial position of the Group as if any such combination had occurred from the date when the Company and the acquired company first came under common control (i.e. no fair value adjustment on the date of combination is required). The difference between the consideration and carrying amount at the time of combination is treated as a merger reserve in equity. The effects of all transactions between the Group and the acquired company, whether occurring before or after the combination, are eliminated in preparing the consolidated financial statements of the Group. The transaction costs for the combination will be expensed in the income statement.

## 2. Summary of significant accounting policies (continued)

### *2.2 Consolidation (continued)*

#### (1) Subsidiaries (continued)

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group not under common control. The cost of such an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed as of the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values as of 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 Group's share of the identifiable net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised 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 Company's balance sheet the investments in subsidiaries are stated at cost less allowance for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

The gain or loss on the disposal of a subsidiary represents the difference between: (a) the proceeds of the sale and, (b) the Group's share of its net assets including goodwill on acquisition net of any accumulated impairment loss and any related accumulated foreign currency translation difference.

Minority interest represent the interests of outside shareholders in the operating results and net assets of subsidiaries.

#### (2) Associates

Associates are all entities over which the Group has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill, net of accumulated impairment loss and any related accumulated foreign currency translation difference.

The Group's share of the post-acquisition profits or losses of associates is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised 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 equals or exceeds its interest in the associate, the Group does not recognise further losses unless the Group has incurred obligations or made payments on behalf of the associates.

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

In the Company's balance sheet the investments in associates are stated at cost less allowance for impairment losses. The results of associates are accounted for by the Company on the basis of dividends received and receivable.

## 2. Summary of significant accounting policies (continued)

### *2.3 Segmental reporting*

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

### *2.4 Foreign currency translation*

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 consolidated financial statements are presented in Hong Kong dollars, which is the Company's functional and presentation currency.

Foreign exchange gains and losses resulting from the settlement of foreign currency transactions using the exchange rates prevailing at the dates of the transactions and monetary assets and liabilities denominated in foreign currencies translated at the rate of exchange at the balance sheet date are recognised directly in the income statement.

Changes in the fair value of monetary securities denominated in foreign currency classified as available-for-sale are analysed between translation differences resulting from changes in the amortised cost of the securities and other changes in the carrying amount of the securities. Translation differences related to changes in the amortised cost are recognised in the income statement, and other changes in the carrying amount are recognised in equity.

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

The results and financial position of all the Group entities that have a functional currency different from Hong Kong dollars are translated into Hong Kong dollars as follows:

- assets and liabilities are translated at the closing rate at the balance sheet date;
- income and expenses are translated at average exchange rates; and
- all resulting exchange differences are recognised in the currency translation reserve in equity.

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

### *2.5 Derivative financial instruments and hedge accounting*

Derivatives are initially recognised at fair value on the date the derivative contract is entered into and are subsequently re-measured at 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 options pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Derivatives are categorised as held for trading unless they are designated as hedges and are effective hedging instruments, then they are subject to measurement under the hedge accounting requirements.

## 2. Summary of significant accounting policies (continued)

### *2.5 Derivative financial instruments and hedge accounting (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).

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 at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement.

The Group designates certain derivatives as hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge). Hedge accounting is used for derivatives designated in this way.

The Group documents at inception the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at the hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values of hedged items. These criteria should be met before a hedge can be qualified to be accounted for under hedge accounting.

Changes in the fair value of derivatives that are designated and qualified as effective fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to the income statement over the period to maturity.

For derivative instruments held for trading changes in their fair value are recognised immediately in the income statement.

### *2.6 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 recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

### *2.7 Interest income and expense and fees and commission income and expense*

Interest income and expense are recognised in the income statement for all financial assets and financial liabilities using the effective interest method.

The effective interest method is a method of calculating the amortised 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 (e.g. prepayment options or incentives relating to residential mortgage loans) but does not consider future credit losses. The calculation includes fees, premiums or discounts and basis points paid or received between parties to the contract, and directly attributable origination fees and costs which represent an integral part of the effective yield are amortised as interest income or expense over the expected life of the financial instrument.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised on the written down value using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Subsequent unwinding of the discount allowance is recognised as interest income.

## 2. Summary of significant accounting policies (continued)

### *2.7 Interest income and expense and fees and commission income and expense (continued)*

Fees and commissions that are not an integral part of the effective yield are recognised on an accrual basis ratably over the period when the related service has been provided, such as administrative fee, asset management fee and custody services fee. Loan syndication fees are recognised 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.

### *2.8 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 financial assets. Management determines the classification of investments at initial recognition. The classification depends on the purpose for which the financial assets were held. All financial assets are recognised initially at fair value. Except for financial assets carried at fair value through profit or loss, all transaction costs of financial assets are included in their amortised costs.

#### (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 incurred principally for the purpose of selling in the short 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. Derivatives are also classified as held for trading unless they are designated as effective hedges.

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

- 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 recognising 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 is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the key management; or
- relates to financial assets containing one or more embedded derivative that significantly modifies the cash flow resulting from those financial assets.

These assets are recognised initially at fair value, with transaction costs taken directly to the consolidated income statement, and are subsequently re-measured at fair value.

Gains and losses from changes in the fair value of such assets (excluding the interest component) are reported in net trading income or net gain/loss on financial instruments designated at fair value through profit or loss. The interest component is reported as part of interest income. Dividends on equity instruments of this category are recognised in the consolidated income statement when the Group's right to receive payment is established.

## 2. Summary of significant accounting policies (continued)

### *2.8 Financial assets (continued)*

#### (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 placements with and advances to banks and other financial institutions, investment debt securities without an active market and loans and advances to customers. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest rate method less allowances for impairment losses.

#### (3) Held-to-maturity

Financial assets classified as held-to-maturity are those 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. They are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method less allowances for impairment losses.

#### (4) Available-for-sale

Financial assets classified as available-for-sale are those 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, and are subsequently measured at fair value. Unrealised gains and losses arising from changes in the fair value of investments are recognised directly in equity, until the financial asset is disposed of or impaired at which time the cumulative gain or loss previously recognised in equity should be transferred to the consolidated income statement. However, interest which includes the amortisation of premium and discount is calculated using the effective interest method and is recognised in the consolidated income statement. Dividends on equity instruments classified as available-for-sale are recognised in the consolidated income statement when the Group's right to receive payment is established.

### *2.9 Financial liabilities*

The Group classifies its financial liabilities under the following categories: trading liabilities, financial liabilities designated at fair value through profit or loss, deposits, debt securities in issue, subordinated liabilities, and other liabilities. All financial liabilities are classified at inception and recognised initially at fair value.

#### (1) Trading liabilities

A financial liability is classified as held for trading if it is incurred principally for the purpose of repurchasing in the short term. Derivatives are also classified as held for trading unless they are designated as effective hedges. It is measured at fair value and any gains and losses from changes in fair value are recognised in the income statement.

## 2. Summary of significant accounting policies (continued)

### *2.9 Financial liabilities (continued)*

#### (2) Financial liabilities designated at fair value through profit or loss

A financial liability can be designated at fair value through profit or loss if it is so designated at inception. Financial liabilities so designated include certain certificates of deposit issued and certain deposits received from customers that are embedded with derivatives. A financial liability is typically so designated if it meets the following criteria:

- eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as 'an accounting mismatch') that would otherwise arise from measuring the financial liabilities or recognising 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 is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the key management; or
- relates to financial liabilities containing one or more embedded derivative that significantly modifies the cash flow resulting from those financial liabilities.

Financial liabilities designated at fair value through profit or loss are measured at fair value and any gains and losses from changes in fair value are recognised in the income statement.

#### (3) Deposits, debt securities in issue, subordinated liabilities and other liabilities

Deposits and debt securities in issue other than those classified as trading liabilities or designated at fair value through profit or loss, together with subordinated liabilities and other liabilities are carried at amortised cost or at cost. Any difference (if available) between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period using the effective interest method.

### *2.10 Recognition and de-recognition of financial instruments*

Purchases and sales of financial assets at fair value through profit or loss, available-for-sale and held-to-maturity are recognised on the trade date, the date on which the Group purchases or sells the assets. Loans and receivables (except investment securities without an active market) are recognised when cash is advanced to the borrowers. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership.

Trading liabilities, financial liabilities designated at fair value through profit or loss and debt securities in issue are recognised on the trade date. Deposits other than trading liabilities are recognised when money is received from customers, other liabilities are recognised when such obligations arise. Financial liabilities are de-recognised from the balance sheet when and only when the obligation specified in the contract is discharged, cancelled or expired. If the Group purchases its own debt, it is removed from the balance sheet, and the difference between the carrying amount of a liability and the consideration paid is included in net trading income.

Securities and bills sold to a counter-party with an obligation to repurchase at a pre-determined price on a specified future date under a repurchase agreement are referred to as Repos. Securities and bills purchased from a counter-party with an obligation to re-sell to the counter-party at a pre-determined price on a specified future date under a resale agreement are referred to as Reverse repos.

## 2. Summary of significant accounting policies (continued)

### *2.10 Recognition and de-recognition of financial instruments (continued)*

Repos or securities lending are initially recorded as due to banks, placements from banks and other financial institutions, as appropriate, at the actual amount of cash received from the counter-party. The financial assets used to collateralise repurchase agreements are recorded as investment securities or financial assets at fair value through profit or loss. Reverse repos or securities borrowing are initially recorded in the balance sheet as cash and due from banks or placements with banks and other financial institutions, as appropriate, at the actual amount of cash paid to the counter-party. The financial assets received as collateral under reverse repurchase agreements are not recorded on the balance sheet. The difference between sale and repurchase price is recognised as interest income or interest expense over the life of the agreements using the effective interest method.

### *2.11 Determination of fair value of financial instruments*

The fair values of financial assets and financial liabilities that are quoted in active markets are based on current bid prices and current ask prices respectively. If the market for financial assets and financial liabilities is not active (such as unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

### *2.12 Precious metals*

Precious metals comprise gold, silver and other precious metals. Precious metals are initially recognised at fair value and subsequently re-measured at their respective market prices as of the balance sheet date. Mark-to-market gains or losses on precious metals are included in net trading income.

### *2.13 Impairment of financial assets*

The Group assesses as of 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 may be impaired includes observable data that comes to the attention of the Group about the following probable 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 payment;

(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 reorganisation;

(v) the disappearance of an active market or downgrading below investment grade level 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.

## 2. Summary of significant accounting policies (continued)

### *2.13 Impairment of financial assets (continued)*

#### (1) Assets carried at amortised cost

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant. 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 together with all other financial assets that are not individually significant or for which impairment has not yet been identified. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

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 recognised 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 collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral.

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.

When a loan is uncollectible, it is written off against the related allowance for impairment losses. 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 impairment losses in the income statement.

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

Loans whose terms have been renegotiated with substantial difference in the terms are no longer considered to be past due but are treated as new loans.

## 2. Summary of significant accounting policies (continued)

### *2.13 Impairment of financial assets (continued)*

#### (2) Assets classified as available-for-sale

If evidence of impairment exists for available-for-sale financial assets, the cumulative losses, measured as the difference between the acquisition cost or amortised cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement, is removed from equity and recognised in the income statement. 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, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement. With respect to equity instruments, such reversals are made through the reserve for fair value change of available-for-sale securities within equity.

### *2.14 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 amortisation, but are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised 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 that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

### *2.15 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 contract between the holder and the debtor.

Financial guarantees are initially recognised as financial liabilities and reported under "Other accounts and provisions" in the financial statements at fair value on the date that the guarantee was given. Subsequent to initial recognition, the Group's liabilities under such guarantees are measured at the higher of (i) the amount determined in accordance with HKAS 37 Provisions, Contingent Liabilities and Contingent Assets and (ii) the amount initially recognised less, where appropriate, cumulative amortisation recognised over the life of the guarantee on a straight-line basis. Any changes in the liability relating to financial guarantees are taken to the income statement.

### *2.16 Fixed assets*

#### (1) Premises, equipment, fixtures and fittings

Premises comprise primarily branches and offices. Premises are shown at fair value based on periodic, but at least annually, valuations by external independent valuers less subsequent depreciation. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. In the intervening periods, the directors review the carrying amount of premises, by reference to the open market value of similar properties, and adjustments are made when there has been a material change. All equipment, fixtures and fittings are stated at historical cost less accumulated depreciation and impairment. Historical cost includes expenditures that are directly attributable to the acquisition and installation of the items.

Subsequent costs are included in an asset's carrying amount or are recognised 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.

## 2. Summary of significant accounting policies (continued)

### *2.16 Fixed assets (continued)*

#### (1) Premises, equipment, fixtures and fittings (continued)

Increases in the carrying amount arising on revaluation of premises are credited to the premises revaluation reserve in shareholders' equity. Decreases that offset previous increases of the same individual asset are charged against premises revaluation reserve directly in equity; all other decreases are expensed in the income statement. Any subsequent increases are credited to the income statement up to the amount previously debited, and then to the premises revaluation reserve. Upon disposal of premises, the relevant portion of the premises revaluation reserve realised in respect of previous valuations is released and transferred from the premises revaluation reserve to retained earnings.

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

| | |
|---|---|
| • Premises | Over the remaining period of lease |
| • Equipment, fixtures and fittings | 3-15 years |

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

At each balance sheet date, both internal and external sources of information are considered to determine whether there is any indication that premises, equipment, fixtures and fittings are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment loss is recognised in the income statement except where the asset is carried at valuation and the impairment loss does not exceed the revaluation surplus for that same asset, in which case it is treated as a revaluation decrease. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. Impairment loss is reversed through the premises revaluation reserve or income statement as appropriate.

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) Property under development

Property under development represents assets under construction or being installed and is stated at cost less impairment losses. Cost includes equipment cost, cost of development, construction, installation, interest and other direct costs attributable to the development. Items classified as property under development are transferred to premises or investment properties when such assets are ready for their intended use, and the depreciation charge commences from the month such assets are transferred to premises.

Impairment losses are recognised for idle projects with respect to which management has determined that resumption in the foreseeable future is not probable. The impairment loss is equal to the extent to which the estimated recoverable amount of a specific project is less than its carrying amount. The recoverable amount is the asset's fair value less costs to sell. Impairment losses or reversals are charged to the income statement.

### *2.17 Investment properties*

Properties that are held for long-term rental yields or for capital appreciation or both, and that are not occupied by the companies in the Group, are classified as investment properties. Properties leased out within group companies are classified as investment properties in individual companies' financial statements and as premises in consolidated financial statements. Land held under operating lease is classified and accounted for as investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it is a finance lease.

## 2. Summary of significant accounting policies (continued)

### *2.17 Investment properties (continued)*

Investment properties are recognised initially at cost, including related transaction costs. After initial recognition, investment properties are measured at fair value assessed by professional valuers on the basis of open market value. If this information is not available, alternative valuation methods are used such as recent prices on less active markets or discounted cash flow projections. These valuations are performed in accordance with the guidance issued by the International Valuation Standards Committee.

Subsequent expenditure is charged to the asset's carrying amount 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 expensed in the income statement during the financial period in which they are incurred.

Any changes in fair value are reported directly in the income statement. Deferred income tax is provided on revaluation surpluses of investment properties in accordance with HKAS-Int 21 "Income Taxes – Recovery of Revalued Non-Depreciable Assets" on HKAS 12 "Income Taxes".

If an investment property becomes owner-occupied, it is reclassified as premises, and its fair value at the date of reclassification becomes its cost for accounting purposes. If an item of premises becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of this item at the date of transfer is recognised in equity as a revaluation of premises under HKAS 16 "Property, Plant and Equipment". However, if a fair value gain reverses a previous revaluation loss or impairment loss, the gain is recognised in the income statement up to the amount previously debited.

### *2.18 Leases*

#### (1) Operating leases

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 recognised as an expense in the period in which termination takes place.

Where the Group is a lessor, the land and buildings subject to the operating lease are accounted for as investment properties. Rental income from operating leases is recognised on a straight-line basis over the lease term.

#### (2) Finance leases on properties

Where the land and buildings elements of leasehold properties held for own use can be split reliably at inception of the lease, leasehold land and land use rights are recognised as operating leases if they have indefinite economic lives. The up-front prepayments made or other costs incurred for acquiring the leasehold land and land use rights are expensed in the income statement on a straight-line basis over the period of the lease. Where there is impairment of the up-front prepayments, the impairment is expensed in the income statement immediately. Where the land and buildings cannot be split reliably at inception of the lease, the land and buildings elements will continue to be treated as finance leases and measured at fair value.

Separate measurements of the land and buildings elements are not required when the Group's interest in both land and buildings is classified as investment properties as if they are finance leases and are measured at fair value.

## 2. Summary of significant accounting policies (continued)

### *2.18 Leases (continued)*

#### (2) Finance leases on properties (continued)

Pursuant to the Bank of China (Hong Kong) Limited (Merger) Ordinance ("Merger Ordinance") 2001, all assets and liabilities of the designated branches and subsidiaries, and the shares of certain entities of the legacy Bank of China Group in Hong Kong were effectively transferred to BOCHK, which was immediately owned by the then newly formed BOC Hong Kong (Holdings) Limited ("the Merger"). This was a significant event and the Group has therefore adopted the valuation at the date of the Merger as the deemed cost for its leasehold properties to reflect the circumstances at the time of the Merger.

On adoption of the deemed cost at the date of Merger, the Group made reference to the independent property valuation conducted as at 31 August 2001 for the purpose of the Merger, which did not split the values of the leasehold properties between the land and buildings elements. Any means of subsequent allocation of the valuation of the leasehold properties at the date of Merger between the land and buildings elements would be notional and therefore would not represent reliable information. It is determined that the values of the land and buildings elements of the Group's leasehold properties cannot be reliably split and the leasehold properties are treated as finance leases. The Group has also adopted the revaluation model under HKAS 16 "Property, Plant and Equipment" by which assets held for own use arising under these finance leases are measured at fair value less any accumulated depreciation and impairment losses.

### *2.19 Insurance contracts*

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

The Group's insurance subsidiary follows the local regulatory requirements to measure its insurance contract liabilities.

The Group's insurance subsidiary issues insurance contracts that transfer significant insurance risk. As a general guideline, the Group defines significant insurance risk as 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's insurance subsidiary issues long term business insurance contracts, which insure events associated with human life (for example death, survival, or total permanent disability) over a long duration. A liability for contractual benefits that are expected to be incurred in the future is recorded when premiums are recognised.

For linked long term insurance contracts with embedded derivatives (which are closely related to the host insurance contracts) 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 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 recognised.

Retirement scheme management category III insurance contracts, as defined in the Insurance Companies Ordinance, insure events associated with human life under retirement schemes. A liability for contractual benefits that are expected to be incurred in the future is recorded when premiums are recognised. The portion of the 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 recognised as revenue when they become payable by the contract holders before the deduction of commissions. Benefits and claims are recorded as an expense when they are incurred.

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).

## 2. Summary of significant accounting policies (continued)

### *2.19 Insurance contracts (continued)*

#### (2) Liability adequacy test

At each balance sheet date, liability adequacy tests are performed to ensure the adequacy of the insurance contract liabilities. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from the assets backing such liabilities, are used. Any deficiency is immediately charged to the consolidated income statement, with a provision established for losses arising from the liability adequacy test.

### *2.20 Cash and cash equivalents*

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise balances with original maturity less than three months from the date of acquisition, including cash, balances with banks and other financial institutions, short-term bills and notes classified as investment securities and certificates of deposit.

### *2.21 Provisions*

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

### *2.22 Employee benefits*

#### (1) Retirement benefit costs

The Group contributes to defined contribution retirement schemes under either recognised ORSO schemes or MPF schemes that are available to the Group's employees. Contributions to the schemes by the Group and employees are calculated as a percentage of employees' basic salaries for the ORSO schemes and in accordance with the MPF rules for MPF schemes. The retirement benefit scheme costs are charged to the income statement as incurred and represent contributions payable by the Group to the schemes. Contributions made by the Group that are forfeited by those employees who leave the ORSO scheme prior to the full vesting of their entitlement to the contributions are used by the Group to reduce the existing level of contributions or to meet its expenses under the trust deed of the ORSO schemes.

The assets of the schemes are held in independently-administered funds separate from those of the Group.

#### (2) Leave entitlements

Employee entitlements to annual leave and sick leave are recognised when they accrue to employees. A provision is made for the estimated liability for unused annual leave and the amount of sick leave expected to be paid as a result of services rendered by employees up to the balance sheet date.

Compensated absences other than annual leave and sick leave are non-accumulating; they lapse if the current period's entitlement is not used in full and do not entitle employees to a cash payment for unused entitlement on leaving the Group. Such compensated absences are recognised when the absences occur.

#### (3) Bonus plans

The expected cost of bonus payments are recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made. Liabilities for bonus plans are expected to be settled within twelve months and are measured at the amounts expected to be paid when they are settled.

## 2. Summary of significant accounting policies (continued)

### *2.23 Current and deferred income taxes*

Tax expenses for the period comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised directly in equity. In this case, the tax is also recognised in equity.

Income tax payable on profits, based on the applicable tax law enacted or substantially enacted at the balance sheet date in each jurisdiction where the Company and the subsidiaries and associates operate and generate taxable income, is recognised as a current income tax expense in the period in which profits arise.

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 realised or the deferred income tax liability is settled.

The principal temporary differences arise from asset impairment provisions, depreciation of property and equipment, revaluation of certain assets including available-for-sale securities and properties, and tax losses carried forward. However, the deferred income tax is not recognised 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 liabilities are provided in full on all taxable temporary differences and deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is charged or credited in the income statement except for deferred income tax relating to fair value re-measurement of available-for-sale investments and revaluation of premises which are charged or credited directly to equity, in which case the deferred income tax is also credited or charged directly to equity and is subsequently recognised in the income statement together with the realisation of the deferred gain and loss.

### *2.24 Repossessed assets*

Repossessed assets are initially recognised at the lower of their fair value less costs to sell and the amortised cost of the related outstanding loans on the date of repossession, and the related loans and advances together with the related impairment allowances are derecognised from the balance sheet. Subsequently, repossessed assets are measured at the lower of their cost and fair values less costs to sell and are reported as ‘Non-current assets held for sale’ under ‘Other assets’.

### *2.25 Fiduciary activities*

The Group commonly acts as a trustee, or in other fiduciary capacities, that result in its holding or managing assets on behalf of individuals, trusts and other institutions. These assets and any income or losses arising thereon are excluded from these financial statements, as they are not assets of the Group.

### *2.26 Contingent liabilities and contingent assets*

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

## 2. Summary of significant accounting policies (continued)

### *2.26 Contingent liabilities and contingent assets (continued)*

A contingent liability is not recognised 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 recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain events not wholly within the control of the Group.

Contingent assets are not recognised but are disclosed in the notes to the financial statements when an inflow of economic benefits is probable. When the inflow is virtually certain, it will be recognised as an asset.

### *2.27 Related parties*

For the purposes of these financial statements, a party is considered to be related to the Group if the Group has the ability, directly and indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control. Related parties may be individuals or entities.

## 3. 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 judgements 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 judgements, which affect the carrying amount of assets and liabilities, are set out below. The effect of changes to either the key assumptions or other estimation uncertainties will be presented below if it is practicable to determine. It is possible that actual results may require material adjustments to the estimates referred to below.

### *3.1 Impairment allowances on loans and advances*

The Group reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgements 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 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.

### *3.2 Impairment of held-to-maturity and available-for-sale investments*

The Group reviews its held-to-maturity and available-for-sale investment portfolios to assess impairment at least on a quarterly basis. In determining whether any of these investments is impaired, risk characteristics and performance such as external credit rating, market price etc will be assessed. The Group makes estimates on the default rate and loss severity of each investment with reference to market performance of the portfolios, current payment status of the issuers or performance of the underlying assets, or economic conditions that correlate with defaults on the collateralised assets.

## 3. Critical accounting estimates and judgements in applying accounting policies (continued)

### *3.2 Impairment of held-to-maturity and available-for-sale investments (continued)*

For asset/mortgage backed securities ("ABS/MBS"), the Group adopts a comprehensive methodology in determining whether a particular security is impaired. Under the methodology, the Group will not only take into consideration the mark-to-market (MTM) price of the issue and its external credit rating, but also other factors including the FICO score, vintage, location, adjustable rate mortgage ("ARM") status, delinquencies, level of collateral protection, loan to value ratio and prepayment speed of the underlying assets. Having considered these factors, the ABS/MBS issue has to further pass the required credit enhancement coverage ratio set by the Group. This ratio is determined by applying assumptions regarding the default rates based on the available delinquency, foreclosure and real estate owned ("REO") data of the ABS/MBS issue.

The methodology and assumptions used for the assessments are reviewed regularly. In evaluating impairment of ABS/MBS during the year, the Group continued to consider a significant decline in market prices of ABS/MBS to be a key indicator of impairment. In addition, due to reduced market liquidity and wider dispersion in indicative prices of certain ABS/MBS held by the Group, the Group also ensured that there was additional objective evidence of credit impairment by considering whether there has been a significant adverse change in the credit enhancement coverage ratio, taking into account the reported delinquencies and credit losses incurred in the underlying mortgage portfolio for each security held by the Group.

Many of the ABS/MBS held by the Group are complex, and involve cashflows over many years. These future cashflows depend on economic factors such as US residential real estate prices and the performance of the US economy. The recoverable amounts of the securities therefore cannot be predicted with certainty at the current balance sheet date, and additional impairment charges – or releases of impairment charges – may be required in future accounting periods.

### *3.3 Fair values of derivatives financial instruments*

The fair values of derivatives 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 with built-in functions available in externally acquired financial analysis or risk management systems widely used by the industry. To the extent practical, the models use only observable data.

### *3.4 Fair value of structured investment vehicle*

One of the Group's non-banking subsidiaries has invested in a structured investment vehicle managed by a third party portfolio manager, which is included in the Group's investment portfolio classified as financial assets at fair value through profit or loss. As there is no active market for this investment, management has assessed the fair value with reference to valuation received from the third party portfolio manager. As at 31 December 2008, the net carrying amount of this investment in the structured investment vehicle was approximately HK$57 million (2007: approximately HK$100 million).

### *3.5 Held-to-maturity investments*

The Group follows the guidance of HKAS 39 in classifying certain non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgement. In making this judgement, 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 HKAS 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. The investments would then be measured at fair value and not amortised cost.

## 3. Critical accounting estimates and judgements in applying accounting policies (continued)

### *3.6 Estimate of future benefit payments and premiums arising from long term insurance contracts*

In determining the Group's long term business fund liabilities under insurance contracts, the Group follows the Insurance Companies Ordinance (Determination of Long Term Liabilities) Regulation and makes prudent assumptions which include appropriate margins for adverse deviation of the relevant factors. Estimates are made as to the expected number of deaths for each of the years in which the Group is exposed to risk. The Group bases these estimates on standard industry and Hong Kong Assured Lives Mortality Table HKA01 that reflect recent historical mortality experience, adjusted where appropriate to reflect the Group's own experience. For contracts that insure the risk of longevity, appropriate prudent allowances are made for expected mortality improvements. The estimated number of deaths determines the value of the benefit payments and the value of the valuation premiums. The main source of uncertainty is that epidemics such as AIDS, SARS, avian flu and wide-ranging lifestyle changes, such as in eating, smoking and exercise habits, could result in future mortality being significantly worse than in the past for the age groups in which the Group has significant exposure to mortality risk. However, continuing improvements in medical care and social conditions could result in improvements in longevity in excess of those allowed for in the estimates used to determine the liability for contracts where the Group is exposed to longevity risk.

Were the number of deaths in future years to differ by 10% from management's estimate, the long term business fund liability would increase by approximately HK$106 million (2007: HK$72.6 million), which accounts for 0.39% (2007: 0.36%) of the liability. In this case, it is assumed there is no relief arising from reinsurance contracts held.

For linked long term insurance contracts with a life cover component, it is assumed that the Group will be able to increase mortality risk charges in future years in line with emerging mortality experience.

Estimates are also made as to future investment income arising from the assets backing long term insurance contracts. These estimates are based on current market returns as well as expectations about future economic and financial developments. Were the average future investment returns to decrease by 50 basis points from management's estimates, the long term business fund liability would increase by approximately HK$998 million (2007: approximately HK$1,009 million). In this case, there is no relief arising from reinsurance contracts held.

The Group has also assessed whether a provision for expense is necessary in accordance with the Insurance Companies Ordinance. A provision for expense is the amount to meet the total net cost that would likely be incurred in fulfilling contracts if the Group were to cease to transact new business 12 months after the valuation date. In the calculation of expense reserve, the Group has assumed it will carry on selling new business rather than ceases in 12 months period.

A resilience reserve was set up and included in long term business fund liabilities in accordance with the Insurance Companies Ordinance (Determination of Long Term Liabilities) Regulations to provide a prudent provision against the effects of possible future changes to the value of the assets to meet the liabilities. The resilience reserve was set up based on the appointed actuary advice of a 15 basis points (2007: 50 basis points) change in market yield of the underlying assets and valuation interest rates. The amount of resilience reserve to be set up depends on the degree of change in interest rate assumed.

### *3.7 Provision*

The Group uses judgment to assess whether the Group has a present legal or constructive obligation as a result of past events at each balance sheet date, and judgment is used to determine if it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and to determine a reliable estimate of the amount of the obligation.

## 4. Financial risk management

The Group is exposed to financial risks as a result of engaging in a variety of business activities. The principal financial risks are credit risk, market risk (including currency risk and interest rate risk) and liquidity risk. This note summarises the Group's exposures to these risks, as well as its objectives, policies and processes for managing and the methods used to measure these risks.

### *Financial risk management framework*

The Group's management governance structure is designed to cover all business processes and ensure various risks are properly managed and controlled in the course of conducting business. The Group has a robust risk management organisational structure with a comprehensive set of policies and procedures to identify, measure, monitor and control various risks that may arise. These risk management policies and procedures are regularly reviewed and modified to reflect changes in markets and business strategies. Various groups of risk takers assume their respective responsibilities for risk management.

The Board of Directors, representing the interests of shareholders, is the highest decision making authority of the Group and has the ultimate responsibility for risk management. The Board, with the assistance of the Risk Committee, has the primary responsibility for the formulation of risk management strategies and for ensuring that the Group has an effective risk management system to implement these strategies.

The Risk Committee ("RC"), a standing committee established by the Board of Directors, is responsible for overseeing the Group's various types of risks, reviewing and approving high-level risk-related policies and overseeing their implementation, reviewing significant or high risk exposures or transactions and exercising its power of veto if it considers that any transaction should not proceed.

The Chief Executive ("CE") is responsible for managing the Group's various types of risks, approving detailed risk management policies, and approving material risk exposures or transactions within his authority delegated by the Board of Directors. The Chief Risk Officer ("CRO") assists the CE in fulfilling his responsibilities for the day-to-day management of risks. The CRO is responsible for initiating new risk management strategies, projects and measures that will enable the Group to better monitor and manage new risk issues or areas that may arise from time to time from new businesses, products and changes in the operating environment. He may also take appropriate initiatives in response to regulatory changes. The CRO is also responsible for reviewing material risk exposures or transactions within his delegated authority and exercising his power of veto if he believes that any transaction should not proceed.

The Group has put in place appropriate internal control systems, including establishment of an organisation structure that sets adequately clear lines of authority and responsibility for monitoring compliance with policies, procedures and limits. Proper reporting lines also provide sufficient independence of the control functions from the business areas, as well as adequate segregation of duties throughout the organisation which helps to promote an appropriate internal control environment.

### *Product development*

To ensure effective risk assessment and monitoring, the Group developed a comprehensive product development and management framework which clearly defines the roles and responsibilities of all related units, and the proper risk assessment procedures for the product development process.

In accordance with the strategic objectives set by the Management, the respective product management units are responsible for formulating business and product development plans, and the department of strategic development shall ensure the plans are aligned with the Bank's overall strategies. Departments that are responsible for risk management, legal and compliance and finance etc. are accountable for risk assessment and review.

Apart from product development, the respective business units shall work closely with relevant risk evaluating departments to identify and assess all the related risks. Based on the consideration of segregation of duties, risk evaluating departments shall conduct independent review on risk management procedures and assessment results. Products can only be launched after the risk management procedures are fulfilled and endorsed by all risk evaluating departments.

## 4. Financial risk management (continued)

### *4.1 Credit Risk*

Credit risk is the risk that a customer or counterparty will be unable to or unwilling to meet its obligations under a contract. It arises principally from lending, trade finance and treasury businesses including inter-bank transactions, investments in bonds and securities.

**Credit risk management framework**

The Group has formulated a comprehensive set of credit risk management policies and procedures, and appropriate credit risk limits to manage and control credit risk that may arise. These policies, procedures and credit risk limits are regularly reviewed to cope with changes in market conditions and business strategies.

The Group's organisation structure establishes a clear set of authority and responsibility for monitoring compliance with policies, procedures and limits.

The Chief Credit Officer ("CCO") reports directly to the CRO and is responsible for the management of credit risk and for the formulation of all credit policies and procedures. Various units of the Group have their respective credit risk management responsibilities. Business units act as the first line of defense while risk management units, which are independent from the business units, are responsible for the day-to-day management of credit risks. The Risk Management Department ("RMD") has the primary responsibility for drafting, reviewing and updating credit risk management policies and procedures. The Group's principal banking subsidiaries, Nanyang, Nanyang (China), and Chiyu, have also formulated their own credit risk policies that are consistent with those of the Group. These subsidiaries execute their risk management strategies independently and report to the Group's management on a regular basis.

The Board of Directors delegates credit approval authority to the CE. The CE can further delegate to the subordinates within his limit authorised by the Board of Directors. The Group sets the limits of credit approval authority according to the business nature, rating, the level of transaction risk, and the extent of the credit exposure.

**Credit risk measurement and control**

In view of the rapidly changing market conditions since the outbreak of the Subprime crisis, the Bank has been continuously revisiting its lending strategies and conducting rigorous reviews on the concerned portfolios.

<u>Loans and advances</u>

Different credit approval and control procedures are adopted according to the level of risk associated with the customer, counterparty or transaction. Corporate and financial institution credit applications are independently reviewed, objectively assessed and monitored by risk management units. A small business credit scorecard as a supplemental tool is used to assist the credit assessment of small enterprise credit facilities. A credit scoring system is used to process retail credit transactions, including residential mortgage loans, personal loans and credit cards while a bank scorecard is used to assist the risk assessment of financial institutions' credit risk. The Credit Risk Assessment Committee comprising experts from the Group's credit and other functions is responsible for making an independent assessment of all credit facilities which require the approval of Deputy Chief Executives or above.

RMD provides regular credit management information reports and ad hoc reports to the Management Committee ("MC"), RC and Board of Directors to facilitate their continuous monitoring of credit risk.

The Group identifies credit concentration risk by industry, geography, customer and counterparty risk. The Group monitors changes to counterparties credit risk, quality of the credit portfolio and risk concentrations, and reports regularly to the Group's management.

The Group's internal loan grading system divides credit assets into 5 categories with reference to HKMA's guidelines.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Credit risk measurement and control (continued)**

Loans and advances (continued)

"Pass" represents loans where the borrower is current in meeting its repayment obligations and full repayment of interest and principal is not in doubt.

"Special Mention" represents loans where the borrowers are experiencing difficulties which may threaten the Group's position. Ultimate loss is not expected at this stage but could occur if adverse conditions persist.

"Substandard" represents loans where the borrower displays a definable weakness that is likely to jeopardise repayment.

"Doubtful" represents loans where collection in full is improbable and the Group expects to sustain a loss of principal and/or interest, taking into account the net realisable value of the collateral.

"Loss" represents loans which are considered uncollectible after all collection options (such as the realisation of collateral or the institution of legal proceedings) have been exhausted.

Debt securities and derivatives

For investments in debt securities and securitisation assets, the external credit rating and assessment on credit quality of the underlying assets are used for managing the credit risk involved. Credit limits are established on a customer and security issuer basis. For derivatives, the Group sets customer limits to manage the credit risk involved and follows the same approval and control processes as loans and advances. On-going monitoring procedures are established.

The Group adopts a comprehensive methodology in determining whether a particular asset/mortgage backed security ("ABS/MBS") is impaired. Under the methodology, the Group will not only take into consideration the mark-to-market (MTM) price of the issue and its external credit rating, but also other factors including the FICO score, vintage, location, adjustable rate mortgage ("ARM") status, delinquencies, level of collateral protection, loan to value ratio and prepayment speed of the underlying assets. Having considered these factors, the ABS/MBS issue has to further pass the required credit enhancement coverage ratio set by the Group. This ratio is determined by applying assumptions regarding the default rates based on the available delinquency, foreclosure and real estate owned ("REO") data of the ABS/MBS issue.

Settlement risk arises mainly from foreign exchange transactions with counterparties and also from derivatives in any situation where a payment in cash, securities or equities is made in the expectation of a corresponding receipt in cash, securities or equities. Daily settlement limits are established for each counterparty or customer to cover all settlement risk arising from the Group's market transactions on any single day.

**Collateral held as security and other credit enhancements**

The valuation and management of collateral have been documented in the policy covering acceptance criteria, validity of collateral, loan-to-value ratio, haircut ratio, valuation and insurance, etc. The collateral is revalued on a regular basis, though the frequency and the method used varies with the type of collateral involved and the nature and the risk of the underlying credit. The Group has established a mechanism to update the value of its main type of collateral, real properties, with the use of public indices on a portfolio basis. Collateral is insured with the Group as the beneficiary. In the personal sector, the main types of collateral are real properties, cash deposits, securities and investment funds. In the commercial and industrial sector, the main types of collateral are real properties, securities, receivables, cash deposits and machinery.

For loans guaranteed by a third party guarantor, the Group will assess the guarantor's financial condition, credit history and ability to meet obligations.

As at 31 December 2008 and 2007, the Group did not hold any collateral permitted to sell or re-pledge in the absence of default by the borrower.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Credit exposures**

Maximum exposures to credit risk before collateral held or other credit enhancements are summarised as follows:

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Credit risk exposures relating to on-balance sheet assets are as follows: | | |
| Cash and balances with banks and other financial institutions | **153,269** | 159,065 |
| Placements with banks and other financial institutions maturing between 1 and 12 months | **89,718** | 53,154 |
| Financial assets at fair value through profit or loss | | |
| – debt securities | **41,438** | 30,856 |
| Derivative financial instruments | **19,628** | 14,477 |
| Hong Kong SAR Government certificates of indebtedness | **34,200** | 32,770 |
| Advances and other accounts | **469,493** | 420,234 |
| Investment in securities | | |
| – debt securities – available-for-sale | **170,935** | 100,073 |
| – debt securities – held-to-maturity | **106,465** | 165,428 |
| – debt securities – loans and receivables | **12,595** | 31,102 |
| Other assets | **13,332** | 20,857 |
| Credit risk exposures relating to off-balance sheet items are as follows: | | |
| Letters of guarantee issued | **11,838** | 9,407 |
| Loan commitment and other credit related liabilities | **241,551** | 221,896 |
| | **1,364,462** | 1,259,319 |

**Gross loans and advances**

Gross loans and advances before loan impairment allowances are summarised by product type as follows:

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Advances to customers | | |
| Personal | | |
| – Mortgages | **130,980** | 121,663 |
| – Credit cards | **6,445** | 5,641 |
| – Others | **14,359** | 14,404 |
| Corporate | | |
| – Commercial loans | **284,108** | 247,079 |
| – Trade finance | **24,555** | 24,275 |
| | **460,447** | 413,062 |
| Trade bills | **7,609** | 5,334 |
| Advances to banks and other financial institutions | **3,738** | 3,223 |
| Total | **471,794** | 421,619 |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

Advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid. Advances repayable by regular instalments are classified as overdue when an instalment payment is past due and remains unpaid. Advances repayable on demand are classified as overdue either when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instruction or when the advances have remained continuously outside the approved limit that was advised to the borrower.

A financial asset 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 and that loss event(s) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

If there is objective evidence that an impairment loss on loans has been incurred, the amount of loss is measured as the difference between the carrying amount and the present value of estimated future cash flows generated by the financial asset. Objective evidence that a financial asset is impaired includes observable data that comes to the attention of the holder of the asset about the loss events.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include:

– Significant financial difficulty incurred by the borrower;

– A breach of contract, such as a default or delinquency in interest or principal payment;

– For economic or legal reasons related to the borrower's financial difficulty, the Group has granted to the borrower a concession that it would not otherwise consider;

– Probable that the borrower will become bankrupt or undergo other financial reorganisation; or

– Other observable data indicating that there is a measurable decrease in the estimated future cash flows from such loans and advances.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(a) Advances neither overdue nor impaired*

Advances that were neither overdue nor impaired are analysed by internal credit grades as follows:

| | **2008** | | | |
|---|---|---|---|---|
| | **Pass HK$'m** | **Special mention HK$'m** | **Substandard or below HK$'m** | **Total HK$'m** |
| Advances to customers | | | | |
| Personal | | | | |
| – Mortgages | **128,545** | **155** | **88** | **128,788** |
| – Credit cards | **6,179** | **–** | **–** | **6,179** |
| – Others | **13,839** | **75** | **10** | **13,924** |
| Corporate | | | | |
| – Commercial loans | **275,844** | **6,349** | **274** | **282,467** |
| – Trade finance | **23,381** | **538** | **5** | **23,924** |
| | **447,788** | **7,117** | **377** | **455,282** |
| Trade bills | **7,084** | **523** | **2** | **7,609** |
| Advances to banks and other financial institutions | **3,738** | **–** | **–** | **3,738** |
| Total | **458,610** | **7,640** | **379** | **466,629** |

| | 2007 | | | |
|---|---|---|---|---|
| | Pass HK$'m | Special mention HK$'m | Substandard or below HK$'m | Total HK$'m |
| Advances to customers | | | | |
| Personal | | | | |
| – Mortgages | 118,583 | 229 | 112 | 118,924 |
| – Credit cards | 5,397 | – | – | 5,397 |
| – Others | 13,737 | 78 | 20 | 13,835 |
| Corporate | | | | |
| – Commercial loans | 243,140 | 908 | 349 | 244,397 |
| – Trade finance | 23,052 | 795 | 4 | 23,851 |
| | 403,909 | 2,010 | 485 | 406,404 |
| Trade bills | 5,255 | 74 | 1 | 5,330 |
| Advances to banks and other financial institutions | 3,223 | – | – | 3,223 |
| Total | 412,387 | 2,084 | 486 | 414,957 |

The occurrence of loss event(s) may not necessarily result in impairment loss where the loans are fully collateralised. While such loans are of "substandard" or lower grades, they are regarded as not being impaired and have been included in the above table.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(b) Advances overdue but not impaired*

The gross amount of advances overdue but not impaired is analysed as follows:

| | 2008 | | | | | |
|---|---|---|---|---|---|---|
| | **Overdue for 3 months or less HK$'m** | **Overdue for 6 months or less but over 3 months HK$'m** | **Overdue for 1 year or less but over 6 months HK$'m** | **Overdue for over 1 year HK$'m** | **Total HK$'m** | **Market value of collateral HK$'m** |
| Advances to customers | | | | | | |
| Personal | | | | | | |
| – Mortgages | **2,065** | **34** | **12** | **30** | **2,141** | **4,870** |
| – Credit cards | **237** | **–** | **–** | **–** | **237** | **–** |
| – Others | **318** | **3** | **3** | **32** | **356** | **731** |
| Corporate | | | | | | |
| – Commercial loans | **832** | **8** | **9** | **156** | **1,005** | **2,437** |
| – Trade finance | **81** | **4** | **–** | **15** | **100** | **178** |
| Total | **3,533** | **49** | **24** | **233** | **3,839** | **8,216** |

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Overdue for 3 months or less HK$'m | Overdue for 6 months or less but over 3 months HK$'m | Overdue for 1 year or less but over 6 months HK$'m | Overdue for over 1 year HK$'m | Total HK$'m | Market value of collateral HK$'m |
| Advances to customers | | | | | | |
| Personal | | | | | | |
| – Mortgages | 2,465 | 77 | 45 | 48 | 2,635 | 5,634 |
| – Credit cards | 221 | – | – | – | 221 | – |
| – Others | 428 | 3 | 12 | 31 | 474 | 875 |
| Corporate | | | | | | |
| – Commercial loans | 1,997 | 54 | 42 | 203 | 2,296 | 4,509 |
| – Trade finance | 315 | 7 | 2 | 11 | 335 | 410 |
| | 5,426 | 141 | 101 | 293 | 5,961 | 11,428 |
| Trade bills | 4 | – | – | – | 4 | – |
| Total | 5,430 | 141 | 101 | 293 | 5,965 | 11,428 |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

(b) *Advances overdue but not impaired (continued)*

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Current market value of collateral held against the covered portion of advances to customers | **8,216** | 11,428 |
| Covered portion of advances to customers | **3,341** | 4,929 |
| Uncovered portion of advances to customers | **498** | 1,032 |

(c) *Impaired advances*

Advances individually identified to be impaired are analysed by product type as follows:

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Gross advances HK$'m** | **Market value of collateral HK$'m** | Gross advances HK$'m | Market value of collateral HK$'m |
| Advances to customers | | | | |
| Personal | | | | |
| – Mortgages | **51** | **50** | 104 | 95 |
| – Credit cards | **29** | **–** | 23 | – |
| – Others | **79** | **21** | 95 | 54 |
| Corporate | | | | |
| – Commercial loans | **636** | **434** | 386 | 392 |
| – Trade finance | **531** | **205** | 89 | 18 |
| Total | **1,326** | **710** | 697 | 559 |
| Loan impairment allowances made in respect of such advances | **829** | | 403 | |

The loan impairment allowances were made after taking into account the value of collateral in respect of impaired advances.

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Current market value of collateral held against the covered portion of advances to customers | **710** | 559 |
| Covered portion of advances to customers | **628** | 410 |
| Uncovered portion of advances to customers | **698** | 287 |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(c) Impaired advances (continued)*

Classified or impaired advances to customers are analysed as follows:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Gross classified or impaired advances to customers | **2,138** | 1,803 |
| Gross classified or impaired advances to customers as a percentage of gross advances to customers | **0.46%** | 0.44% |
| Individually assessed loan impairment allowances made in respect of such advances | **800** | 381 |

Classified or impaired advances to customers follow the definitions set out in the Banking (Disclosure) Rules and represent advances which are either classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

*(d) Advances overdue for more than 3 months*

The gross amount of advances overdue for more than 3 months is analysed as follows:

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Amount HK$'m** | **% of gross advances to customers** | Amount HK$'m | % of gross advances to customers |
| Gross advances to customers which have been overdue for: | | | | |
| – six months or less but over three months | **339** | **0.07%** | 242 | 0.06% |
| – one year or less but over six months | **66** | **0.02%** | 163 | 0.04% |
| – over one year | **571** | **0.12%** | 652 | 0.16% |
| Advances overdue for over three months | **976** | **0.21%** | 1,057 | 0.26% |
| Individually assessed loan impairment allowances made in respect of such advances | **439** | | 305 | |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(d) Advances overdue for more than 3 months (continued)*

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Current market value of collateral held against the covered portion of advances to customers | **1,436** | 1,970 |
| Covered portion of advances to customers | **604** | 847 |
| Uncovered portion of advances to customers | **372** | 210 |

Collateral held against overdue or impaired loans is principally represented by charges over business assets such as commercial and residential premises for corporate loans and mortgages over residential properties for personal loans.

As at 31 December 2008 and 2007, there were no advances to banks and other financial institutions overdue for more than three months.

*(e) Rescheduled advances*

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Amount HK$'m** | **% of gross advances to customers** | Amount HK$'m | % of gross advances to customers |
| Rescheduled advances to customers net of amounts included in advances overdue for more than 3 months | **127** | **0.03%** | 186 | 0.05% |

As at 31 December 2008, the total rescheduled advances to customers during the year amounted to HK$54 million (2007: HK$88 million).

As at 31 December 2008 and 2007, there were no rescheduled advances to banks and other financial institutions.

Rescheduled advances are those advances that have been restructured or renegotiated because of deterioration in the financial position of the borrower or of the inability of the borrower to meet the original repayment schedule and for which the revised repayment terms, either of interest or of repayment period, are non-commercial. Rescheduled advances, which have been overdue for more than three months under the revised repayment terms, are included in overdue advances.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(f) Concentration of advances to customers*

(i) Sectoral analysis of gross advances to customers

The information concerning gross advances to customers has been analysed into loans used inside or outside Hong Kong by industry sectors of the borrowers as follows:

| | 2008 | | | | | |
|---|---|---|---|---|---|---|
| | Gross advances HK$'m | % Covered by collateral or other security | Classified or impaired HK$'m | Overdue* HK$'m | Individually assessed impairment allowances HK$'m | Collectively assessed impairment allowances HK$'m |
| Loans for use in Hong Kong | | | | | | |
| Industrial, commercial and financial | | | | | | |
| – Property development | 19,856 | 40.49% | 2 | 14 | 1 | 66 |
| – Property investment | 71,374 | 88.00% | 294 | 585 | 30 | 312 |
| – Financial concerns | 11,547 | 8.63% | – | – | 1 | 56 |
| – Stockbrokers | 124 | 10.33% | – | – | – | – |
| – Wholesale and retail trade | 18,156 | 52.85% | 218 | 300 | 71 | 98 |
| – Manufacturing | 16,410 | 53.67% | 234 | 298 | 138 | 80 |
| – Transport and transport equipment | 21,590 | 13.82% | 2 | 9 | 1 | 81 |
| – Recreational activities | 139 | 46.87% | – | – | – | – |
| – Information technology | 6,049 | 2.21% | – | 3 | – | 19 |
| – Others | 23,529 | 26.91% | 68 | 213 | 13 | 83 |
| Individuals | | | | | | |
| – Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme | 13,477 | 99.91% | 98 | 510 | 4 | 12 |
| – Loans for purchase of other residential properties | 116,303 | 99.97% | 153 | 1,650 | 7 | 74 |
| – Credit card advances | 6,553 | – | 30 | 273 | – | 71 |
| – Others | 11,490 | 77.92% | 107 | 333 | 57 | 20 |
| Total loans for use in Hong Kong | 336,597 | 70.84% | 1,206 | 4,188 | 323 | 972 |
| Trade finance | 24,555 | 30.36% | 560 | 494 | 355 | 108 |
| Loans for use outside Hong Kong | 99,295 | 22.38% | 372 | 235 | 122 | 421 |
| Gross advances to customers | 460,447 | 58.23% | 2,138 | 4,917 | 800 | 1,501 |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(f) Concentration of advances to customers (continued)*

(i) Sectoral analysis of gross advances to customers (continued)

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Gross advances HK$'m | % Covered by collateral or other security | Classified or impaired HK$'m | Overdue* HK$'m | Individually assessed impairment allowances HK$'m | Collectively assessed impairment allowances HK$'m |
| Loans for use in Hong Kong | | | | | | |
| Industrial, commercial and financial | | | | | | |
| – Property development | 17,979 | 33.97% | 16 | 18 | 3 | 52 |
| – Property investment | 65,963 | 86.50% | 343 | 961 | 14 | 187 |
| – Financial concerns | 12,346 | 6.05% | – | 14 | – | 43 |
| – Stockbrokers | 242 | 12.10% | – | – | – | – |
| – Wholesale and retail trade | 13,572 | 65.05% | 238 | 382 | 85 | 41 |
| – Manufacturing | 14,468 | 58.08% | 138 | 550 | 37 | 48 |
| – Transport and transport equipment | 21,001 | 21.11% | 3 | 25 | 1 | 60 |
| – Recreational activities | 30 | 93.53% | – | – | – | – |
| – Information technology | 2,009 | 37.39% | – | 2 | – | 6 |
| – Others | 21,046 | 41.70% | 90 | 584 | 16 | 65 |
| Individuals | | | | | | |
| – Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme | 13,969 | 99.78% | 129 | 599 | 8 | 13 |
| – Loans for purchase of other residential properties | 106,583 | 99.87% | 284 | 2,078 | 18 | 81 |
| – Credit card advances | 5,761 | – | 23 | 245 | – | 63 |
| – Others | 10,708 | 79.61% | 119 | 314 | 50 | 14 |
| Total loans for use in Hong Kong | 305,677 | 73.31% | 1,383 | 5,772 | 232 | 673 |
| Trade finance | 24,275 | 40.71% | 105 | 399 | 73 | 77 |
| Loans for use outside Hong Kong | 83,110 | 39.76% | 315 | 375 | 76 | 254 |
| Gross advances to customers | 413,062 | 64.64% | 1,803 | 6,546 | 381 | 1,004 |

* Advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(f) Concentration of advances to customers (continued)*

(i) Sectoral analysis of gross advances to customers (continued)

The amount of new impairment allowances charged to the income statement, and classified or impaired loans written off during the year are shown below:

| | 2008 | | 2007 | |
|---|---|---|---|---|
| | New impairment allowances HK$'m | Classified or impaired loans written off HK$'m | New impairment allowances HK$'m | Classified or impaired loans written off HK$'m |
| Loans for use in Hong Kong | | | | |
| Industrial, commercial and financial | | | | |
| – Property development | 28 | – | 25 | – |
| – Property investment | 139 | 5 | 99 | 9 |
| – Financial concerns | 24 | – | 22 | – |
| – Stockbrokers | – | – | – | – |
| – Wholesale and retail trade | 120 | 103 | 149 | 98 |
| – Manufacturing | 249 | 125 | 58 | 18 |
| – Transport and transport equipment | 34 | – | 31 | – |
| – Recreational activities | – | – | – | – |
| – Information technology | 9 | – | 3 | – |
| – Others | 34 | 8 | 77 | 5 |
| Individuals | | | | |
| – Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme | 1 | 1 | 13 | 4 |
| – Loans for purchase of other residential properties | 8 | – | 79 | 1 |
| – Credit card advances | 157 | 141 | 124 | 126 |
| – Others | 61 | 47 | 50 | 50 |
| Total loans for use in Hong Kong | 864 | 430 | 730 | 311 |
| Trade finance | 374 | 26 | 76 | 15 |
| Loans for use outside Hong Kong | 266 | 19 | 149 | 1 |
| Gross advances to customers | 1,504 | 475 | 955 | 327 |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(f) Concentration of advances to customers (continued)*

(ii) Geographical analysis of gross advances to customers and overdue advances

The following geographical analysis of gross advances to customers and overdue advances is based on the location of the counterparties, after taking into account the transfer of risk in respect of such advances where appropriate.

**Gross advances to customers**

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Hong Kong | **374,506** | 351,102 |
| Mainland China | **55,318** | 39,050 |
| Others | **30,623** | 22,910 |
| | **460,447** | 413,062 |
| **Collectively assessed loan impairment allowances in respect of the gross advances to customers** | | |
| Hong Kong | **1,172** | 827 |
| Mainland China | **221** | 124 |
| Others | **108** | 53 |
| | **1,501** | 1,004 |

**Overdue advances**

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Hong Kong | **4,622** | 6,221 |
| Mainland China | **266** | 278 |
| Others | **29** | 47 |
| | **4,917** | 6,546 |
| **Individually assessed loan impairment allowances in respect of the overdue advances** | | |
| Hong Kong | **554** | 284 |
| Mainland China | **99** | 46 |
| Others | **21** | 2 |
| | **674** | 332 |
| **Collectively assessed loan impairment allowances in respect of the overdue advances** | | |
| Hong Kong | **50** | 60 |
| Mainland China | **6** | 10 |
| | **56** | 70 |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Gross loans and advances (continued)**

*(f) Concentration of advances to customers (continued)*

(ii) Geographical analysis of gross advances to customers and overdue advances (continued)

**Classified or impaired advances**

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Hong Kong | **1,792** | 1,572 |
| Mainland China | **323** | 223 |
| Others | **23** | 8 |
| | **2,138** | 1,803 |
| **Individually assessed loan impairment allowances in respect of the classified or impaired advances** | | |
| Hong Kong | **677** | 333 |
| Mainland China | **100** | 46 |
| Others | **23** | 2 |
| | **800** | 381 |
| **Collectively assessed loan impairment allowances in respect of the classified or impaired advances** | | |
| Hong Kong | **26** | 19 |
| Mainland China | **7** | 6 |
| | **33** | 25 |

**Repossessed assets**

During the year, the Group obtained assets by taking possession of collateral held as security. The nature and carrying value of such assets are summarised as follows:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Commercial properties | **18** | 10 |
| Residential properties | **85** | 43 |
| | **103** | 53 |

The estimated market value of repossessed assets held by the Group as at 31 December 2008 amounted to HK$173 million (2007: HK$116 million). They comprise properties in respect of which the Group has acquired access or control (e.g. through court proceedings or voluntary actions by the borrowers concerned) for release in full or in part of the obligations of the borrowers.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Repossessed assets (continued)**

When the repossessed assets are not readily convertible into cash, the Group may consider the following alternatives:

– adjusting the selling prices

– selling the loans together with the assets

– arranging loan restructuring

**Balances and placements with banks and other financial institutions**

The following table presents an analysis of balances and placements with banks and other financial institutions that are neither overdue nor impaired as at 31 December by rating agency designation, based on Moody's ratings or their equivalent.

| | **2008** | | | |
|---|---|---|---|---|
| | **Aaa to A3 HK$'m** | **Lower than A3 HK$'m** | **Unrated HK$'m** | **Total HK$'m** |
| Central banks | **66,158** | **–** | **–** | **66,158** |
| Banks and other financial institutions | **168,456** | **586** | **3,555** | **172,597** |
| | **234,614** | **586** | **3,555** | **238,755** |

| | 2007 | | | |
|---|---|---|---|---|
| | Aaa to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m |
| Central banks | 30,627 | – | – | 30,627 |
| Banks and other financial institutions | 173,248 | 2,047 | 2,963 | 178,258 |
| | 203,875 | 2,047 | 2,963 | 208,885 |

As at 31 December 2008 and 2007, there were no overdue or impaired balances and placements with banks and other financial institutions.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

#### Debt securities

The table below represents an analysis of the carrying value of debt securities by credit rating and credit risk characteristic, based on Moody's ratings or their equivalent to the respective issues of the debt securities.

| | 2008 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | Unrated | | | |
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Hong Kong government and government bodies HK$'m | Other governments and government agencies HK$'m | Other HK$'m | Total HK$'m |
| **Investment in securities** | | | | | | | | |
| US non-agency residential mortgage-backed | | | | | | | | |
| – Subprime | 913 | – | 30 | 104 | – | – | – | 1,047 |
| – Alt-A | 1,245 | 383 | 274 | 432 | – | – | – | 2,334 |
| – Prime | 9,549 | 1,558 | 2,878 | 1,950 | – | – | – | 15,935 |
| Fannie Mae | | | | | | | | |
| – issued debt securities | 1,504 | – | – | – | – | – | – | 1,504 |
| – mortgage-backed securities | – | – | – | – | – | 88 | – | 88 |
| Freddie Mac | | | | | | | | |
| – issued debt securities | 864 | 162 | – | – | – | – | – | 1,026 |
| – mortgage-backed securities | – | – | – | – | – | 1,633 | – | 1,633 |
| Other MBS/ABS | 6,874 | 24 | 63 | – | – | 3,807 | – | 10,768 |
| Other debt securities | 40,537 | 83,827 | 27,509 | 4,371 | 12,175 | 51,368 | 35,873 | 255,660 |
| Subtotal | 61,486 | 85,954 | 30,754 | 6,857 | 12,175 | 56,896 | 35,873 | 289,995 |
| **Financial assets at fair value through profit or loss** | | | | | | | | |
| Fannie Mae | | | | | | | | |
| – issued debt securities | 287 | – | – | – | – | – | – | 287 |
| Other MBS/ABS | 27 | – | – | – | – | – | – | 27 |
| Other debt securities | 2,304 | 15,417 | 10,233 | 1,457 | 11,358 | – | 355 | 41,124 |
| Subtotal | 2,618 | 15,417 | 10,233 | 1,457 | 11,358 | – | 355 | 41,438 |
| Total | 64,104 | 101,371 | 40,987 | 8,314 | 23,533 | 56,896 | 36,228 | 331,433 |

Note: In 2007, securities issued by Ginnie Mae of HK$3,365 million were disclosed as Aaa rating, whereas for the current year such securities of HK$3,807 million have been included in above as "Unrated – Other governments and government agencies".

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Debt securities (continued)**

| | 2007 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | Unrated | | | |
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Hong Kong government and government bodies HK$'m | Other governments and government agencies HK$'m | Other HK$'m | Total HK$'m |
| **Investment in securities** | | | | | | | | |
| US non-agency residential mortgage-backed | | | | | | | | |
| – Subprime | 4,118 | – | – | – | – | – | – | 4,118 |
| – Alt-A | 6,567 | – | – | – | – | – | – | 6,567 |
| – Prime | 29,014 | – | – | – | – | – | – | 29,014 |
| Fannie Mae | | | | | | | | |
| – issued debt securities | 4,243 | – | – | – | – | – | – | 4,243 |
| – mortgage-backed securities | – | – | – | – | – | 104 | – | 104 |
| Freddie Mac | | | | | | | | |
| – issued debt securities | 2,753 | 165 | – | – | – | – | – | 2,918 |
| – mortgage-backed securities | – | – | – | – | – | 1,683 | – | 1,683 |
| Other MBS/ABS | 14,105 | 78 | – | – | – | – | 139 | 14,322 |
| Other debt securities | 33,572 | 88,709 | 27,062 | 2,772 | 6,946 | – | 74,573 | 233,634 |
| Subtotal | 94,372 | 88,952 | 27,062 | 2,772 | 6,946 | 1,787 | 74,712 | 296,603 |
| **Financial assets at fair value through profit or loss** | | | | | | | | |
| Fannie Mae | | | | | | | | |
| – issued debt securities | 268 | – | – | – | – | – | – | 268 |
| Other MBS/ABS | 40 | – | – | – | – | – | – | 40 |
| Other debt securities | 2,986 | 12,238 | 7,370 | 1,136 | 3,518 | – | 3,300 | 30,548 |
| Subtotal | 3,294 | 12,238 | 7,370 | 1,136 | 3,518 | – | 3,300 | 30,856 |
| Total | 97,666 | 101,190 | 34,432 | 3,908 | 10,464 | 1,787 | 78,012 | 327,459 |

The total amount of unrated issues amounted to HK$116,657 million (2007: HK$90,263 million) as at 31 December 2008, of which only HK$8,975 million (2007: HK$10,672 million) were without issuer ratings. For details, please refer to page 140.

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Debt securities (continued)**

For the above debt securities with no issue rating, their issuer ratings are analysed as follows:

| | 2008 | | | | | |
|---|---|---|---|---|---|---|
| | **Aaa HK$'m** | **Aa1 to Aa3 HK$'m** | **A1 to A3 HK$'m** | **Lower than A3 HK$'m** | **Unrated HK$'m** | **Total HK$'m** |
| Available-for-sale securities | **18,180** | **49,408** | **3,293** | **35** | **5,481** | **76,397** |
| Held-to-maturity securities | **624** | **10,140** | **2,037** | **–** | **3,151** | **15,952** |
| Loans and receivables | **3,386** | **8,768** | **397** | **–** | **44** | **12,595** |
| Financial assets at fair value through profit or loss | **1** | **11,413** | **–** | **–** | **299** | **11,713** |
| Total | **22,191** | **79,729** | **5,727** | **35** | **8,975** | **116,657** |

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m |
| Available-for-sale securities | 2,486 | 8,166 | 3,818 | 440 | 1,708 | 16,618 |
| Held-to-maturity securities | 5,859 | 20,467 | 3,765 | 50 | 5,584 | 35,725 |
| Loans and receivables | 8,572 | 19,365 | 80 | – | 3,085 | 31,102 |
| Financial assets at fair value through profit or loss | 29 | 4,234 | 2,085 | 175 | 295 | 6,818 |
| Total | 16,946 | 52,232 | 9,748 | 665 | 10,672 | 90,263 |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Debt securities (continued)**

The following table presents an analysis of debt securities neither overdue nor impaired as at 31 December by rating agency designation, based on Moody's ratings or their equivalent to the respective issues of the debt securities.

| | 2008 | | | | | |
|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m |
| Available-for-sale securities | **32,231** | **41,722** | **12,752** | **1,839** | **76,362** | **164,906** |
| Held-to-maturity securities | **22,667** | **42,554** | **16,201** | **2,067** | **15,952** | **99,441** |
| Loans and receivables | **–** | **–** | **–** | **–** | **12,595** | **12,595** |
| Financial assets at fair value through profit or loss | **2,618** | **15,417** | **10,233** | **1,457** | **11,709** | **41,434** |
| Total | **57,516** | **99,693** | **39,186** | **5,363** | **116,618** | **318,376** |

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m |
| Available-for-sale securities | 42,166 | 28,588 | 10,686 | 1,459 | 16,618 | 99,517 |
| Held-to-maturity securities | 47,912 | 60,364 | 16,376 | 1,313 | 35,725 | 161,690 |
| Loans and receivables | – | – | – | – | 31,102 | 31,102 |
| Financial assets at fair value through profit or loss | 3,294 | 12,238 | 7,370 | 1,136 | 6,818 | 30,856 |
| Total | 93,372 | 101,190 | 34,432 | 3,908 | 90,263 | 323,165 |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Debt securities (continued)**

The carrying values of impaired debt securities by credit rating are analysed as follows:

| | 2008 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m | Of which impairment allowances HK$'m |
| Available-for-sale securities | 3,451 | 814 | 542 | 1,187 | 35 | 6,029 | 4,561 |
| Held-to-maturity securities | 3,137 | 864 | 1,259 | 1,764 | – | 7,024 | 4,440 |
| Total | 6,588 | 1,678 | 1,801 | 2,951 | 35 | 13,053 | 9,001 |
| Of which impairment allowances | 4,195 | 1,400 | 976 | 2,078 | 352 | 9,001 | |

| | 2007 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m | Of which impairment allowances HK$'m |
| Available-for-sale securities | 556 | – | – | – | – | 556 | 190 |
| Held-to-maturity securities | 3,738 | – | – | – | – | 3,738 | 1,682 |
| Total | 4,294 | – | – | – | – | 4,294 | 1,872 |
| Of which impairment allowances | 1,872 | – | – | – | – | 1,872 | |

Debt securities overdue but not impaired are analysed as follows:

| | Overdue for 6 months or less but over 3 months | |
|---|---|---|
| | 2008 HK$'m | 2007 HK$'m |
| Financial assets at fair value through profit or loss | 4 | – |

Note: Impairment is not measured for financial assets at fair value through profit or loss as assets are managed according to movements in fair value, and the fair value movement is taken directly to the income statement. Consequently, such overdue debt securities are reported under "overdue but not impaired".

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Debt securities (continued)**

Debt securities overdue for more than 3 months are analysed as follows:

| | Overdue for 6 months or less but over 3 months | |
|---|---|---|
| | **2008 HK$'m** | 2007 HK$'m |
| Available-for-sale securities | **35** | – |
| Financial assets at fair value through profit or loss | **4** | – |
| | **39** | – |

***MBS/ABS***

The table below represents an analysis of the Group's exposure to MBS/ABS by geographical location.

| | 2008 | | |
|---|---|---|---|
| | **Carrying values HK$'m** | **Of which impaired HK$'m** | **Of which impairment allowances HK$'m** |
| **US MBS/ABS** | | | |
| Non-agency residential mortgage-backed | | | |
| – Subprime | **1,047** | **829** | **339** |
| – Alt-A | **2,334** | **1,750** | **1,302** |
| – Prime | **15,935** | **9,594** | **6,479** |
| Ginnie Mae | **3,807** | **–** | **–** |
| Fannie Mae | **88** | **–** | **–** |
| Freddie Mac | **1,633** | **–** | **–** |
| Commercial mortgage-backed | **929** | **–** | **–** |
| Others | **2,806** | **–** | **–** |
| | **28,579** | **12,173** | **8,120** |
| **Other countries MBS/ABS** | | | |
| Residential mortgage-backed | **2,649** | **69** | **27** |
| Commercial mortgage-backed | **454** | **–** | **–** |
| Others | **150** | **–** | **–** |
| | **3,253** | **69** | **27** |
| Total MBS/ABS | **31,832** | **12,242** | **8,147** |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Debt securities (continued)**

***MBS/ABS (continued)***

| | 2007 | | |
|---|---|---|---|
| | Carrying values HK$'m | Of which impaired HK$'m | Of which impairment allowances HK$'m |
| **US MBS/ABS** | | | |
| Non-agency residential mortgage-backed | | | |
| – Subprime | 4,118 | 2,856 | 1,253 |
| – Alt-A | 6,567 | 1,380 | 573 |
| – Prime | 29,014 | 58 | 46 |
| Ginnie Mae | 3,365 | – | – |
| Fannie Mae | 104 | – | – |
| Freddie Mac | 1,683 | – | – |
| Commercial mortgage-backed | 997 | – | – |
| Others | 3,692 | – | – |
| | 49,540 | 4,294 | 1,872 |
| **Other countries MBS/ABS** | | | |
| Residential mortgage-backed | 5,189 | – | – |
| Commercial mortgage-backed | 561 | – | – |
| Others | 558 | – | – |
| | 6,308 | – | – |
| Total MBS/ABS | 55,848 | 4,294 | 1,872 |

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Fair value movement taken to available-for-sale reserve on MBS/ABS for the year (net of impairment charges taken to income statement excluding deferred tax impact) | **(1,340)** | (364) |
| Closing balance of available-for-sale reserve relating to MBS/ABS (excluding deferred tax impact) | **(1,707)** | (367) |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Debt securities (continued)**

***MBS/ABS (continued)***

The carrying values of impaired MBS/ABS by credit rating are analysed as follows:

| | 2008 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m | Of which impairment allowances HK$'m |
| **US MBS/ABS** | | | | | | | |
| Non-agency residential mortgage-backed | | | | | | | |
| – Subprime | 695 | – | 30 | 104 | – | 829 | 339 |
| – Alt-A | 662 | 383 | 274 | 431 | – | 1,750 | 1,302 |
| – Prime | 5,162 | 1,295 | 1,312 | 1,825 | – | 9,594 | 6,479 |
| | 6,519 | 1,678 | 1,616 | 2,360 | – | 12,173 | 8,120 |
| **Other countries MBS/ABS** | | | | | | | |
| Residential mortgage-backed | 69 | – | – | – | – | 69 | 27 |
| Total MBS/ABS | 6,588 | 1,678 | 1,616 | 2,360 | – | 12,242 | 8,147 |
| Of which impairment allowances | 4,195 | 1,400 | 938 | 1,614 | – | 8,147 | |

| | 2007 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m | Of which impairment allowances HK$'m |
| **US MBS/ABS** | | | | | | | |
| Non-agency residential mortgage-backed | | | | | | | |
| – Subprime | 2,856 | – | – | – | – | 2,856 | 1,253 |
| – Alt-A | 1,380 | – | – | – | – | 1,380 | 573 |
| – Prime | 58 | – | – | – | – | 58 | 46 |
| Total MBS/ABS | 4,294 | – | – | – | – | 4,294 | 1,872 |
| Of which impairment allowances | 1,872 | – | – | – | – | 1,872 | |

## 4. Financial risk management (continued)

### *4.1 Credit Risk (continued)*

**Debt securities (continued)**

***MBS/ABS (continued)***

The table below represents an analysis of impairment charges for the year for MBS/ABS held as at 31 December.

| | 2008 | | | | | |
|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m |
| **US MBS/ABS** | | | | | | |
| Non-agency residential mortgage-backed | | | | | | |
| – Subprime | (90) | – | 27 | 27 | – | (36) |
| – Alt-A | 394 | 299 | 157 | 359 | – | 1,209 |
| – Prime | 3,725 | 1,055 | 658 | 1,094 | – | 6,532 |
| | 4,029 | 1,354 | 842 | 1,480 | – | 7,705 |
| **Other countries MBS/ABS** | | | | | | |
| Residential mortgage-backed | 27 | – | – | – | – | 27 |
| Total MBS/ABS | 4,056 | 1,354 | 842 | 1,480 | – | 7,732 |

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m |
| **US MBS/ABS** | | | | | | |
| Non-agency residential mortgage-backed | | | | | | |
| – Subprime | 1,253 | – | – | – | – | 1,253 |
| – Alt-A | 573 | – | – | – | – | 573 |
| – Prime | 46 | – | – | – | – | 46 |
| Total MBS/ABS | 1,872 | – | – | – | – | 1,872 |

### *4.2 Market Risk*

Market risk is the risk of loss that results from movements in market rates and prices. The Group's market risk in trading book arises from trading positions taken from customer-related business and proprietary trading. These positions are subject to daily mark-to-market valuation. The risk includes potential losses arising from changes in foreign exchange and interest rates as well as equities and commodities prices. On the other hand, the major market risk in banking book arises from the group's investment portfolio. The risk includes potential losses arising from changes in market parameters such as credit, liquidity, and interest rate risk and price movements which prevent the Group from realising its investment securities at their carrying amounts. These positions are subject to monthly mark-to-market valuation. The Group manages market risk in its trading book separately from its banking book.

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

**Market risk management framework**

The Group's risk management objective is to enhance shareholder value by maintaining risk exposures within acceptable limits. Market risk management framework of the Group comprises three levels. The Board of Directors and its Risk Committee are the ultimate decision making authorities. Formulation of the risk management procedures and implementation mechanism, and monitoring of the compliance are mainly responsible by senior management (including CE and CRO). RMD is responsible for the oversight of the Group's market risk to ensure that overall and individual market risks are within the Group's risk tolerance. Risk exposures are monitored on a day-to-day basis to ensure that they are within established risk limits and are regularly reported to the senior management. Nanyang, Chiyu and BOC Life have their own independent risk monitoring units to monitor limit compliance on a daily basis.

The Group's control of market risk is based on restricting individual operations to trading within various market risk limits approved by the RC, and a list of permissible instruments authorised by senior management, as well as enforcing rigorous new product approval procedures to ensure all risks arising are thoroughly identified, properly measured and adequately controlled.

Market risk arising from the trading book is managed within various major risk limits approved by the RC, including risk positions and/or risk factor sensitivities. Since April 2007 BOCHK has also formally applied Value-at-Risk (VAR) limit as a daily risk management tool. These overall risk limits are divided into sub-limits by reference to different risk products, including interest rate, foreign exchange rate, commodity price and equity products. Transactions are classified into different risk product categories according to the prominent type of risk inherent in the transactions.

The Group also uses the VAR technique to measure potential losses and market risks of its trading book for reporting to the RC and senior management on a periodic basis. VAR is a statistical technique which estimates the potential losses that could occur on risk positions taken over a specified time horizon within a given level of confidence. BOCHK, being the banking entity within the Group with the major trading positions, which are mainly foreign currency positions in major currencies, uses VAR technique to monitor and control market risk on a daily basis.

The Group has changed its VAR calculation from a variance/co-variance basis to historical simulation basis with effect from April 2007. The Group uses historical movements in market rates and prices, a 99% confidence level and a 1-day holding period to calculate portfolio and individual VAR. Movements in market prices are calculated by reference to market data from the last two years.

**VAR**

The following table sets out the VAR for all trading market risk exposure[1] of BOCHK.

| HK$'m | | At 31 December | Minimum for the year | Maximum for the year | Average for the year |
|---|---|---|---|---|---|
| VAR for all market risk | – 2008 | 12.6 | 3.0 | 13.5 | 6.5 |
| | – 2007 | 3.2 | 1.4 | 10.4 | 4.1 |
| VAR for foreign exchange risk products | – 2008 | 13.1 | 2.5 | 14.2 | 6.0 |
| | – 2007 | 2.7 | 1.0 | 9.4 | 4.0 |
| VAR for interest rate risk products | – 2008 | 4.2 | 1.0 | 5.9 | 2.9 |
| | – 2007 | 1.5 | 0.5 | 3.9 | 1.6 |
| VAR for equity risk products | – 2008 | 0.2 | 0.1 | 2.8 | 0.5 |
| | – 2007 | 0.4 | 0.1 | 1.1 | 0.4 |
| VAR for commodity risk products | – 2008 | 0.0 | 0.0 | 0.5 | 0.0 |
| | – 2007 | 0.0 | 0.0 | 0.4 | 0.1 |

In 2008, the average daily revenue[2] of BOCHK earned from market risk-related trading activities was HK$5.35 million (2007: HK$3.06 million).

1 Structural FX positions have been excluded.

2 Revenues from structural FX positions and back to back transactions have been excluded.

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

#### VAR (continued)

Predictive power of the VaR measure is monitored by backtesting, which compares the calculated VaR figure of those trading positions of each business day with the actual revenues arising on those positions on the next business day. These actual revenues exclude non-trading income including fees and commissions. If backtesting revenues are negative and exceed the VaR, a "backtesting exception" is noted. Backtesting results are reported to the Group's senior management, including CE and CRO.

Although it is a valuable guide to risk, VAR should always be viewed in the context of its limitations. For example:

– the use of historical data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;

– the use of a one-day holding period assumes that all positions can be liquidated or hedged in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day holding period may be insufficient to liquidate or hedge all positions fully;

– the use of a 99 per cent confidence level, by definition, does not take into account losses that might occur beyond this level of confidence; and

– VAR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

The Group recognises these limitations by augmenting its VAR limits with other position and sensitivity limit structures.

Additionally, the Group applies a wide range of stress testing, both on individual portfolios and on the Group's consolidated positions. Stress testing program of the trading book includes sensitivity testing on changes in risk factors with various degrees of severity, as well as scenario analysis on historical events including the 1987 Equity Market Crash, 1994 Bond Market Crash, the 1997 Asian Crisis and the 11 September Event in 2001. The Group also reassessed the stress testing programme to ensure its rigour and robustness in view of the financial crisis in 2008. The Group's stress-testing regime provides senior management with an assessment of the financial impact of identified extreme events on the market risk exposures of the Group.

For BOCHK, market risk arising from the banking book is managed within various risk limits such as P/L Management Alert Limit (P/L MAL) and P/L Management Alert Trigger (P/L MAT), and the AFS economic value at risk sub-limit for the available-for-sale debt securities portfolio to control the price risk impact on our CAR. The mark-to-market result is reported to ALCO on a monthly basis.

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

#### Currency risk

The tables below summarise the Group's exposure to foreign currency exchange rate risk as at 31 December. Included in the tables are the Group's assets and liabilities at carrying amounts in HK$ equivalent, categorised by the original currency.

| | 2008 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Renminbi HK$'m | US Dollars HK$'m | HK Dollars HK$'m | EURO HK$'m | Japanese Yen HK$'m | Pound Sterling HK$'m | Others HK$'m | Total HK$'m |
| **Assets** | | | | | | | | |
| Cash and balances with banks and other financial institutions | 53,381 | 36,592 | 53,720 | 2,662 | 1,425 | 3,163 | 2,326 | 153,269 |
| Placements with banks and other financial institutions maturing between one and twelve months | 504 | 31,441 | 38,728 | 5,924 | – | 6,487 | 6,634 | 89,718 |
| Financial assets at fair value through profit or loss | 1,274 | 7,670 | 34,817 | – | – | – | 51 | 43,812 |
| Derivative financial instruments | – | 485 | 19,032 | 99 | 1 | – | 11 | 19,628 |
| Hong Kong SAR Government certificates of indebtedness | – | – | 34,200 | – | – | – | – | 34,200 |
| Advances and other accounts | 15,056 | 97,002 | 347,249 | 2,915 | 1,622 | 1,002 | 4,647 | 469,493 |
| Investment in securities | | | | | | | | |
| – Available-for-sale securities | 828 | 71,883 | 25,396 | 21,160 | 40,652 | 1,651 | 11,051 | 172,621 |
| – Held-to-maturity securities | 2,165 | 52,352 | 33,652 | 6,132 | 1,823 | 791 | 9,550 | 106,465 |
| – Loans and receivables | – | 2,243 | 9,039 | 108 | – | 110 | 1,095 | 12,595 |
| Interests in associates | – | – | 88 | – | – | – | – | 88 |
| Investment properties | 63 | – | 7,664 | – | – | – | – | 7,727 |
| Properties, plant and equipment | 98 | – | 22,697 | – | – | – | – | 22,795 |
| Other assets (including deferred tax assets) | 121 | 244 | 13,545 | 596 | 220 | 19 | 88 | 14,833 |
| **Total assets** | 73,490 | 299,912 | 639,827 | 39,596 | 45,743 | 13,223 | 35,453 | 1,147,244 |
| **Liabilities** | | | | | | | | |
| Hong Kong SAR currency notes in circulation | – | – | 34,200 | – | – | – | – | 34,200 |
| Deposits and balances of banks and other financial institutions | 38,131 | 24,191 | 18,558 | 2,251 | 693 | 2,494 | 2,461 | 88,779 |
| Financial liabilities at fair value through profit or loss | – | 1,852 | 19,890 | – | – | – | 196 | 21,938 |
| Derivative financial instruments | – | 513 | 19,622 | 297 | 1 | – | 17 | 20,450 |
| Deposits from customers | 30,518 | 193,952 | 502,199 | 15,584 | 2,135 | 13,445 | 44,744 | 802,577 |
| Debt securities in issue at amortised cost | – | 148 | 845 | – | – | – | 49 | 1,042 |
| Other accounts and provisions (including current and deferred tax liabilities) | 1,331 | 9,682 | 17,874 | 325 | 7,907 | 348 | 646 | 38,113 |
| Insurance contract liabilities | – | 4,447 | 23,827 | – | – | – | – | 28,274 |
| Subordinated liabilities | – | 19,394 | 735 | 7,210 | – | – | – | 27,339 |
| **Total liabilities** | 69,980 | 254,179 | 637,750 | 25,667 | 10,736 | 16,287 | 48,113 | 1,062,712 |
| Net on-balance sheet position | 3,510 | 45,733 | 2,077 | 13,929 | 35,007 | (3,064) | (12,660) | 84,532 |
| Off-balance sheet net notional position* | (4) | (33,929) | 68,465 | (13,826) | (34,817) | 3,043 | 12,542 | 1,474 |
| Contingent liabilities and commitments | 9,132 | 62,401 | 176,092 | 3,032 | 551 | 303 | 1,878 | 253,389 |

* Off-balance sheet net notional position represents the net notional amounts of foreign currency derivative financial instruments, which are principally used to reduce the Group's exposure to currency movements.

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

### Currency risk (continued)

| | 2007 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Renminbi HK$'m | US Dollars HK$'m | HK Dollars HK$'m | EURO HK$'m | Japanese Yen HK$'m | Pound Sterling HK$'m | Others HK$'m | Total HK$'m |
| **Assets** | | | | | | | | |
| Cash and balances with banks and other financial institutions | 30,849 | 49,833 | 71,731 | 1,147 | 160 | 1,815 | 3,530 | 159,065 |
| Placements with banks and other financial institutions maturing between one and twelve months | 375 | 23,854 | 28,750 | – | – | – | 175 | 53,154 |
| Financial assets at fair value through profit or loss | 917 | 8,997 | 24,286 | – | – | – | 240 | 34,440 |
| Derivative financial instruments | – | 773 | 13,703 | – | – | – | 1 | 14,477 |
| Hong Kong SAR Government certificates of indebtedness | – | – | 32,770 | – | – | – | – | 32,770 |
| Advances and other accounts | 13,335 | 71,309 | 323,495 | 4,202 | 1,667 | 1,006 | 5,220 | 420,234 |
| Investment in securities | | | | | | | | |
| – Available-for-sale securities | 90 | 62,612 | 26,697 | 7,005 | 28 | 1,321 | 6,900 | 104,653 |
| – Held-to-maturity securities | 864 | 84,686 | 59,565 | 2,486 | – | 1,554 | 16,273 | 165,428 |
| – Loans and receivables | – | 3,594 | 26,511 | 428 | – | – | 569 | 31,102 |
| Interests in associates | – | – | 83 | – | – | – | – | 83 |
| Investment properties | – | – | 8,058 | – | – | – | – | 8,058 |
| Properties, plant and equipment | 72 | 1 | 23,220 | – | – | – | – | 23,293 |
| Other assets (including deferred tax assets) | 69 | 947 | 19,361 | 161 | 61 | 145 | 136 | 20,880 |
| **Total assets** | 46,571 | 306,606 | 658,230 | 15,429 | 1,916 | 5,841 | 33,044 | 1,067,637 |
| **Liabilities** | | | | | | | | |
| Hong Kong SAR currency notes in circulation | – | – | 32,770 | – | – | – | – | 32,770 |
| Deposits and balances of banks and other financial institutions | 27,173 | 19,422 | 9,090 | 147 | 2,141 | 92 | 2,534 | 60,599 |
| Financial liabilities at fair value through profit or loss | – | 2,717 | 8,688 | – | – | – | – | 11,405 |
| Derivative financial instruments | – | 1,257 | 9,824 | – | – | – | 11 | 11,092 |
| Deposits from customers | 17,360 | 166,416 | 548,223 | 8,432 | 2,492 | 12,284 | 38,399 | 793,606 |
| Debt securities in issue at amortised cost | – | 667 | 1,422 | – | – | – | – | 2,089 |
| Other accounts and provisions (including current and deferred tax liabilities) | 574 | 9,751 | 26,706 | 311 | 31 | 387 | 761 | 38,521 |
| Insurance contract liabilities | – | 4,284 | 18,213 | – | – | – | – | 22,497 |
| **Total liabilities** | 45,107 | 204,514 | 654,936 | 8,890 | 4,664 | 12,763 | 41,705 | 972,579 |
| Net on-balance sheet position | 1,464 | 102,092 | 3,294 | 6,539 | (2,748) | (6,922) | (8,661) | 95,058 |
| Off-balance sheet net notional position | 394 | (97,215) | 89,481 | (6,478) | 2,436 | 7,050 | 8,975 | 4,643 |
| Contingent liabilities and commitments | 4,873 | 55,183 | 163,697 | 4,693 | 1,017 | 259 | 1,581 | 231,303 |

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

**Interest rate risk**

BOCHK has formulated an "Interest Rate Risk Management Policy" which sets out the framework and the methodologies to identify, measure, monitor and control interest rate risk.

Both the members of the Asset and Liability Management Committee ("ALCO") and Risk Committee ("RC") are responsible for interest rate risk management. ALCO maintains oversight of interest rate risk and RC sanctions the interest rate risk management policies formulated by ALCO. The interest rate risk is identified and measured on a daily basis. The Treasury Department manages the interest rate risk according to the established policies. The Finance Department closely monitors the related risks according to approved limits and reports the results to ALCO regularly. The Risk Management Department reviews the policies, guidelines and limits proposed by Treasury Department.

The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

– repricing risk – mismatches in the maturity or repricing periods of assets and liabilities

– yield curve risk – non-parallel shifts in the yield curve, e.g. steepening or flattening yield curves, causing adverse effects on net interest income or economic value

– basis risk – different pricing basis for different transactions so that yield on assets and cost of liabilities may change by different amounts within the same repricing period

– option risk – exercise of the options embedded in assets, liabilities and off-balance sheet items inducing a change in the cashflows of assets and liabilities

Gap analysis is one of the tools used to measure the Group's exposure to repricing risk and yield curve risk. As the risk is complicated by having optionality embedded in certain products, the behavioural assumptions are made to reflect more accurately the interest rate risk exposures. The key assumption in gap analysis includes the replacement of contractual maturity of fixed rate mortgage-backed (US prime and Alt-A) securities by behavioural maturity. This gap analysis provides the Group with a static view of the maturity and repricing characteristics of its interest rate sensitive balance sheet positions.

Based on repricing gap, sensitivities of earnings and economic value to interest rate changes (Earnings at Risk and Economic Value at Risk) are assessed through a hypothetical interest rate shock of 200 basis points across the yield curve assuming parallel shifts on both sides. Limits on Earnings at Risk and Economic Value at Risk, which are the risk appetites sanctioned by RC, are controlled respectively within an approved percentage of the projected net interest income for the year and the latest capital base. The results are reported to ALCO and RC on a monthly basis respectively.

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

**Interest rate risk (continued)**

Yield curve risk is also assessed by the impacts on earnings and economic value arising from steepening or flattening of the yield curve.

The impact of basis risk is gauged by the projected change in net interest income under scenarios of imperfect correlation in the adjustment of the rates earned and paid on different instruments. Ratios of assets to liabilities with similar pricing basis are established to monitor such risk.

In addition, the impact of optionality on non-maturity liabilities and prepayment of mortgage loans are evaluated under different stress scenarios.

The interest rate risk exposures in BOCHK are controlled through the use of limits:

1. Earnings at Risk limit

2. Economic Value at Risk limit

3. Interest Rate Mismatch Gap limits

In addition to adopting limits for interest rate risk control, the Group hedges its interest rate exposures by interest rate derivatives, of which plain vanilla interest rate swaps are used in most cases.

Before launching a new product or business, relevant departments are required to go through a risk assessment process, which include assessment of underlying interest rate risk and consideration of the adequacy of current risk management mechanism. Any material impact on interest rate risk noted during the risk assessment process will be reported to the Chief Financial Officer.

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

#### Interest rate risk (continued)

The tables below summarise the Group's exposure to interest rate risk as at 31 December. Included in the tables are the Group's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

| | 2008 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Up to 1 month HK$'m | 1-3 months HK$'m | 3-12 months HK$'m | 1-5 years HK$'m | Over 5 years HK$'m | Non-interest bearing HK$'m | Total HK$'m |
| **Assets** | | | | | | | |
| Cash and balances with banks and other financial institutions | 134,723 | – | – | – | – | 18,546 | 153,269 |
| Placements with banks and other financial institutions maturing between one and twelve months | – | 38,622 | 51,096 | – | – | – | 89,718 |
| Financial assets at fair value through profit or loss | 5,103 | 7,473 | 2,311 | 9,415 | 17,136 | 2,374 | 43,812 |
| Derivative financial instruments | – | – | – | – | – | 19,628 | 19,628 |
| Hong Kong SAR Government certificates of indebtedness | – | – | – | – | – | 34,200 | 34,200 |
| Advances and other accounts | 366,619 | 76,378 | 20,873 | 1,258 | 159 | 4,206 | 469,493 |
| Investment in securities | | | | | | | |
| – Available-for-sale securities | 31,282 | 28,066 | 42,437 | 47,155 | 21,995 | 1,686 | 172,621 |
| – Held-to-maturity securities | 24,837 | 38,406 | 12,514 | 17,371 | 13,337 | – | 106,465 |
| – Loans and receivables | 1,755 | 2,675 | 8,165 | – | – | – | 12,595 |
| Interests in associates | – | – | – | – | – | 88 | 88 |
| Investment properties | – | – | – | – | – | 7,727 | 7,727 |
| Properties, plant and equipment | – | – | – | – | – | 22,795 | 22,795 |
| Other assets (including deferred tax assets) | – | – | – | – | – | 14,833 | 14,833 |
| **Total assets** | 564,319 | 191,620 | 137,396 | 75,199 | 52,627 | 126,083 | 1,147,244 |
| **Liabilities** | | | | | | | |
| Hong Kong SAR currency notes in circulation | – | – | – | – | – | 34,200 | 34,200 |
| Deposits and balances of banks and other financial institutions | 55,274 | 10,655 | 3,272 | – | – | 19,578 | 88,779 |
| Financial liabilities at fair value through profit or loss | 6,769 | 13,412 | 1,749 | 8 | – | – | 21,938 |
| Derivative financial instruments | – | – | – | – | – | 20,450 | 20,450 |
| Deposits from customers | 629,855 | 102,169 | 32,532 | 253 | – | 37,768 | 802,577 |
| Debt securities in issue at amortised cost | 459 | 148 | 435 | – | – | – | 1,042 |
| Other accounts and provisions (including current and deferred tax liabilities) | 8,036 | 116 | 493 | 136 | – | 29,332 | 38,113 |
| Insurance contract liabilities | – | – | – | – | – | 28,274 | 28,274 |
| Subordinated liabilities | – | 735 | 26,604 | – | – | – | 27,339 |
| **Total liabilities** | 700,393 | 127,235 | 65,085 | 397 | – | 169,602 | 1,062,712 |
| Interest sensitivity gap | (136,074) | 64,385 | 72,311 | 74,802 | 52,627 | (43,519) | 84,532 |

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

### Interest rate risk (continued)

| | 2007 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Up to 1 month HK$'m | 1-3 months HK$'m | 3-12 months HK$'m | 1-5 years HK$'m | Over 5 years HK$'m | Non-interest bearing HK$'m | Total HK$'m |
| **Assets** | | | | | | | |
| Cash and balances with banks and other financial institutions | 152,746 | – | – | – | – | 6,319 | 159,065 |
| Placements with banks and other financial institutions maturing between one and twelve months | – | 42,230 | 10,924 | – | – | – | 53,154 |
| Financial assets at fair value through profit or loss | 3,562 | 1,839 | 2,164 | 5,894 | 17,397 | 3,584 | 34,440 |
| Derivative financial instruments | – | – | – | – | – | 14,477 | 14,477 |
| Hong Kong SAR Government certificates of indebtedness | – | – | – | – | – | 32,770 | 32,770 |
| Advances and other accounts | 328,750 | 58,396 | 19,372 | 9,487 | 643 | 3,586 | 420,234 |
| Investment in securities | | | | | | | |
| – Available-for-sale securities | 11,668 | 21,320 | 6,257 | 19,959 | 40,869 | 4,580 | 104,653 |
| – Held-to-maturity securities | 25,562 | 43,920 | 18,534 | 43,022 | 34,390 | – | 165,428 |
| – Loans and receivables | 7,459 | 11,444 | 12,199 | – | – | – | 31,102 |
| Interests in associates | – | – | – | – | – | 83 | 83 |
| Investment properties | – | – | – | – | – | 8,058 | 8,058 |
| Properties, plant and equipment | – | – | – | – | – | 23,293 | 23,293 |
| Other assets (including deferred tax assets) | – | – | – | – | – | 20,880 | 20,880 |
| **Total assets** | 529,747 | 179,149 | 69,450 | 78,362 | 93,299 | 117,630 | 1,067,637 |
| **Liabilities** | | | | | | | |
| Hong Kong SAR currency notes in circulation | – | – | – | – | – | 32,770 | 32,770 |
| Deposits and balances of banks and other financial institutions | 45,728 | 3,428 | 6,897 | – | – | 4,546 | 60,599 |
| Financial liabilities at fair value through profit or loss | 6,600 | 2,355 | 1,531 | 919 | – | – | 11,405 |
| Derivative financial instruments | – | – | – | – | – | 11,092 | 11,092 |
| Deposits from customers | 623,009 | 98,440 | 35,157 | 547 | – | 36,453 | 793,606 |
| Debt securities in issue at amortised cost | – | – | 1,977 | 112 | – | – | 2,089 |
| Other accounts and provisions (including current and deferred tax liabilities) | 7,624 | 107 | – | 128 | – | 30,662 | 38,521 |
| Insurance contract liabilities | – | – | – | – | – | 22,497 | 22,497 |
| **Total liabilities** | 682,961 | 104,330 | 45,562 | 1,706 | – | 138,020 | 972,579 |
| Interest sensitivity gap | (153,214) | 74,819 | 23,888 | 76,656 | 93,299 | (20,390) | 95,058 |

## 4. Financial risk management (continued)

### *4.2 Market Risk (continued)*

**Interest rate risk (continued)**

*Sensitivity analysis to market risk exposure of banking book of the Group*

The Group is principally exposed to HKD and USD in terms of interest rate risk. At 31 December 2008, if HKD and USD market interest rates had been 100 basis point higher with other variables held constant, profit after tax for the year would have been reduced by HK$89 million (2007: HK$102 million). The negative impact is reduced compared with 2007 because the short term negative interest sensitivity gaps are narrowed. Reserves would have been reduced by HK$1,390 million (2007: HK$1,598 million) of the expected reduction in valuation of available-for-sale portfolio due to the above simulated market rates movement. The sensitivity analysis set out above is illustrative only.

*Interest rate exposures in banking book*

The following is a summary of possible effects of market interest rates shocks on the Group's interest rate exposure for major currencies in its banking book:

| | Impact on positions at 31 December | |
|---|---|---|
| **Earnings perspective**<br>**Scenarios** | **2008**<br>**HK$'m** | 2007<br>HK$'m |
| Down 100 basis points parallel shift in HK dollar yield curves | **(257)** | (402) |
| Up 100 basis points parallel shift in US dollar yield curves | **(364)** | (562) |

Note:

BOC Life and BOC-CC are excluded from the analysis in 2007.

BOC Life and BOC-CC are included in the analysis in 2008.

The projections illustrate that stressful changes in market interest rates in response to exceptional but plausible events would have adverse effects both on earnings over the next twelve months and economic value. While the possible effect of interest rates shock on earnings is assessed by changes in net interest income, the possible impact on economic value is measured in terms of expected net future cash flow discounted by projected market rates. To construct stressful scenarios, severe assumptions are made, including a change in the correlation between HK dollar and US dollar interest rates, on the two separate perspectives of earnings and economic value. Other assumptions are also made on the projections, such as a parallel movement of interest rates for the banking book positions of all repricing or maturity dates. In the absence of actions that would be taken to mitigate the impact of interest rates shock, all positions are assumed to run to maturity and reprice or mature simultaneously within a given time band. The stress tests set out above are illustrative only.

## 4. Financial risk management (continued)

### *4.3 Liquidity Risk*

Liquidity risk is the risk that the Group may not be able to fund increases in assets or meet obligations as they fall due without incurring unacceptable losses.

**Liquidity risk management framework**

The liquidity risk management framework of the Group comprises three levels. The Board of Directors and the Risk Committee are the ultimate decision making authority and are responsible for the compliance with regulatory requirements. Formulation of the risk management procedures and implementation mechanism and monitoring of the compliance are mainly the responsibilities of senior management (including Chief Executive, Chief Financial Officer, Chief Risk Officer and the Asset and Liability Management Committee). Daily management of liquidity is carried out by the treasury functions, which is assisted by other functional departments, including the finance and risk management departments which monitor the liquidity risk and provide regular reports to the management and local regulatory bodies.

The liquidity management process is adopted at the Group level. The principal subsidiaries of the Group execute their risk management strategies independently, subject to risk policies that are consistent with those of the Group, and report to the Group's management on a regular basis.

The Group funds its operations principally by accepting deposits from retail and corporate depositors. In addition, the Group may issue certificates of deposit to secure long-term funds. Funding may also be secured through adjusting the asset mix in the Group's investment portfolio. The Group uses the majority of funds raised to extend loans, to purchase debt securities or to conduct inter-bank placements.

The Group has developed a robust liquidity risk management mechanism which aims at enabling the Group to meet, even under adverse market conditions, all its maturing repayment obligations on time, and to fund all its asset growth and strategic opportunities without forced liquidation of its assets at short notice. The objective is achieved through maintenance of a highly-liquefiable assets portfolio and establishment of a diversified portfolio of liabilities.

Risk management process includes:

– Perform cash-flow projections under normal and stressed scenarios, using the net mismatch gap between assets and liabilities to estimate the prospective net funding requirements;

– Maintain a minimum mismatch ratio to control the size of the cumulative net mismatch positions;

– Maintain strong liquidity ratios to comply with both internal and external regulatory requirements;

– Ensure sound and sufficient funding sources and maintain stable and diversified core deposits;

– Maintain a proper level of highly liquid assets to serve as a liquidity buffer for emergency needs;

– Monitor the structure and stability of the deposit portfolio;

– Assess the ability to borrow from the inter-bank money market and monitor the portfolio of lenders to avoid over-reliance on the money market for funding;

– Maintain a proper contingency plan, which includes setting early warning signals (including internal indicators and market indicators) with timely monitoring procedures and establishing a management reporting system and contingency procedures.

## 4. Financial risk management (continued)

### *4.3 Liquidity Risk (continued)*

**Liquidity risk management framework (continued)**

The Group has set up three Key Risk Indicators: 1-month liquidity ratio, 1-month mismatch ratio and loan-to-deposit ratio which are used as the major tools in the identification, measurement, monitoring and control of the liquidity risk by setting limits on, assess and monitor the ratios on a regular basis. The Group also utilises cash flow analysis, and monitors deposit stability, concentration of deposits from large depositors and liquidity profile of the investment portfolio.

Before launching a new product or business, relevant departments are required to go through a risk assessment process, which includes assessment of underlying liquidity risk and consideration of the adequacy of the current risk management mechanism. Any material impact on liquidity risk noted during the risk assessment process will be reported both to the Chief Risk Officer and the Chief Financial Officer.

#### (a) Analysis of undiscounted cash flows by contractual maturities

*Non-derivative cash flows*

The table below presents the cash flows payable by the Group as at 31 December for non-derivative financial liabilities by remaining contractual maturities.

| | **2008** | | | | | |
|---|---|---|---|---|---|---|
| | **Up to 1 month HK$'m** | **1-3 months HK$'m** | **3-12 months HK$'m** | **1-5 years HK$'m** | **Over 5 years HK$'m** | **Total HK$'m** |
| Hong Kong SAR currency notes in circulation | **34,200** | **–** | **–** | **–** | **–** | **34,200** |
| Deposits and balances of banks and other financial institutions | **74,864** | **10,696** | **3,291** | **–** | **–** | **88,851** |
| Financial liabilities at fair value through profit or loss | **6,114** | **6,404** | **9,077** | **253** | **294** | **22,142** |
| Deposits from customers | **667,726** | **101,097** | **33,052** | **1,392** | **–** | **803,267** |
| Debt securities in issue at amortised cost | **459** | **148** | **436** | **–** | **–** | **1,043** |
| Subordinated liabilities | **–** | **7** | **1,051** | **4,978** | **32,233** | **38,269** |
| Other financial liabilities | **27,329** | **198** | **1,836** | **4** | **238** | **29,605** |
| | **810,692** | **118,550** | **48,743** | **6,627** | **32,765** | **1,017,377** |

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Up to 1 month HK$'m | 1-3 months HK$'m | 3-12 months HK$'m | 1-5 years HK$'m | Over 5 years HK$'m | Total HK$'m |
| Hong Kong SAR currency notes in circulation | 32,770 | – | – | – | – | 32,770 |
| Deposits and balances of banks and other financial institutions | 50,290 | 3,456 | 6,951 | – | – | 60,697 |
| Financial liabilities at fair value through profit or loss | 2,563 | 1,966 | 4,788 | 1,976 | 364 | 11,657 |
| Deposits from customers | 659,884 | 99,025 | 35,789 | 585 | – | 795,283 |
| Debt securities in issue at amortised cost | 7 | 13 | 2,021 | 116 | – | 2,157 |
| Other financial liabilities | 29,192 | 412 | 450 | 133 | 501 | 30,688 |
| | 774,706 | 104,872 | 49,999 | 2,810 | 865 | 933,252 |

## 4. Financial risk management (continued)

### *4.3 Liquidity Risk (continued)*

#### (a) Analysis of undiscounted cash flows by contractual maturities (continued)

*Derivative cash flows*

(i) Derivatives settled on a net basis

The Group's derivatives that will be settled on a net basis include:

- Foreign exchange derivatives: non-deliverable OTC currency options, currency futures, non-deliverable currency forwards;
- Interest rate derivatives: interest rate swaps;
- Equity derivatives: exchange traded equity options; and
- Bullion derivatives: bullion margin contracts.

The table below analyses the Group's derivative financial liabilities as at 31 December that will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows of derivatives with net negative fair value.

| | **2008** | | | | | |
|---|---|---|---|---|---|---|
| | **Up to 1 month HK$'m** | **1-3 months HK$'m** | **3-12 months HK$'m** | **1-5 years HK$'m** | **Over 5 years HK$'m** | **Total HK$'m** |
| Derivatives settled on a net basis | | | | | | |
| – Foreign exchange derivatives | **(10,465)** | **(99)** | **(235)** | **–** | **–** | **(10,799)** |
| – Interest rate derivatives | **–** | **(178)** | **(884)** | **(3,023)** | **(724)** | **(4,809)** |
| – Bullion derivatives | **(91)** | **–** | **–** | **–** | **–** | **(91)** |
| | **(10,556)** | **(277)** | **(1,119)** | **(3,023)** | **(724)** | **(15,699)** |

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Up to 1 month HK$'m | 1-3 months HK$'m | 3-12 months HK$'m | 1-5 years HK$'m | Over 5 years HK$'m | Total HK$'m |
| Derivatives settled on a net basis | | | | | | |
| – Foreign exchange derivatives | (7,221) | (12) | 456 | 21 | – | (6,756) |
| – Interest rate derivatives | (1) | (23) | (143) | (309) | (66) | (542) |
| – Equity derivatives | – | (58) | – | – | – | (58) |
| – Bullion derivatives | (1,110) | – | – | – | – | (1,110) |
| | (8,332) | (93) | 313 | (288) | (66) | (8,466) |

## 4. Financial risk management (continued)

### *4.3 Liquidity Risk (continued)*

**(a) Analysis of undiscounted cash flows by contractual maturities (continued)**

*Derivative cash flows (continued)*

(ii) Derivatives settled on a gross basis

The Group's derivatives that will be settled on a gross basis include OTC currency options, currency forwards and cross currency interest rate swaps, OTC equity options, equity linked swaps and bullion swaps.

The table below analyses the Group's derivative financial instruments as at 31 December that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the gross contractual undiscounted cash flows for all derivatives that are settled on a gross basis.

| | 2008 | | | | |
|---|---|---|---|---|---|
| | Up to 1 month HK$'m | 1-3 months HK$'m | 3-12 months HK$'m | 1-5 years HK$'m | Total HK$'m |
| Derivatives settled on a gross basis | | | | | |
| – Foreign exchange derivatives: | | | | | |
| – Outflow | (146,872) | (69,270) | (62,608) | (1,722) | (280,472) |
| – Inflow | 145,552 | 68,892 | 62,246 | 1,709 | 278,399 |
| – Interest rate derivatives: | | | | | |
| – Outflow | – | – | – | – | – |
| – Inflow | 316 | – | – | – | 316 |
| – Equity derivatives: | | | | | |
| – Outflow | (444) | (236) | (1,659) | – | (2,339) |
| – Inflow | 462 | 237 | 1,659 | – | 2,358 |
| – Bullion derivatives: | | | | | |
| – Outflow | (226) | (131) | – | – | (357) |
| – Inflow | – | – | – | – | – |
| **Total outflow** | (147,542) | (69,637) | (64,267) | (1,722) | (283,168) |
| **Total inflow** | 146,330 | 69,129 | 63,905 | 1,709 | 281,073 |

## 4. Financial risk management (continued)

### *4.3 Liquidity Risk (continued)*

#### (a) Analysis of undiscounted cash flows by contractual maturities (continued)

*Derivative cash flows (continued)*

(ii) Derivatives settled on a gross basis (continued)

| | 2007 | | | | |
|---|---|---|---|---|---|
| | Up to 1 month HK$'m | 1-3 months HK$'m | 3-12 months HK$'m | 1-5 years HK$'m | Total HK$'m |
| Derivatives settled on a gross basis | | | | | |
| – Foreign exchange derivatives: | | | | | |
| – Outflow | (96,928) | (52,508) | (24,477) | (1,869) | (175,782) |
| – Inflow | 96,743 | 52,301 | 24,380 | 1,866 | 175,290 |
| – Interest rate derivatives: | | | | | |
| – Outflow | – | – | – | – | – |
| – Inflow | – | 316 | – | – | 316 |
| – Equity derivatives: | | | | | |
| – Outflow | (128) | (70) | (1,002) | (28) | (1,228) |
| – Inflow | 221 | 99 | 1,002 | 28 | 1,350 |
| – Bullion derivatives: | | | | | |
| – Outflow | (223) | (427) | (715) | – | (1,365) |
| – Inflow | – | – | – | – | – |
| **Total outflow** | (97,279) | (53,005) | (26,194) | (1,897) | (178,375) |
| **Total inflow** | 96,964 | 52,716 | 25,382 | 1,894 | 176,956 |

*Off-balance sheet items*

Loan commitments

The contractual amounts of the Group's off-balance sheet financial instruments as at 31 December 2008 that commit to extend credit to customers and other facilities amounting to HK$219,336 million (2007: HK$193,027 million) are maturing no later than 1 year.

Financial guarantees and other financial facilities

Financial guarantees as at 31 December 2008 amounting to HK$34,053 million (2007: HK$38,276 million) are maturing no later than 1 year.

## 4. Financial risk management (continued)

### *4.3 Liquidity Risk (continued)*

#### (b) Maturity analysis

Tables below analyse assets and liabilities of the Group as at 31 December into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

| | 2008 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | On demand HK$'m | Up to 1 month HK$'m | 1-3 months HK$'m | 3-12 months HK$'m | 1-5 years HK$'m | Over 5 years HK$'m | Indefinite HK$'m | Total HK$'m |
| **Assets** | | | | | | | | |
| Cash and balances with banks and other financial institutions | 77,935 | 75,334 | – | – | – | – | – | 153,269 |
| Placements with banks and other financial institutions maturing between one and twelve months | – | – | 38,622 | 51,096 | – | – | – | 89,718 |
| Financial assets at fair value through profit or loss | | | | | | | | |
| – debt securities held for trading | | | | | | | | |
| – certificates of deposit held | – | – | – | – | – | – | – | – |
| – others | – | 4,628 | 6,685 | 1,927 | 685 | 6 | – | 13,931 |
| – debt securities designated at fair value through profit or loss | | | | | | | | |
| – certificates of deposit held | – | 25 | – | – | 2,008 | 1,536 | – | 3,569 |
| – others | – | 226 | 426 | 384 | 7,058 | 15,840 | 4 | 23,938 |
| – equity securities | – | – | – | – | – | – | 2,374 | 2,374 |
| Derivative financial instruments | 14,844 | 756 | 1,253 | 1,439 | 1,216 | 120 | – | 19,628 |
| Hong Kong SAR Government certificates of indebtedness | 34,200 | – | – | – | – | – | – | 34,200 |
| Advances and other accounts | | | | | | | | |
| – advances to customers | 21,980 | 17,656 | 31,084 | 51,336 | 197,399 | 137,684 | 1,007 | 458,146 |
| – trade bills | – | 2,910 | 4,022 | 677 | – | – | – | 7,609 |
| – advances to banks and other financial institutions | 27 | – | – | 885 | 2,826 | – | – | 3,738 |
| Investment in securities | | | | | | | | |
| – debt securities held for available-for-sale | | | | | | | | |
| – certificates of deposit held | – | – | 23 | 5,236 | 2,096 | – | – | 7,355 |
| – others | – | 19,849 | 13,349 | 40,054 | 58,135 | 26,164 | 6,029 | 163,580 |
| – debt securities held for held-to-maturity | | | | | | | | |
| – certificates of deposit held | – | 2,040 | 2,173 | 2,162 | 6,073 | – | – | 12,448 |
| – others | – | 2,115 | 4,933 | 14,560 | 49,480 | 15,905 | 7,024 | 94,017 |
| – debt securities held for loans and receivables | – | 1,755 | 2,675 | 8,165 | – | – | – | 12,595 |
| – equity securities | – | – | – | – | – | – | 1,686 | 1,686 |
| Interests in associates | – | – | – | – | – | – | 88 | 88 |
| Investment properties | – | – | – | – | – | – | 7,727 | 7,727 |
| Properties, plant and equipment | – | – | – | – | – | – | 22,795 | 22,795 |
| Other assets (including deferred tax assets) | 2,185 | 12,027 | 11 | 126 | 157 | – | 327 | 14,833 |
| **Total assets** | 151,171 | 139,321 | 105,256 | 178,047 | 327,133 | 197,255 | 49,061 | 1,147,244 |
| **Liabilities** | | | | | | | | |
| Hong Kong SAR currency notes in circulation | 34,200 | – | – | – | – | – | – | 34,200 |
| Deposits and balances of banks and other financial institutions | 61,206 | 13,646 | 10,655 | 3,272 | – | – | – | 88,779 |
| Financial liabilities at fair value through profit or loss | | | | | | | | |
| – certificates of deposit issued | – | – | – | 858 | – | – | – | 858 |
| – others | – | 6,111 | 6,363 | 8,170 | 166 | 270 | – | 21,080 |
| Derivative financial instruments | 10,556 | 2,137 | 1,689 | 1,967 | 2,822 | 1,279 | – | 20,450 |
| Deposits from customers | 428,849 | 238,769 | 100,891 | 32,696 | 1,372 | – | – | 802,577 |
| Debt securities in issue at amortised cost | – | 459 | 148 | 435 | – | – | – | 1,042 |
| Other accounts and provisions (including current and deferred tax liabilities) | 16,328 | 16,003 | 204 | 2,341 | 2,857 | 232 | 148 | 38,113 |
| Insurance contract liabilities | 1,406 | 792 | 2 | 16 | 18,033 | 8,025 | – | 28,274 |
| Subordinated liabilities | – | – | – | 21 | 735 | 26,583 | – | 27,339 |
| **Total liabilities** | 552,545 | 277,917 | 119,952 | 49,776 | 25,985 | 36,389 | 148 | 1,062,712 |
| Net liquidity gap | (401,374) | (138,596) | (14,696) | 128,271 | 301,148 | 160,866 | 48,913 | 84,532 |

## 4. Financial risk management (continued)

### *4.3 Liquidity Risk (continued)*

### (b) Maturity analysis (continued)

| | 2007 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | On demand HK$'m | Up to 1 month HK$'m | 1-3 months HK$'m | 3-12 months HK$'m | 1-5 years HK$'m | Over 5 years HK$'m | Indefinite HK$'m | Total HK$'m |
| **Assets** | | | | | | | | |
| Cash and balances with banks and other financial institutions | 40,100 | 118,965 | – | – | – | – | – | 159,065 |
| Placements with banks and other financial institutions maturing between one and twelve months | – | – | 42,230 | 10,924 | – | – | – | 53,154 |
| Financial assets at fair value through profit or loss | | | | | | | | |
| – debt securities held for trading | | | | | | | | |
| – certificates of deposit held | – | – | – | 80 | – | – | – | 80 |
| – others | – | 1,697 | 779 | 2,342 | 1,307 | 32 | – | 6,157 |
| – debt securities designated at fair value through profit or loss | | | | | | | | |
| – certificates of deposit held | – | – | – | 415 | 393 | 2,316 | – | 3,124 |
| – others | – | 36 | 343 | 272 | 5,376 | 15,468 | – | 21,495 |
| – equity securities | – | – | – | – | – | – | 3,584 | 3,584 |
| Derivative financial instruments | 12,686 | 228 | 129 | 929 | 459 | 46 | – | 14,477 |
| Hong Kong SAR Government certificates of indebtedness | 32,770 | – | – | – | – | – | – | 32,770 |
| Advances and other accounts | | | | | | | | |
| – advances to customers | 21,196 | 16,345 | 25,968 | 43,608 | 173,120 | 130,067 | 1,373 | 411,677 |
| – trade bills | 12 | 2,815 | 2,227 | 280 | – | – | – | 5,334 |
| – advances to banks and other financial institutions | 27 | – | 600 | 440 | 2,156 | – | – | 3,223 |
| Investment in securities | | | | | | | | |
| – debt securities held for available-for-sale | | | | | | | | |
| – certificates of deposit held | – | 701 | 462 | 2,614 | 3,689 | – | – | 7,466 |
| – others | – | 5,886 | 3,776 | 7,515 | 30,790 | 44,084 | 556 | 92,607 |
| – debt securities held for held-to-maturity | | | | | | | | |
| – certificates of deposit held | – | 1,097 | 1,490 | 2,426 | 6,351 | 624 | – | 11,988 |
| – others | – | 4,278 | 12,309 | 17,166 | 81,918 | 34,031 | 3,738 | 153,440 |
| – debt securities held for loans and receivables | – | 7,459 | 11,444 | 12,199 | – | – | – | 31,102 |
| – equity securities | – | – | – | – | – | – | 4,580 | 4,580 |
| Interests in associates | – | – | – | – | – | – | 83 | 83 |
| Investment properties | – | – | – | – | – | – | 8,058 | 8,058 |
| Properties, plant and equipment | – | – | – | – | – | – | 23,293 | 23,293 |
| Other assets (including deferred tax assets) | 3,360 | 16,219 | 24 | 174 | 202 | – | 901 | 20,880 |
| **Total assets** | 110,151 | 175,726 | 101,781 | 101,384 | 305,761 | 226,668 | 46,166 | 1,067,637 |
| **Liabilities** | | | | | | | | |
| Hong Kong SAR currency notes in circulation | 32,770 | – | – | – | – | – | – | 32,770 |
| Deposits and balances of banks and other financial institutions | 28,200 | 22,074 | 3,428 | 6,897 | – | – | – | 60,599 |
| Financial liabilities at fair value through profit or loss | | | | | | | | |
| – certificates of deposit issued | – | – | – | 1,086 | 868 | – | – | 1,954 |
| – others | – | 2,554 | 1,925 | 3,680 | 983 | 309 | – | 9,451 |
| Derivative financial instruments | 8,320 | 418 | 355 | 954 | 831 | 214 | – | 11,092 |
| Deposits from customers | 329,544 | 329,918 | 98,440 | 35,157 | 547 | – | – | 793,606 |
| Debt securities in issue at amortised cost | – | – | – | 1,977 | 112 | – | – | 2,089 |
| Other accounts and provisions (including current and deferred tax liabilities) | 15,446 | 15,543 | 1,071 | 1,660 | 4,100 | – | 701 | 38,521 |
| Insurance contract liabilities | 2,054 | – | – | 535 | 13,786 | 6,122 | – | 22,497 |
| **Total liabilities** | 416,334 | 370,507 | 105,219 | 51,946 | 21,227 | 6,645 | 701 | 972,579 |
| Net liquidity gap | (306,183) | (194,781) | (3,438) | 49,438 | 284,534 | 220,023 | 45,465 | 95,058 |

## 4. Financial risk management (continued)

### *4.3 Liquidity Risk (continued)*

#### (b) Maturity analysis (continued)

The above maturity classifications have been prepared in accordance with relevant provisions under the Banking (Disclosure) Rules. The Group has reported assets such as advances and debt securities which have been overdue for not more than one month as "Repayable on demand". In the case of an asset that is repayable by different payments or instalments, only that portion of the asset that is actually overdue is reported as overdue. Any part of the asset that is not due is reported according to the residual maturity unless the repayment of the asset is in doubt in which case the amount is reported as "Indefinite". The above assets are stated after deduction of provisions, if any.

The analysis of debt securities by remaining period to maturity is disclosed in order to comply with relevant provisions under the Banking (Disclosure) Rules. The disclosure does not imply that the securities will be held to maturity.

The above analysis in respect of insurance contract liabilities represents the estimated timing of net cash outflows resulting from recognised insurance contract liabilities on the balance sheet as at 31 December.

### *4.4 Insurance Risk*

The Group is in the business of insuring against the risk of mortality, morbidity, disability, critical illness, accidents and related risks. The Group manages these risks through the application of its underwriting policies and reinsurance arrangement.

The underwriting strategy is intended to set premium pricing at an appropriate level that corresponds with the underlying exposure of the risks underwritten. Screening processes, such as the review of health condition and family medical history, are also included in the Group's underwriting procedures.

Within the insurance process, concentrations of risk may arise where a particular event or series of events could impact heavily upon the Group's liabilities. Such concentrations may arise from a single insurance contract or through a small number of related contracts, and relate to circumstances where significant liabilities could arise.

For the in-force insurance contracts, most of the underlying insurance liabilities are related to endowment and unit-linked insurance products.

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 and persistency. In order to assess the uncertainty due to the mortality assumption and lapse assumption, the Group conducts mortality study and lapse study in order to determine the appropriate assumptions. In these studies, consistent results are reflected in both assumptions with appropriate margins.

## 4. Financial risk management (continued)

### *4.5 Capital Management*

The major objective of the Group's capital management is to maximise total shareholders' return while maintaining a capital adequacy position in relation to the Group's overall risk profile. The Group periodically reviews its capital structure and adjusts the capital mix where appropriate to achieve the required rate of return on capital.

The Group has developed and maintained a sound framework of policies and controls on capital management to support the development of the Group's business and to meet the statutory capital adequacy ratio. ALCO monitors the Group's capital adequacy. The Group has complied with all the statutory capital standards for all the periods.

For the implementation of Basel II in 2007, the Group has adopted the standardised approach under Pillar one to calculate the capital charge on credit risk, market risk and operational risk in compliance with the Banking (Capital) Rules. This new regulatory capital framework aligns regulatory capital requirements more closely with the inherent risks.

In 2007, the Group established an Internal Capital Adequacy Assessment Process (ICAAP). Through this process, each material risk from the Group's main activities is assessed by pre-defined assessment models, and a comprehensive judgment of the overall risk profile is decided subsequently by taking into account the Group's governance culture. Finally, the minimum CAR is derived through the procedures to relate the Group's overall risk profile to its capital adequacy. The minimum CAR aims to cover the various material risks undertaken by the Group. The Group considers this ICAAP process as an on-going process for capital management and periodically reviews its capital structure and adjusts it in relation to the overall risk profile.

In addition, the annual capital plans of the Group are drawn up and discussed by the ALCO and submitted to the board for approval. The plan is built up by assessing the impacts by various factors upon CAR such as the business strategies, return on equity, risk appetite, credit rating, as well as regulatory requirements, and based on this study to derive our future capital demand and the way to obtain the capital sources. The plan is to ensure the Group's capital adequacy and achieve optimal capital structure in order to align with its business development needs and risk profile.

#### (a) Capital adequacy ratio

| | **2008** | 2007 |
|---|---|---|
| Capital adequacy ratio | **16.17%** | 13.08% |
| Core capital ratio | **10.86%** | 12.23% |

The capital ratios are computed on the consolidated basis that comprises the positions of BOCHK and certain subsidiaries specified by the HKMA for its regulatory purposes and in accordance with the Banking (Capital) Rules.

The differences between the basis of consolidation for accounting and regulatory purposes are described in "Appendix – Subsidiaries of the Company" on page 227.

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

#### (b) Components of capital base after deductions

The consolidated capital base after deductions used in the calculation of the above capital adequacy ratio as at 31 December and reported to the HKMA is analysed as follows:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Core capital: | | |
| Paid up ordinary share capital | **43,043** | 43,043 |
| Reserves | **18,049** | 22,611 |
| Profit and loss account | **2,956** | 207 |
| Minority interests | **1,124** | 1,284 |
| | **65,172** | 67,145 |
| Deductions from core capital | **(1,536)** | (483) |
| Core capital | **63,636** | 66,662 |
| Supplementary capital: | | |
| Fair value gains arising from holdings of available-for-sale securities | **87** | 18 |
| Fair value gains arising from holdings of securities designated at fair value through profit or loss | **–** | 9 |
| Collective loan impairment allowances | **1,502** | 1,004 |
| Regulatory reserve | **4,503** | 4,130 |
| Term subordinated debt | **26,583** | – |
| | **32,675** | 5,161 |
| Deductions from supplementary capital | **(1,536)** | (483) |
| Supplementary capital | **31,139** | 4,678 |
| Total capital base after deductions | **94,775** | 71,340 |

Subsidiaries which are not included in the consolidation group for the calculation of capital adequacy ratios are denoted in "Appendix – Subsidiaries of the Company" on page 227. Investment costs in such subsidiaries are deducted from the capital base.

Term subordinated debt represents subordinated loans qualified as Tier 2 Capital of BOCHK pursuant to the regulatory requirements of the HKMA. Going forward, BOCHK will continue to take proactive measures to manage its capital, with a view to meet its strategic development needs.

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

#### (c) Capital charge for credit, market and operational risks

The capital adequacy ratios shown above are calculated on the consolidation basis for regulatory purposes in accordance with the Banking (Capital) Rules. The table below summaries the capital requirements and capital charge calculated by applying 8% on the risk-weighted amounts, computed on the same consolidation basis for credit, market, and operational risks.

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Credit risk | **43,609** | 40,878 |
| Market risk | **728** | 640 |
| Operational risk | **3,531** | 3,131 |
| | **47,868** | 44,649 |

*(i) Capital requirements for credit risk*

| | 2008 | | | | | |
|---|---|---|---|---|---|---|
| | Total exposures HK$'m | Exposures after CRM* Rated HK$'m | Exposures after CRM* Unrated HK$'m | Risk-weighted amount Rated HK$'m | Risk-weighted amount Unrated HK$'m | Capital requirement** HK$'m |
| On-balance sheet exposures | | | | | | |
| Sovereign | 137,693 | 142,513 | – | 602 | – | 48 |
| Public sector entity | 5,289 | 21,507 | – | 4,301 | – | 344 |
| Multilateral development bank | 5,887 | 5,887 | – | – | – | – |
| Bank | 321,992 | 318,872 | 12,807 | 96,789 | 5,909 | 8,216 |
| Securities firm | 12 | – | – | – | – | – |
| Corporate | 321,192 | 67,091 | 234,426 | 34,821 | 234,426 | 21,540 |
| Cash items | 39,451 | – | 39,451 | – | – | – |
| Regulatory retail | 31,919 | – | 30,312 | – | 22,734 | 1,819 |
| Residential mortgage loans | 149,084 | – | 132,716 | – | 53,708 | 4,296 |
| Other exposures which are not past due | 34,896 | – | 34,313 | – | 34,313 | 2,745 |
| Past due exposures | 800 | – | 800 | – | 871 | 70 |
| Total for on-balance sheet exposures | 1,048,215 | 555,870 | 484,825 | 136,513 | 351,961 | 39,078 |
| Off-balance sheet exposures | | | | | | |
| Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts | 46,045 | 11,156 | 34,889 | 6,144 | 34,113 | 3,221 |
| OTC derivative transactions | 6,243 | 5,750 | 493 | 1,871 | 448 | 186 |
| Total for off-balance sheet exposures | 52,288 | 16,906 | 35,382 | 8,015 | 34,561 | 3,407 |
| Total for non-securitisation exposures | 1,100,503 | 572,776 | 520,207 | 144,528 | 386,522 | 42,485 |
| Securitisation exposures | 24,144 | 24,144 | – | 14,057 | – | 1,124 |
| | 1,124,647 | 596,920 | 520,207 | 158,585 | 386,522 | 43,609 |

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

#### (c) Capital charge for credit, market and operational risks (continued)

*(i) Capital requirements for credit risk (continued)*

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Total exposures HK$'m | Exposures after CRM* Rated HK$'m | Exposures after CRM* Unrated HK$'m | Risk-weighted amount Rated HK$'m | Risk-weighted amount Unrated HK$'m | Capital requirement** HK$'m |
| On-balance sheet exposures | | | | | | |
| Sovereign | 46,140 | 47,096 | – | 603 | – | 48 |
| Public sector entity | 6,091 | 22,366 | – | 4,473 | – | 358 |
| Multilateral development bank | 1,396 | 1,396 | – | – | – | – |
| Bank | 357,628 | 349,758 | 12,481 | 90,907 | 4,856 | 7,661 |
| Securities firm | 34 | – | 13 | – | 6 | 1 |
| Corporate | 297,638 | 77,134 | 208,248 | 34,861 | 208,248 | 19,449 |
| Cash items | 37,446 | – | 37,446 | – | – | – |
| Regulatory retail | 29,867 | – | 28,232 | – | 21,174 | 1,694 |
| Residential mortgage loans | 137,562 | – | 121,271 | – | 48,718 | 3,897 |
| Other exposures which are not past due | 37,667 | – | 36,892 | – | 36,891 | 2,951 |
| Past due exposures | 1,080 | 71 | 1,009 | 14 | 1,095 | 89 |
| Total for on-balance sheet exposures | 952,549 | 497,821 | 445,592 | 130,858 | 320,988 | 36,148 |
| Off-balance sheet exposures | | | | | | |
| Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts | 54,841 | 8,046 | 46,795 | 4,864 | 42,494 | 3,789 |
| OTC derivative transactions | 3,717 | 2,565 | 1,152 | 643 | 1,101 | 139 |
| Total for off-balance sheet exposures | 58,558 | 10,611 | 47,947 | 5,507 | 43,595 | 3,928 |
| Total for non-securitisation exposures | 1,011,107 | 508,432 | 493,539 | 136,365 | 364,583 | 40,076 |
| Securitisation exposures | 50,110 | 50,110 | – | 10,022 | – | 802 |
| | 1,061,217 | 558,542 | 493,539 | 146,387 | 364,583 | 40,878 |

* Recognised credit risk mitigation satisfying the requirements and conditions set out in the Banking (Capital) Rules.

** For disclosure purposes, capital requirement is calculated by applying 8% on the risk-weighted amount, which may differ from the Group's actual regulatory capital.

As at 31 December 2008, credit exposures deducted from the capital base amounted to HK$2,571 million (2007: HK$472 million).

The Group used the STC approach for calculation of credit risk.

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

#### (c) Capital charge for credit, market and operational risks (continued)

*(i) Capital requirements for credit risk (continued)*

The ECAIs recognised by the Group includes Standard & Poor's, Moody's and Fitch. The Group adopted external rating based approach to determine the risk weight of the following classes of exposures, including those of securitisation exposures:

– Sovereign

– Public sector entity

– Multilateral development bank

– Bank

– Securities firm

– Corporate

The process the Group used to map ECAI issuer ratings to exposures booked in the banking book is a process prescribed in Part 4 of the Banking (Capital) Rules.

Counterparty credit risk exposures

The Group's counterparty credit risk arising from over-the-counter ("OTC") derivative transactions, repo-style transactions both in trading and banking book is subject to the same risk management framework as above mentioned. The Group established credit limit through formal credit approval procedures to control the pre-settlement credit risk arising from derivatives transactions and settlement limit to control the settlement risk arising from foreign exchange-related transactions in both the trading book and banking book. The Group monitors the risk exposure due to fluctuations in the market value by determining the current exposure value of the transactions. Exceptions or excesses are timely and closely identified and monitored by credit risk management units.

As the Group has not implemented capital allocation policy, there is no internal capital assigned for counterparty credit exposures.

The Group's policy for securing and managing collateral is applicable in managing counterparty credit risk. Besides, we established prudent eligibility criteria and haircut policy of debt securities secured as collateral for repo-style transactions.

The Group formulated policy for classification of credit assets according to the probability of default of individual counterparty and the period of overdue. If there is objective evidence that an impairment loss has been incurred, impairment allowance will be provided according to regulatory and HK accounting requirements.

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

#### (c) Capital charge for credit, market and operational risks (continued)

*(i) Capital requirements for credit risk (continued)*

Counterparty credit risk exposures (continued)

The following table summarises the Group's exposures to counterparty credit risk arising from OTC derivative transactions:

| | **2008**<br>**HK$'m** | 2007<br>HK$'m |
|---|---|---|
| Gross total positive fair value | **3,120** | 1,239 |
| Credit equivalent amount | **6,243** | 3,717 |
| Less: recognised collateral | **–** | – |
| Net credit equivalent amount | **6,243** | 3,717 |
| Net credit equivalent amount analysed by type of issuer: | | |
| Sovereign | **4** | 8 |
| Bank | **5,830** | 2,654 |
| Corporate | **406** | 1,006 |
| Others | **3** | 49 |
| | **6,243** | 3,717 |
| Risk weighted amount analysed by type of issuer: | | |
| Sovereign | **4** | 8 |
| Bank | **1,908** | 685 |
| Corporate | **405** | 1,002 |
| Others | **3** | 49 |
| | **2,320** | 1,744 |
| Notional amount of recognised credit derivative contracts which provide credit protection | **–** | – |

There is no effect of valid bilateral netting agreement on the credit equivalent amounts of the derivative transactions as at 31 December 2008 (2007: Nil).

There are no outstanding repo-style transactions or credit derivative contracts as at 31 December 2008 and 2007.

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

### (c) Capital charge for credit, market and operational risks (continued)

*(i) Capital requirements for credit risk (continued)*

Credit risk mitigation

For those collaterals recognised under capital management, the Group has well-defined policies and procedures for collateral valuation and management which is compliant with the operational requirements for recognised collateral for credit risk mitigation stated in the Banking (Capital) Rules.

The main types of recognised collaterals include cash deposit, gold bullion, debt securities, equities and funds for non past-due exposures. In addition, real property collateral is also recognised for past due exposures. Those collaterals taken by the Group are compliant with the comprehensive approach in its treatment of recognised collateral for credit risk mitigation in capital calculation as mentioned in the Banking (Capital) Rules.

According to the Banking (Capital) Rules, the recognised guarantees for credit risk mitigation under STC approach includes the guarantee given by sovereign, public sector entity, multilateral development bank, bank, securities firm with a lower risk weights than the counterparty; or corporate with external credit rating A- or above.

The concentration risk management for collaterals is embedded in the collateral management policy, including stress testing. To cope with the requirement under Pillar two, we have adopted a scorecard methodology to assess our credit concentration risk and consider whether add-on capital charge is needed to cover this risk.

Up to the date of report, the Group has not used any recognised credit derivative contracts, on- or off-balance sheet recognised netting for credit risk mitigation yet.

Exposures, other than those arising from OTC derivative transactions and repo-style transactions, covered by recognised credit risk mitigation are analysed as follows:

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Covered by recognised collateral HK$'m** | **Covered by recognised guarantees HK$'m** | Covered by recognised collateral HK$'m | Covered by recognised guarantees HK$'m |
| On-balance sheet exposures | | | | |
| Public sector entity | **–** | **70** | – | – |
| Securities firm | **12** | **–** | 21 | – |
| Corporate | **5,266** | **23,915** | 6,593 | 16,950 |
| Regulatory retail | **1,575** | **40** | 1,590 | 45 |
| Residential mortgage loans | **84** | **16,283** | 157 | 16,134 |
| Other exposures which are not past due | **583** | **–** | 775 | – |
| Past due exposures | **688** | **34** | 862 | 74 |
| Off-balance sheet exposures | **11,145** | **8,161** | 9,069 | 8,612 |
| | **19,353** | **48,503** | 19,067 | 41,815 |

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

#### (c) Capital charge for credit, market and operational risks (continued)

*(i) Capital requirements for credit risk (continued)*

Asset securitisation

The Group has not acted as an originating institution in respect of securitisation transactions during the year. Securitisation exposures arising from the Group's investing activities are analysed as follows:

| | **2008** | | | |
|---|---|---|---|---|
| | **Total exposures HK$'m** | **Risk weighted amounts HK$'m** | **Capital requirement HK$'m** | **Exposures deducted from capital base HK$'m** |
| Traditional securitisations | | | | |
| Residential mortgages | **19,830** | **13,175** | **1,054** | **1,769** |
| Commercial mortgages | **1,382** | **277** | **22** | **–** |
| Student loans | **1,953** | **390** | **31** | **–** |
| Auto loans | **785** | **176** | **14** | **–** |
| Credit card receivables | **194** | **39** | **3** | **–** |
| | **24,144** | **14,057** | **1,124** | **1,769** |

| | 2007 | | | |
|---|---|---|---|---|
| | Total exposures HK$'m | Risk weighted amounts HK$'m | Capital requirement HK$'m | Exposures deducted from capital base HK$'m |
| Traditional securitisations | | | | |
| Residential mortgages | 44,370 | 8,874 | 710 | – |
| Commercial mortgages | 1,560 | 312 | 25 | – |
| Student loans | 1,641 | 328 | 26 | – |
| Auto loans | 1,760 | 352 | 28 | – |
| Credit card receivables | 779 | 156 | 13 | – |
| | 50,110 | 10,022 | 802 | – |

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

#### (c) Capital charge for credit, market and operational risks (continued)

*(ii) Capital charge for market risk*

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Interest rate exposures | **569** | 450 |
| Equity exposures | **14** | 56 |
| Foreign exchange exposures | **142** | 132 |
| Commodity exposures | **3** | 2 |
| | **728** | 640 |

The Group used the STM approach for calculation of market risk.

The Group's positions covered by the STM approach are as follows:

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Long HK$'m** | **Short HK$'m** | Long HK$'m | Short HK$'m |
| Interest rate exposures | **383,286** | **382,934** | 208,062 | 207,180 |
| Equity exposures | **82** | **22** | 333 | 303 |
| Foreign exchange exposures (Net) | **1,463** | **–** | 1,458 | – |
| Commodities exposures | **11** | **15** | 11 | 20 |
| | **384,842** | **382,971** | 209,864 | 207,503 |

Equity exposures in banking book

Equity holdings in other entities are accounted for in accordance with the underlying intentions of holdings, at the outset of the acquisition of the respective equity exposures. Bookings for the equity holdings taken for relationship and strategic reasons will be separated from the bookings for equity holdings taken for other reasons (including the reason of capital appreciation).

Gains or losses related to equity exposures are summarised below:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Realised gains from sales or liquidations | **97** | 1 |
| Unrealised gains on revaluation recognised in reserves but not through profit or loss | **163** | 27 |
| Unrealised gains included in supplementary capital | **87** | 18 |

## 4. Financial risk management (continued)

### *4.5 Capital Management (continued)*

#### (c) Capital charge for credit, market and operational risks (continued)

*(iii) Capital charge for operational risk*

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Capital charge for operational risk | **3,531** | 3,131 |

The Group used the STO approach for calculation of operational risk.

### *4.6 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 various financial instruments. The following methods and assumptions have been used to estimate the fair value of each class of financial instrument as far as practicable.

**Balances with banks and other financial institutions and Trade bills**

The maturities of these financial assets and liabilities are within one year and the carrying value approximates fair value.

**Advances to customers, banks and other financial institutions**

Substantially all the advances to customers, banks and other financial institutions are on floating rate terms, bear interest at prevailing market interest rates and their carrying value approximates fair value.

**Held-to-maturity securities**

Fair value for held-to-maturity securities is based on 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. The carrying value and fair value as at 31 December 2008 amounted to HK$106,465 million (2007: HK$165,428 million) and HK$103,220 million (2007: HK$166,110 million) respectively.

**Loans and receivables, Certificates of deposit issued and Debt securities in issue**

A discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity and their carrying value approximates fair value.

**Deposits from customers**

Substantially all the deposits from customers mature within one year from balance sheet date and their carrying value approximates fair value.

**Subordinated liabilities**

All the subordinated liabilities are on floating rate terms, bear interest at prevailing market interest rates and their carrying value approximates fair value.

## 5. Net interest income

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| **Interest income** | | |
| Cash and due from banks and other financial institutions | **5,523** | 8,311 |
| Advances to customers | **16,246** | 20,803 |
| Listed investments | **3,042** | 2,593 |
| Unlisted investments | **10,067** | 13,698 |
| Others | **403** | 651 |
| | **35,281** | 46,056 |
| **Interest expense** | | |
| Due to banks, customers and other financial institutions | **(13,968)** | (25,787) |
| Debt securities in issue | **(130)** | (103) |
| Subordinated liabilities | **(250)** | – |
| Others | **(776)** | (771) |
| | **(15,124)** | (26,661) |
| **Net interest income** | **20,157** | 19,395 |

Included within interest income is HK$20 million (2007: HK$47 million) of interest with respect to income recognised on advances classified as impaired for the year ended 31 December 2008. Interest accrued on impaired investment in securities amounted to HK$362 million (2007: HK$1 million).

Included within interest income and interest expense are HK$33,664 million (2007: HK$44,791 million) and HK$14,338 million (2007: HK$25,907 million) for financial assets and financial liabilities that are not recognised at fair value through profit or loss respectively.

## 6. Net fees and commission income

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| **Fees and commission income** | | |
| Securities brokerage | | |
| – Stockbroking | **2,380** | 3,560 |
| – Bonds | **259** | 211 |
| Credit cards | **1,220** | 1,027 |
| Bills commissions | **683** | 588 |
| Loan commissions | **513** | 347 |
| Payment services | **486** | 464 |
| Asset management | **218** | 683 |
| Insurance | **209** | 153 |
| Trust services | **173** | 153 |
| Guarantees | **37** | 32 |
| Others | | |
| – RMB business | **223** | 137 |
| – currency exchange | **204** | 184 |
| – safe deposit box | **188** | 182 |
| – information search | **44** | 42 |
| – correspondent banking | **44** | 37 |
| – low deposit balance accounts | **28** | 33 |
| – postage and telegrams | **18** | 27 |
| – dormant accounts | **17** | 20 |
| – agency services | **16** | 20 |
| – BOC cards | **10** | 28 |
| – sundries | **244** | 249 |
| | **7,214** | 8,177 |
| **Fees and commission expenses** | **(2,035)** | (1,903) |
| **Net fees and commission income** | **5,179** | 6,274 |
| Of which arise from | | |
| – financial assets or financial liabilities not at fair value through profit or loss | | |
| – Fees and commission income | **680** | 403 |
| – Fees and commission expenses | **(42)** | (58) |
| | **638** | 345 |
| – trust and other fiduciary activities | | |
| – Fees and commission income | **296** | 254 |
| – Fees and commission expenses | **(6)** | (6) |
| | **290** | 248 |

## 7. Net trading income

| | 2008<br>HK$'m | 2007<br>HK$'m |
|---|---|---|
| Net gain/(loss) from: | | |
| – foreign exchange and foreign exchange products | **1,809** | 800 |
| – interest rate instruments | **(127)** | 30 |
| – equity instruments | **119** | 181 |
| – commodities | **113** | 2 |
| | **1,914** | 1,013 |

## 8. Net loss on investment in securities

| | 2008<br>HK$'m | 2007<br>HK$'m |
|---|---|---|
| Net loss from disposal of available-for-sale securities | **(14)** | (55) |
| Net gain from redemption of held-to-maturity securities | **–** | 2 |
| Net loss from disposal of loans and receivables | **(1)** | – |
| | **(15)** | (53) |

## 9. Net insurance premium income

| | 2008<br>HK$'m | 2007<br>HK$'m |
|---|---|---|
| Gross earned premiums | **5,921** | 8,435 |
| Less: Gross written premiums ceded to reinsurers | **(30)** | (9) |
| Net insurance premium income | **5,891** | 8,426 |

## 10. Other operating income

| | 2008<br>HK$'m | 2007<br>HK$'m |
|---|---|---|
| Dividend income from investment in securities | | |
| – listed investments | **109** | – |
| – unlisted investments | **17** | 15 |
| Gross rental income from investment properties | **320** | 254 |
| Less: Outgoings in respect of investment properties | **(52)** | (52) |
| Others | **167** | 554 |
| | **561** | 771 |

Included in the "Outgoings in respect of investment properties" is HK$2 million (2007: HK$3 million) of direct operating expenses related to investment properties that were not let during the year.

## 11. Net insurance benefits and claims

| | **2008** **HK$'m** | 2007 HK$'m |
|---|---|---|
| Claims, benefits and surrenders paid | **1,297** | 1,360 |
| Movement in liabilities | **6,419** | 8,084 |
| Gross claims, benefits and surrenders paid and movement in liabilities | **7,716** | 9,444 |
| Less: Reinsurers' share of claims, benefits and surrenders paid and movement in liabilities | **(7)** | (4) |
| Net insurance claims, benefits and surrenders paid and movement in liabilities | **7,709** | 9,440 |

## 12. Net charge of impairment allowances

| | **2008** **HK$'m** | 2007 HK$'m |
|---|---|---|
| **Advances to customers** | | |
| Individually assessed | | |
| – new allowances | **813** | 330 |
| – releases | **(83)** | (299) |
| – recoveries | **(722)** | (1,311) |
| Net charge/(reversal) of individually assessed loan impairment allowances (Note 27) | **8** | (1,280) |
| Collectively assessed | | |
| – new allowances | **691** | 625 |
| – releases | **(10)** | – |
| – recoveries | **(28)** | (30) |
| Net charge of collectively assessed loan impairment allowances (Note 27) | **653** | 595 |
| Net charge/(reversal) of loan impairment allowances | **661** | (685) |
| **Available-for-sale securities** | | |
| Net charge of impairment losses on available-for-sale securities Individually assessed | **7,839** | 289 |
| **Held-to-maturity securities** | | |
| Net charge of impairment allowances on held-to-maturity securities Individually assessed (Note 28) | **4,061** | 1,844 |
| **Others** | **12** | – |
| **Net charge of impairment allowances** | **12,573** | 1,448 |

## 13. Operating expenses

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Staff costs (including directors' emoluments) | | |
| – salaries and other costs | **4,128** | 4,341 |
| – termination benefit | **55** | 14 |
| – pension cost | **371** | 301 |
| | **4,554** | 4,656 |
| Premises and equipment expenses (excluding depreciation) | | |
| – rental of premises | **408** | 347 |
| – information technology | **411** | 378 |
| – others | **257** | 233 |
| | **1,076** | 958 |
| Depreciation (Note 32) | **992** | 787 |
| Auditors' remuneration | | |
| – audit services | **33** | 32 |
| – non-audit services | **5** | 5 |
| Other operating expenses | **2,111** | 1,335 |
| | **8,771** | 7,773 |

## 14. Net (loss)/gain from disposal of/fair value adjustments on investment properties

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Net gain on disposal of investment properties | **14** | 8 |
| Net (loss)/gain on fair value adjustments on investment properties (Note 31) | **(132)** | 1,056 |
| | **(118)** | 1,064 |

## 15. Net gain from disposal/revaluation of properties, plant and equipment

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Net gain on disposal of premises | **35** | 23 |
| Net loss on disposal of other fixed assets | **(4)** | (16) |
| Net (loss)/gain on revaluation of premises (Note 32) | **(24)** | 19 |
| | **7** | 26 |

## 16. Taxation

Taxation in the income statement represents:

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Hong Kong profits tax | | |
| Current tax | | |
| – current year taxation | **1,326** | 2,985 |
| – over-provision in prior years | **(13)** | (29) |
| | **1,313** | 2,956 |
| Deferred tax (credit)/charge (Note 39) | | |
| – origination and reversal of temporary differences | **(341)** | 252 |
| – impact of change of Hong Kong tax rate | **(123)** | – |
| | **(464)** | 252 |
| Hong Kong profits tax | **849** | 3,208 |
| Overseas taxation | **222** | 101 |
| | **1,071** | 3,309 |

Hong Kong profits tax has been provided at the rate of 16.5% (2007: 17.5%) on the estimated assessable profits arising in Hong Kong during the year. Taxation on overseas profits has been calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the countries in which the Group operates.

The taxation on the Group's profit before taxation that differs from the theoretical amount that would arise using the taxation rate of Hong Kong is as follows:

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Profit before taxation | **4,078** | 19,126 |
| Calculated at a taxation rate of 16.5% (2007: 17.5%) | **673** | 3,347 |
| Effect of different taxation rates in other countries | **64** | 5 |
| Income not subject to taxation | **(295)** | (121) |
| Expenses not deductible for taxation purposes | **522** | 107 |
| Tax losses not recognised | **137** | 1 |
| Utilisation of previously unrecognised tax losses | **(17)** | (1) |
| Over-provision in prior years | **(13)** | (29) |
| Taxation charge | **1,071** | 3,309 |
| Effective tax rate | **26.3%** | 17.3 % |

## 17. Profit attributable to equity holders of the Company

The profit of the Company for the year ended 31 December 2008 attributable to equity holders of the Company and dealt with in the financial statements of the Company amounted to HK$1,372 million (2007: HK$14,441 million).

## 18. Dividends

| | 2008 | | 2007 | |
|---|---|---|---|---|
| | **Per share HK$** | **Total HK$'m** | Per share HK$ | Total HK$'m |
| Interim dividend paid | **0.438** | **4,631** | 0.428 | 4,525 |
| Proposed final dividend | **–** | **–** | 0.487 | 5,149 |
| | **0.438** | **4,631** | 0.915 | 9,674 |

At a meeting held on 28 August 2008, the Board declared an interim dividend of HK$0.438 per ordinary share for the first half of 2008 amounting to approximately HK$4,631 million.

At a meeting held on 24 March 2009, the Board recommended keeping sufficient funds for operation in the future and does not propose any final dividend for the year ended 31 December 2008.

## 19. Earnings per share for profit attributable to the equity holders of the Company

The calculation of basic earnings per share is based on the consolidated profit attributable to the equity holders of the Company for the year ended 31 December 2008 of approximately HK$3,343 million (2007: HK$15,446 million) and on the ordinary shares in issue of 10,572,780,266 shares (2007: 10,572,780,266 ordinary shares).

There was no dilution of earnings per share as no potential ordinary shares were in issue for the year ended 31 December 2008 (2007: Nil).

## 20. Retirement benefit costs

The principal defined contribution schemes for the Group's employees are ORSO schemes exempted under the MPF Schemes Ordinance and the BOC-Prudential Easy Choice MPF Scheme. Under the ORSO schemes, employees make monthly contributions to the ORSO schemes equal to 5% of their basic salaries, while the employer makes monthly contributions equal to 5% to 15% of the employees' monthly basic salaries, depending on years of service. The employees are entitled to receive 100% of the employer's contributions upon termination of employment after completing 20 years of service, or at a scale ranging from 20% to 95% for employees who have completed between 3 to 20 years of service, on conditions of retirement, early retirement, permanent incapacity and ill-health or termination of employment other than summary dismissal.

With the implementation of the MPF Schemes Ordinance on 1 December 2000, the Group also participates in the BOC-Prudential Easy Choice MPF Scheme, of which the trustee is BOCI-Prudential Trustee and the investment manager is BOCI-Prudential Manager, which are related parties of the Company.

The Group's total contributions made to the ORSO schemes for the year ended 31 December 2008 amounted to approximately HK$312 million (2007: approximately HK$261 million), after a deduction of forfeited contributions of approximately HK$10 million (2007: approximately HK$15 million). For the MPF Scheme, the Group contributed approximately HK$38 million (2007: approximately HK$28 million) for the year ended 31 December 2008.

## 21. Share option schemes

### (a) *Share Option Scheme and Sharesave Plan*

The principal terms of the Share Option Scheme and the Sharesave Plan were approved and adopted by written resolutions of all the shareholders of the Company dated 10 July 2002.

The purpose of the Share Option Scheme is to provide the participants with the opportunity to acquire proprietary interests in the Company. The Board may, in its absolute discretion, offer to grant options under the Share Option Scheme to any person as the Board may select. The subscription price for the shares shall be determined on the date of grant by the Board as an amount per share calculated on the basis of established rules. An option may be exercised in whole or in part at any time after the date prescribed by the Board and from time to time as specified in the offer and on or before the termination date prescribed by the Board.

The purpose of the Sharesave Plan is to encourage broad-based employee ownership of the shares of the Company. The amount of the monthly contribution under the savings contract to be made in connection with an option shall be the amount which the relevant eligible employee is willing to contribute, which amount shall not be less than 1% and not more than 10% of the eligible employee's monthly salary as at the date of application or such other maximum or minimum amounts as permitted by the Board. When an option is exercised during an exercise period, it may be exercised in whole or in part.

No options were granted pursuant to the Share Option Scheme or the Sharesave Plan during the year 2008 (2007: Nil).

### (b) *Pre-Listing Share Option Scheme*

On 5 July 2002, several directors together with approximately 60 senior management personnel of the Group and employees of BOC were granted options by BOC (BVI), the immediate holding company of the Company, pursuant to a Pre-Listing Share Option Scheme to purchase from BOC (BVI) an aggregate of 31,132,600 existing issued shares of the Company. The Group has taken advantage of the transitional provisions set out in paragraph 53 of HKFRS 2 under which the new recognition and measurement policies have not been applied to all options granted to employees on or before 7 November 2002.

Details of the share options outstanding as at 31 December 2008 are disclosed as follows:

| | Directors | Senior management | Others* | Total number of share options | Average exercise price (HK$ per share) |
|---|---|---|---|---|---|
| At 1 January 2008 | **6,651,600** | **2,253,100** | **1,446,000** | **10,350,700** | **8.5** |
| Less: Share options exercised during the year | **(361,500)** | **(891,900)** | **(1,446,000)** | **(2,699,400)** | **8.5** |
| At 31 December 2008 | **6,290,100** | **1,361,200** | **–** | **7,651,300** | **8.5** |
| Exercisable at 31 December 2008 | **6,290,100** | **1,361,200** | **–** | **7,651,300** | **8.5** |
| At 1 January 2007 | 8,459,100 | 3,980,450 | 1,446,000 | 13,885,550 | 8.5 |
| Transfer | (1,446,000) | – | 1,446,000 | – | 8.5 |
| Less: Share options exercised during the year | (361,500) | (1,727,350) | (1,446,000) | (3,534,850) | 8.5 |
| At 31 December 2007 | 6,651,600 | 2,253,100 | 1,446,000 | 10,350,700 | 8.5 |
| Exercisable at 31 December 2007 | 6,651,600 | 2,253,100 | 1,446,000 | 10,350,700 | 8.5 |

* Represented share options held by ex-directors of the Group.

## 21. Share option schemes (continued)

### *(b) Pre-Listing Share Option Scheme (continued)*

Share options were exercised on a regular basis throughout the year, the weighted average share price during the year was HK$18.65 (2007: HK$19.38).

The options granted under this scheme can be exercised at HK$8.50 per share in respect of the option price of HK$1.00. These options have a vesting period of four years from the date on which dealings in the shares commenced on the Stock Exchange with a valid exercise period of ten years. No offer to grant any options under the Pre-Listing Share Option Scheme will be made on or after the date on which dealings in the shares commenced on the Stock Exchange.

## 22. Directors' and senior management's emoluments

### *(a) Directors' emoluments*

Details of the emoluments paid to or receivable by the directors of the Company in respect of their services rendered for the Company and managing the subsidiaries within the Group during the year are as follows:

| For the year 2008 | Directors' fees HK$'000 | Basic salaries, allowances and benefits in kind HK$'000 | Contributions to pension schemes HK$'000 | Bonus HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|
| **Executive Directors** | | | | | |
| He Guangbei | 100 | 6,013 | – | – | 6,113 |
| Lee Raymond Wing Hung | 414 | 6,979 | 247 | – | 7,640 |
| Gao Yingxin | 100 | 4,308 | – | – | 4,408 |
| | 614 | 17,300 | 247 | – | 18,161 |
| **Non-executive Directors** | | | | | |
| Xiao Gang | – | – | – | – | – |
| Sun Changji | 300 | – | – | – | 300 |
| Li Zaohang | 250 | – | – | – | 250 |
| Zhou Zaiqun | 365 | – | – | – | 365 |
| Zhang Yanling | 250 | – | – | – | 250 |
| Fung Victor Kwok King* | 300 | – | – | – | 300 |
| Koh Beng Seng* | 350 | – | – | – | 350 |
| Shan Weijian* | 350 | – | – | – | 350 |
| Tung Chee Chen* | 300 | – | – | – | 300 |
| Tung Savio Wai-Hok* | 350 | – | – | – | 350 |
| Yang Linda Tsao* | 400 | – | – | – | 400 |
| | 3,215 | – | – | – | 3,215 |
| | 3,829 | 17,300 | 247 | – | 21,376 |

Note: Basic salaries, allowances and benefits in kind for the year 2008 include fixed guaranteed bonus.

## 22. Directors' and senior management's emoluments (continued)

### *(a) Directors' emoluments (continued)*

| For the year 2007 | Directors' fees HK$'000 | Basic salaries, allowances and benefits in kind HK$'000 | Contributions to pension schemes HK$'000 | Bonus HK$'000 | Total HK$'000 |
|---|---|---|---|---|---|
| **Executive Directors** | | | | | |
| He Guangbei | 100 | 5,326 | – | 3,000 | 8,426 |
| Lee Raymond Wing Hung** | 259 | 3,044 | 112 | 1,339 | 4,754 |
| Gao Yingxin** | 100 | 2,278 | – | 1,120 | 3,498 |
| | 459 | 10,648 | 112 | 5,459 | 16,678 |
| **Non-executive Directors** | | | | | |
| Xiao Gang | – | – | – | – | – |
| Sun Changji | 300 | – | – | – | 300 |
| Hua Qingshan | 137 | – | – | – | 137 |
| Li Zaohang | 250 | – | – | – | 250 |
| Zhou Zaiqun | 300 | – | – | – | 300 |
| Zhang Yanling | 250 | – | – | – | 250 |
| Fung Victor Kwok King* | 300 | – | – | – | 300 |
| Koh Beng Seng* | 350 | – | – | – | 350 |
| Shan Weijian* | 350 | – | – | – | 350 |
| Tung Chee Chen* | 300 | – | – | – | 300 |
| Tung Savio Wai-Hok* | 350 | – | – | – | 350 |
| Yang Linda Tsao* | 400 | – | – | – | 400 |
| | 3,287 | – | – | – | 3,287 |
| | 3,746 | 10,648 | 112 | 5,459 | 19,965 |

Note:

* Independent Non-executive Directors

** The directors were appointed on 25 May 2007, therefore the amounts of their emoluments for 2007 were disclosed on a pro-rata basis.

In July 2002, options were granted to several directors of the Company by the immediate holding company, BOC (BVI), under the Pre-Listing Share Option Scheme as set out in Note 21(b). Full details of the scheme are stated in Note 21. During the year, certain options were exercised, but no benefits arising from the granting of these share options were included in the directors' emoluments disclosed above or recognised in the income statement.

For the year ended 31 December 2008, one of the directors waived emoluments of HK$200,000 (2007: HK$200,000).

## 22. Directors' and senior management's emoluments (continued)

### *(b) Five highest paid individuals*

The five individuals whose emoluments were the highest in the Group for the year include 2 (2007: 2) directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining 3 (2007: 3) individuals during the year are as follows:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Basic salaries and allowances | **13** | 11 |
| Bonuses | **–** | 4 |
| Contributions to pension schemes | **1** | 1 |
| Director's fee from subsidiaries | **1** | – |
| Amount paid as an inducement to join the Group | **–** | 4 |
| | **15** | 20 |

Note: Basic salaries and allowances for the year 2008 include fixed guaranteed bonus.

Emoluments of individuals were within the following bands:

| | **Number of individuals** | |
|---|---|---|
| | **2008** | 2007 |
| HK$4,000,001 – HK$4,500,000 | **1** | – |
| HK$4,500,001 – HK$5,000,000 | **1** | – |
| HK$5,500,001 – HK$6,000,000 | **1** | 1 |
| HK$6,500,001 – HK$7,000,000 | **–** | 1 |
| HK$7,500,001 – HK$8,000,000 | **–** | 1 |

## 23. Cash and balances with banks and other financial institutions

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Cash | **4,232** | 3,334 |
| Balances with central banks | **66,158** | 30,627 |
| Balances with banks and other financial institutions | **7,545** | 6,139 |
| Placements with banks and other financial institutions maturing within one month | **75,334** | 118,965 |
| | **153,269** | 159,065 |

## 24. Financial assets at fair value through profit or loss

| | Trading securities | | Financial assets designated at fair value through profit or loss | | Total | |
|---|---|---|---|---|---|---|
| | **2008 HK$'m** | 2007 HK$'m | **2008 HK$'m** | 2007 HK$'m | **2008 HK$'m** | 2007 HK$'m |
| At fair value | | | | | | |
| Debt securities | | | | | | |
| – Listed in Hong Kong | **412** | 190 | **557** | 895 | **969** | 1,085 |
| – Listed outside Hong Kong | **35** | 537 | **3,095** | 2,687 | **3,130** | 3,224 |
| | **447** | 727 | **3,652** | 3,582 | **4,099** | 4,309 |
| – Unlisted | **13,484** | 5,510 | **23,855** | 21,037 | **37,339** | 26,547 |
| | **13,931** | 6,237 | **27,507** | 24,619 | **41,438** | 30,856 |
| Fund | | | | | | |
| – Unlisted | **–** | – | **2,168** | 2,814 | **2,168** | 2,814 |
| Equity securities | | | | | | |
| – Listed in Hong Kong | **20** | 327 | **124** | 349 | **144** | 676 |
| – Unlisted | **62** | 94 | **–** | – | **62** | 94 |
| | **82** | 421 | **124** | 349 | **206** | 770 |
| Total | **14,013** | 6,658 | **29,799** | 27,782 | **43,812** | 34,440 |

Financial assets at fair value through profit or loss are analysed by type of issuer as follows:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Sovereigns | **13,082** | 4,197 |
| Public sector entities | **1,791** | 1,333 |
| Banks and other financial institutions | **25,668** | 24,820 |
| Corporate entities | **3,271** | 4,090 |
| | **43,812** | 34,440 |

Financial assets at fair value through profit or loss are analysed as follows:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Treasury bills | **12,458** | 3,517 |
| Certificates of deposit held | **3,569** | 3,204 |
| Other financial assets at fair value through profit or loss | **27,785** | 27,719 |
| | **43,812** | 34,440 |

## 25. Derivative financial instruments and hedge accounting

The Group enters into the following equity, foreign exchange, interest rate and precious metal related derivative financial instruments for trading and risk management purposes:

Currency forwards represent commitments to purchase and sell foreign currency on a future date. Interest rate futures are contractual obligations to receive or pay a net amount based on changes in interest rates or buy or sell interest rate financial instruments on a future date at an agreed price in the financial market under the administration of the stock exchange. Forward rate agreements are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contracted rate of interest and the current market rate, based on a notional principal amount.

Currency, interest rate and precious metal swaps are commitments to exchange one set of cash flows or commodity for another. Swaps result in an exchange of currencies, interest rates (for example, fixed rate for floating rate), or precious metals (for example, silver swaps) 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, interest rate, equity and precious metal 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 the financial instrument at a predetermined price. In consideration for the assumption of foreign exchange and interest rate risk, the seller receives a premium from the purchaser. Options are negotiated over-the-counter ("OTC") between the Group and its counterparty or traded through the stock exchange (for example, exchange-traded stock option).

The contract/notional amounts and fair values of derivative financial instruments held by the Group are set out in the following tables. The contract/notional amounts of these instruments indicate the volume of transactions outstanding at the balance sheet dates and certain of them provide a basis for comparison with fair value instruments recognised on the consolidated balance sheet. However, they do not necessarily indicate the amounts of future cash flows involved or the current fair values of the instruments and, therefore, do not indicate the Group's exposure to credit or market risks. The derivative financial instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates, foreign exchange rates or equity and metal prices relative to their terms. The aggregate fair values of derivative financial instruments assets and liabilities can fluctuate significantly from time to time.

### *(a) Derivative financial instruments*

The Group trades derivative products (both exchange-traded or OTC) mainly for customer business. The Group strictly follows risk management policies in providing derivative products to our customers and in trading of derivative products in the interbank market.

Derivatives are also used to manage the interest rate risk of the banking book. A derivative instrument must be included in the approved product list before any transactions for that instrument can be made. There are limits to control the notional amount of exposure arising from derivative transactions, and the maximum tenor of the deal and management alert limit (MAL) in profit and loss is set. Every derivative transaction must be input into the relevant system for settlement, mark to market revaluation, reporting and control.

## 25. Derivative financial instruments and hedge accounting (continued)

### *(a) Derivative financial instruments (continued)*

The following tables summarise the contract/notional amounts of each significant type of derivative financial instrument as at 31 December:

| | 2008 | | | |
|---|---|---|---|---|
| | Trading HK$'m | Hedging HK$'m | Not qualified for hedge accounting* HK$'m | Total HK$'m |
| Exchange rate contracts | | | | |
| Spot and forwards | 182,624 | – | – | 182,624 |
| Swaps | 248,956 | – | 68 | 249,024 |
| Foreign currency option contracts | | | | |
| – Options purchased | 2,518 | – | – | 2,518 |
| – Options written | 2,754 | – | – | 2,754 |
| | 436,852 | – | 68 | 436,920 |
| Interest rate contracts | | | | |
| Futures | 4,290 | – | – | 4,290 |
| Swaps | 68,392 | 19,931 | 10,045 | 98,368 |
| Interest rate option contracts | | | | |
| – Bond options written | 775 | – | – | 775 |
| | 73,457 | 19,931 | 10,045 | 103,433 |
| Bullion contracts | 3,880 | – | – | 3,880 |
| Equity contracts | 5,070 | – | – | 5,070 |
| Other contracts | 144 | – | – | 144 |
| Total | 519,403 | 19,931 | 10,113 | 549,447 |

* Derivative transactions which do not qualify as hedges for accounting purposes but are managed in conjunction with the financial instruments designated at fair value through profit or loss are separately disclosed in compliance with the requirements set out in the Banking (Disclosure) Rules.

## 25. Derivative financial instruments and hedge accounting (continued)

### *(a) Derivative financial instruments (continued)*

| | 2007 | | | |
|---|---|---|---|---|
| | Trading HK$'m | Hedging HK$'m | Not qualified for hedge accounting HK$'m | Total HK$'m |
| Exchange rate contracts | | | | |
| Spot and forwards | 258,556 | – | 1,495 | 260,051 |
| Swaps | 156,554 | – | – | 156,554 |
| Foreign currency option contracts | | | | |
| – Options purchased | 5,607 | – | – | 5,607 |
| – Options written | 5,875 | – | – | 5,875 |
| | 426,592 | – | 1,495 | 428,087 |
| Interest rate contracts | | | | |
| Futures | 226 | – | – | 226 |
| Swaps | 36,714 | 6,708 | 3,253 | 46,675 |
| Interest rate option contracts | | | | |
| – Swaptions written | 780 | – | – | 780 |
| – Bond options written | 780 | – | – | 780 |
| | 38,500 | 6,708 | 3,253 | 48,461 |
| Bullion contracts | 12,950 | – | – | 12,950 |
| Equity contracts | 5,378 | – | – | 5,378 |
| Other contracts | 172 | – | – | 172 |
| Total | 483,592 | 6,708 | 4,748 | 495,048 |

## 25. Derivative financial instruments and hedge accounting (continued)

### *(a) Derivative financial instruments (continued)*

The following tables summarise the fair values of each class of derivative financial instrument as at 31 December:

| | 2008 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Fair value assets | | | | Fair value liabilities | | | |
| | Trading HK$'m | Hedging HK$'m | Not qualified for hedge accounting HK$'m | Total HK$'m | Trading HK$'m | Hedging HK$'m | Not qualified for hedge accounting HK$'m | Total HK$'m |
| Exchange rate contracts | | | | | | | | |
| Spot and forwards | 15,152 | – | – | 15,152 | (10,962) | – | – | (10,962) |
| Swaps | 1,624 | – | 1 | 1,625 | (3,933) | – | (3) | (3,936) |
| Foreign currency option contracts | | | | | | | | |
| – Options purchased | 21 | – | – | 21 | – | – | – | – |
| – Options written | – | – | – | – | (24) | – | – | (24) |
| | 16,797 | – | 1 | 16,798 | (14,919) | – | (3) | (14,922) |
| Interest rate contracts | | | | | | | | |
| Futures | 2 | – | – | 2 | (6) | – | – | (6) |
| Swaps | 1,420 | – | 18 | 1,438 | (2,329) | (1,769) | (166) | (4,264) |
| Interest rate option contracts | | | | | | | | |
| – Bond options written | – | – | – | – | (25) | – | – | (25) |
| | 1,422 | – | 18 | 1,440 | (2,360) | (1,769) | (166) | (4,295) |
| Bullion contracts | 248 | – | – | 248 | (91) | – | – | (91) |
| Equity contracts | 1,142 | – | – | 1,142 | (1,142) | – | – | (1,142) |
| Total | 19,609 | – | 19 | 19,628 | (18,512) | (1,769) | (169) | (20,450) |

## 25. Derivative financial instruments and hedge accounting (continued)

### *(a) Derivative financial instruments (continued)*

| | 2007 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Fair value assets | | | | Fair value liabilities | | | |
| | Trading HK$'m | Hedging HK$'m | Not qualified for hedge accounting HK$'m | Total HK$'m | Trading HK$'m | Hedging HK$'m | Not qualified for hedge accounting HK$'m | Total HK$'m |
| Exchange rate contracts | | | | | | | | |
| Spot and forwards | 12,588 | – | – | 12,588 | (7,822) | – | (10) | (7,832) |
| Swaps | 269 | – | – | 269 | (634) | – | – | (634) |
| Foreign currency option contracts | | | | | | | | |
| – Options purchased | 48 | – | – | 48 | – | – | – | – |
| – Options written | – | – | – | – | (51) | – | – | (51) |
| | 12,905 | – | – | 12,905 | (8,507) | – | (10) | (8,517) |
| Interest rate contracts | | | | | | | | |
| Swaps | 492 | 10 | 23 | 525 | (885) | (124) | (90) | (1,099) |
| Interest rate option contracts | | | | | | | | |
| – Swaptions written | – | – | – | – | (17) | – | – | (17) |
| – Bond options written | – | – | – | – | (23) | – | – | (23) |
| | 492 | 10 | 23 | 525 | (925) | (124) | (90) | (1,139) |
| Bullion contracts | 774 | – | – | 774 | (1,110) | – | – | (1,110) |
| Equity contracts | 273 | – | – | 273 | (326) | – | – | (326) |
| Total | 14,444 | 10 | 23 | 14,477 | (10,868) | (124) | (100) | (11,092) |

## 25. Derivative financial instruments and hedge accounting (continued)

### (a) *Derivative financial instruments (continued)*

The credit risk weighted amounts of the above derivative financial instruments are as follows:

| | **2008**<br>**HK$'m** | 2007<br>HK$'m |
|---|---|---|
| Exchange rate contracts | | |
| Forwards | **318** | 1,017 |
| Swaps | **1,377** | 492 |
| Foreign currency option contracts | | |
| – Options purchased | **4** | 19 |
| Interest rate contracts | | |
| Futures | **2** | – |
| Swaps | **577** | 104 |
| Bullion contracts | **5** | 63 |
| Equity contracts | **37** | 49 |
| | **2,320** | 1,744 |

The credit risk weighted amounts are the amounts that have been calculated in accordance with the Banking (Capital) Rules. The amounts calculated are dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

There is no effect of valid bilateral netting agreement on the fair values or the credit risk-weighted amounts of the derivative financial instruments.

Approximately 69% (2007: 52%) of the Group's transactions in derivative contracts are conducted with other financial institutions.

### (b) *Hedge accounting*

The Group designated all derivatives held for hedging as fair value hedges.

The Group uses interest rate swaps to hedge against change in fair value of financial assets arising from movements in market rates.

Gains or losses on fair value hedges for the year are as follows:

| | **2008**<br>**HK$'m** | 2007<br>HK$'m |
|---|---|---|
| Net gain/(loss) on | | |
| – hedging instruments | **(1,656)** | (125) |
| – hedged items | **1,677** | 114 |
| | **21** | (11) |

## 26. Advances and other accounts

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Personal loans and advances | 151,784 | 141,708 |
| Corporate loans and advances | 308,663 | 271,354 |
| Advances to customers | 460,447 | 413,062 |
| Loan impairment allowances | | |
| – Individually assessed | (800) | (381) |
| – Collectively assessed | (1,501) | (1,004) |
| | 458,146 | 411,677 |
| Trade bills | 7,609 | 5,334 |
| Advances to banks and other financial institutions | 3,738 | 3,223 |
| Total | 469,493 | 420,234 |

As at 31 December 2008, advances to customers included accrued interest on gross advances of HK$1,293 million (2007: HK$1,454 million).

As at 31 December 2008 and 2007, no impairment allowance was made in respect of trade bills and advances to banks and other financial institutions.

## 27. Loan impairment allowances

| | 2008 | | |
|---|---|---|---|
| | Individual assessment | | |
| | Personal HK$'m | Corporate HK$'m | Total HK$'m |
| At 1 January 2008 | 82 | 299 | 381 |
| (Credited)/charged to income statement (Note 12) | (30) | 38 | 8 |
| Loans written off during the year as uncollectible | (13) | (286) | (299) |
| Recoveries | 33 | 689 | 722 |
| Unwind of discount on allowance | (1) | (11) | (12) |
| At 31 December 2008 | 71 | 729 | 800 |

| | 2008 | | |
|---|---|---|---|
| | Collective assessment | | |
| | Personal HK$'m | Corporate HK$'m | Total HK$'m |
| At 1 January 2008 | 173 | 831 | 1,004 |
| Charged to income statement (Note 12) | 156 | 497 | 653 |
| Loans written off during the year as uncollectible | (175) | (1) | (176) |
| Recoveries | 28 | – | 28 |
| Unwind of discount on allowance | (3) | (5) | (8) |
| At 31 December 2008 | 179 | 1,322 | 1,501 |

## 27. Loan impairment allowances (continued)

| | 2007 | | |
|---|---|---|---|
| | Individual assessment | | |
| | Personal HK$'m | Corporate HK$'m | Total HK$'m |
| At 1 January 2007 | 117 | 429 | 546 |
| Credited to income statement (Note 12) | (52) | (1,228) | (1,280) |
| Loans written off during the year as uncollectible | (27) | (145) | (172) |
| Recoveries | 50 | 1,261 | 1,311 |
| Unwind of discount on allowance | (6) | (18) | (24) |
| At 31 December 2007 | 82 | 299 | 381 |

| | 2007 | | |
|---|---|---|---|
| | Collective assessment | | |
| | Personal HK$'m | Corporate HK$'m | Total HK$'m |
| At 1 January 2007 | 107 | 450 | 557 |
| Charged to income statement (Note 12) | 197 | 398 | 595 |
| Loans written off during the year as uncollectible | (155) | – | (155) |
| Recoveries | 30 | – | 30 |
| Unwind of discount on allowance | (6) | (17) | (23) |
| At 31 December 2007 | 173 | 831 | 1,004 |

## 28. Investment in securities

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| **The Group** | | |
| **(a) Available-for-sale securities** | | |
| Debt securities, at fair value | | |
| – Listed in Hong Kong | **4,588** | 3,659 |
| – Listed outside Hong Kong | **44,692** | 18,455 |
| | **49,280** | 22,114 |
| – Unlisted | **121,655** | 77,959 |
| | **170,935** | 100,073 |
| Equity securities, at fair value | | |
| – Listed in Hong Kong | **1,256** | 4,135 |
| – Unlisted | **430** | 445 |
| | **1,686** | 4,580 |
| | **172,621** | 104,653 |
| **(b) Held-to-maturity securities** | | |
| Listed, at amortised cost | | |
| – in Hong Kong | **4,082** | 4,107 |
| – outside Hong Kong | **21,302** | 21,078 |
| | **25,384** | 25,185 |
| Unlisted, at amortised cost | **85,521** | 141,925 |
| | **110,905** | 167,110 |
| Impairment allowances | **(4,440)** | (1,682) |
| | **106,465** | 165,428 |
| **(c) Loans and receivables** | | |
| Unlisted, at amortised cost | **12,595** | 31,102 |
| **Total** | **291,681** | 301,183 |
| Market value of listed held-to-maturity securities | **24,354** | 24,776 |

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| **The Company** | | |
| **Available-for-sale securities** | | |
| Equity securities, at fair value | | |
| – Listed in Hong Kong | **1,256** | 4,135 |

## 28. Investment in securities (continued)

Investment in securities is analysed by type of issuer as follows:

| | **2008** | | | |
|---|---|---|---|---|
| | **Available-for-sale securities HK$'m** | **Held-to-maturity securities HK$'m** | **Loans and receivables HK$'m** | **Total HK$'m** |
| **The Group** | | | | |
| Sovereigns | **70,274** | **1,079** | **–** | **71,353** |
| Public sector entities | **9,202** | **12,481** | **–** | **21,683** |
| Banks and other financial institutions | **71,832** | **72,498** | **12,595** | **156,925** |
| Corporate entities | **21,313** | **20,407** | **–** | **41,720** |
| | **172,621** | **106,465** | **12,595** | **291,681** |

| | 2007 | | | |
|---|---|---|---|---|
| | Available-for-sale securities HK$'m | Held-to-maturity securities HK$'m | Loans and receivables HK$'m | Total HK$'m |
| **The Group** | | | | |
| Sovereigns | 13,402 | 1,814 | – | 15,216 |
| Public sector entities | 9,673 | 20,530 | – | 30,203 |
| Banks and other financial institutions | 47,989 | 108,547 | 31,102 | 187,638 |
| Corporate entities | 33,589 | 34,537 | – | 68,126 |
| | 104,653 | 165,428 | 31,102 | 301,183 |

As at 31 December 2008 and 2007, all of the available-for-sale securities held by the Company are issued by banks and other financial institutions.

The movements in investment in securities are summarised as follows:

| | **2008** | | |
|---|---|---|---|
| | **Available-for-sale securities HK$'m** | **Held-to-maturity securities HK$'m** | **Loans and receivables HK$'m** |
| **The Group** | | | |
| At 1 January 2008 | **104,653** | **165,428** | **31,102** |
| Additions | **182,457** | **57,186** | **33,918** |
| Disposals, redemptions and maturity | **(101,229)** | **(106,014)** | **(52,627)** |
| Amortisation | **544** | **(1,035)** | **640** |
| Change in fair value | **(10,570)** | **–** | **–** |
| Impairment losses | **–** | **(4,061)** | **–** |
| Exchange differences | **(3,234)** | **(5,039)** | **(438)** |
| At 31 December 2008 | **172,621** | **106,465** | **12,595** |

## 28. Investment in securities (continued)

| | 2007 | | |
|---|---|---|---|
| | Available-for-sale securities HK$'m | Held-to-maturity securities HK$'m | Loans and receivables HK$'m |
| **The Group** | | | |
| At 1 January 2007 | 100,389 | 165,588 | 36,114 |
| Additions | 107,581 | 93,912 | 59,147 |
| Disposals, redemptions and maturity | (104,590) | (94,989) | (65,713) |
| Amortisation | 378 | 225 | 1,472 |
| Change in fair value | (654) | – | – |
| Impairment losses | – | (1,844) | – |
| Exchange differences | 1,549 | 2,536 | 82 |
| At 31 December 2007 | 104,653 | 165,428 | 31,102 |

| | Available-for-sale securities | |
|---|---|---|
| | **2008 HK$'m** | 2007 HK$'m |
| **The Company** | | |
| At 1 January | **4,135** | – |
| Additions | **–** | 3,986 |
| Change in fair value | **(2,879)** | 149 |
| At 31 December | **1,256** | 4,135 |

Available-for-sale and held-to-maturity securities are analysed as follows:

| | Available-for-sale securities | | Held-to-maturity securities | |
|---|---|---|---|---|
| | **2008 HK$'m** | 2007 HK$'m | **2008 HK$'m** | 2007 HK$'m |
| **The Group** | | | | |
| Treasury bills | **60,980** | 9,396 | **100** | 200 |
| Certificates of deposit held | **7,355** | 7,466 | **12,448** | 11,988 |
| Others | **104,286** | 87,791 | **93,917** | 153,240 |
| | **172,621** | 104,653 | **106,465** | 165,428 |

## 28. Investment in securities (continued)

The movements in impairment allowances on held-to-maturity securities are summarised as follows:

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| **The Group** | | |
| At 1 January | **1,682** | – |
| Charged to income statement (Note 12) | **4,061** | 1,844 |
| Disposals | **(1,303)** | (162) |
| At 31 December | **4,440** | 1,682 |

## 29. Investment in subsidiaries

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Unlisted shares, at cost | **54,019** | 53,764 |

The particulars of all direct and indirect subsidiaries of the Company are set out in the Appendix of the Annual Report, "Subsidiaries of the Company". The following is a list of principal subsidiaries as at 31 December 2008:

| Name | Country of incorporation & place of operation | Particulars of issued share capital | Interest held | Principal activities |
|---|---|---|---|---|
| Bank of China (Hong Kong) Limited | Hong Kong | 43,042,840,858 ordinary shares of HK$1 each | *100% | Banking business |
| BOC Group Life Assurance Company Limited | Hong Kong | 136,800,000 ordinary shares of HK$10 each | *51% | Life insurance business |
| Nanyang Commercial Bank, Limited | Hong Kong | 6,000,000 ordinary shares of HK$100 each | 100% | Banking business |
| Chiyu Banking Corporation Limited | Hong Kong | 3,000,000 ordinary shares of HK$100 each | 70.49% | Banking business |
| BOC Credit Card (International) Limited | Hong Kong | 4,800,000 ordinary shares of HK$100 each | 100% | Credit card services |
| Po Sang Futures Limited | Hong Kong | 250,000 ordinary shares of HK$100 each | 100% | Commodities brokerage |

* Shares held directly by the Company

## 30. Interests in associates

| | **2008** **HK$'m** | 2007 HK$'m |
|---|---|---|
| At 1 January | **83** | 60 |
| Investment cost addition | **–** | 24 |
| Share of result | **9** | 4 |
| Share of tax | **(2)** | (1) |
| Dividends received | **(2)** | (3) |
| Dissolution of an associate | **–** | (1) |
| At 31 December | **88** | 83 |

The Group's interests in its associates, all of which are unlisted, are as follows:

| **Name** | **CJM Insurance Brokers Limited** | | **Joint Electronic Teller Services Limited** | | **BOC Services Company Limited** | |
|---|---|---|---|---|---|---|
| **Place of incorporation** | **2008** and 2007 **Hong Kong** | | **2008** and 2007 **Hong Kong** | | **2008** and 2007 **PRC** | |
| **Particulars of issued share capital/registered capital** | **6,000,000 ordinary shares of HK$1 each** | | **100,238 ordinary shares of HK$100 each** | | **Registered capital RMB50,000,000** | |
| **Principal activities** | **Insurance broker** | | **Operation of a private inter-bank message switching network in respect of ATM services** | | **Credit card back-end service support** | |
| | **2008 HK$'000** | 2007 HK$'000 | **2008 HK$'000** | 2007 HK$'000 | **2008 HK$'000** | 2007 HK$'000 |
| **Assets** | **47,846** | 64,331 | **371,144** | 354,104 | **108,145** | 53,677 |
| **Liabilities** | **35,310** | 51,815 | **86,283** | 77,593 | **45,250** | – |
| **Revenues** | **11,389** | 10,330 | **75,297** | 70,033 | **118,274** | – |
| **Profit after taxation** | **1,519** | 1,481 | **34,752** | 33,649 | **5,166** | – |
| | **2008** | 2007 | **2008** | 2007 | **2008** | 2007 |
| **Interest held** | **33.33%** | 33.33% | **19.96%** | 19.96% | **45.00%** | 45.00% |

## 31. Investment properties

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| At 1 January | **8,058** | 7,481 |
| Disposals | **(186)** | (200) |
| Fair value (losses)/gains (Note 14) | **(132)** | 1,056 |
| Reclassification to properties, plant and equipment (Note 32) | **(13)** | (279) |
| At 31 December | **7,727** | 8,058 |

As at 31 December 2008, investment properties are included in the consolidated balance sheet at valuation carried out at 31 December 2008 on the basis of their fair value by an independent firm of chartered surveyors, Knight Frank Petty Limited.

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

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Held in Hong Kong | | |
| On long-term lease (over 50 years) | **7,040** | 7,251 |
| On medium-term lease (10 – 50 years) | **505** | 528 |
| On short-term lease (less than 10 years) | **–** | 48 |
| Held outside Hong Kong | | |
| On long-term lease (over 50 years) | **1** | 3 |
| On medium-term lease (10 – 50 years) | **177** | 224 |
| On short-term lease (less than 10 years) | **4** | 4 |
| | **7,727** | 8,058 |

## 32. Properties, plant and equipment

| | Premises HK$'m | Equipment, fixtures and fittings HK$'m | Total HK$'m |
|---|---|---|---|
| Net book value at 1 January 2008 | **20,783** | **2,510** | **23,293** |
| Additions | **42** | **776** | **818** |
| Disposals | **(68)** | **(5)** | **(73)** |
| Revaluation | **(265)** | **–** | **(265)** |
| Depreciation for the year (Note 13) | **(400)** | **(592)** | **(992)** |
| Reclassification from investment properties (Note 31) | **13** | **–** | **13** |
| Exchange difference | **–** | **1** | **1** |
| Net book value at 31 December 2008 | **20,105** | **2,690** | **22,795** |
| At 31 December 2008 | | | |
| Cost or valuation | **20,105** | **6,239** | **26,344** |
| Accumulated depreciation and impairment | **–** | **(3,549)** | **(3,549)** |
| Net book value at 31 December 2008 | **20,105** | **2,690** | **22,795** |
| Net book value at 1 January 2007 | 17,906 | 1,834 | 19,740 |
| Additions | – | 1,147 | 1,147 |
| Disposals | (16) | (17) | (33) |
| Revaluation | 2,946 | – | 2,946 |
| Depreciation for the year (Note 13) | (332) | (455) | (787) |
| Reclassification from investment properties (Note 31) | 279 | – | 279 |
| Exchange difference | – | 1 | 1 |
| Net book value at 31 December 2007 | 20,783 | 2,510 | 23,293 |
| At 31 December 2007 | | | |
| Cost or valuation | 20,783 | 5,642 | 26,425 |
| Accumulated depreciation and impairment | – | (3,132) | (3,132) |
| Net book value at 31 December 2007 | 20,783 | 2,510 | 23,293 |
| The analysis of cost or valuation of the above assets is as follows: | | | |
| At 31 December 2008 | | | |
| At cost | **–** | **6,239** | **6,239** |
| At valuation | **20,105** | **–** | **20,105** |
| | **20,105** | **6,239** | **26,344** |
| At 31 December 2007 | | | |
| At cost | – | 5,642 | 5,642 |
| At valuation | 20,783 | – | 20,783 |
| | 20,783 | 5,642 | 26,425 |

## 32. Properties, plant and equipment (continued)

The carrying value of premises is analysed based on the remaining terms of the leases as follows:

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Held in Hong Kong | | |
| On long-term lease (over 50 years) | **12,825** | 12,955 |
| On medium-term lease (10 – 50 years) | **6,873** | 7,584 |
| Held outside Hong Kong | | |
| On long-term lease (over 50 years) | **75** | 57 |
| On medium-term lease (10 – 50 years) | **306** | 170 |
| On short-term lease (less than 10 years) | **26** | 17 |
| | **20,105** | 20,783 |

As at 31 December 2008, premises are included in the consolidated balance sheet at valuation carried out at 31 December 2008 on the basis of their fair value by an independent firm of chartered surveyors, Knight Frank Petty Limited.

As a result of the above-mentioned revaluations, changes in value of the Group's premises were recognised in the Group's premises revaluation reserve, the income statement and minority interests respectively as follows:

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| (Decrease)/increase in valuation (charged)/credited to premises revaluation reserve | **(250)** | 2,910 |
| (Decrease)/increase in valuation (charged)/credited to income statement (Note 15) | **(24)** | 19 |
| Increase in valuation credited to minority interests | **9** | 17 |
| | **(265)** | 2,946 |

As at 31 December 2008, the net book value of premises that would have been included in the Group's consolidated balance sheet had the assets been carried at cost less accumulated depreciation and impairment losses was HK$6,123 million (2007: HK$6,072 million).

## 33. Other assets

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Repossessed assets | **124** | 76 |
| Precious metals | **1,347** | 1,741 |
| Accounts receivable and prepayments | **13,208** | 19,040 |
| | **14,679** | 20,857 |

## 34. Hong Kong SAR currency notes in circulation

The Hong Kong SAR currency notes in circulation are secured by deposit of funds in respect of which the Hong Kong SAR Government certificates of indebtedness are held.

## 35. Financial liabilities at fair value through profit or loss

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Trading liabilities | | |
| – Short positions in Exchange Fund Bills (Note 38) | **12,141** | 3,492 |
| Financial liabilities designated at fair value through profit or loss | | |
| – Structured deposits (Note 36) | **8,939** | 5,959 |
| – Certificates of deposit issued | **858** | 1,954 |
| | **9,797** | 7,913 |
| | **21,938** | 11,405 |

The carrying amount of financial liabilities designated at fair value through profit or loss as at 31 December 2008 is more than the amount that the Group would be contractually required to pay at maturity to the holders by HK$5 million, and it was less than the amount that the Group would be contractually required to pay at maturity to the holders by HK$44 million as at 31 December 2007. The amount of change in the fair values of financial liabilities at fair value through profit or loss, during the year and cumulatively, attributable to changes in credit risk is insignificant.

## 36. Deposits from customers

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Current, savings and other deposit accounts (per consolidated balance sheet) | **802,577** | 793,606 |
| Structured deposits reported as financial liabilities at fair value through profit or loss (Note 35) | **8,939** | 5,959 |
| | **811,516** | 799,565 |
| Analysed by: | | |
| Demand deposits and current accounts | | |
| – corporate customers | **35,867** | 32,645 |
| – individual customers | **10,175** | 7,854 |
| | **46,042** | 40,499 |
| Savings deposits | | |
| – corporate customers | **115,918** | 76,668 |
| – individual customers | **261,355** | 209,985 |
| | **377,273** | 286,653 |
| Time, call and notice deposits | | |
| – corporate customers | **150,526** | 172,342 |
| – individual customers | **237,675** | 300,071 |
| | **388,201** | 472,413 |
| | **811,516** | 799,565 |

## 37. Other accounts and provisions

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Other accounts payable | **34,297** | 33,335 |
| Provisions | **576** | 9 |
| | **34,873** | 33,344 |

## 38. Assets pledged as security

As at 31 December 2008, liabilities of the Group amounting to HK$12,141 million (2007: HK$3,492 million) were secured by assets deposited with central depositories to facilitate settlement operations. The amount of assets pledged by the Group to secure these liabilities was HK$12,243 million (2007: HK$3,836 million) included in "Trading securities" and "Available-for-sale securities".

## 39. Deferred taxation

Deferred tax is recognised in respect of the temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements in accordance with HKAS 12 "Income Taxes".

The major components of deferred tax assets and liabilities recorded in the consolidated balance sheet, and the movements during the year are as follows:

| | **2008** | | | | | |
|---|---|---|---|---|---|---|
| | **Accelerated tax depreciation HK$'m** | **Asset revaluation HK$'m** | **Losses HK$'m** | **Impairment allowance HK$'m** | **Other temporary differences HK$'m** | **Total HK$'m** |
| At 1 January 2008 | **533** | **3,777** | **(15)** | **(169)** | **(182)** | **3,944** |
| Charged/(credited) to income statement (Note 16) | **12** | **(205)** | **(111)** | **(85)** | **(75)** | **(464)** |
| Credited to equity and minority interests | **–** | **(108)** | **–** | **–** | **(727)** | **(835)** |
| At 31 December 2008 | **545** | **3,464** | **(126)** | **(254)** | **(984)** | **2,645** |

| | 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Accelerated tax depreciation HK$'m | Asset revaluation HK$'m | Losses HK$'m | Impairment allowance HK$'m | Other temporary differences HK$'m | Total HK$'m |
| At 1 January 2007 | 401 | 3,155 | (71) | (89) | (74) | 3,322 |
| Charged/(credited) to income statement (Note 16) | 132 | 143 | 56 | (80) | 1 | 252 |
| Charged/(credited) to equity and minority interests | – | 479 | – | – | (109) | 370 |
| At 31 December 2007 | 533 | 3,777 | (15) | (169) | (182) | 3,944 |

## 39. Deferred taxation (continued)

Deferred tax assets and liabilities are offset on an individual entity basis when there is a legal right to set off current tax assets against current tax liabilities and when the deferred taxation relates to the same authority. The following amounts, determined after appropriate offsetting, are shown in the consolidated balance sheet:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Deferred tax assets | **(154)** | (23) |
| Deferred tax liabilities | **2,799** | 3,967 |
| | **2,645** | 3,944 |

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Deferred tax assets to be recovered after more than twelve months | **(154)** | (23) |
| Deferred tax liabilities to be settled after more than twelve months | **3,762** | 4,115 |
| | **3,608** | 4,092 |

The deferred tax (credited)/charged to equity during the year is as follows:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Fair value reserves in shareholders' equity: | | |
| – premises | **(109)** | 476 |
| – available-for-sale securities | **(727)** | (109) |
| – minority interests | **1** | 3 |
| | **(835)** | 370 |

## 40. Insurance contract liabilities

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Gross and net | | |
| At 1 January | **22,497** | 14,239 |
| Benefits paid | **(1,359)** | (881) |
| Claims incurred and movement in liabilities | **7,136** | 9,139 |
| At 31 December | **28,274** | 22,497 |

## 41. Subordinated liabilities

| | | | Carrying amount at 31 December | |
|---|---|---|---|---|
| **Principal amount** | **Interest rate** | **Due date** | **2008 HK$'m** | 2007 HK$'m |
| **Subordinated loans** | | | | |
| EUR 660m | 6-month EURIBOR + 0.85%* | June 2018 | **7,210** | – |
| USD2,500m | 6-month LIBOR + 2.00%** | December 2018 | **19,394** | – |
| HKD735m | 3-month HIBOR + 3.00%*** | October 2013 | **735** | – |
| | | | **27,339** | – |

During 2008, the Group obtained floating-rate subordinated loans from BOC, the intermediate holding company. The EUR 660 million and USD2,500 million subordinated loans are repayable prior to maturity after the first 5-year tenure at the option of the borrower. Amounts qualified as supplementary capital for regulatory purposes as shown in Note 4.5(b).

* 6-month EURIBOR plus 0.85% for the first 5 years, 6-month EURIBOR plus 1.35% for the remaining tenure payable semi-annually.

** 6-month LIBOR plus 2.00% for the first 5 years, 6-month LIBOR plus 2.50% for the remaining tenure payable semi-annually.

*** 3-month HIBOR plus 3.00% for the 5 year tenure payable quarterly.

## 42. Share capital

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Authorised:<br>20,000,000,000 ordinary shares of HK$5 each | **100,000** | 100,000 |
| Issued and fully paid:<br>10,572,780,266 ordinary shares of HK$5 each | **52,864** | 52,864 |

## 43. Reserves

The Group's and the Company's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity and statement of changes in equity respectively on pages 97 to 99 of the financial statements.

## 44. Notes to consolidated cash flow statement

### *(a) Reconciliation of operating profit to operating cash inflow before taxation*

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Operating profit | **4,182** | 18,033 |
| Depreciation | **992** | 787 |
| Net charge of impairment allowances | **12,573** | 1,448 |
| Unwind of discount on impairment | **(20)** | (47) |
| Advances written off net of recoveries | **275** | 1,014 |
| Interest expense on subordinated liabilities | **250** | – |
| Change in cash and balances with banks and other financial institutions with original maturity over three months | **7,781** | (27,873) |
| Change in placements with banks and other financial institutions with original maturity over three months | **(26,893)** | (2,613) |
| Change in financial assets at fair value through profit or loss | **(1,096)** | (5,297) |
| Change in derivative financial instruments | **4,207** | (44) |
| Change in advances and other accounts | **(50,175)** | (67,658) |
| Change in investment in securities | **(3,954)** | 1,053 |
| Change in other assets | **6,166** | (6,317) |
| Change in deposits and balances of banks and other financial institutions | **28,180** | 11,565 |
| Change in financial liabilities at fair value through profit or loss | **10,533** | (3,722) |
| Change in deposits from customers | **8,971** | 98,915 |
| Change in debt securities in issue at amortised cost | **(1,047)** | 2,089 |
| Change in other accounts and provisions | **1,529** | 7,443 |
| Change in insurance contract liabilities | **5,777** | 8,258 |
| Exchange difference | **(728)** | 13 |
| Operating cash inflow before taxation | **7,503** | 37,047 |
| Cash flows from operating activities included: | | |
| – Interest received | **36,379** | 44,927 |
| – Interest paid | **15,206** | 27,023 |
| – Dividend received | **126** | 15 |

### *(b) Analysis of the balances of cash and cash equivalents*

| | 2008 HK$'m | 2007 HK$'m |
|---|---|---|
| Cash and balances with banks and other financial institutions with original maturity within three months | **128,004** | 126,019 |
| Placements with banks and other financial institutions with original maturity within three months | **23,610** | 13,939 |
| Treasury bills with original maturity within three months | **22,277** | 10,244 |
| Certificates of deposit held with original maturity within three months | **1,035** | 1,868 |
| | **174,926** | 152,070 |

## 45. Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liability and commitment and the corresponding aggregate credit risk weighted amount:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Direct credit substitutes | **1,419** | 2,120 |
| Transaction-related contingencies | **10,153** | 7,075 |
| Trade-related contingencies | **22,481** | 29,081 |
| Commitments that are unconditionally cancellable without prior notice | **103,684** | 50,034 |
| Other commitments with an original maturity of | | |
| – up to one year | **63,252** | 84,804 |
| – over one year | **52,400** | 58,189 |
| | **253,389** | 231,303 |
| Credit risk weighted amount | **40,251** | 47,356 |

The calculation basis of credit risk weighted amount has been set out in Note 25 to the financial statements.

## 46. Capital commitments

The Group has the following outstanding capital commitments not provided for in the financial statements:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Authorised and contracted for but not provided for | **121** | 165 |
| Authorised but not contracted for | **15** | 1 |
| | **136** | 166 |

The above capital commitments mainly relate to commitments to purchase computer equipment and software, and to renovate the Group's premises.

## 47. Operating lease commitments

### *(a) The Group as lessee*

The Group has commitments to make the following future minimum lease payments under non-cancellable operating leases:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Land and buildings | | |
| – not later than one year | **427** | 321 |
| – later than one year but not later than five years | **531** | 297 |
| – later than five years | **14** | – |
| | **972** | 618 |

Certain non-cancellable operating leases included in the tables above were subject to renegotiation and rent adjustment with reference to market rates prevailing at specified agreed dates.

## 47. Operating lease commitments (continued)

### *(b) The Group as lessor*

The Group has contracted with tenants for the following future minimum lease receivables under non-cancellable operating leases:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Land and buildings | | |
| – not later than one year | **270** | 251 |
| – later than one year but not later than five years | **234** | 215 |
| | **504** | 466 |

The Group leases its investment properties (Note 31) under operating lease arrangements, with leases typically for a period from one to three years. The terms of the leases generally require the tenants to pay security deposits and provide for periodic rent adjustments according to the prevailing market conditions. None of the leases includes contingent rentals.

## 48. Litigation

The Group is currently being served a number of claims and counterclaims by various independent parties. These claims and counterclaims are in relation to the normal commercial activities of the Group.

No material provision was made against these claims and counterclaims because the directors believe that the Group has meritorious defences against the claimants or the amounts involved in these claims are not expected to be material.

## 49. Segmental reporting

The Group engages in many businesses in several regions. For segmental reporting purposes, information is solely provided in respect of business segments. Geographical segment information is not presented because over 90% of the Group's revenues, profits before tax and assets are derived from Hong Kong.

Information about four business segments is provided in segmental reporting. They are Personal Banking, Corporate Banking, Treasury and Insurance.

Both Personal Banking and Corporate Banking segments provide general banking services. Personal Banking serves individual customers while Corporate Banking deals with non individual customers. The Treasury segment is responsible for managing the capital, liquidity, and the interest rate and foreign exchange positions of the Group in addition to proprietary trades. The Insurance segment shows business relates to the Group's long-term life insurance products, including traditional and linked individual life insurance and group life insurance products. "Others" refers to those items related to the Group as a whole but independent of the other four business segments, including the Group's holdings of premises, investment properties, equity investments and interests in associates.

Revenues, expenses, assets and liabilities of any business segment mainly include items directly attributable to the segment. In relation to occupation of the Group's premises, rentals are internally charged on market rates according to the areas occupied. For management overheads, allocations are made on reasonable bases. Inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group. The charge on any such funding is mainly made by reference to the corresponding money market rate.

## 49. Segmental reporting (continued)

| | 2008 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Personal HK$'m | Corporate HK$'m | Treasury HK$'m | Insurance HK$'m | Others HK$'m | Subtotal HK$'m | Eliminations HK$'m | Consolidated HK$'m |
| Net interest (expenses)/income | | | | | | | | |
| – external | (3,241) | 6,924 | 15,322 | 1,122 | 30 | 20,157 | – | 20,157 |
| – inter-segment | 9,752 | (975) | (8,144) | – | (633) | – | – | – |
| | 6,511 | 5,949 | 7,178 | 1,122 | (603) | 20,157 | – | 20,157 |
| Net fees and commission income/(expenses) | 3,597 | 2,032 | (95) | (277) | 35 | 5,292 | (113) | 5,179 |
| Net trading income/(expenses) | 548 | 186 | 1,298 | – | (119) | 1,913 | 1 | 1,914 |
| Net loss on financial instruments designated at fair value through profit or loss | – | – | (316) | (136) | – | (452) | – | (452) |
| Net loss on investment in securities | – | – | (15) | – | – | (15) | – | (15) |
| Net insurance premium income | – | – | – | 5,899 | – | 5,899 | (8) | 5,891 |
| Other operating income | 34 | 44 | 7 | 17 | 1,829 | 1,931 | (1,370) | 561 |
| **Total operating income** | 10,690 | 8,211 | 8,057 | 6,625 | 1,142 | 34,725 | (1,490) | 33,235 |
| Net insurance benefits and claims | – | – | – | (7,709) | – | (7,709) | – | (7,709) |
| **Net operating income/(expense) before impairment allowances** | 10,690 | 8,211 | 8,057 | (1,084) | 1,142 | 27,016 | (1,490) | 25,526 |
| Net charge of impairment allowances | (129) | (544) | (9,170) | – | (2,730) | (12,573) | – | (12,573) |
| **Net operating income/(expense)** | 10,561 | 7,667 | (1,113) | (1,084) | (1,588) | 14,443 | (1,490) | 12,953 |
| Operating expenses | (5,669) | (2,143) | (831) | (147) | (1,471) | (10,261) | 1,490 | (8,771) |
| **Operating profit/(loss)** | 4,892 | 5,524 | (1,944) | (1,231) | (3,059) | 4,182 | – | 4,182 |
| Net loss from disposal of/fair value adjustments on investment properties | – | – | – | – | (118) | (118) | – | (118) |
| Net gain from disposal/revaluation of properties, plant and equipment | – | – | – | – | 7 | 7 | – | 7 |
| Share of profits less losses of associates | – | – | – | – | 7 | 7 | – | 7 |
| **Profit/(loss) before taxation** | 4,892 | 5,524 | (1,944) | (1,231) | (3,163) | 4,078 | – | 4,078 |
| **Assets** | | | | | | | | |
| Segment assets | 165,148 | 324,606 | 603,965 | 31,703 | 32,016 | 1,157,438 | (10,844) | 1,146,594 |
| Interests in associates | – | – | – | – | 88 | 88 | – | 88 |
| Unallocated corporate assets | – | – | – | – | 562 | 562 | – | 562 |
| | 165,148 | 324,606 | 603,965 | 31,703 | 32,666 | 1,158,088 | (10,844) | 1,147,244 |
| **Liabilities** | | | | | | | | |
| Segment liabilities | 523,682 | 309,254 | 203,481 | 30,977 | 1,447 | 1,068,841 | (10,844) | 1,057,997 |
| Unallocated corporate liabilities | – | – | – | – | 4,715 | 4,715 | – | 4,715 |
| | 523,682 | 309,254 | 203,481 | 30,977 | 6,162 | 1,073,556 | (10,844) | 1,062,712 |
| **Other information** | | | | | | | | |
| Additions of properties, plant and equipment | 12 | 5 | – | 5 | 796 | 818 | – | 818 |
| Depreciation | 271 | 132 | 108 | 3 | 478 | 992 | – | 992 |
| Amortisation of securities | – | – | 149 | – | – | 149 | – | 149 |

## 49. Segmental reporting (continued)

| | 2007 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Personal HK$'m | Corporate HK$'m | Treasury HK$'m | Insurance HK$'m | Others HK$'m | Subtotal HK$'m | Eliminations HK$'m | Consolidated HK$'m |
| Net interest (expenses)/income | | | | | | | | |
| – external | (8,552) | 5,067 | 22,015 | 788 | 77 | 19,395 | – | 19,395 |
| – inter-segment | 16,696 | 672 | (16,146) | – | (1,222) | – | – | – |
| | 8,144 | 5,739 | 5,869 | 788 | (1,145) | 19,395 | – | 19,395 |
| Net fees and commission income/ (expenses) | 4,983 | 1,778 | 47 | (307) | (116) | 6,385 | (111) | 6,274 |
| Net trading income | 538 | 151 | 236 | – | 87 | 1,012 | 1 | 1,013 |
| Net (loss)/gain on financial instruments designated at fair value through profit or loss | – | – | (25) | 893 | – | 868 | – | 868 |
| Net loss on investment in securities | – | – | (53) | – | – | (53) | – | (53) |
| Net insurance premium income | – | – | – | 8,429 | – | 8,429 | (3) | 8,426 |
| Other operating income | 410 | 1 | 1 | 15 | 1,688 | 2,115 | (1,344) | 771 |
| **Total operating income** | 14,075 | 7,669 | 6,075 | 9,818 | 514 | 38,151 | (1,457) | 36,694 |
| Net insurance benefits and claims | – | – | – | (9,440) | – | (9,440) | – | (9,440) |
| **Net operating income before impairment allowances** | 14,075 | 7,669 | 6,075 | 378 | 514 | 28,711 | (1,457) | 27,254 |
| Net (charge)/reversal of impairment allowances | (112) | 797 | (2,133) | – | – | (1,448) | – | (1,448) |
| **Net operating income** | 13,963 | 8,466 | 3,942 | 378 | 514 | 27,263 | (1,457) | 25,806 |
| Operating expenses | (5,829) | (1,940) | (627) | (117) | (717) | (9,230) | 1,457 | (7,773) |
| **Operating profit/(loss)** | 8,134 | 6,526 | 3,315 | 261 | (203) | 18,033 | – | 18,033 |
| Net gain from disposal of/fair value adjustments on investment properties | – | – | – | – | 1,064 | 1,064 | – | 1,064 |
| Net (loss)/gain from disposal/revaluation of properties, plant and equipment | (5) | – | – | – | 31 | 26 | – | 26 |
| Share of profits less losses of associates | – | – | – | – | 3 | 3 | – | 3 |
| **Profit before taxation** | 8,129 | 6,526 | 3,315 | 261 | 895 | 19,126 | – | 19,126 |
| **Assets** | | | | | | | | |
| Segment assets | 162,634 | 281,680 | 566,661 | 24,545 | 37,567 | 1,073,087 | (5,771) | 1,067,316 |
| Interests in associates | – | – | – | – | 83 | 83 | – | 83 |
| Unallocated corporate assets | – | – | – | – | 238 | 238 | – | 238 |
| | 162,634 | 281,680 | 566,661 | 24,545 | 37,888 | 1,073,408 | (5,771) | 1,067,637 |
| **Liabilities** | | | | | | | | |
| Segment liabilities | 545,397 | 284,353 | 116,095 | 23,182 | 2,539 | 971,566 | (5,771) | 965,795 |
| Unallocated corporate liabilities | – | – | – | – | 6,784 | 6,784 | – | 6,784 |
| | 545,397 | 284,353 | 116,095 | 23,182 | 9,323 | 978,350 | (5,771) | 972,579 |
| **Other information** | | | | | | | | |
| Additions of properties, plant and equipment | 14 | 8 | – | 2 | 1,123 | 1,147 | – | 1,147 |
| Depreciation | 234 | 90 | 56 | 2 | 405 | 787 | – | 787 |
| Amortisation of securities | – | – | 2,075 | – | – | 2,075 | – | 2,075 |

## 50. Loans to directors and officers

Particulars of advances made to directors and officers of the Company pursuant to section 161B of the Hong Kong Companies Ordinance are as follows:

| | **2008** **HK$'m** | 2007 HK$'m |
|---|---|---|
| Aggregate amount of relevant loans outstanding at year end | **655** | 622 |
| Maximum aggregate amount of relevant loans outstanding during the year | **667** | 839 |

## 51. Significant related party transactions

Related parties are those parties that have the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating 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 provides loans and credit facilities to related parties in the normal course of business. Such transactions are conducted with terms that are no more favourable than those contracted with third party customers of the Group.

Transactions with related parties, which the Group entered into during the year are summarised as follows:

### *(a) Advances to third parties guaranteed by BOC group companies*

As at 31 December 2008, BOC, the intermediate holding company, provided guarantees for loans in favour of the Group amounting to HK$6,980 million (2007: HK$3,693 million) to certain third parties. BOC held equity interests of not more than 20% in these third parties.

### *(b) Advances acquired from BOC*

During 2008, the Group has entered into an agreement with BOC to acquire advances amounting to USD300 million arising from trade finance facilities granted to customers. The outstanding amount of such advances at balance sheet date has been included as "advances to customers" in the financial statements.

## 51. Significant related party transactions (continued)

### *(c) Summary of transactions entered into during the ordinary course of business with BOC group companies*

The aggregate income and expenses arising from related party transactions with the immediate holding company, the intermediate holding companies, associates of the Company as well as subsidiaries and associates of BOC are summarised as follows:

| | | 2008 | | |
|---|---|---|---|---|
| | Notes | **Immediate and intermediate holding companies HK$'m** | **Associates HK$'m** | **Other related parties[1] HK$'m** |
| Income statement items: | | | | |
| Interest income | (i) | **1,047** | **–** | **23** |
| Interest expense | (ii) | **(672)** | **(1)** | **(119)** |
| Insurance commission received (net) | (iii) | **–** | **–** | **9** |
| Administrative services fees received/receivable | (iv) | **33** | **–** | **19** |
| Rental fees received/receivable | (iv) | **4** | **–** | **56** |
| Credit card commission paid/payable (net) | (v) | **(56)** | **–** | **(3)** |
| Securities brokerage commission paid/payable (net) | (v) | **–** | **–** | **(322)** |
| Rental, property management and letting agency fees paid/payable | (v) | **–** | **–** | **(94)** |
| Funds selling commission received | (vi) | **–** | **–** | **70** |
| Correspondent banking fee received | (vii) | **13** | **–** | **–** |
| Net insurance premium income | (iii) | **–** | **–** | **1** |
| Loans services fees received | | **–** | **–** | **2** |
| Net trading gains/(losses) | | **692** | **–** | **(30)** |

## 51. Significant related party transactions (continued)

### *(c) Summary of transactions entered into during the ordinary course of business with BOC group companies (continued)*

| | | 2007 | | |
|---|---|---|---|---|
| | Notes | Immediate and intermediate holding companies HK$'m | Associates HK$'m | Other related parties[1] HK$'m |
| Income statement items: | | | | |
| Interest income | (i) | 596 | – | 25 |
| Interest expense | (ii) | (442) | (3) | (332) |
| (Insurance premium paid)/insurance commission received (net) | (iii) | – | (2) | 28 |
| Administrative services fees received/ receivable | (iv) | 33 | – | 43 |
| Rental fees received/receivable | (iv) | – | – | 29 |
| Credit card commission paid/ payable (net) | (v) | (96) | – | (3) |
| Securities brokerage commission paid/payable (net) | (v) | – | – | (496) |
| Rental, property management and letting agency fees paid/payable | (v) | – | – | (82) |
| Funds selling commission received | (vi) | – | – | 224 |
| Correspondent banking fee received | (vii) | 14 | – | – |
| Loans services fees received | | – | – | 2 |
| Net trading gains/(losses) | | 11 | – | (96) |

## 51. Significant related party transactions (continued)

### *(c) Summary of transactions entered into during the ordinary course of business with BOC group companies (continued)*

| | | 2008 | | |
|---|---|---|---|---|
| | Notes | Immediate and intermediate holding companies HK$'m | Associates HK$'m | Other related parties[1] HK$'m |
| Balance sheet items: | | | | |
| Cash and balances with banks and other financial institutions | (i) | 25,614 | – | 26 |
| Placements with banks and other financial institutions maturing between one and twelve months | (i) | 8,489 | – | – |
| Financial assets at fair value through profit or loss | | 618 | – | 2,087 |
| Derivative financial instruments assets | (viii) | 782 | – | 4 |
| Advances and other accounts | (i) | 1 | – | 854 |
| Investment in securities | (i) | 1,280 | – | – |
| Other assets | (ix) | 55 | – | 2,050 |
| Deposits and balances of banks and other financial institutions | (ii) | 31,497 | – | 463 |
| Deposits from customers | (ii) | 97 | 46 | 8,019 |
| Derivative financial instruments liabilities | (viii) | 68 | – | 161 |
| Other accounts and provisions | (ix) | 99 | – | 2,210 |
| Subordinated liabilities | (x) | 27,339 | – | – |
| Off-balance sheet items: | | | | |
| Contingent liabilities and commitments | (xi) | 9,037 | – | 4,222 |

## 51. Significant related party transactions (continued)

### *(c) Summary of transactions entered into during the ordinary course of business with BOC group companies (continued)*

| | | 2007 | | |
|---|---|---|---|---|
| | Notes | Immediate and intermediate holding companies HK$'m | Associates HK$'m | Other related parties[1] HK$'m |
| Balance sheet items: | | | | |
| Cash and balances with banks and other financial institutions | (i) | 22,854 | – | 30 |
| Placements with banks and other financial institutions maturing between one and twelve months | (i) | 8,917 | – | – |
| Financial assets at fair value through profit or loss | | 438 | – | 2,097 |
| Derivative financial instruments assets | (viii) | 30 | – | 3 |
| Advances and other accounts | (i) | 21 | – | – |
| Investment in securities | (i) | 347 | – | – |
| Other assets | (ix) | 64 | – | 5,154 |
| Deposits and balances of banks and other financial institutions | (ii) | 15,478 | – | 680 |
| Deposits from customers | (ii) | 74 | 85 | 7,158 |
| Derivative financial instruments liabilities | (viii) | 14 | – | 23 |
| Other accounts and provisions | (ix) | 100 | – | 5,538 |
| Off-balance sheet items: | | | | |
| Contingent liabilities and commitments | (xi) | 2,248 | – | 3,722 |

[1] Subsidiaries and associates of BOC and post-employment benefit plans for the benefit of employees of the Company are collectively disclosed as other related parties and certain of which are state-controlled entities.

Notes:

**(i) Interest income**

In the ordinary course of business, the Group enters into various transactions with BOC group companies including deposit of cash and balances with banks and other financial institutions, placement of interbank deposits, investment in securities and provision of loans and credit facilities. The transactions were conducted at prices and terms that are no more favourable than those charged to and contracted with other third party customers of the Group.

**(ii) Interest expense**

In the ordinary course of business, the Group accepts interbank deposits and current, fixed, savings and other deposits from BOC group companies at the relevant market rates at the time of the transactions. Interest on subordinated loans is charged at the contracted rate as denoted in Note 41.

**(iii) Insurance premium paid/insurance commission received (net) and net insurance premium income**

In the ordinary course of business, the Group renders insurance polices and agency services to and purchases general insurance policies from BOC group companies at the relevant market rates at the time of the transactions.

## 51. Significant related party transactions (continued)

### *(c) Summary of transactions entered into during the ordinary course of business with BOC group companies (continued)*

Notes: (continued)

**(iv) Administrative services fees and rental fees received/receivable**

In the ordinary course of business, the Group receives administrative services fees for the provision of various administrative services including internal audit, technology, human resources support and training to BOC group companies mainly on the basis of cost plus a margin of 5%, and receives office premises rental fees from BOC group companies at the relevant market rates at the time of the transactions.

**(v) Commission, property management, letting agency fees and rental fees paid/payable**

In the ordinary course of business, the Group pays commission fees for credit card administrative and promotional services, securities brokerage services, property management and letting agency fees to BOC group companies. The Group also pays rental fees to BOC group companies. These transactions have been entered into in the ordinary course of business and were priced at the relevant market rates at the time of the transactions.

**(vi) Funds selling commission received**

In the ordinary course of business, the Group receives commission for engaging in promotion and sale of fund products of a BOC group company to customers of the Group at the relevant market rates at the time of the transactions.

**(vii) Correspondent banking fee received**

In the ordinary course of business, BOC provides services to the Group's customers including remittance services and advising on and collecting letters of credit issued by the Group. The Group shares the fees paid by its customers with BOC on the basis agreed between the parties from time to time.

**(viii) Derivative financial instruments assets/liabilities**

In the ordinary course of business, the Group enters into foreign exchange contracts and interest rate contracts with BOC group companies. As at 31 December 2008 the aggregate notional amount of such derivative transactions amounted to HK$25,236 million (2007: HK$13,219 million) whilst the corresponding derivative financial instruments assets and liabilities amounted to HK$786 million (2007: HK$33 million) and HK$229 million (2007: HK$37 million) respectively. These transactions are executed at the relevant market rates at the time of the transactions.

**(ix) Other assets and other accounts and provisions**

Included within "Other assets" and "Other accounts and provisions" are receivables from and payables to BOC group companies. The amounts mainly represent the account receivables from and payables to a subsidiary of BOC in relation to dealing in securities trading transactions on behalf of the Group's customers. The receivables and payables arose from transactions carried out in the normal course of business.

**(x) Subordinated liabilities**

The Group entered into subordinated credit facility agreements with BOC for the purposes of capital management. Major commercial terms of the loans are stated in Note 41.

**(xi) Contingent liabilities and commitments**

In the ordinary course of business, the Group provides loan facilities and trade finance services to, and guarantees for the obligations of BOC and its subsidiaries and associates on normal commercial terms.

## 51. Significant related party transactions (continued)

### (d) *Key management personnel*

Key management are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including directors and senior management. The Group accepts deposits from and grants loans and credit facilities to key management personnel in the ordinary course of business. During both the current and prior years, no material transaction was conducted with key management personnel of BOCHK, its holding companies and parties related to them.

The key management compensation for the year ended 31 December 2008 and 2007 is detailed as follows:

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Salaries and other short-term employee benefits | **53** | 43 |
| Post-employment benefits | **1** | 1 |
| | **54** | 44 |

### (e) *Transactions with Ministry of Finance and The People's Bank of China*

The Group enters into banking transactions with these entities in the normal course of business. These include purchases and redemption of treasury bonds and money market transactions. The outstanding balances at the year end, and the related income and expenses for the year are as follows:

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Interest income/ (expense) HK$'m** | **Outstanding balance at end of the year HK$'m** | Interest income/ (expense) HK$'m | Outstanding balance at end of the year HK$'m |
| Advances and other accounts | **4** | **81** | 8 | 120 |
| Treasury bonds | **79** | **1,776** | 62 | 1,600 |
| Due from banks and other financial institutions | **660** | **51,769** | 262 | 29,405 |
| Due to banks and other financial institutions | **(1)** | **2** | (1) | 1 |

## 51. Significant related party transactions (continued)

### *(f) Transactions with Central SAFE and other companies controlled by Central SAFE*

Central SAFE is the controlling entity of BOC. Central SAFE is approved by the State Council of the PRC to assume the rights and obligations of the equity owner on behalf of the State. Accordingly, Central SAFE, acting on behalf of the State, has become the ultimate holding company of the Company by virtue of its interest in BOC.

The Group did not have any balances or enter into any transactions with Central SAFE for the year ended 31 December 2008 (2007: Nil).

Central SAFE has controlling equity interests in certain other entities in the PRC. The Group enters into banking transactions with these companies in the normal course of business. These include loans, investment securities and money market transactions. The outstanding balances at the year end, and the related income and expenses for the year are as follows:

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Interest income/ (expense) HK$'m** | **Outstanding balance at end of the year HK$'m** | Interest income/ (expense) HK$'m | Outstanding balance at end of the year HK$'m |
| Advances and other accounts | **–** | **–** | – | 23 |
| Investment in securities | **196** | **5,479** | 89 | 2,433 |
| Financial assets at fair value through profit or loss | **–** | **20** | – | 9 |
| Due from banks and other financial institutions | **171** | **3,780** | 85 | 1,443 |
| Due to banks and other financial institutions | **(67)** | **1,214** | (21) | 2,417 |

### *(g) Transactions with other state-controlled entities*

The state-controlled entities are those, other than BOC (the intermediate holding company and its subsidiaries) and Central SAFE and its controlled companies over which the PRC government directly or indirectly holds over 50% of the outstanding shares or voting rights, and has the ability to control or the power to govern their financial or operational policies through its government authorities, agencies and affiliates. The Group has extensive transactions with other state controlled entities. These transactions, conducted in the ordinary course of business, may include, but are not limited to, the following:

– lending, provision of credits 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;

– provision of fiduciary activities; and

– purchase of utilities, transport, telecommunication and postal services.

## 51. Significant related party transactions (continued)

### *(g) Transactions with other state-controlled entities (continued)*

Utilities, transport, telecommunication and postal services are charged by service providers at market rates. Management believes that, based on their assessment, the amounts of such related party transactions are insignificant for the year and therefore are not disclosed.

Details of other transactions and balances with state-controlled entities conducted in the ordinary course of business are set forth below:

#### (i) Financial assets/financial liabilities

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Interest income/ (expense) HK$'m** | **Outstanding balance at end of the year HK$'m** | Interest income/ (expense) HK$'m | Outstanding balance at end of the year HK$'m |
| Advances and other accounts (Gross) | **1,870** | **57,260** | 1,899 | 39,828 |
| Individually assessed loan impairment allowances | **–** | **122** | – | 28 |
| Investment in securities | **276** | **6,153** | 323 | 7,158 |
| Financial assets at fair value through profit or loss | **44** | **847** | 31 | 1,219 |
| Due from banks and other financial institutions | **107** | **2,155** | 452 | 6,970 |
| Due to banks and other financial institutions | **(237)** | **25,082** | (286) | 18,667 |
| Deposits from customers | **(808)** | **59,983** | (1,163) | 29,927 |

#### (ii) Contingent liabilities and commitments (including guarantees)

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Contingent liabilities and commitments (including guarantees) | **43,866** | 36,145 |

#### (iii) Outstanding derivative transactions (notional amount)

| | **2008 HK$'m** | 2007 HK$'m |
|---|---|---|
| Outstanding derivative transactions (notional amount) | **6,685** | 1,686 |

## 52. Liquidity ratio

| | **2008** | 2007 |
|---|---|---|
| Average liquidity ratio | **41.74 %** | 50.92 % |

The average liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio of BOCHK for the year.

The liquidity ratio is computed on the solo basis (the Hong Kong offices only) and is in accordance with the Fourth Schedule to the Banking Ordinance.

## 53. Currency concentrations

The following is a summary of the major foreign currency exposures arising from trading, non-trading and structural positions. The net options position is calculated based on the basis of delta-weighted positions of all foreign exchange options contracts.

| | **2008** | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Equivalent in million of HK$** | | | | | | | |
| | **US Dollars** | **Japanese Yen** | **Euro** | **Australian Dollars** | **Pound Sterling** | **Renminbi Yuan** | **Others** | **Total** |
| Spot assets | **329,063** | **45,677** | **39,953** | **26,578** | **13,662** | **69,588** | **11,006** | **535,527** |
| Spot liabilities | **(282,888)** | **(10,671)** | **(26,033)** | **(28,009)** | **(16,730)** | **(68,161)** | **(22,252)** | **(454,744)** |
| Forward purchases | **328,459** | **28,024** | **31,497** | **17,948** | **18,249** | **22,282** | **39,376** | **485,835** |
| Forward sales | **(364,547)** | **(62,847)** | **(45,720)** | **(16,688)** | **(15,190)** | **(22,273)** | **(28,126)** | **(555,391)** |
| Net options position | **131** | **2** | **7** | **8** | **(9)** | **–** | **3** | **142** |
| Net long/(short) position | **10,218** | **185** | **(296)** | **(163)** | **(18)** | **1,436** | **7** | **11,369** |
| Net structural position | **158** | **–** | **–** | **–** | **–** | **1,719** | **–** | **1,877** |

| | 2007 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Equivalent in million of HK$ | | | | | | | |
| | US Dollars | Japanese Yen | Euro | Australian Dollars | Pound Sterling | Renminbi Yuan | Others | Total |
| Spot assets | 327,003 | 2,019 | 15,739 | 27,376 | 6,028 | 44,929 | 7,364 | 430,458 |
| Spot liabilities | (224,622) | (4,764) | (9,215) | (24,055) | (12,951) | (44,055) | (19,615) | (339,277) |
| Forward purchases | 159,983 | 22,718 | 25,775 | 22,051 | 25,907 | 26,760 | 43,162 | 326,356 |
| Forward sales | (257,677) | (20,215) | (32,238) | (25,426) | (18,858) | (26,322) | (30,823) | (411,559) |
| Net options position | 107 | (16) | (17) | 22 | (5) | – | (9) | 82 |
| Net long/(short) position | 4,794 | (258) | 44 | (32) | 121 | 1,312 | 79 | 6,060 |
| Net structural position | 84 | – | – | – | – | 459 | – | 543 |

## 54. Cross-border claims

The information on cross-border claims discloses exposures to foreign counterparties on which the ultimate risk lies, and is derived according to the location of the counterparties after taking into account any transfer of risk. In general, such transfer of risk takes place if the claims are guaranteed by a party in a country, which is different from that of the counterparty, or if the claims are on an overseas branch of a bank whose head office is located in another country. Only regions constituting 10% or more of the aggregate cross-border claims are analysed by geographical areas and disclosed as follows:

| | Banks HK$'m | Public sector entities HK$'m | Others HK$'m | Total HK$'m |
|---|---|---|---|---|
| **At 31 December 2008** | | | | |
| Asia, other than Hong Kong | | | | |
| – Mainland China | 62,948 | 52,228 | 47,650 | 162,826 |
| – Japan | 19,475 | 39,462 | 1,522 | 60,459 |
| – Others | 46,292 | 54 | 16,293 | 62,639 |
| | 128,715 | 91,744 | 65,465 | 285,924 |
| North America | | | | |
| – United States | 8,235 | 29,065 | 62,240 | 99,540 |
| – Others | 20,380 | 686 | 150 | 21,216 |
| | 28,615 | 29,751 | 62,390 | 120,756 |
| Western Europe | | | | |
| – Germany | 37,262 | 664 | 1,252 | 39,178 |
| – Others | 135,312 | 353 | 6,992 | 142,657 |
| | 172,574 | 1,017 | 8,244 | 181,835 |
| Total | 329,904 | 122,512 | 136,099 | 588,515 |

## 54. Cross-border claims (continued)

| | Banks HK$'m | Public sector entities HK$'m | Others HK$'m | Total HK$'m |
|---|---|---|---|---|
| At 31 December 2007 | | | | |
| Asia, other than Hong Kong | | | | |
| – Mainland China | 56,017 | 30,926 | 29,699 | 116,642 |
| – Japan | 26,513 | – | 2,222 | 28,735 |
| – Others | 49,254 | 469 | 17,363 | 67,086 |
| | 131,784 | 31,395 | 49,284 | 212,463 |
| North America | | | | |
| – United States | 9,726 | 27,179 | 78,144 | 115,049 |
| – Others | 18,081 | 95 | 68 | 18,244 |
| | 27,807 | 27,274 | 78,212 | 133,293 |
| Western Europe | | | | |
| – Germany | 42,651 | – | 2,331 | 44,982 |
| – Others | 155,136 | 3 | 11,827 | 166,966 |
| | 197,787 | 3 | 14,158 | 211,948 |
| Total | 357,378 | 58,672 | 141,654 | 557,704 |

## 55. Non-bank Mainland China exposures

Non-bank counterparties are identified in accordance with the definitions set out in the prudential return "Quarterly Analysis of Loans and Advances and Provisions" issued by the HKMA. Exposures in Mainland China arising from non-bank counterparties at 31 December are summarised as follows:

| | **2008** | | | |
|---|---|---|---|---|
| | **On-balance sheet exposure HK$'m** | **Off-balance sheet exposure HK$'m** | **Total exposure HK$'m** | **Individually assessed impairment allowances HK$'m** |
| Mainland China entities | **78,600** | **66,102** | **144,702** | **53** |
| Companies and individuals outside Mainland China where the credit is granted for use in Mainland China | **25,979** | **13,701** | **39,680** | **119** |
| Other non-bank Mainland China exposures | **14,095** | **7,824** | **21,919** | **56** |
| | **118,674** | **87,627** | **206,301** | **228** |

## 55. Non-bank Mainland China exposures (continued)

| | 2007 | | | |
|---|---|---|---|---|
| | On-balance sheet exposure HK$'m | Off-balance sheet exposure HK$'m | Total exposure HK$'m | Individually assessed impairment allowances HK$'m |
| Mainland China entities | 60,275 | 44,693 | 104,968 | 23 |
| Companies and individuals outside Mainland China where the credit is granted for use in Mainland China | 23,142 | 17,535 | 40,677 | 13 |
| Other non-bank Mainland China exposures | 10,133 | 8,261 | 18,394 | 8 |
| | 93,550 | 70,489 | 164,039 | 44 |

## 56. Ultimate holding company

Central SAFE, acting on behalf of the State, is the ultimate holding company of the Company whilst BOC is the Company's intermediate holding company.

## 57. Approval of financial statements

The financial statements were approved and authorised for issue by the Board of Directors on 24 March 2009.

# UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

## 1. Connected transactions

In 2008, BOCHK, a wholly owned subsidiary of the Company, and its subsidiaries engaged on a regular basis in the usual course of their business in numerous transactions with BOC and its Associates. As BOC is the Company's controlling shareholder and therefore a connected person of the Company, all such transactions constituted connected transactions for the purposes of the Listing Rules. Central SAFE is the ultimate controlling shareholder of the Company, with the stated purpose of exercising the rights of an equity investor on behalf of the PRC Government and not to have any commercial operations. For the purposes of this report, therefore, Central SAFE and her associates has not been treated as connected persons to the Company.

The transactions fell into the following three categories:

1. exempted transactions entered into in the usual course of business and under normal commercial terms. Such transactions were exempted from disclosure and independent shareholder approval by virtue of Rules 14A.31,14A.33 and 14A.65 of the Listing Rules;

2. certain regular banking transactions entered into on a continual basis throughout the year. On 2 January 2008 the Company made an announcement (the "Announcement") in accordance with Rule 14A.47 of the Listing Rules, and has got the approval from the independent shareholders on 20 May 2008. The Announcement listed those continuing connected transactions that exceeded the de minimus threshold and set out caps in respect of such transactions for the three years 2008-2010. These transactions were conducted in the ordinary course of its business and on normal commercial terms. Details of these continuing connected transactions are set out below and are described in the announcements which may be viewed at the Company's website.

| **Type of Transaction** | **2008 Cap (HK$'m)** | **2008 Actual Amount (HK$'m)** |
|---|---|---|
| Securities Transactions | **2,700** | **324** |
| Fund Distribution Transactions | **2,700** | **70** |
| Credit Card Services | **1,100** | **116** |
| Information Technology Services | **1,100** | **42** |
| Property Transactions | **1,100** | **104** |
| Bank-note Delivery | **1,100** | **88** |
| Insurance Agency | **2,700** | **343** |
| Provision of Insurance Cover | **1,100** | **105** |
| Foreign Exchange Transactions | **2,700** | **200** |
| Trading of Financial Assets | **50,000** | **4,150** |
| Inter-bank Capital Markets | **50,000** | **1,709** |

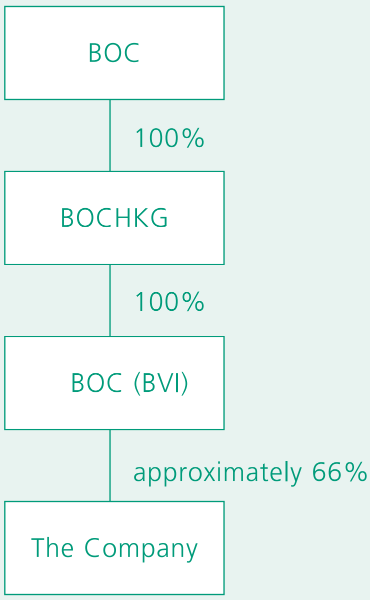
3. The Company disclosed in two connected transactions announcements on 25 June 2008 and 12 December 2008 respectively that it entered into two subordinated credit facility agreements with BOC. Pursuant to such agreements, BOC extended a €660,000,000 subordinated credit facility and a US$2,500,000,000 subordinated credit facility to BOCHK respectively. The terms of the subordinated credit facilities were negotiated on an arm's length basis between the two parties and the subordinated loans were provided on normal commercial terms. With the benefit of advice by an independent financial adviser in each transaction, the independent board committee considers that the terms are fair and reasonable. Details of these connected transactions are described in the announcements which may be viewed at the Company's website.

## 2. Reconciliation between HKFRSs vs IFRS/CAS

The Company understands that BOC, an intermediate holding company as well as controlling shareholder of the Company, will prepare and disclose consolidated financial information in accordance with IFRS and CAS for which the Company and its subsidiaries will form part of the consolidated financial statements. CAS is the new set of PRC accounting standards that has been effective for annual periods beginning on or after 1 January 2007 for companies publicly listed in PRC. The requirements of CAS have substantially converged with IFRS and HKFRSs.

The consolidated financial information of "BOC Hong Kong Group" for the periods disclosed by BOC in its consolidated financial statements is not the same as the consolidated financial information of the Group for the periods published by the Company pursuant to applicable laws and regulations in Hong Kong. There are two reasons for this.

First, the definitions of "BOC Hong Kong Group" (as adopted by BOC for the purpose of its own financial disclosure) and "Group" (as adopted by the Company in preparing and presenting its consolidated financial information) are different: "BOC Hong Kong Group" refers to BOCHKG and its subsidiaries, whereas "Group" refers to the Company and its subsidiaries (see the below organisation chart). Though there is difference in definitions between "BOC Hong Kong Group" and "Group", their financial results for the periods presented are substantially the same. This is because BOCHKG and BOC (BVI) are holding companies only and have no substantive operations of their own.




Second, the Group has prepared its consolidated financial statements in accordance with HK GAAP prior to 1 January 2005 and as from 1 January 2005 onwards in accordance with HKFRSs; whereas the consolidated financial information reported to BOC is prepared in accordance with IFRS and CAS respectively. Despite the fact that HKFRSs have converged with IFRS, there is a timing difference in the initial adoption of HKFRSs and IFRS by the Group and by BOC respectively.

The Board considers that the best way to ensure that shareholders and the investing public understand the material differences between the consolidated financial information of the Group published by the Company on the one hand, and the consolidated financial information of BOC Hong Kong Group disclosed by BOC in its financial statements on the other hand, is to present reconciliations of the profit after tax/net assets of the Group prepared under HKFRSs to the profit after tax/net assets of the Group prepared under IFRS and CAS respectively for the periods presented.

## 2. Reconciliation between HKFRSs vs IFRS/CAS (continued)

The major differences between HKFRSs and IFRS/CAS, which arise from the difference in measurement basis in IFRS or CAS and the timing difference in the initial adoption of HKFRSs and IFRS relate to the following:

– re-measurement of carrying value of treasury products;
– restatement of carrying value of bank premises; and
– deferred taxation impact arising from the above different measurement basis.

### *(a) Re-measurement of carrying value of treasury products*

Due to the difference in the timing of first adoption of HKFRSs and IFRS, classification and measurement of certain investment securities under HK GAAP/HKFRSs and IFRS were different. Therefore, investment securities were reclassified and re-measured to align with the accounting policies of BOC for the relevant periods. Classification and measurement under IFRS and CAS is basically the same.

### *(b) Restatement of carrying value of bank premises*

The Company has elected for a revaluation basis rather than cost basis to account for bank premises and investment properties under HKFRSs. On the contrary, BOC has elected for the cost convention for bank premises and revaluation basis for investment properties under IFRS and CAS. Therefore, adjustments have been made to the carrying value of bank premises as well as to re-calculate the depreciation charge and disposal gain/loss under IFRS and CAS.

### *(c) Deferred tax adjustments*

These represent the deferred tax effect of the aforesaid adjustments.

Going forward, the differences relating to the restatement of carrying value of bank premises as a result of the election of the different measurement basis allowed under HKFRSs, IFRS and CAS will be recurring in the future, while the timing difference related to the measurement of investment securities will be reversed gradually and eliminated in future years.

**Profit after tax/Net assets reconciliation**

*HKFRSs Vs IFRS/CAS*

| | Profit after tax | | Net assets | |
|---|---|---|---|---|
| | **2008 HK$'m** | 2007 HK$'m | **2008 HK$'m** | 2007 HK$'m |
| **Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under HKFRSs** | **3,007** | 15,817 | **84,532** | 95,058 |
| Add: IFRS/CAS adjustments | | | | |
| Re-measurement of carrying value of treasury products | **(54)** | (146) | **35** | 1 |
| Restatement of carrying value of bank premises | **280** | 125 | **(9,445)** | (9,990) |
| Deferred tax adjustments | **(51)** | (3) | **1,534** | 1,692 |
| **Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under IFRS/CAS** | **3,182** | 15,793 | **76,656** | 86,761 |

# APPENDIX

## Subsidiaries of the Company

The particulars of our subsidiaries are as follows:

| Name of company | Country/place and date of incorporation/ operation | Issued and fully paid up share capital/registered capital | Percentage of attributable equity interest | Principal activities |
|---|---|---|---|---|
| **Directly held:** | | | | |
| Bank of China (Hong Kong) Limited | Hong Kong 16 October 1964 | Ordinary shares HK$43,042,840,858 | 100.00% | Banking business |
| BOC Group Life Assurance Company Limited* | Hong Kong 12 March 1997 | Ordinary shares HK$1,368,000,000 | 51.00% | Life insurance business |
| **Indirectly held:** | | | | |
| Nanyang Commercial Bank, Limited | Hong Kong 2 February 1948 | Ordinary shares HK$600,000,000 | 100.00% | Banking business |
| Chiyu Banking Corporation Limited | Hong Kong 24 April 1947 | Ordinary shares HK$300,000,000 | 70.49% | Banking business |
| BOC Credit Card (International) Limited | Hong Kong 9 September 1980 | Ordinary shares HK$480,000,000 | 100.00% | Credit card services |
| Arene Trading Limited | Hong Kong 22 August 1978 | Ordinary shares HK$500,000 | 100.00% | Property holding and investment |
| Bank of China (Hong Kong) Nominees Limited* | Hong Kong 1 October 1985 | Ordinary shares HK$2 | 100.00% | Nominee services |
| Bank of China (Hong Kong) Trustees Limited* | Hong Kong 6 November 1987 | Ordinary shares HK$3,000,000 | 100.00% | Trustee and agency services |
| BOC Group Trustee Company Limited* | Hong Kong 1 December 1997 | Ordinary shares HK$200,000,000 | 64.20% | Trustee services |
| BOC Travel Services Limited | Hong Kong 24 August 1982 | Ordinary shares HK$2,000,000 | 100.00% | Travel services |
| BOCHK Financial Products (Cayman) Limited | Cayman 10 November 2006 | Ordinary shares US$50,000 | 100.00% | Note issuing |
| BOCHK Information Technology (Shenzhen) Co., Ltd.* | PRC 16 April 1990 | Registered capital HK$70,000,000 | 100.00% | Property holding and investment |
| BOCHK Information Technology Services (Shenzhen) Ltd* | PRC 26 May 1993 | Registered capital HK$40,000,000 | 100.00% | Information technology services |
| BOCI-Prudential Trustee Limited* | Hong Kong 11 October 1999 | Ordinary shares HK$300,000,000 | 41.10% | Trustee services |
| Che Hsing (Nominees) Limited* | Hong Kong 23 April 1980 | Ordinary shares HK$10,000 | 100.00% | Nominee services |
| Chiyu Banking Corporation (Nominees) Limited* | Hong Kong 3 November 1981 | Ordinary shares HK$100,000 | 70.49% | Investment holding |
| Chung Chiat Company Limited | Hong Kong 9 April 1980 | Ordinary shares HK$200 | 100.00% | Property holding and investment |
| Dwell Bay Limited | Hong Kong 19 December 1980 | Ordinary shares HK$100,000 | 100.00% | Property holding and investment |

## Subsidiaries of the Company (continued)

| Name of company | Country/place and date of incorporation/ operation | Issued and fully paid up share capital/registered capital | Percentage of attributable equity interest | Principal activities |
|---|---|---|---|---|
| Glister Company Limited* | Hong Kong<br>26 March 2001 | Ordinary shares<br>HK$2 | 70.49% | Investment holding |
| Glory Cardinal Limited* | Hong Kong<br>4 May 2001 | Ordinary shares<br>HK$2 | 70.49% | Investment holding |
| Grace Charter Limited* | Hong Kong<br>4 May 2001 | Ordinary shares<br>HK$2 | 70.49% | Investment holding |
| G.Z.Y. Microfilm Technology (Shenzhen) Co., Ltd.* | PRC<br>24 September 1993 | Registered capital<br>HK$40,000,000 | 100.00% | Property holding and investment |
| Hua Chiao Commercial (Nominees) Limited* | Hong Kong<br>28 October 1986 | Ordinary shares<br>HK$10,000 | 100.00% | Nominee services |
| Kincheng Finance (H.K.) Limited | Hong Kong<br>30 March 1979 | Ordinary shares<br>HK$100 | 100.00% | Loan financing |
| Kincheng Investments & Developments (H.K.) Limited | Hong Kong<br>15 May 1981 | Ordinary shares<br>HK$6,000 | 100.00% | Property holding and investment |
| Kincheng (Nominees) Limited* | Hong Kong<br>12 December 1980 | Ordinary shares<br>HK$100,000 | 100.00% | Nominee services |
| Kiu Nam Investment Corporation Limited | Hong Kong<br>9 November 1963 | Ordinary shares<br>HK$2,000,000 | 100.00% | Property holding and investment |
| Kwong Li Nam Investment Agency Limited* | Hong Kong<br>25 May 1984 | Ordinary shares<br>HK$3,050,000 | 100.00% | Investment agency |
| Nan Song Company, Limited* | Hong Kong<br>13 April 1965 | Ordinary shares<br>HK$1,000,000 | 100.00% | Property investment and investment holding |
| Nanyang Commercial Bank (China) Limited | PRC<br>14 December 2007 | Registered capital<br>RMB2,500,000,000 | 100.00% | Banking business |
| Nanyang Commercial Bank (Nominees) Limited* | Hong Kong<br>22 August 1980 | Ordinary shares<br>HK$50,000 | 100.00% | Nominee services |
| Nanyang Commercial Bank Trustee Limited* | Hong Kong<br>22 October 1976 | Ordinary shares<br>HK$3,000,000 | 100.00% | Trustee services |
| Nanyang Finance Company Limited | Hong Kong<br>16 March 1979 | Ordinary shares<br>HK$50,000,000 | 100.00% | Financial services |
| Pacific Trend Profits Corporation* | British Virgin Islands<br>20 April 2001 | Registered shares<br>US$1 | 70.49% | Investment holding |
| Patson (HK) Limited* | Hong Kong<br>18 August 1970 | Ordinary shares<br>HK$1,000,000 | 100.00% | Property investment |
| Perento Limited | Hong Kong<br>27 September 1983 | Ordinary shares<br>HK$10,000 | 100.00% | Property holding and investment |
| Po Hay Enterprises Limited | Hong Kong<br>2 October 1979 | Ordinary shares<br>HK$100,000 | 100.00% | Property holding and investment |
| Po Sang Financial Investment Services Company Limited* | Hong Kong<br>23 September 1980 | Ordinary shares<br>HK$25,000,000 | 100.00% | Gold trading and investment holding |

## Subsidiaries of the Company (continued)

| Name of company | Country/place and date of incorporation/ operation | Issued and fully paid up share capital/registered capital | Percentage of attributable equity interest | Principal activities |
|---|---|---|---|---|
| Po Sang Futures Limited* | Hong Kong 19 October 1993 | Ordinary shares HK$25,000,000 | 100.00% | Commodities brokerage |
| Po Sang (Nominees) Limited* | Hong Kong 29 April 1993 | Ordinary shares HK$10,000 | 100.00% | Nominee services |
| Rams City (Nominees) Limited* | Hong Kong 2 May 1986 | Ordinary shares HK$2,000,000 | 100.00% | Nominee services |
| Sanicon Investment Limited | Hong Kong 24 January 2000 | Ordinary shares HK$2 | 100.00% | Property holding and investment |
| Seng Sun Development Company, Limited* | Hong Kong 11 December 1961 | Ordinary shares HK$2,800,000 | 70.49% | Investment holding |
| Shenstone Limited | Hong Kong 4 September 1979 | Ordinary shares HK$2 | 100.00% | Property holding and investment |
| Sin Chiao Enterprises Corporation, Limited* | Hong Kong 13 September 1961 | Ordinary shares HK$3,000,000 | 100.00% | Property holding and investment |
| Sin Hua Trustee Limited* | Hong Kong 27 October 1978 | Ordinary shares HK$3,000,000 | 100.00% | Trustee services |
| Sin Mei (Nominee) Limited* | Hong Kong 27 April 1982 | Ordinary shares HK$100,000 | 100.00% | Nominee services |
| Sin Yeh Shing Company Limited | Hong Kong 28 November 1980 | Ordinary shares HK$100,000 | 100.00% | Property holding and investment |
| Sino Information Services Company Limited | Hong Kong 11 February 1993 | Ordinary shares HK$7,000,000 | 100.00% | Information services |
| The China-South Sea (Nominees) Services Limited* | Hong Kong 13 February 1981 | Ordinary shares HK$100,000 | 100.00% | Nominee services |
| The China State (Nominees) Limited* | Hong Kong 14 May 1982 | Ordinary shares HK$100,000 | 100.00% | Nominee services |
| The China State Trustee Limited* | Hong Kong 17 July 1981 | Ordinary shares HK$3,000,000 | 100.00% | Trustee services |
| Track Link Investment Limited | Hong Kong 8 February 1994 | Ordinary shares HK$2 | 100.00% | Property holding and investment |
| Yien Yieh (Nominee) Limited* | Hong Kong 26 June 2001 | Ordinary shares HK$2,000 | 100.00% | Nominee services |

Po Sang (Nominees) Limited will dissolve in May 2009.

Remarks:
Name of subsidiaries which are not included in the consolidation group for regulatory purposes in respect of capital adequacy is marked with * in the above table. BOCHK and its subsidiaries specified by the HKMA form the basis of consolidation for its regulatory purposes in accordance with the Banking (Capital) Rules. For accounting purposes, subsidiaries are consolidated in accordance with the accounting standards issued by the HKICPA pursuant to section 18A of the Professional Accountants Ordinance.

# DEFINITIONS

In this Annual Report, unless the context otherwise requires, the following terms shall have the meanings set out below:

| Terms | Meanings |
|---|---|
| "ABS" | Asset-backed securities |
| "AC" | The Audit Committee |
| "ADR" | American Depositary Receipt |
| "ADS(s)" | American Depositary Share(s) |
| "ALCO" | The Asset and Liability Management Committee |
| "ATM" | Automated Teller Machine |
| "Associate(s)" | has the meaning ascribed to "associate(s)" in the Listing Rules |
| "Board" or "Board of Directors" | the Board of Directors of the Company |
| "BOC" | Bank of China Limited, a joint stock commercial bank with limited liability established under the laws of the PRC, the H shares and A shares of which are listed on the Hong Kong Stock Exchange and the Shanghai Stock Exchange respectively |
| "BOC (BVI)" | BOC Hong Kong (BVI) Limited, a company incorporated under the laws of the British Virgin Islands and a wholly owned subsidiary of BOCHKG |
| "BOC Insurance" | Bank of China Group Insurance Company Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOC |
| "BOC Life" | BOC Group Life Assurance Company Limited, a company incorporated under the laws of Hong Kong, in which the Group and BOC Insurance hold equity interests of 51% and 49% respectively |
| "BOC-CC" | BOC Credit Card (International) Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOCHK |
| "BOCHK" or "the Bank" | Bank of China (Hong Kong) Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of the Company |
| "BOCHK Charitable Foundation" | Bank of China (Hong Kong) Limited Charitable Foundation (formerly known as the "Bank of China Group Charitable Foundation"), a charitable foundation being established in July 1994 |
| "BOCHKG" | BOC Hong Kong (Group) Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOC |
| "BOCI" | BOC International Holdings Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOC |
| "BOCI-Prudential Manager" | BOCI-Prudential Asset Management Limited, a company incorporated under the laws of Hong Kong, in which BOCI Asset Management Limited, a wholly owned subsidiary of BOC International Holdings Limited, and Prudential Corporation Holdings Limited hold equity interests of 64% and 36% respectively |
| "BOCI-Prudential Trustee" | BOCI-Prudential Trustee Limited, a company incorporated under the laws of Hong Kong, in which BOC Group Trustee Company Limited and Prudential Corporation Holdings Limited hold equity interests of 64% and 36% respectively |
| "CAR" | Capital Adequacy Ratio, computed on the consolidated basis that comprises the positions of BOCHK and certain subsidiaries specified by the HKMA for its regulatory purposes and in accordance with the Banking (Capital) Rules |

| Terms | Meanings |
|---|---|
| "CAS" | China Accounting Standards |
| "CBS" | Corporate Banking Services |
| "CCO" | Chief Credit Officer |
| "CE" | Chief Executive |
| "CRO" | Chief Risk Officer |
| "Central SAFE" | Central SAFE Investments Limited |
| "Chiyu" | Chiyu Banking Corporation Limited, a company incorporated under the laws of Hong Kong, in which BOCHK holds an equity interest of 70.49% |
| "Company" | BOC Hong Kong (Holdings) Limited, a company incorporated under the laws of Hong Kong |
| "ECAI(s)" | External Credit Assessment Institution(s) |
| "ESPD" | The Economics & Strategic Planning Department |
| "EURIBOR" | Euro Interbank Offered Rate |
| "Fitch" | Fitch Ratings |
| "GDP" | Gross Domestic Product |
| "Group" | the Company and its subsidiaries collectively referred as the Group |
| "HIBOR" | Hong Kong Interbank Offered Rate |
| "HK GAAP" | Generally Accepted Accounting Principles in Hong Kong |
| "HKAS(s)" | Hong Kong Accounting Standard(s) |
| "HKAS-Int" | HKAS Interpretation |
| "HKFRS(s)" | Hong Kong Financial Reporting Standard(s) |
| "HKICPA" | Hong Kong Institute of Certified Public Accountants |
| "HKMA" | Hong Kong Monetary Authority |
| "Hong Kong" or "Hong Kong SAR" | Hong Kong Special Administrative Region |
| "IPO" | Initial Public Offering |
| "IT" | Information Technology |
| "LIBOR" | London Interbank Offered Rate |
| "Listing Rules" | The Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited |
| "The Mainland" or "Mainland China" or "The Mainland of China" | The mainland of the PRC |
| "MBS" | Mortgage-backed securities |
| "MPF" | Mandatory Provident Fund |

| Terms | Meanings |
|---|---|
| "MPF Schemes Ordinance" | the Mandatory Provident Fund Schemes Ordinance, Chapter 485 of the Laws of Hong Kong, as amended |
| "MSCI Index" | Morgan Stanley Capital International Index |
| "Moody's" | Moody's Investors Service |
| "Nanyang" | Nanyang Commercial Bank, Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOCHK |
| "Nanyang (China)" | Nanyang Commercial Bank (China) Limited, a company incorporated under the laws of the PRC and a wholly owned subsidiary of Nanyang |
| "ORSO schemes" | the Occupational Retirement Schemes under Occupational Retirement Schemes Ordinance, Chapter 426 of the Laws of Hong Kong |
| "PRC" | The People's Republic of China |
| "QDII(s)" | Qualified Domestic Institutional Investor(s) |
| "QFII" | Qualified Foreign Institutional Investor |
| "RC" | The Risk Committee |
| "RMB" or "Renminbi" | Renminbi, the lawful currency of the PRC |
| "RMD" | The Risk Management Department |
| "SFO" | the Securities and Futures Ordinance, Chapter 571 of the Laws of Hong Kong |
| "SME(s)" | Small and medium-sized enterprise(s) |
| "STC approach" | Standardised (Credit Risk) Approach |
| "STM approach" | Standardised (Market Risk) Approach |
| "STO approach" | Standardised (Operational Risk) Approach |
| "Share Option Scheme" | the Share Option Scheme conditionally approved and adopted by the shareholders of the Company on 10 July 2002 |
| "Sharesave Plan" | the Sharesave Plan conditionally approved and adopted by the shareholders of the Company on 10 July 2002 |
| "Standard & Poor's" | Standard & Poor's Ratings Services |
| "Stock Exchange" or "Stock Exchange of Hong Kong" | The Stock Exchange of Hong Kong Limited |
| "TD" | The Treasury Department |
| "UK" | United Kingdom |
| "US" or "USA" | The United States of America |
| "VAR" | Value at Risk |

# BRANCH NETWORK & CORPORATE BANKING CENTRES

## Bank of China (Hong Kong) – Branch Network
## Hong Kong Island

| Branch | Address | Telephone |
|---|---|---|
| **Central & Western District** | | |
| Bank of China Tower Branch | 1 Garden Road, Hong Kong | 2826 6888 |
| Sheung Wan Branch | 252 Des Voeux Road Central, Hong Kong | 2541 1601 |
| Queen's Road West (Sheung Wan) Branch | 2-12 Queen's Road West, Sheung Wan, Hong Kong | 2815 6888 |
| Connaught Road Central Branch | 13-14 Connaught Road Central, Hong Kong | 2841 0410 |
| Central District Branch | 2A Des Voeux Road Central, Hong Kong | 2160 8888 |
| Central District (Wing On House) Branch | 71 Des Voeux Road Central, Hong Kong | 2843 6111 |
| Shek Tong Tsui Branch | 534 Queen's Road West, Shek Tong Tsui, Hong Kong | 2819 7277 |
| Western District Branch | 386-388 Des Voeux Road West, Hong Kong | 2549 9828 |
| Shun Tak Centre Branch | Shop 225, 2/F, Shun Tak Centre, 200 Connaught Road Central, Hong Kong | 2291 6081 |
| Queen's Road Central Branch | 81-83 Queen's Road Central, Hong Kong | 2588 1288 |
| Bonham Road Branch | 63 Bonham Road, Hong Kong | 2517 7066 |
| IFC Wealth Management Centre | Shop 3001, Level 3, IFC Mall, 1 Harbour View Street, Central, Hong Kong | 2523 8180 |
| Kennedy Town Branch | Harbour View Garden, 2-2F Catchick Street, Kennedy Town, Hong Kong | 2818 6162 |
| Caine Road Branch | 57 Caine Road, Hong Kong | 2521 3318 |
| First Street Branch | 55A First Street, Sai Ying Pun, Hong Kong | 2517 3399 |
| United Centre Branch | Shop 1021, United Centre, 95 Queensway, Hong Kong | 2861 1889 |
| Wyndham Street Branch | 1-3 Wyndham Street, Central, Hong Kong | 2843 2888 |
| Des Voeux Road West Branch | 111-119 Des Voeux Road West, Hong Kong | 2546 1134 |
| Gilman Street Branch | 136 Des Voeux Road Central, Hong Kong | 2135 1123 |
| **Wan Chai District** | | |
| 409 Hennessy Road Branch | 409-415 Hennessy Road, Wan Chai, Hong Kong | 2835 6118 |
| Johnston Road Branch | 152-158 Johnston Road, Wan Chai, Hong Kong | 2574 8257 |
| Harbour Road Branch | Shop 4, G/F, Causeway Centre, 28 Harbour Road, Wan Chai, Hong Kong | 2827 8407 |
| Jardine's Bazaar Branch | G/F, Siki Centre, No.23 Jardine's Bazaar, Causeway Bay, Hong Kong | 2882 1383 |
| Happy Valley Branch | 11 King Kwong Street, Happy Valley, Hong Kong | 2838 6668 |
| Causeway Bay Branch | 18 Percival Street, Causeway Bay, Hong Kong | 2572 4273 |
| Wan Chai (China Overseas Building) Branch | 139 Hennessy Road, Wan Chai, Hong Kong | 2529 0866 |
| Wan Chai (Wu Chung House) Branch | 213 Queen's Road East, Wan Chai, Hong Kong | 2892 0909 |
| Hennessy Road (Wan Chai) Branch | 310-312 Hennessy Road, Wan Chai, Hong Kong | 2923 5628 |
| Wan Chai Road Branch | 127-135 Wan Chai Road, Wan Chai, Hong Kong | 2577 4862 |
| **Eastern District** | | |
| Siu Sai Wan Branch | Shop 19, Cheerful Garden, Siu Sai Wan, Hong Kong | 2505 2399 |
| Taikoo Shing Branch | Shop G1012, Yiu Sing Mansion, Taikoo Shing, Hong Kong | 2886 0612 |
| Taikoo Shing Branch Safe Box Service Centre | Shop G1006, Hoi Shing Mansion, Taikoo Shing, Hong Kong | 2885 4582 |
| North Point Branch | Roca Centre, 464 King's Road, North Point, Hong Kong | 2811 8880 |
| North Point (King's Centre) Branch | 193-209 King's Road, North Point, Hong Kong | 2286 2000 |
| North Point (Hang Ying Building) Branch | Shop B1, 318-328 King's Road, North Point, Hong Kong | 2887 1199 |
| North Point (Kiu Fai Mansion) Branch | 413-415 King's Road, North Point, Hong Kong | 2562 6108 |
| Sai Wan Ho Branch | 142-146 Shau Kei Wan Road, Sai Wan Ho, Hong Kong | 2886 3344 |
| Lee Chung Street Branch | 29-31 Lee Chung Street, Chai Wan, Hong Kong | 2557 3283 |
| Heng Fa Chuen Branch | Shop 205-208, East Wing Shopping Centre, Heng Fa Chuen, Chai Wan, Hong Kong | 2897 1131 |
| Kam Wa Street Branch | 3 Kam Wa Street, Shau Kei Wan, Hong Kong | 2885 9311 |
| City Garden Branch | 233 Electric Road, North Point, Hong Kong | 2571 2878 |
| King's Road Branch | 131-133 King's Road, North Point, Hong Kong | 2887 0282 |
| Chai Wan Branch | Block B, Walton Estate, 341-343 Chai Wan Road, Chai Wan, Hong Kong | 2558 6433 |
| Chai Wan Branch Safe Box Service Centre | 27 Gold Mine Building, 345 Chai Wan Road, Chai Wan, Hong Kong | 2557 0248 |
| Healthy Village Branch | Shop 1&2, Healthy Village Phase II, 668 King's Road, North Point, Hong Kong | 2563 2278 |
| Sheung On Street Branch | 77 Sheung On Street, Chai Wan, Hong Kong | 2897 0923 |
| Aldrich Garden Branch | Shop 58, Aldrich Garden, Shau Kei Wan, Hong Kong | 3196 4956 |

| Branch | Address | Telephone |
|---|---|---|
| Shau Kei Wan (Po Man Building) Branch | 260-262 Shau Kei Wan Road, Shau Kei Wan, Hong Kong | 2568 5211 |
| Quarry Bay Branch | Parkvale, 1060 King's Road, Quarry Bay, Hong Kong | 2564 0333 |
| **Southern District** | | |
| Tin Wan Branch | 2-12 Ka Wo Street, Tin Wan, Hong Kong | 2553 0135 |
| Stanley Branch | Shop 401, Shopping Centre, Stanley Plaza, Hong Kong | 2813 2290 |
| Aberdeen Branch | 25 Wu Pak Street, Aberdeen, Hong Kong | 2553 4165 |
| South Horizons Branch | G38, West Centre Marina Square, South Horizons, Ap Lei Chau, Hong Kong | 2580 0345 |
| South Horizons Branch Safe Box Service Centre | Shop 118, Marina Square East Centre, Ap Lei Chau, Hong Kong | 2555 7477 |
| Wah Kwai Estate Branch | Shop 17, Shopping Centre, Wah Kwai Estate, Hong Kong | 2550 2298 |
| Wong Chuk Hang Road Branch | 40 Wong Chuk Hang Road, Hong Kong | 2814 8272 |
| Chi Fu Landmark Branch | Shop 510, Chi Fu Landmark, Pok Fu Lam, Hong Kong | 2551 2282 |
| Ap Lei Chau Branch | 13-15 Wai Fung Street, Ap Lei Chau, Hong Kong | 2554 6487 |

## Kowloon

| Branch | Address | Telephone |
|---|---|---|
| **Kowloon City District** | | |
| Prince Edward Road (Kowloon City) Branch | 382-384 Prince Edward Road, Kowloon City, Kowloon | 2926 6038 |
| To Kwa Wan Branch | 80N To Kwa Wan Road, To Kwa Wan, Kowloon | 2364 4344 |
| Pak Tai Street Branch | 4-6 Pak Tai Street, To Kwa Wan, Kowloon | 2760 7773 |
| Hung Hom Wealth Management Centre | 37-39 Ma Tau Wai Road, Hung Hom, Kowloon | 2170 0888 |
| Hung Hom (Eldex Industrial Building) Branch | 21 Ma Tau Wai Road, Hung Hom, Kowloon | 2764 8363 |
| OUHK Branch | The Open University of Hong Kong, 30 Good Shepherd Street, Ho Man Tin, Kowloon | 2760 9099 |
| Ma Tau Kok Road Branch | 39-45 Ma Tau Kok Road, To Kwa Wan, Kowloon | 2714 9118 |
| Ma Tau Wai Road Branch | 47-49 Ma Tau Wai Road, Hung Hom, Kowloon | 2926 5123 |
| Site 11 Whampoa Garden Branch | Shop G6, Site 11 Whampoa Garden, Hung Hom, Kowloon | 2363 3982 |
| Whampoa Garden Branch | Shop G8B, Site 1, Whampoa Garden, Hung Hom, Kowloon | 2764 7233 |
| Nga Tsin Wai Road Branch | 25 Nga Tsin Wai Road, Kowloon City, Kowloon | 2383 2316 |
| Waterloo Road Branch | Shop A2, Man Kee Mansion, 86 Waterloo Road, Kowloon | 2363 9231 |
| **Wong Tai Sin District** | | |
| Tai Yau Street Branch | 35 Tai Yau Street, San Po Kong, Kowloon | 2328 0087 |
| Chuk Yuen Estate Branch | Shop S1, Chuk Yuen Shopping Centre, Chuk Yuen South Estate, Kowloon | 2325 5261 |
| Choi Hung Branch | 19 Clear Water Bay Road, Ngau Chi Wan, Kowloon | 2327 0271 |
| Choi Hung Road Branch | 58-68 Choi Hung Road, San Po Kong, Kowloon | 2927 6111 |
| Choi Wan Estate Branch | A3-18 Commercial Complex, Choi Wan Estate, Kowloon | 2754 5911 |
| Wong Tai Sin Branch | Shop G13, Wong Tai Sin Shopping Centre, Wong Tai Sin, Kowloon | 2327 8147 |
| San Po Kong (Wing Lok Building) Branch | 28-34 Tseuk Luk Street, San Po Kong, Kowloon | 2328 7915 |
| Yuk Wah Street Branch | 46-48 Yuk Wah Street, Tsz Wan Shan, Kowloon | 2927 6655 |
| Lok Fu Branch | Shop 2, Lok Fu Plaza II, Lok Fu, Kowloon | 2337 0271 |
| Tseuk Luk Street Wealth Management Centre | 86 Tseuk Luk Street, San Po Kong, Kowloon | 2326 2883 |
| Sheung Fung Street Branch | 66-68 Sheung Fung Street, Tsz Wan Shan, Kowloon | 2327 8118 |
| Diamond Hill Branch | G107 Plaza Hollywood, Diamond Hill, Kowloon | 2955 5088 |
| **Kwun Tong District** | | |
| Kowloon Bay Wealth Management Centre | Shop 2, Telford House, 16 Wang Hoi Road, Kowloon Bay, Kowloon | 2759 9339 |
| Kowloon Bay Branch | 17 Wang Hoi Road, Kowloon Bay, Kowloon | 2331 3783 |
| Ngau Tau Kok (Garden Estate) Branch | Shop 6, Lotus Tower 2, Kwun Tong Garden Estate, 297 Ngau Tau Kok Road, Ngau Tau Kok, Kowloon | 2763 5456 |
| 169 Ngau Tau Kok Road Branch | 169 Ngau Tau Kok Road, Ngau Tau Kok, Kowloon | 2750 7311 |
| 177 Ngau Tau Kok Road Branch | 177 Ngau Tau Kok Road, Ngau Tau Kok, Kowloon | 2927 4321 |

## Bank of China (Hong Kong) – Branch Network (continued)

| Branch | Address | Telephone |
|---|---|---|
| Ping Tin Estate Branch | Shop 225, 2/F Ping Tin Shopping Centre, Lam Tin, Kowloon | 2927 7828 |
| Wang Kwun Road Branch | Unit G1, Nan Fung Commercial Centre, Wang Kwun Road, Kowloon Bay, Kowloon | 2755 0268 |
| Sau Mau Ping Branch | Shop 214, Sau Mau Ping Shopping Centre, Sau Mau Ping, Kowloon | 2772 0028 |
| Hip Wo Street Branch | 195-197 Hip Wo Street, Kwun Tong, Kowloon | 2345 0102 |
| Ting Fu Street Branch | 11-13 Ting Fu Street, Ngau Tau Kok, Kowloon | 2756 4621 |
| Yau Tong Branch | Shop G1-G27, Ka Fu Arcade, Yau Tong Centre, Kowloon | 2349 9191 |
| Hoi Yuen Road Branch | 55 Hoi Yuen Road, Kwun Tong, Kowloon | 2763 2127 |
| Tsui Ping Estate Branch | Shop 116, 1/F Shopping Circuit, Tsui Ping Estate, Kwun Tong, Kowloon | 2345 3238 |
| 26 Fu Yan Street Branch | 26-32 Fu Yan Street, Kwun Tong, Kowloon | 2342 5262 |
| 95 Fu Yan Street Branch | 95 Fu Yan Street, Kwun Tong, Kowloon | 2343 4141 |
| Telford Gardens Wealth Management Centre | Shop P8A, Telford Gardens, Kowloon Bay, Kowloon | 2758 3987 |
| Telford Gardens Branch | Shop P2, Telford Gardens, Kowloon Bay, Kowloon | 2796 1551 |
| Lam Tin Branch | Shop 12, 49 Kai Tin Road, Lam Tin, Kowloon | 2347 1456 |
| Kwun Tong Branch | 20-24 Yue Man Square, Kwun Tong, Kowloon | 2344 4116 |
| Ngau Tau Kok Road (Kwun Tong) Branch | 327 Ngau Tau Kok Road, Kwun Tong, Kowloon | 2389 3301 |
| Kwun Tong Plaza Branch | G1 Kwun Tong Plaza, 68 Hoi Yuen Road, Kwun Tong, Kowloon | 2342 4295 |
| **Yau Tsim Mong District** | | |
| Tai Kok Tsui Branch | 73-77 Tai Kok Tsui Road, Tai Kok Tsui, Kowloon | 2395 3269 |
| Shan Tung Street Branch | 42-48 Shan Tung Street, Mong Kok, Kowloon | 2332 5461 |
| China Hong Kong City Branch | Shop 28, UG/F, China Hong Kong City, 33 Canton Road, Tsim Sha Tsui, Kowloon | 2367 6164 |
| Shanghai Street (Prince Edward) Branch | 689-693 Shanghai Street, Mong Kok, Kowloon | 2391 0502 |
| Prince Edward Branch | 774 Nathan Road, Kowloon | 2399 3000 |
| Tsim Sha Tsui Branch | 24-28 Carnarvon Road, Tsim Sha Tsui, Kowloon | 2721 6242 |
| Tsim Sha Tsui East Branch | Shop G02-03, Inter-Continental Plaza, 94 Granville Road, Tsim Sha Tsui, Kowloon | 2739 0308 |
| Jordan Branch | 328-330 Nathan Road, Kowloon | 2928 6111 |
| Jordan Road Branch | 1/F, Sino Cheer Plaza, 23-29 Jordan Road, Kowloon | 2730 0883 |
| Shanghai Street (Mong Kok) Branch | 611-617 Shanghai Street, Mong Kok, Kowloon | 2394 4181 |
| Mong Kok Branch | 589 Nathan Road, Mong Kok, Kowloon | 2332 0111 |
| Prince Edward Road West (Mong Kok) Branch | 116-118 Prince Edward Road West, Mong Kok, Kowloon | 2928 4138 |
| Mong Kok Road Branch | 50-52 Mong Kok Road, Mong Kok, Kowloon | 2395 3263 |
| Mong Kok (Silvercorp Int'l Tower) Branch | Shop B, 707-713 Nathan Road, Mong Kok, Kowloon | 2391 6677 |
| Mong Kok (President Commercial Centre) Branch | 608 Nathan Road, Mong Kok, Kowloon | 2384 7191 |
| Yau Ma Tei Branch | 471 Nathan Road, Yau Ma Tei, Kowloon | 2780 2307 |
| Kimberley Road Branch | 37 Kimberley Road, Tsim Sha Tsui, Kowloon | 2739 1886 |
| Cameron Road Wealth Management Centre | 30 Cameron Road, Tsim Sha Tsui, Kowloon | 2312 0010 |
| Humphrey's Avenue Branch | 4-4A Humphrey's Avenue, Tsim Sha Tsui, Kowloon | 2311 3822 |
| Olympian City Branch | Shop 133, 1/F, Olympian City 2, 18 Hoi Ting Road, Kowloon | 2749 2110 |
| Fuk Tsun Street Branch | 32-40 Fuk Tsun Street, Tai Kok Tsui, Kowloon | 2391 8468 |
| Canton Road Branch | 60 Canton Road, Tsim Sha Tsui, Kowloon | 2730 0688 |
| **Sham Shui Po District** | | |
| Kowloon Plaza Branch | Unit 1, Kowloon Plaza, 485 Castle Peak Road, Kowloon | 2370 8928 |
| Festival Walk Branch | Unit LG256, Festival Walk, Kowloon Tong, Kowloon | 2265 7288 |
| Yu Chau Street Branch | 42-46 Yu Chau Street, Sham Shui Po, Kowloon | 2397 1123 |
| Dragon Centre Branch | Shop 206A, Dragon Centre, 37K Yen Chow Street, Sham Shui Po, Kowloon | 2788 3238 |
| Lei Cheng Uk Estate Branch | Shop 108, Lei Cheng Uk Commercial Centre, Lei Cheng Uk Estate, Kowloon | 2729 8251 |
| Castle Peak Road (Cheung Sha Wan) Branch | 365-371 Castle Peak Road, Cheung Sha Wan, Kowloon | 2728 3311 |
| 108 Cheung Sha Wan Road Branch | 108 Cheung Sha Wan Road, Sham Shui Po, Kowloon | 2779 0157 |
| 194 Cheung Sha Wan Road Branch | 194-196 Cheung Sha Wan Road, Sham Shui Po, Kowloon | 2728 9389 |
| Cheung Sha Wan Plaza Branch | Shop G08, Cheung Sha Wan Plaza, 833 Cheung Sha Wan Road, Kowloon | 2745 7088 |
| 248 Castle Peak Road Branch | 244-248 Castle Peak Road, Cheung Sha Wan, Kowloon | 2386 1233 |
| 223 Nam Cheong Street Branch | 223 Nam Cheong Street, Sham Shui Po, Kowloon | 2928 2088 |
| Stage 2 Mei Foo Sun Chuen Branch | 19 Glee Path, Mei Foo Sun Chuen, Kowloon | 2370 8382 |
| Mei Foo VIP Centre | Shop N47-49, Mount Sterling Mall, Mei Foo Sun Chuen, Kowloon | 2742 8003 |
| Mei Foo Mount Sterling Mall Branch | 17-B Mount Sterling Mall, Mei Foo Sun Chuen, Kowloon | 2742 6611 |
| Lai Chi Kok Road Branch | 282-284 Lai Chi Kok Road, Sham Shui Po, Kowloon | 2728 7216 |
| Sham Shui Po Branch | 207-211 Nam Cheong Street, Sham Shui Po, Kowloon | 2777 0171 |
| Sham Shui Po (On Ning Building) Branch | 147-149 Castle Peak Road, Sham Shui Po, Kowloon | 2708 3678 |

## New Territories & Outlying Islands

| Branch | Address | Telephone |
|---|---|---|
| **Sha Tin District** | | |
| Jat Min Chuen Branch | Shop 1, G/F Ming Yiu Lau, Jat Min Chuen, Sha Tin, New Territories | 2647 8784 |
| 41 Tai Wai Road Branch | 41-45 Tai Wai Road, Sha Tin, New Territories | 2929 4288 |
| 74 Tai Wai Road Branch | 74-76 Tai Wai Road, Sha Tin, New Territories | 2699 9523 |
| Fo Tan Branch | No 2, 1/F Shatin Galleria, 18-24 Shan Mei Street, Fo Tan, New Territories | 2691 7193 |
| Lucky Plaza Branch | Lucky Plaza, Wang Pok Street, Sha Tin, New Territories | 2605 6556 |
| City One Sha Tin Branch | Shop A, 16-20 Ngan Shing Commercial Centre, City One, Sha Tin, New Territories | 2648 8083 |
| Sha Tin VIP Centre | Shop 18, L1, Shatin Plaza, Sha Tin, New Territories | 2688 7668 |
| Sha Kok Estate Branch | Shop 39, Sha Kok Shopping Centre, Sha Kok Estate, Sha Tin, New Territories | 2648 0302 |
| Heng On Estate Branch | Shop 203, Commercial Centre, Heng On Estate, Ma On Shan, New Territories | 2642 0111 |
| Ma On Shan Plaza Branch | Shop 2103, Level 2, Ma On Shan Plaza, Sai Sha Road, Ma On Shan, New Territories | 2631 0063 |
| Lung Hang Estate Branch | 103 Lung Hang Commercial Centre, Sha Tin, New Territories | 2605 8618 |
| New Town Plaza Branch | Shop 608, Level 6 Phase One, New Town Plaza, Sha Tin, New Territories | 2606 6163 |
| Sunshine City Branch | Shop 16, Blocks C & D, Sunshine City, Ma On Shan, New Territories | 2631 1011 |
| Lek Yuen Branch | No 1, Fook Hoi House, Lek Yuen Estate, Sha Tin, New Territories | 2605 3021 |
| **Tai Po District** | | |
| Tai Kwong Lane Branch | 16-22 Tai Kwong Lane, Tai Po Market, New Territories | 2652 2133 |
| Tai Po Branch | 68-70 Po Heung Street, Tai Po Market, New Territories | 2657 2121 |
| Tai Po Plaza Branch | Unit 4, Level 1 Tai Po Plaza, 1 On Tai Road, Tai Po, New Territories | 2665 5890 |
| On Chee Road Branch | Shop 10-11, Jade Plaza, 3 On Chee Road, Tai Po, New Territories | 2665 1966 |
| Fu Heng Estate Branch | Shop 1-2, Fu Heng Shopping Centre, Tai Po, New Territories | 2661 6278 |
| Fu Shin Estate Branch | Shop G11, Fu Shin Shopping Centre, Tai Po, New Territories | 2663 2788 |
| Kwong Fuk Road Branch | 40-50 Kwong Fuk Road, Tai Po Market, New Territories | 2658 2268 |
| **Sai Kung District** | | |
| Sai Kung Branch | 7-11 Wan King Path, Sai Kung, New Territories | 2792 1465 |
| East Point City Branch | Shop 101, East Point City, Tseung Kwan O, New Territories | 2628 7238 |
| Hau Tak Estate Branch | Shop 15, Hau Tak Shopping Centre, Tseung Kwan O, New Territories | 2703 5203 |
| HKUST Branch | The Hong Kong University of Science & Technology, Clear Water Bay Road, New Territories | 2358 2345 |
| Tseung Kwan O Plaza Branch | Shop 112-125, Level 1, Tseung Kwan O Plaza, Tseung Kwan O, New Territories | 2702 0282 |
| Metro City Branch | Shop 209, Level 2, Metro City Phase 1, Tseung Kwan O, New Territories | 2701 4962 |
| **Tsuen Wan District** | | |
| Tai Wo Hau Branch | 5-9 Tai Ha Street, Tai Wo Hau, Tsuen Wan, New Territories | 2429 0304 |
| 407 Castle Peak Road Branch | 407-411 Castle Peak Road, Tsuen Wan, New Territories | 2920 3211 |
| Clague Garden Branch | Shop 1-3, Commercial Complex, Clague Garden Estate, 24 Hoi Shing Road, Tsuen Wan, New Territories | 2412 2202 |
| Tsuen Wan Branch | 297-299 & 313 Sha Tsui Road, Tsuen Wan, New Territories | 2411 1321 |
| Castle Peak Road (Tsuen Wan) Wealth Management Centre | 167 Castle Peak Road, Tsuen Wan, New Territories | 2406 9932 |
| Castle Peak Road (Tsuen Wan) Branch | 201-207 Castle Peak Road, Tsuen Wan, New Territories | 2416 6577 |

## Bank of China (Hong Kong) – Branch Network (continued)

| Branch | Address | Telephone |
|---|---|---|
| Tsuen Wan VIP Centre | 31-33 Chung On Street, Tsuen Wan, New Territories | 2406 8908 |
| Sham Tseng Branch | Shop G1 & G2, Rhine Garden, Sham Tseng, New Territories | 2491 0038 |
| Fuk Loi Estate Branch | 129-135 Sha Tsui Road, Tsuen Wan, New Territories | 2499 0755 |
| Texaco Road Branch | Shop A112, East Asia Gardens, 36 Texaco Road, Tsuen Wan, New Territories | 2414 4287 |
| **Kwai Tsing District** | | |
| Ha Kwai Chung Branch | 192-194 Hing Fong Road, Kwai Chung, New Territories | 2424 9823 |
| Sheung Kwai Chung Branch | 7-11 Shek Yi Road, Sheung Kwai Chung, New Territories | 2480 6161 |
| Cheung Hong Estate Branch | 201-202 Commercial Centre No 2, Cheung Hong Estate, Tsing Yi Island, New Territories | 2497 7718 |
| Cheung Fat Estate Branch | Shop 317, Cheung Fat Shopping Centre, Tsing Yi Island, New Territories | 2433 1689 |
| Cheung Hong Estate Commercial Centre Branch | 2 G/F, Commercial Centre, Cheung Hong Estate, Tsing Yi Island, New Territories | 2497 0325 |
| Maritime Square Branch | Shop 115, Maritime Square, Tsing Yi Island, New Territories | 2436 9298 |
| Lei Muk Shue Branch | Shop 22, Lei Muk Shue Shopping Centre, Kwai Chung, New Territories | 2428 5731 |
| Metroplaza Branch | Shop 260-265, Metroplaza, 223 Hing Fong Road, Kwai Chung, New Territories | 2420 2686 |
| Kwai Cheong Road Branch | 40 Kwai Cheong Road, Kwai Chung, New Territories | 2480 3311 |
| Kwai Chung Branch | 432-436 Castle Peak Road, Kwai Chung, New Territories | 2410 9133 |
| Kwai Chung Road Branch | 1009 Kwai Chung Road, Kwai Chung, New Territories | 2424 3021 |
| Kwai Chung Plaza Branch | A18-20, G/F Kwai Chung Plaza, 7-11 Kwai Foo Road, Kwai Chung, New Territories | 2920 2468 |
| **Tuen Mun District** | | |
| Tuen Mun Wealth Management Centre | Shop 5, Level 1, North Wing, Trend Plaza, Tuen Mun, New Territories | 2404 9777 |
| Tuen Mun Town Plaza Branch | Shop 2, Tuen Mun Town Plaza phase II, Tuen Mun, New Territories | 2450 8877 |
| Tuen Mun Fa Yuen Branch | Shop G & H, 6 Tsing Hoi Circuit, Tuen Mun, New Territories | 2458 1033 |
| Tuen Mun San Hui Branch | G13-G14 Eldo Court, Heung Sze Wui Road, Tuen Mun, New Territories | 2457 3501 |
| Siu Hong Court Branch | 226 Commercial Centre, Siu Hong Court, Tuen Mun, New Territories | 2466 6703 |
| Leung King Estate Branch | Shop 211, Leung King Shopping Centre, Tuen Mun, New Territories | 2463 3855 |
| Kin Wing Street Branch | 24-30 Kin Wing Street, Tuen Mun, New Territories | 2465 2212 |
| Venice Gardens Branch | Shop13-15, G/F Venice Gardens, Leung Tak Street, Tuen Mun, New Territories | 2455 1288 |
| Butterfly Estate Branch | Shop 123-130, Tip Ling House, Butterfly Estate, Tuen Mun, New Territories | 2920 5188 |
| **Yuen Long District** | | |
| Tai Tong Road Branch | Shop A135, 1/F Hop Yick Plaza, 23 Tai Tong Road, Yuen Long, New Territories | 2479 2113 |
| Yuen Long Branch | 102-108 Castle Peak Road, Yuen Long, New Territories | 2474 2211 |
| Castle Peak Road (Yuen Long) Branch | 162 Castle Peak Road, Yuen Long, New Territories | 2476 2193 |
| Yuen Long (Hang Fat Mansion) Branch | 8-18 Castle Peak Road, Yuen Long, New Territories | 2475 3777 |
| Tin Shui Estate Branch | Shop 108-109, Tin Shui Shopping Centre, Tin Shui Wai, New Territories | 2445 8728 |
| Kau Yuk Road Branch | 18-24 Kau Yuk Road, Yuen Long, New Territories | 2473 2833 |
| Kingswood Villas Branch | A189 Kingswood Richly Plaza, Tin Shui Wai, New Territories | 2448 3313 |
| Kingswood Ginza Branch | Shop G73, Phase 1 Kingswood Ginza, Tin Shui Wai, New Territories | 2616 4233 |
| **North District** | | |
| Sheung Shui Centre Branch | Shop 1007-1009, Level 1, Sheung Shui Centre, Sheung Shui, New Territories | 2670 3131 |
| Sheung Shui Branch | 61 San Fung Avenue, Sheung Shui, New Territories | 2671 0155 |
| Sheung Shui VIP Centre | 33 San Fung Avenue, Sheung Shui, New Territories | 2639 9233 |
| Sha Tau Kok Branch | Block 16-18, Sha Tau Kok Chuen, Sha Tau Kok, New Territories | 2674 4011 |
| Flora Plaza Branch | Shop 28, Flora Plaza, 88 Pak Wo Road, Fanling, New Territories | 2675 6683 |
| Fanling Centre Branch | Shop 2D-E & H, Fanling Centre, Fanling, New Territories | 2669 7899 |
| 136 San Fung Ave Branch | 136 San Fung Avenue, Sheung Shui, New Territories | 2670 6138 |
| Luen Wo Market Branch | 17-19 Wo Fung Street, Luen Wo Market, Fanling, New Territories | 2675 5113 |
| Luen Shing Street Branch | Shop B, 10-16 Luen Shing Street, Luen Wo Market, Fanling, New Territories | 2675 6113 |
| **Outlying Island District** | | |
| Cheung Chau Branch | 53-55 Tai Sun Street, Cheung Chau, New Territories | 2981 0021 |
| Hong Kong International Airport Branch | Unit 7T075, Passenger Terminal Building, Hong Kong International Airport | 2326 1883 |

## Mainland Branches

| Branch | Address | Telephone |
|---|---|---|
| Shenzhen Branch | G/F, The Kwangtung Provincial Bank Building, 1013 Ren Min Nan Road, Shenzhen, China | (86-755) 8233 0230 |
| Shenzhen Baoan Sub-Branch | Unit 108 Xushida Garden, Xin An Si Road, Baoan District 34-2, Shenzhen, China | (86-755) 2785 3302 |
| Shenzhen Futian Sub-Branch | 1/F, Shen Ye Garden Club House, Caitian Road, Futian District, Shenzhen, China | (86-755) 8294 2929 |
| Shantou Branch | G/F, 3 Yingbin Road, Shantou, China | (86-754) 8826 8266 |
| Shanghai Branch | Room B201-B202, 2/F Tomorrow Square, 389 Nanjing West Road, Shanghai, China | (86-21) 2306 9090 |
| Qingdao Branch | G/F, 2nd Building, 41 West Donghai Road, Qingdao, China | (86-532) 6670 7676 |

## Corporate Banking Centres & SME Centres

| Network & Centres | Address | Telephone |
|---|---|---|
| Corporate Business | 10/F, Bank of China Tower, 1 Garden Road, Hong Kong | 2826 6889 |
| Corporate Finance | 10/F, Bank of China Tower, 1 Garden Road, Hong Kong | 2826 6491 |
| Commercial Business I | 9/F, Bank of China Tower, 1 Garden Road, Hong Kong | 3419 3509 |
| Commercial Business II | 9/F, Bank of China Tower, 1 Garden Road, Hong Kong | 3419 3555 |
| Commercial Business III | Unit 701-706, The Gateway Tower 3 (Prudential Tower), 21 Canton Road, Tsim Sha Tsui, Kowloon | 2247 8888 |
| Financial Institutions | 33/F, Bank of China Tower, 1 Garden Road, Hong Kong | 2903 6666 |
| Hong Kong Central and West Commercial Centre<br>Hong Kong Central and West SME Centre | 24/F, Bank of China Tower, 1 Garden Road, Hong Kong | 3419 3513 |
| Central District Commercial Centre<br>Central District SME Centre | 1/F, Wing On House, 71 Des Voeux Road Central, Hong Kong | 2109 5888 |
| Hong Kong East Commercial Centre<br>Hong Kong East SME Centre | 13/F, Cambridge House, Taikoo Place, 981 King's Road, Island East, Hong Kong | 2910 9393 |
| Causeway Bay Commercial Centre<br>Causeway Bay SME Centre | 3/F, Eastern Commercial Centre, 393-407 Hennessy Road, Wan Chai, Hong Kong | 2833 8790 |
| Kowloon East Commercial Centre<br>Kowloon East SME Centre | Room 607-610, 6/F, Telford House, 16 Wang Hoi Road, Kowloon Bay, Kowloon | 3406 7300 |
| San Po Kong Commercial Centre<br>San Po Kong SME Centre | Room 601, 6/F, Stelux House, 698 Prince Edward Road East, San Po Kong, Kowloon | 2263 4900 |
| Hung Hom Commercial Centre<br>Hung Hom SME Centre | Room 506-507, 5/F, Tower A, Hung Hom Commercial Centre, 37-39 Ma Tau Wai Road, Hung Hom, Kowloon | 2197 0188 |
| Kowloon West Commercial Centre<br>Kowloon West SME Centre | 9/F, Kwangtung Provincial Bank Building, 589 Nathan Road, Mongkok, Kowloon | 3412 1688 |
| Tsim Sha Tsui Commercial Centre<br>Tsim Sha Tsui SME Centre | Shop UG 01, Inter-Continental Plaza, 94 Granville Road, Tsim Sha Tsui, Kowloon | 2301 9788 |
| New Territories East Commercial Centre<br>New Territories East SME Centre | 3/F, 68-70 Po Heung Street, Tai Po Market, New Territories | 2654 3222 |
| Fo Tan Commercial Centre<br>Fo Tan SME Centre | Room 7-12, 15-17 &19, 14/F, Shatin Galleria, 18-24 Shan Mei Street, Fo Tan, Shatin, New Territories | 2687 5665 |
| New Territories West Commercial Centre<br>New Territories West SME Centre | Room 1720-1724 & 1716B-1719, Nan Fung Centre, 264-298 Castle Peak Road, Tsuen Wan, New Territories | 3412 7044 |

## Corporate Banking Centres & SME Centres (continued)

| Network & Centres | Address | Telephone |
|---|---|---|
| Yuen Long Commercial Centre<br>Yuen Long SME Centre | 4/F, The Kwangtung Provincial Bank Building, 102-108 Castle Peak Road, Yuen Long, New Territories | 2442 8788 |
| Trade Product | 5/F, Bank of China Centre, Olympian City, 11 Hoi Fai Road, West Kowloon | 3198 3544 |
| Shun Tak Centre Commercial Services Centre | Shop 225, 2/F, Shun Tak Centre, 200 Connaught Road Central, Sheung Wan, Hong Kong | 2108 9662 |
| Cheung Sha Wan Commercial Services Centre | Unit 1, Kowloon Plaza, 485 Castle Peak Road, Kowloon | 2370 8928 |

## Nanyang Commercial Bank – Branch Network

| Branch | Address | Telephone |
|---|---|---|
| Head Office | 151 Des Voeux Road, Central, Hong Kong | 2852 0888 |
| **Hong Kong Island** | | |
| Western Branch | 128 Bonham Strand East, Sheung Wan, Hong Kong | 2851 1100 |
| Causeway Bay Branch | 472 Hennessy Road, Causeway Bay, Hong Kong | 2832 9888 |
| Happy Valley Branch | 29 Wong Nei Chung Road, Happy Valley, Hong Kong | 2893 3383 |
| Kennedy Town Branch | 86 Belcher's Street, Kennedy Town, Hong Kong | 2817 1946 |
| Quarry Bay Branch | 1014 King's Road, Quarry Bay, Hong Kong | 2563 2286 |
| Des Voeux Road West Branch | 334 Des Voeux Road West, Hong Kong | 2540 4532 |
| Aberdeen Branch | 171 Aberdeen Main Road, Aberdeen, Hong Kong | 2553 4115 |
| North Point Branch | 351 King's Road, North Point, Hong Kong | 2566 8116 |
| Sheung Wan Branch | 21 Connaught Road West, Sheung Wan, Hong Kong | 2559 0888 |
| Sai Wan Ho Branch | 63 Shaukeiwan Road, Sai Wan Ho, Hong Kong | 2567 0315 |
| Wanchai Branch | 123 Johnston Road, Wanchai, Hong Kong | 2574 8118 |
| Causeway Centre Branch | Shop 9-10, Causeway Centre, 28 Harbour Road, Wanchai, Hong Kong | 2827 6338 |
| Central District Branch | 2/F Century Square, 1-13 D'Aguilar Street, Central, Hong Kong | 2522 5011 |
| Sunning Road Branch | 8 Sunning Road, Causeway Bay, Hong Kong | 2882 7668 |
| **Kowloon** | | |
| Mongkok Branch | 727 Nathan Road, Mongkok, Kowloon | 2394 8206 |
| Yaumati Branch | 309 Nathan Road, Yaumati, Kowloon | 2782 9888 |
| Ferry Point Branch | Shops D-F, G/F, Best-O-Best Commercial Centre, 32-36 Ferry Street, Yaumati, Kowloon | 2332 0738 |
| Homantin Branch | 71A Waterloo Road, Homantin, Kowloon | 2715 7518 |
| Nathan Road Branch | 570 Nathan Road, Mongkok, Kowloon | 2780 0166 |
| Laichikok Road Branch | 236 Laichikok Road, Shamshuipo, Kowloon | 2396 4164 |
| Jordan Road Branch | 20 Jordan Road, Yaumati, Kowloon | 2735 3301 |
| Tokwawan Branch | 62 Tokwawan Road, Kowloon | 2764 6666 |
| Kwun Tong Branch | G/F Shop 1, 1/F Shop 2, 410 Kwun Tong Road, Kowloon | 2389 6266 |
| Tsimshatsui Branch | Shop A, 1/F, Hong Kong Pacific Centre, 28 Hankow Road, Tsimshatsui, Kowloon | 2376 3988 |
| Hunghom Branch | 69A Wuhu Street, Hunghom, Kowloon | 2362 2301 |
| Shamshuipo Branch | 198-200 Tai Po Road, Shamshuipo, Kowloon | 2777 0147 |
| Yee On Street Branch | Shops 4-6, G/F, Yee On Centre, 45 Hong Ning Road, Kowloon | 2790 6688 |
| Peninsula Centre Branch | Shop G48 Peninsula Centre, 67 Mody Road, Tsimshatsui, Kowloon | 2722 0823 |
| San Po Kong Branch | 41-45, Yin Hing Street, San Po Kong, Kowloon | 2328 5555 |
| Kowloon City Branch | 86 Nga Tsin Wai Road, Kowloon City, Kowloon | 2716 6033 |
| Laguna City Branch | Shop No. 26, Phase 1 Laguna City, Cha Kwo Ling Road, Kowloon | 2772 3336 |
| **New Territories** | | |
| Kwai Chung Branch | 100 Lei Muk Road, Kwai Chung, New Territories | 2480 1118 |
| Tai Po Branch | Shop No. 11, G/F, Treasure Garden, 1 On Chee Road, Tai Po, New Territories | 2656 5201 |
| Yuen Long Branch | G/F, Tung Yik Building, Tai Tong Road, Yuen Long, New Territories | 2479 0231 |
| Ha Kwai Chung Branch | 180 Hing Fong Road, Kwai Chung, New Territories | 2429 4242 |
| Tsuen Wan Branch | 78 Chung On Street, Tsuen Wan, New Territories | 2492 0243 |
| Sheung Shui Branch | 31 Fu Hing Street, Sheung Shui, New Territories | 2679 4333 |
| Tuen Mun Branch | Forward Mansion, Yan Ching Circuit, Tuen Mun, New Territories | 2459 8181 |
| Shatin Branch | Shop 7-8, Lucky Plaza, Shatin, New Territories | 2605 9188 |
| Fou Wah Centre Branch | Shop A, 2/F, Fou Wah Centre, 210 Castle Peak Road, Tsuen Wan, New Territories | 2498 4411 |
| Sai Kung Branch | Shop 11-12 Sai Kung Garden, Man Nin Street, New Territories | 2791 1122 |
| Cheung Sha Wan Commercial Banking Centre | Unit 1005, 10/F, Tower II, Cheung Sha Wan Plaza, 833 Cheung Sha Wan Road, Kowloon | 2785 6182 |
| **Overseas** | | |
| San Francisco Branch | 31/F, 50 California Street, San Francisco, CA94111, USA | (1-415) 398 8866 |

## Nanyang Commercial Bank (China) – Branch Network

| Branch | Address | Telephone |
|---|---|---|
| **The Mainland of China** | | |
| Head Office | 19-20/F, Mirae Asset Tower, 166 Lujiazui Ring Road, Pudong, Shanghai, China | (86-21) 3856 6666 |
| Shenzhen Branch | Nanyang Mansion, 2002 Jian She Road, Luohu District, Shenzhen, China | (86-755) 2515 6333 |
| Shenzhen Shekou Sub-Branch | G/F, Finance Centre, No.22,Taizi Road, Shekou, Shenzhen, China | (86-755) 2682 8788 |
| Haikou Branch | 1st Floor, Time Square, No.2, Guomao Road, Haikou, Hainan, China | (86-898) 6650 0038 |
| Guangzhou Branch | Room 402, Skygalleria CITIC Plaza, 233 Tianhe North Road, Guangzhou, China | (86-20) 3891 2668 |
| Guangzhou Panyu Sub-branch | C001-C008 & C101-C106, No. 2, Fuhua West Road, Shiqiao, Panyu, Guangzhou, China | (86-20) 3451 0228 |
| Dalian Branch | B1/F,1/F,2/F,3/F,5/F Anho Building, No.87 Renmin Road, Dalian, China | (86-411) 3984 8888 |
| Beijing Branch | No. 8B, Jian Guo Men Wai Da Jie, Chaoyang District, Beijing, China | (86-10) 6568 4728 |
| Shanghai Branch | Room A103-A107, Tomorrow Square, 389 Nanjing West Road, Shanghai, China | (86-21) 6375 5858 |
| Shanghai Xuhui Sub-branch | Huafu City, No.1, Lane 500, Tian Yao Qiao Ro, Xuhui District, Shanghai, China | (86-21) 6468 1999 |
| Hangzhou Branch | 1-2/F, International Business Building, 195-1 Qingchun Road, Hangzhou, Zhejiang, China | (86-571) 8703 8080 |
| Nanning Branch | 1/F-2/F, Kings Wealth CBD Modern Town, No.63, Jinhu Road, Nanning, Guangxi, China | (86-771) 555 8333 |

## Chiyu Banking Corporation – Branch Network

| Branch | Address | Telephone |
|---|---|---|
| Head Office | 78 Des Voeux Road Central, Hong Kong | 2843 0111 |
| **Hong Kong Island** | | |
| North Point Branch | 390-394 King's Road, North Point, Hong Kong | 2570 6381 |
| Wanchai Branch | 325 Hennessy Road, Wanchai, Hong Kong | 2572 2823 |
| Sheung Wan Branch | Shop 3, G/F, Lee Fung Building, 315-319 Queen's Road Central, Hong Kong | 2544 1678 |
| Western Branch | 443 Queen's Road West, Hong Kong | 2548 2298 |
| Quarry Bay Branch | 967-967A, King's Road, Quarry Bay, Hong Kong | 2811 3131 |
| Aberdeen Branch | G/F, 138-140, Aberdeen Main Road, Aberdeen, Hong Kong | 2553 0603 |
| **Kowloon** | | |
| Hung Hom Branch | 23-25 Gillies Avenue, Hung Hom, Kowloon | 2362 0051 |
| Kwun Tong Branch | 42-44 Mut Wah Street, Kwun Tong, Kowloon | 2343 4174 |
| Sham Shui Po Branch | 235-237 Laichikok Road, Kowloon | 2789 8668 |
| San Po Kong Branch | 61-63 Hong Keung Street, San Po Kong, Kowloon | 2328 5691 |
| Yau Ma Tei Branch | 117-119 Shanghai Street, Yaumatei, Kowloon | 2332 2533 |
| Castle Peak Road Branch | 226-228 Castle Peak Road, Kowloon | 2720 5187 |
| Kowloon Bay Branch | Shop 10, G/F, Kai Lok House, Kai Yip Estate, Kowloon Bay, Kowloon | 2796 8968 |
| Tokwawan Branch | G/F, Shop11-13, 78 Tokwawan Road, Kowloon | 2765 6118 |
| Tsz Wan Shan Branch | Shop 703A, 7/F, Tsz Wan Shan Shopping Centre, 23 Yuk Wah Street, Tsz Wan Shan, Kowloon | 2322 3313 |
| **New Territories** | | |
| Yau Oi Estate Branch | Shop 103-104, G/F, Restaurant Block, Yau Oi Estate, Tuen Mun, New Territories | 2452 3666 |
| Kwai Hing Estate Branch | Shop 1, G/F, Hing Yat House, Kwai Hing Estate, Kwai Chung, New Territories | 2487 3332 |
| Tai Wo Estate Branch | Shop 112-114, G/F, On Wo House, Tai Wo Estate, Tai Po, New Territories | 2656 3386 |
| Belvedere Garden Branch | Shop 5A, G/F, Belvedere Square, Tsuen Wan, New Territories | 2411 6789 |
| Tsuen Wan Branch | Shop 1 & 1d, Level 2, Discovery Park Commercial Centre, Tsuen Wan, New Territories | 2413 8111 |
| Sui Wo Court Branch | Shop F7, Commercial Centre, Sui Wo Court, Shatin, New Territories | 2601 5888 |
| Ma On Shan Branch | Shop 313, Level 3, Ma On Shan Plaza, Bayshore Tower, Ma On Shan, New Territories | 2640 0733 |
| Sheung Tak Estate Branch | Shop 238, Sheung Tak Shopping Centre, Sheung Tak Estate, Tseung Kwan O, New Territories | 2178 2278 |
| **The Mainland of China** | | |
| Xiamen Branch | 1/F, 859 Xiahe Road, Xiamen, Fujian Province, China | (86-592) 5851 691 |
| Fuzhou Branch | 1/F, International Building, 210 Wusi Road, Fuzhou Fujian Province, China | (86-591) 8781 0078 |
| Xiamen Jimei Sub-branch | No.88 Jiyuan Road Jimei Xiamen | (86-592) 6193 302 |

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As a good corporate citizen, we do not use lamination and spot UV as normally adopted by the industry in our Annual Report 2008. Instead, we use varnishing, an environmentally friendly technique. The whole report is also printed on recyclable and elemental chlorine-free paper. This demonstrates our efforts in working for the betterment of our future generations.

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