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

# 2011 INTERIM REPORT

Stock code: 2388

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# FINANCIAL HIGHLIGHTS

| For the period/year | **30 June 2011 HK$'m** | 30 June 2010[7] HK$'m | 31 December 2010 HK$'m |
|---|---|---|---|
| Net operating income before impairment allowances | **15,126** | 12,541 | 27,508 |
| Operating profit | **13,103** | 8,168 | 18,239 |
| Profit before taxation | **14,587** | 8,767 | 19,742 |
| Profit for the period/year | **12,354** | 7,355 | 16,690 |
| Profit attributable to the equity holders of the Company | **11,993** | 7,192 | 16,196 |
| **Per share** | **HK$** | HK$ | HK$ |
| Basic earnings per share | **1.1343** | 0.6802 | 1.5319 |
| Dividend per share | **0.6300** | 0.4000 | 0.9720 |
| **At period/year end** | **HK$'m** | HK$'m | HK$'m |
| Capital and reserves attributable to the equity holders of the Company | **126,163** | 107,991 | 115,181 |
| Issued and fully paid share capital | **52,864** | 52,864 | 52,864 |
| Total assets | **1,830,379** | 1,302,179 | 1,661,040 |
| **Financial ratios** | **%** | % | % |
| Return on average total assets[1] | **1.33** | 1.17 | 1.21 |
| Return on average shareholders' equity[2] | **19.88** | 13.56 | 14.77 |
| Cost to income ratio[3] | **13.18** | 36.15 | 34.84 |
| Loan to deposit ratio[4] | **60.95** | 64.02 | 59.69 |
| Average liquidity ratio[5] | **36.38** | 37.81 | 38.77 |
| Capital adequacy ratio[6] | **17.62** | 16.17 | 16.14 |

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

2. Return on average shareholders' equity

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

3. In calculating cost to income ratio for the first half of 2011, cost includes the amount recovered from Lehman Brothers minibonds.

4. Loan to deposit ratio is calculated as at 30 June 2011, 30 June 2010 and 31 December 2010. Loan represents gross advances to customers. Deposit includes structured deposits reported as "Financial liabilities at fair value through profit or loss".

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

6. 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. The Group adopted the foundation internal ratings-based ("FIRB") approach to calculate credit risk and BOCHK adopted the internal models approach to calculate general market risk for interest rate and exchange rate exposures as at 30 June 2011, as opposed to the STC approach and STM approach that were used as at 31 December 2010. As a result of the change in the basis used, the capital ratios shown above are not directly comparable.

7. Certain comparative amounts have been restated to reflect the early adoption of HKAS 12 (Amendment) "Income Taxes".

# CHAIRMAN'S STATEMENT

In the first six months of 2011, the Group continued to adopt a proactive growth strategy and delivered satisfactory results. Our results were solid and well-balanced, with continued growth in core businesses while maintaining a strong financial position and sound risk management. As at end June 2011, the Group's total assets grew 10.2% to HK$1,830.4 billion. Operating income before impairment allowances increased by 20.6% year-on-year to HK$15,126 million. Operating profit before impairment allowances increased by 64.0% to HK$13,133 million. The Group's profit attributable to shareholders increased by 66.8% year-on-year to HK$11,993 million or HK$1.1343 per share. The increase in net profit was mainly attributable to the growth of our core businesses and the Lehman-minibonds related recovery. The Board has declared an interim dividend of HK$0.63 per share, representing an increase of 57.5% compared to HK$0.40 per share for the same period last year.

During the first half of the year, loan demand in Hong Kong remained very robust but deposit growth continued to lag behind. This has raised market concerns about the continued rapid pace of credit growth and the pressure it may pose on banks' liquidity and risk management. As demonstrated in our 2010 results, our balanced growth strategy which aims at delivering sustainable results has been proven effective. During the period, we continued our business strategy and maintained a reasonable growth pace. While capturing growth opportunities, we maintained stringent risk control and proactively managed our assets and liabilities. We strictly adhered to our credit policies and focused on customer selection to ensure quality growth. As at end June 2011, we further expanded our loan book in a sustainable manner with a growth of 9.7%. In addition, loan quality remained strong with classified or impaired loan ratio slightly reduced to 0.10% from 0.14% at end 2010. Amid intensified deposit competition, we adopted proactive deposit-taking initiatives, including product improvement and marketing campaigns, to support our business growth. Our customer deposits increased by 7.5%. Loan-to-deposit ratio was at 60.95% compared to 59.69% at end 2010 while our liquidity position remained solid at 36.38%.

2011 marked an important development of our capital management. We have migrated to the foundation internal ratings-based ("FIRB") approach under the Basel II capital adequacy framework to quantify our credit risk. Our capital adequacy ratio maintained at a solid level of 17.62% as at end June 2011. The implementation of FIRB provides an important support for the Group's credit business and risk management. We believe a strong capital base will provide us with greater flexibility to fund future business growth and offer a safeguard against market uncertainties. We will continue to pursue prudent and proactive capital and liquidity management in response to the changing market environment and more stringent regulatory requirements.

As for our business development, we continued to enhance our business platform and deepen our customer relationship for the Group's long-term sustainable growth. We see considerable business opportunities for the Group leveraging our strong customer base and business franchise. With our Global Relationship Manager Programme, we closely collaborated with BOC and offered total solutions to core corporate clients. We also broadened our high-quality and cross-border customer base by offering differentiated services to our wealth management customers. The offshore RMB business is another key area which enables us to capture more business opportunities and enhance our customer relationships. During the period, we continued to expand our RMB deposit base and our trade settlement and exchange transactions also recorded satisfactory growth. We also diversified the uses of RMB funds and broadened the RMB product spectrum in order to enhance profitability and service capability. As the sole Clearing Bank ("CB") of the RMB banking business in Hong Kong, we are fully committed to the healthy and orderly development of the offshore RMB market. We aim to provide comprehensive and efficient clearing services for all the RMB Participating Banks ("PBs"). In the first half, we have introduced the RMB Repo Facilities to enhance the liquidity of Hong Kong's RMB market. We have also launched the RMB Fiduciary Account Scheme which enables the PBs to better manage their exposure to CB.

Regarding the Lehman Brothers Mini-bonds issue, I am pleased with the implementation of the final resolution. Investors recovered the collaterals for the relevant series, bringing the matter to a close. I would like to take this opportunity to thank our customers, shareholders and stakeholders for their understanding and support throughout the process. We deeply value the long-term associations that we have developed with our customers over many years and look forward to further enhancing these important relationships. One of our key missions is to provide professional service to meet the needs and expectations of all our customers.

Looking into the second half of the year, we may face increasing uncertainty and volatility in the market. The slow recovery of the US economy, ever evolving European debt crisis, Japan's pending recovery from the earthquake as well as the rising inflationary pressure may lead to softening growth of the global markets. Lately, the global financial markets reeled amid concern over worsening global economic outlook triggered by the downgrade of the US sovereign credit rating. Looking forward, we need to stay alert and be prepared. We will remain focused on proactively and prudently managing our capital, liquidity and risks. We will continue our growth in a sustainable and balanced manner. On the back of the Group's financial strengths and proactive management, we believe we will be strongly positioned to safeguard against market uncertainties while capturing the emerging growth opportunities.

The consistently solid performance of the Group reflected the dedication and diligence of our management and staff. I wish to take this opportunity to thank them for their contributions. I would also like to thank our customers and shareholders for their continuous support and the Board for their wisdom and counsel. My colleagues and I will continue to work tirelessly for continual improvement and creating greater value for our shareholders.

**XIAO Gang**
*Chairman*

24 August 2011

# CHIEF EXECUTIVE'S REPORT

I am pleased to report that in the first half of 2011, we were able to capitalise on our core competencies and premier position to achieve strong growth in income and earnings while reinforcing our market lead in major business segments. We attained record interim highs in our net operating income before impairment allowances, operating profit and profit attributable to shareholders. Our interim dividends to shareholders also increased to a new level.

During the interim period, we were operating in a mixed environment where opportunities and uncertainties appeared side by side. The external situation remained volatile, especially in Europe, the US and Japan. However, the Asian economy in general fared better, led by the strong economic performance of the Mainland of China. Benefiting from this, Hong Kong experienced robust GDP growth. For the local banking sector, the demand for credit facilities and financial services was on the rise and the market for offshore RMB banking business expanded rapidly. Yet, banks continued to be confronted with challenges like mounting inflationary pressure, exceptionally low interest rates and intensifying competition.

Fully alert to the volatilities and challenges in the market, we have been implementing a proactive management strategy to drive steady and sustainable growth. While maintaining rigorous risk management, we have been taking full advantage of the reviving economy and capturing new business opportunities to grow our income and earnings in a balanced manner. At the same time, we have been highly vigilant with regard to our major financial ratios and would adjust our strategies when and where necessary. Furthermore, as a forward-looking banking group, we put particular emphasis on the quality and sustainability of growth to ensure that we strike a right balance among growth, return and risks.

## Performance Highlights

Our major achievements in the first half of 2011 once again demonstrated our capabilities in delivering solid and sustained growth for our shareholders.

- We recorded broad-based growth in income and profit. All our core businesses, including Personal Banking, Corporate Banking, Treasury, RMB Banking and Insurance, registered healthy growth. There was satisfactory growth in all our income streams, including net interest income, net fee and commission income as well as net trading income.

- We spearheaded the growth of RMB banking businesses by broadening our service scope to create new demand and enlarge our customer base. We launched a number of RMB products for individual and corporate customers. By registering encouraging growth in both business volume and income, the RMB-related business has become a new growth engine and profit stream for the Group.

- With our focus on the quality of growth, we therefore adhered to our prudent credit policy and continued to grow our lending business in a balanced manner. We also achieved an inspiring increase in customers' deposits amid keen competition in the market. As the gap between our loan growth and deposit growth was narrower than that of the industry as a whole, we kept our loan-to-deposit ratio at a healthy level.

- Capitalising on the advantages of our traditional businesses, we scored satisfactory growth in fee and commission income, covering such areas as credit cards, insurance, loans, bills, currency exchange and other services. In particular, we significantly expanded our fund distribution business on the back of improved investment sentiment. Our life insurance business maintained its strong growth momentum in both premium income and profit, and captured a bigger market share.

- While delivering robust business results, we also excelled in cost management. Our cost-to-income ratio was the best in the local market.

- Through effective management, we maintained our strong financial position and superior asset quality. We are well-capitalised, with our capital adequacy ratio among the best in the local industry. Our classified or impaired loan ratio further improved and remained the lowest in the market.

- Besides, we brought the Lehman Brothers Minibonds issue to a satisfactory conclusion, thus recovering a substantial part of the expenses previously incurred.

## Financial Performance

In the first six months of 2011, the Group's profit attributable to shareholders increased strongly by 66.8% to HK$11,993 million, which was made possible by the growth in profit of our core businesses and net recovery from the underlying collateral of the Lehman Brothers Minibonds amounting to HK$2,854 million. Should the impact of the above-mentioned net recovery and the Lehman Brothers-related expenses be excluded, the profit attributable to shareholders would still have grown by a solid 33.4% to HK$9,679 million.

The Group's net operating income before impairment allowances was HK$15,126 million, up 20.6% year-on-year. Operating profit before impairment allowances was HK$13,133 million, up 64.0% year-on-year.

Return on average total assets (ROA) and return on average shareholders' equity (ROE) were 1.33% and 19.88% respectively, versus 1.17% and 13.56% respectively for the first half of 2010.

Despite persistently low interest rates continuing to compress interest spreads, net interest income increased by 13.8% year-on-year to HK$10,205 million. This was mainly attributable to an increase of 48.7% in our average interest-earning assets, offsetting the narrowing of the net interest margin (NIM) by 37 basis points to 1.21% during the six-month period. The narrowing of NIM was partly caused by the diluting effect of BOCHK's function as Hong Kong's RMB clearing bank. Should this effect be discounted, the NIM would have narrowed by 16 basis points to 1.48%.

Net fee and commission income grew by 17.3% year-on-year to HK$3,986 million. This was led mainly by the surge in commission income from insurance (+177.3%), fund distribution (+162.7%) and bills business (+12.7%). There were also increases in fee income from credit cards (+31.7%), currency exchange (+79.2%), trust services (+25.5%) and payment services (+11.4%).

The Group recorded a net trading gain of HK$761 million in the 2011 interim period versus a net trading loss of HK$36 million in the same period in 2010. The rebound was led by the rise in net trading income from foreign exchange and related products as well as the drastic decrease in the loss arising from interest rate instruments.

Under a proactive management strategy, we recorded steady loan growth. Total loans and advances to customers saw a total increase of 9.7% to reach HK$672,858 million, which was mainly contributed by growth in corporate loans (+8.5%) and residential mortgage loans (+14.0%). Loans for use in Hong Kong were up 12.3% whereas loans for use outside Hong Kong, up 3.3%. In anticipation of changes in the market condition, we were more discreet in conducting our lending business while taking initiatives to improve the pricing of new corporate loans during the period.

There was an increase of 7.5% in deposits from customers to HK$1,104,004 million. As a reflection of customers' preference, RMB deposits rose by 39.9% to HK$218,823 million. The Group's loan-to-deposit ratio stayed at 60.95% as at the end of June.

The Group's total assets increased to HK$1,830,379 million as of 30 June 2011, up 10.2% over the six-month period. Effective risk management ensured the quality of our assets. The classified or impaired loan ratio for the first half of 2011 edged lower to 0.10% from 0.14% six months ago and 0.23% twelve months ago, now being the lowest in the market.

In view of escalating inflation and aiming to further enhance our productivity, we employed the same disciplined approach, as always, to managing costs. Total operating expenses dropped by 56.0% year-on-year due to the impact of Lehman Brothers-related products. Without this reversal, total operating expenses would have increased by 8.3% to HK$4,828 million. This was mainly necessitated by the rise in staff costs to reward good performance and the increase in headcount to support business development. Our core cost-to-income ratio (excluding the impact of Lehman Brothers-related products) was 31.92%, the best in the market.

Our capital and liquidity positions remained strong. As from 1 January 2011, the Group adopts the foundation internal ratings-based (FIRB) approach in calculating the capital adequacy ratio (CAR). This new approach enables us to manage our business more effectively with a greater emphasis on risk control. Consolidated CAR as at 30 June 2011 was 17.62%, of which core capital ratio was 12.87%. The Group's average liquidity ratio stayed at the healthy level of 36.38%.

# CHIEF EXECUTIVE'S REPORT

## Business Review

The Group's major business segments achieved higher income and profit overall.

The **Personal Banking** business maintained its growth momentum and expanded steadily. Operating income increased by 4.6% to HK$5,563 million while profit before taxation increased by 22.1% to HK$2,723 million.

The improved performance was witnessed in a wide spectrum of businesses. As the property market was thriving, we took initiatives to meet the rising demand for residential mortgage loans. By introducing new mortgage products and cooperating with major developers, we grew our residential property mortgage by 14.0%. More importantly, in view of higher funding costs, we adjusted the pricing of HIBOR-based mortgage loans to ensure improved yield. To capitalise on the surge in consumer spending by both local residents and incoming tourists, we stepped up our effort in growing our credit card business. This resulted in rapid growth in cardholder spending (+26.2%) and merchant acquiring volume (+38.4%). Through service enhancement and product innovation, we continued to lead the market in the RMB-HKD dual currency card business. Our Bancassurance business also flourished under an effective strategy covering sales, marketing and service enhancement. The development of the fund distribution business deserves special mention. By strengthening our retail fund advisory service through setting up the Investment Product Specialist Team, we grew our distribution volume by nearly 2.4 folds year-on-year.

We upgraded and optimised our distribution channels to better serve local and cross-border customers. In the Group's service network, there was a total of 132 wealth management centres and 21 dedicated Mainland customers service centres as at the end of June. In the first six months of the year, the number of wealth management customers and total assets maintained with the Group grew by 9.7% and 4.0% respectively.

The Group's **Corporate Banking** business also flourished in the interim period. Operating income increased by 29.7% to HK$5,785 million while profit before taxation went up by 32.6% to HK$4,453 million.

Corporate loans increased by 8.5% year-on-year. At the same time, the pricing of loans and loan quality improved. We upgraded and expanded our financial services for corporate clients, both local and cross-border. Underpinned by the revival of global trade, we grew our trade finance volume substantially. In particular, our cross-border trade settlement volume soared by 138%. We made further progress in developing our custody service by securing mandates to provide global custody services to a number of QDIIs and other financial institutions. At the end of June 2011, total assets under our custody were valued at HK$481.7 billion. Meanwhile, we have been on track in expanding our cash management business, especially with regard to RMB cash management. We enhanced our services for local SMEs with sound fundamentals and succeeded in growing our business.

The Group's **Treasury** segment delivered very good results in the first half. Operating income increased by 32.4% to HK$3,145 million. Profit before taxation was up 35.3% to HK$2,865 million. Under our strategy of proactive management with liquidity and safety as our top priorities, we succeeded in diversifying the Group's investment portfolio and reducing our exposure to high-risk investments. Our exposure to PIIGS, the 5 European countries affected by the debt crisis, dropped to an insignificant level. Meanwhile, we took advantage of the steepening yield curve and increased our investment in fixed-rate debt securities, particularly government-related securities and high-quality financial institution bonds and corporate bonds as well. In response to rapid changes in the market, we adjusted our investment strategy from time to time to guard against potential risks while maximising returns.

Our **Mainland** business continued to develop steadily. There was improvement in our asset and loan structure. Deposits increased by 34.9% year-on-year, leading to a substantial improvement in the loan-to-deposit ratio. There was also an increase in net interest income. We enlarged our customer base and further expanded our branch network in the Mainland. In respect of service enhancement, we have been enriching our wealth management product range and upgrading our online platform to better serve corporate customers.

The Group's **Insurance** business performed impressively in the interim period. There was an increase of 101.4% in net operating income which amounted to HK$423 million. Profit before taxation nearly tripled to HK$291 million. Thanks to the substantial growth registered by regular-premium products, gross insurance premium income surged by 132.1%. By enriching our product offerings, particularly regular-premium products (including RMB products), and enhancing our service, we succeeded in growing our market share and reinforcing our market position.

The development of our **Offshore RMB Banking** business has been one of our strategic focuses. The progress we made in this area extended to all of our business segments. We are pleased to see that RMB banking has grown into an increasingly important growth driver and profit stream for the Group. We maintained our market lead by expanding the scope of RMB products and enhancing our service capability to cater for the diverse needs of local, cross-border and overseas customers. We continued to grow our RMB deposit base and lead the market in conducting the RMB trade settlement business. Aside from introducing the BOC CUP Dual Currency Commercial Card, the first of its kind in the market, we initiated a new series of RMB insurance products, which have been very well received so far. We took the lead in offering RMB cashier service order, RMB bill payment service via cheque deposit machine as well as cross-border bill payment service. For corporate clients, we launched a number of RMB payment and receivable products, including the RMB payroll, RMB autopay and RMB dividend payment for RMB-denominated securities. To enhance the return of RMB assets within the policy framework, we expanded the use of RMB funds in our lending and investment businesses. In the interim period, we launched the first "BOCHK RMB Bond Fund" for high net-worth customers.

## Outlook

The second half of the year started with tremendous market volatility, particularly after the downgrade of the US government's credit rating and the intensification of the debt crisis in the Euro zone. We expect the operating environment in the remaining months to be more challenging. While it is too early to assess the full impact of the recent developments, it is likely that the pace of economic recovery for the world as a whole would slow down. Interest rates will stay at the current low level for an extended period of time but inflation will linger. The greater volatility in global financial markets would presumably have a negative impact on investors' confidence.

Despite the above challenges, we believe there would still be opportunities for growth in Hong Kong, particularly in the RMB-related business and cross-border financial services. We will therefore continue to adopt a proactive management strategy for sustainable growth. By leveraging our core competencies and unique market positions, we will seek to drive quality growth in revenue and profit, and to maintain our solid financial position to support our growth and fend off any headwinds.

As we keep constant vigilance to changes in the market, we will strive to grow our core businesses by broadening our product and service offerings, upgrading our service capability, and improving our service quality. We will strengthen customer relationships, expand both our local and cross-border customer bases, and foster closer collaboration with BOC as well as its overseas branches. We will stay focused on core segments and formulate strategies for each of them in accordance with the changes in market situation.

More specifically, we will forge ahead with the development of the offshore RMB banking business by broadening and deepening the scope of our service. We will continue to take the lead in driving the growth of RMB-related business in Hong Kong through product innovation and service enhancement. We will also further expand the range of our cross-border banking services, with a view to providing total solutions to both individual and corporate customers. It is essential for us to step up our cooperation with BOC in this regard. We will also enlarge our presence in the Mainland by expanding the branch network of NCB (China).

While driving for growth, we will exercise a high degree of prudence in cost management. At the same time, we will continue to invest in strategic growth initiatives across the business by upgrading our service infrastructure and human resources, both indispensable for the Group's long-term development. Given the heightened market uncertainty and weaker-than-expected economic growth, it is important for us to safeguard our strong financial position and good asset quality. We will monitor our investment portfolio very closely and make adjustment as and when the situation evolves.

To conclude, I am pleased that we have been making good progress in implementing our business strategy. With the continued support of the Board of Directors, shareholders, customers and all my colleagues, we should be in a good position to withstand the challenges we face and take advantage of any opportunities the market presents in the time ahead.

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

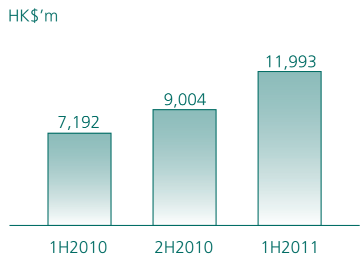
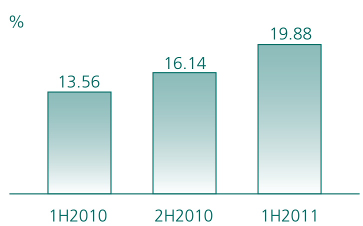
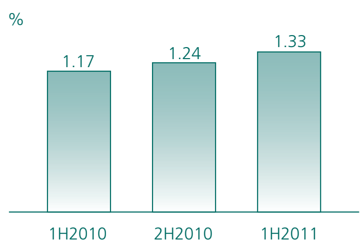
24 August 2011

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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

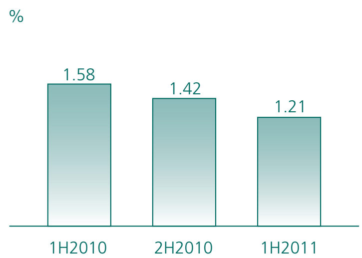
## FINANCIAL PERFORMANCE AND CONDITION IN BRIEF

The following table is a summary of the Group's key financial results for the first half of 2011 with a comparison with the previous two half-yearly periods.

<table>
<tr><th colspan="2">Financial Indicators</th><th>2011 First Half Performance</th></tr>
<tr><td>1. Profit Attributable to Shareholders</td><td>
</td><td>Profit attributable to shareholders<br>• The Group's profit continued to grow. Profit attributable to shareholders was HK$11,993 million, up HK$4,801 million, or 66.8%, year-on-year.<br>• The Group recorded a net recovery from the underlying collateral of the Lehman Brothers Minibonds amounting to HK$2,854 million*.<br>• Should the impact of the above-mentioned net recovery together with the expenses of Lehman Brothers-related products (hereafter called "impact of Lehman Brothers-related products") be excluded, profit attributable to shareholders would have been HK$9,679 million, up HK$2,423 million or 33.4% year-on-year, a record high since listing.<br>* Refer to Note 2 and Note 11 to the Interim Financial Information.</td></tr>
<tr><td>2. Return on Average Shareholders' Equity ("ROE")[1]</td><td>
</td><td>ROE<br>• ROE was 19.88%, increasing by 6.32 percentage points year-on-year.<br>• Excluding the impact of the Lehman Brothers-related products, ROE would have been 15.75%, up 2.49 percentage points year-on-year.</td></tr>
<tr><td>3. Return on Average Total Assets ("ROA")[2]</td><td>
</td><td>ROA<br>• ROA was 1.33%, up 0.16 percentage point year-on-year.<br>• Excluding the impact of the Lehman Brothers-related products, ROA would have been 1.07%, down 0.11 percentage point year-on-year. The decrease was due to the expansion of the Group's average asset base with the growth of advances to customers and RMB interbank balances and placements.</td></tr>
</table>

| Financial Indicators | 2011 First Half Performance |
|---|---|

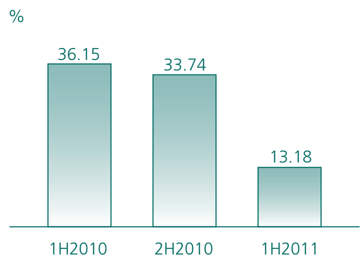
**4. Net Interest Margin (“NIM”)**




**NIM**

- NIM was 1.21%, down 37 basis points year-on-year due to the increase in market rate-based loans under the low interest rate environment, intense competition for deposits and the diluting effect of RMB business in Hong Kong.
- Excluding the estimated impact of RMB clearing services performed by BOCHK, NIM would have been 1.48%, down 16 basis points year-on-year.

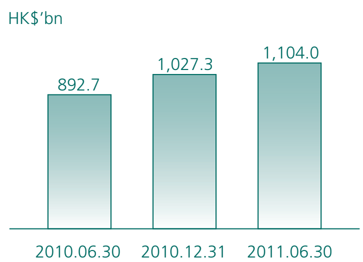
**5. Cost-to-Income Ratio (“CIR”)**




**CIR**

- CIR was 13.18%, down 22.97 percentage points year-on-year, mainly due to the net recovery from the underlying collateral of the Lehman Brothers Minibonds.
- Should the impact of the Lehman Brothers-related products be excluded, CIR would have been 31.92%, down 3.62 percentage points year-on-year.

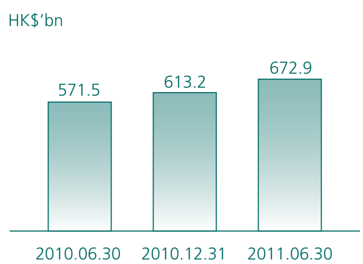
**6. Deposits from Customers (including structured deposits)**




**Deposits from Customers**

- Total deposits increased by 7.5% from the end of 2010, with the strong performance of RMB and USD deposits.

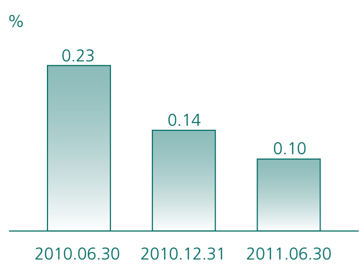
**7. Advances to Customers**




**Advances to Customers**

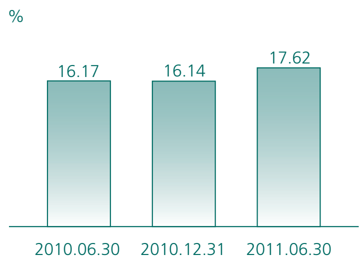
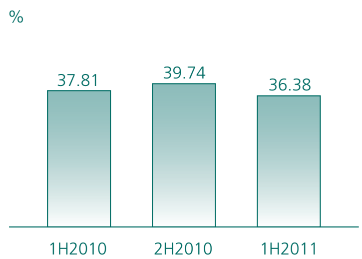
- Advances to customers grew healthily by 9.7% from the end of 2010. The Group also improved the pricing of loans.

**8. Classified or Impaired Loan Ratio[3]**




**Classified or Impaired Loan Ratio**

- Classified or impaired loan ratio was 0.10%, down 0.04 percentage point from the end of 2010.
- Formation of new classified loans remained at a low level, representing approximately 0.03% of total loans.

<table>
<tr><th>Financial Indicators</th><th></th><th>2011 First Half Performance</th></tr>
<tr><td>9. Capital Adequacy Ratio ("CAR")[4]</td><td></td><td>CAR<br>• CAR was maintained at a high level of 17.62%.<br>• Core capital ratio was 12.87%.</td></tr>
<tr><td>10. Average Liquidity Ratio</td><td></td><td>Average Liquidity Ratio<br>• Average liquidity ratio was at a healthy level of 36.38%.</td></tr>
</table>

1 Return on Average Shareholders' Equity of the Company as defined in "Financial Highlights".

2 Return on Average Total Assets as defined in "Financial Highlights".

3 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.

4 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. The Group adopted the foundation internal ratings-based ("FIRB") approach to calculate credit risk and BOCHK adopted the internal models approach to calculate general market risk for interest rate and exchange rate exposures as at 30 June 2011, as opposed to the standardised (credit risk) ("STC") approach and standardised market risk ("STM") approach that were used as at 31 December 2010. As a result of the change in the basis used, the capital ratios shown above are not directly comparable.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## ECONOMIC BACKGROUND AND OPERATING ENVIRONMENT

The Hong Kong economy continued to recover despite uncertainties such as the European debt crisis and the negative impact of the earthquake tragedy in Japan. Supported by strong private consumption and merchandise exports, Hong Kong's annualised GDP grew by 6.3% in the first half of the year. The labour market continued to improve, with the unemployment rate falling to 3.5% in the second quarter of the year. Inflationary pressures increased, driving up the overall consumer prices by 5.6% in June 2011 compared to a year ago. Market interest rates remained low, with the average 1-month HIBOR staying at around 0.18% in the first half of 2011.

The property market remained buoyant. The average price of private domestic properties showed an increase of 14.0% in the first half of 2011, following a 21.0% increase in 2010. Measures were taken by the government and regulatory body to ensure a more stable property market and mortgage environment. These included the Government's plan to increase land supply and the Hong Kong Monetary Authority's new guidelines to lower the loan-to-value ratio for mortgage loans. Meanwhile, in view of higher funding costs, banks raised the HIBOR-based mortgage rates several times in the first half of the year.

The Hong Kong stock market was adversely affected by the European debt crisis, concern over a slowdown in the global economy and the Mainland's credit tightening policy. As a result, investment sentiments turned weak in the first half.

The growth momentum of loans remained strong in the market due to the rise in demand, which was partly caused by the tightening of credit in the Mainland. Meanwhile, competition for deposits intensified and led to a rise in funding costs.

The offshore RMB market in Hong Kong expanded in an incremental and orderly manner. The demands for RMB trade settlement grew rapidly while RMB deposits in Hong Kong saw solid growth. Permission was granted to offshore monetary authorities and eligible banks to access the Mainland's RMB bond market. With regard to the RMB clearing bank business in Hong Kong, a major development was that the RMB Fiduciary Account Service was introduced to help Participating Banks to better manage their credit exposure to the Clearing Bank.

In summary, the operating environment for the banking industry remained challenging in the first half of 2011. Banks were faced with the narrowing of net interest margins. Inflationary pressure also put pressure on banks' profitability. Nevertheless, the surging demand for loans and the rapid expansion of RMB market presented significant business opportunities for the banking sector.

Looking ahead to the remainder of the year, the Hong Kong economy is still subject to uncertainties in view of the unresolved European debt crisis and sluggish economic recovery in the United States. Lately, the global financial markets reeled amid concern over worsening global economic outlook triggered by the downgrade of the US sovereign credit rating. The potential impact of these factors on the financial markets and the banking sector cannot be ignored.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## CONSOLIDATED FINANCIAL REVIEW

### *Financial Highlights*

| HK$'m, except percentage amounts | **Half-year ended 30 June 2011** | Half-year ended 31 December 2010 | Half-year ended 30 June 2010 |
|---|---|---|---|
| Net interest income | **10,205** | 9,770 | 8,964 |
| Other operating income | **4,921** | 5,197 | 3,577 |
| Net operating income before impairment allowances | **15,126** | 14,967 | 12,541 |
| Operating expenses | **(1,993)** | (5,050) | (4,534) |
| Operating profit before impairment allowances | **13,133** | 9,917 | 8,007 |
| Net (charge)/reversal of impairment allowances | **(30)** | 154 | 161 |
| Others | **1,484** | 904 | 599 |
| Profit before taxation | **14,587** | 10,975 | 8,767 |
| Profit attributable to equity holders of the Company | **11,993** | 9,004 | 7,192 |
| Earnings per share (HK$) | **1.1343** | 0.8517 | 0.6802 |
| Return on average total assets | **1.33%** | 1.24% | 1.17% |
| Return on average shareholders' equity | **19.88%** | 16.14% | 13.56% |
| Net interest margin | **1.21%** | 1.42% | 1.58% |
| Non-interest income ratio | **32.53%** | 34.72% | 28.52% |
| Cost-to-income ratio | **13.18%** | 33.74% | 36.15% |

In the first half of 2011, the Group continued to strive for balanced growth that supports long-term development. By tapping into opportunities arising from the economic recovery and the fast-expanding offshore RMB market, the Group achieved encouraging results. At the same time, it stayed alert to various risks in its operating environment and continued to exercise prudent risk management.

Compared to the first half of 2010, the Group's net operating income before impairment allowances increased by HK$2,585 million or 20.6% to HK$15,126 million. The increase was mainly attributable to higher net interest income, net fee and commission income as well as net trading gain. Operating expenses decreased sharply primarily due to the net recovery from the underlying collateral of the Lehman Brothers Minibonds. The Group recorded a modest amount of net charge of impairment allowances. The net gain on property revaluation also rose year-on-year. The Group's profit attributable to equity holders increased by HK$4,801 million, or 66.8%, to HK$11,993 million. Earnings per share were HK$1.1343, up HK$0.4541 from the same period last year. ROA and ROE stood at 1.33% and 19.88% respectively.

As compared to the second half of 2010, the Group's profit attributable to equity holders increased by HK$2,989 million, or 33.2% mainly due to the growth in net operating income, the net recovery from the underlying collateral of the Lehman Brothers Minibonds and the increase in net gain on property revaluation. Both net interest income and net fee and commission income rose, while net trading gain registered a decline due to mark-to-market changes of certain financial instruments.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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 | **Half-year ended 30 June 2011** | Half-year ended 31 December 2010 | Half-year ended 30 June 2010 |
|---|---|---|---|
| Interest income | **15,156** | 12,778 | 10,671 |
| Interest expense | **(4,951)** | (3,008) | (1,707) |
| Net interest income | **10,205** | 9,770 | 8,964 |
| Average interest-earning assets | **1,698,704** | 1,367,524 | 1,142,383 |
| Net interest spread | **1.14%** | 1.35% | 1.53% |
| Net interest margin | **1.21%** | 1.42% | 1.58% |
| Adjusted net interest margin* (adjusted for clearing bank function) | **1.48%** | 1.55% | 1.64% |

* The adjusted net interest margin excludes the estimated impact of RMB clearing services performed by BOCHK. Since December 2003, the Bank has been appointed as the clearing bank to provide RMB clearing services in Hong Kong.

Compared to the first half of 2010, the Group's net interest income increased by HK$1,241 million or 13.8% on the back of growth in average interest-earning assets. Net interest income continued to be compressed by the narrowing of net interest spread.

In the first half of 2011, average interest-earning assets increased by HK$556,321 million or 48.7% year-on-year, mainly supported by the increase in both customer deposits and RMB funds from the clearing bank business. Net interest margin was 1.21%, down 37 basis points compared to the first half of 2010. Should the estimated impact of BOCHK's RMB clearing function in Hong Kong be excluded, the adjusted net interest margin would have been 1.48%, down 16 basis points.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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

| ASSETS | **Half-year ended 30 June 2011** | | Half-year ended 31 December 2010 | | Half-year ended 30 June 2010 | |
|---|---|---|---|---|---|---|
| | **Average balance HK$'m** | **Average yield %** | Average balance HK$'m | Average yield % | Average balance HK$'m | Average yield % |
| Balances and placements with banks and other financial institutions | **628,593** | **1.21** | 341,069 | 1.15 | 211,521 | 0.95 |
| Debt securities investments | **423,344** | **2.36** | 418,023 | 2.20 | 369,306 | 2.28 |
| Loans and advances to customers | **630,343** | **2.02** | 593,731 | 2.02 | 547,281 | 2.00 |
| Other interest-earning assets | **16,424** | **1.74** | 14,701 | 1.48 | 14,275 | 1.26 |
| Total interest-earning assets | **1,698,704** | **1.80** | 1,367,524 | 1.85 | 1,142,383 | 1.88 |
| Non interest-earning assets | **160,827** | **–** | 136,300 | – | 116,018 | – |
| Total assets | **1,859,531** | **1.64** | 1,503,824 | 1.69 | 1,258,401 | 1.71 |

| LIABILITIES | **Half-year ended 30 June 2011** | | Half-year ended 31 December 2010 | | Half-year ended 30 June 2010 | |
|---|---|---|---|---|---|---|
| | **Average balance HK$'m** | **Average rate %** | Average balance HK$'m | Average rate % | Average balance HK$'m | Average rate % |
| Deposits and balances from banks and other financial institutions | **441,309** | **0.89** | 179,419 | 0.87 | 105,914 | 0.58 |
| Current, savings and fixed deposits | **1,000,360** | **0.53** | 910,007 | 0.41 | 807,886 | 0.27 |
| Subordinated liabilities | **27,094** | **2.11** | 27,840 | 1.68 | 26,373 | 2.10 |
| Other interest-bearing liabilities | **41,910** | **0.40** | 68,091 | 0.35 | 39,572 | 0.31 |
| Total interest-bearing liabilities | **1,510,673** | **0.66** | 1,185,357 | 0.50 | 979,745 | 0.35 |
| Non interest-bearing deposits | **67,777** | **–** | 76,078 | – | 57,847 | – |
| Shareholders' funds# and non interest-bearing liabilities | **281,081** | **–** | 242,389 | – | 220,809 | – |
| Total liabilities | **1,859,531** | **0.54** | 1,503,824 | 0.40 | 1,258,401 | 0.27 |

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

Average yield of interest-earning assets fell by 8 basis points while the average rate of interest-bearing liabilities increased by 31 basis points. As a result, the net interest spread decreased year-on-year by 39 basis points. Contribution from net free fund increased by 2 basis points.

The increased proportion of loans and advances with pricing based on interbank market rates (hereafter called "market rate-based loans") put pressure on asset yield. Meanwhile, the local RMB deposits (including those arising from the clearing bank business and the Group's customers) grew significantly. However, the spread remained low as the use of offshore RMB fund was still limited. Deposit costs also rose amid keen market competition.

The adverse impact from the above-mentioned factors was moderated by the Group's growth in higher-yielding assets such as loans and advances to customers. The Group also focused on enhancing the pricing of its corporate lending and improved the pricing of new corporate loans during the period. In the second quarter of 2011, the Group raised the pricing of HIBOR-based residential mortgage loans several times.

Compared to the second half of 2010, net interest income increased by HK$435 million or 4.5% primarily due to the growth in average interest-earning assets. Net interest margin was 1.21%, down 21 basis points. Should the estimated impact of BOCHK's RMB clearing function in Hong Kong be excluded, the adjusted net interest margin would have been 1.48%, down 7 basis points.

Persistently low market interest rates, increased deposit costs, higher proportion of market rate-based loans coupled with the growth in local RMB assets put pressure on the Group's net interest margin. These negative factors were partly counterbalanced by the growth in higher-yielding assets such as loans and advances to customers and debt securities investments.

### *Net Fee and Commission Income*

| HK$'m | **Half-year ended 30 June 2011** | Half-year ended 31 December 2010 | Half-year ended 30 June 2010 |
|---|---|---|---|
| Securities brokerage | **1,485** | 1,829 | 1,509 |
| Credit cards | **1,189** | 1,100 | 903 |
| Insurance | **610** | 341 | 220 |
| Loan commissions | **588** | 338 | 623 |
| Bills commissions | **418** | 380 | 371 |
| Payment services | **303** | 296 | 272 |
| Currency exchange | **224** | 207 | 125 |
| Funds distribution | **176** | 93 | 67 |
| Trust services | **123** | 108 | 98 |
| Safe deposit box | **107** | 97 | 103 |
| Others | **209** | 209 | 190 |
| Fee and commission income | **5,432** | 4,998 | 4,481 |
| Fee and commission expenses | **(1,446)** | (1,351) | (1,084) |
| Net fee and commission income | **3,986** | 3,647 | 3,397 |

Net fee and commission income rose by HK$589 million or 17.3% year-on-year to HK$3,986 million, primarily due to the increase of HK$390 million or 177.3% in commission income from the insurance business and HK$109 million or 162.7% from fund distribution. The commission income from insurance, comprising life insurance, general insurance and reinsurance, grew with the rise in business volume. To boost the sale of funds, the Group stepped up its marketing efforts and enhanced its customer services through an investment product specialist team. Fee income from credit cards grew as the cardholder spending and merchant acquiring volume increased by 26.2% and 38.4% respectively. Fee and commission income from currency exchange, bills, trusts and payment services also recorded satisfactory growth. Fee and commission expenses rose by HK$362 million or 33.4%, mainly due to the increases in credit cards and insurance commission expenses.

Compared to the second half of 2010, net fee and commission income increased by HK$339 million or 9.3%. The growth was mainly driven by the HK$250 million or 74.0% increase in loan commissions and HK$269 million or 78.9% rise in insurance commission income. At the same time, fee income from credit card business rose by HK$89 million or 8.1% while commission from fund distribution grew by HK$83 million or 89.2%. Fee income from other traditional businesses such as bills, currency exchange and trust services also grew. Fee income from securities brokerage declined by HK$344 million or 18.8% as investment sentiments turned weaker in the first half of 2011.

### *Net Trading Gain/(Loss)*

| HK$'m | **Half-year ended 30 June 2011** | Half-year ended 31 December 2010 | Half-year ended 30 June 2010 |
|---|---|---|---|
| Foreign exchange and foreign exchange products | **662** | 649 | 350 |
| Interest rate instruments and items under fair value hedge | **(4)** | 686 | (424) |
| Equity instruments | **32** | 12 | (20) |
| Commodities | **71** | 58 | 58 |
| Net trading gain/(loss) | **761** | 1,405 | (36) |

Net trading gain was HK$761 million, increasing by HK$797 million from the first half of 2010. The growth was mainly driven by the increase in net trading gain from foreign exchange and related products as well as the decrease in net trading loss of interest rate instruments and items under fair value hedge. Net trading gain from foreign exchange and related products rose by HK$312 million or 89.1%, which was mainly attributable to the fast-growing currency exchange activities. The decrease in net trading loss from interest rate instruments and items under fair value hedge was primarily due to the change in mark-to-market values of certain interest rate swap contracts.

Compared to the second half of 2010, net trading gain declined by HK$644 million or 45.8%. The decrease was mainly due to the decline in mark-to-market gain on certain interest rate instruments.

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

| HK$'m | **Half-year ended 30 June 2011** | Half-year ended 31 December 2010 | Half-year ended 30 June 2010 |
|---|---|---|---|
| Banking business of the Group | **18** | (5) | 49 |
| BOC Life | **380** | 107 | 591 |
| Net gain on financial instruments designated at fair value through profit or loss | **398** | 102 | 640 |

The Group recorded a net gain of HK$398 million on financial instruments designated at fair value through profit or loss in the first half of 2011, falling by HK$242 million or 37.8% from the same period last year. The decrease was mainly due to the decline in mark-to-market gain on certain debt securities of BOC Life caused by the movement of market interest rates. These mark-to-market changes were substantially offset by the corresponding changes in policy reserves, as reflected in the changes in net insurance benefits and claims which were attributable to the movement of market interest rates.

Compared to the second half of 2010, net gain on financial instruments designated at fair value through profit or loss increased by HK$296 million. The growth was mainly attributable to the mark-to-market gain of certain debt securities investments of BOC Life.

### *Operating Expenses*

| HK$'m, except percentage amounts | **Half-year ended 30 June 2011** | Half-year ended 31 December 2010 | Half-year ended 30 June 2010 |
|---|---|---|---|
| Staff costs | **2,740** | 2,831 | 2,526 |
| Premises and equipment expenses (excluding depreciation) | **610** | 627 | 574 |
| Depreciation on owned fixed assets | **614** | 575 | 556 |
| Other operating expenses | **864** | 1,005 | 801 |
| Core operating expenses | **4,828** | 5,038 | 4,457 |
| Impact of Lehman Brothers-related products* | **(2,835)** | 12 | 77 |
| Total operating expenses | **1,993** | 5,050 | 4,534 |
| Cost-to-income ratio | **13.18%** | 33.74% | 36.15% |
| Core cost-to-income ratio | **31.92%** | 33.66% | 35.54% |

* For details, see Note 2 and Note 11 to the Interim Financial Information.

The Group's total operating expenses dropped by HK$2,541 million, or 56.0%, to HK$1,993 million. The decrease was mainly due to the net recovery of HK$2,854 million from the underlying collateral of the Lehman Brothers Minibonds. The Group's core operating expenses increased by HK$371 million or 8.3%. In the first half of 2011, the Group focused on enhancing operational efficiency and investing for business development.

Staff costs increased by HK$214 million or 8.5%, mainly due to the increase in headcount, in particular front-line staff, and higher salaries and performance-related remuneration. Compared to 30 June 2010, headcount measured in full-time equivalents rose by 675 to 14,104 as at 30 June 2011.

Premises and equipment expenses increased by HK$36 million or 6.3%, as a result of higher rental for branches in Hong Kong and the Mainland. Depreciation on owned fixed assets rose by HK$58 million or 10.4%, which was attributable to larger depreciation charge on premises following the upward revaluation.

Other operating expenses rose by HK$63 million or 7.9% mainly due to higher marketing and promotion expenses as well as expenses connected with the growth in business volume.

Compared to the second half of 2010, operating expenses declined by HK$3,057 million or 60.5%. This was largely due to the impact of the Lehman Brothers-related products as well as lower staff costs and promotional expenses in the first half of 2011.

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

| HK$'m | **Half-year ended 30 June 2011** | Half-year ended 31 December 2010 | Half-year ended 30 June 2010 |
|---|---|---|---|
| Net reversal/(charge) of allowances before recoveries | | | |
| – individual assessment | **42** | 93 | 56 |
| – collective assessment | **(295)** | (272) | (256) |
| Recoveries | **216** | 155 | 294 |
| Net (charge)/reversal of loan impairment allowances | **(37)** | (24) | 94 |

The Group registered a modest amount of net charge of loan impairment allowances of HK$37 million in the first half of 2011.

As the economic environment continued to improve, the Group recorded a net reversal of individual impairment allowances before recoveries in the current period amounting to HK$42 million. Meanwhile, net charge of collective impairment allowances before recoveries increased by HK$39 million or 15.2% year-on-year to HK$295 million mainly due to loan growth and the periodic review of the parameter values in the assessment model.

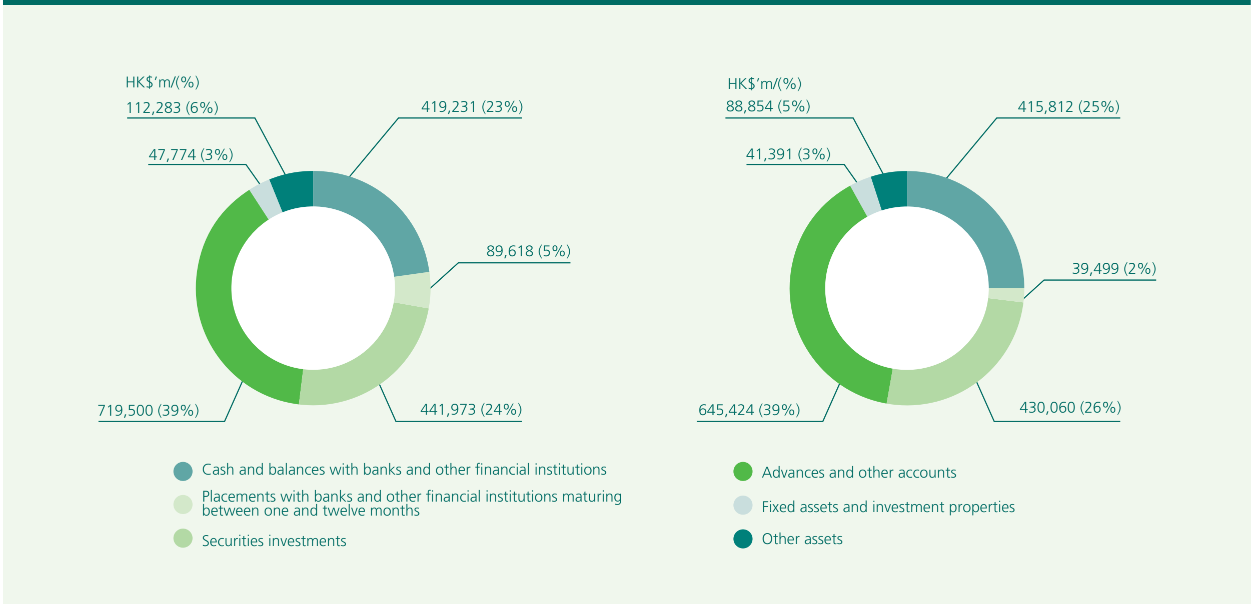
Compared to the second half of 2010, net charge of loan impairment allowances increased by HK$13 million or 54.2%. Net charge of collective impairment allowances before recoveries increased mainly due to loan growth in the first half of 2011.

### *Financial Position*

| HK$'m, except percentage amounts | **At 30 June 2011** | At 31 December 2010 |
|---|---|---|
| Cash and balances with banks and other financial institutions | **419,231** | 415,812 |
| Placements with banks and other financial institutions maturing between one and twelve months | **89,618** | 39,499 |
| Hong Kong SAR Government certificates of indebtedness | **54,460** | 46,990 |
| Securities investments[1] | **441,973** | 430,060 |
| Advances and other accounts | **719,500** | 645,424 |
| Fixed assets and investment properties | **47,774** | 41,391 |
| Other assets[2] | **57,823** | 41,864 |
| Total assets | **1,830,379** | 1,661,040 |
| Hong Kong SAR currency notes in circulation | **54,460** | 46,990 |
| Deposits and balances from banks and other financial institutions | **386,904** | 313,784 |
| Deposits from customers | **1,103,435** | 1,027,033 |
| Insurance contract liabilities | **43,045** | 39,807 |
| Other accounts and provisions[3] | **85,074** | 88,260 |
| Subordinated liabilities[4] | **27,838** | 26,877 |
| Total liabilities | **1,700,756** | 1,542,751 |
| Non-controlling interests | **3,460** | 3,108 |
| Capital and reserves attributable to the equity holders of the Company | **126,163** | 115,181 |
| Total liabilities and equity | **1,830,379** | 1,661,040 |
| Loan-to-deposit ratio[5] | **60.95%** | 59.69% |

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 Financial liabilities at fair value through profit or loss, derivative financial liabilities, debt securities in issue at amortised cost, current tax liabilities and deferred tax liabilities are included in other accounts and provisions.
4 Subordinated liabilities comprise USD subordinated notes issued in 2010 and EUR subordinated loans granted by BOC in 2008.
5 The deposit base also includes structured deposits reported as "Financial liabilities at fair value through profit or loss".

Balance Sheet Mix as at 30 June 2011 | Balance Sheet Mix as at 31 December 2010




As at 30 June 2011, the Group's total assets amounted to HK$1,830,379 million, up HK$169,339 million or 10.2% from the end of 2010. The overall asset growth was primarily driven by the expansion of the Group's core banking businesses and RMB business in Hong Kong. Key changes include:

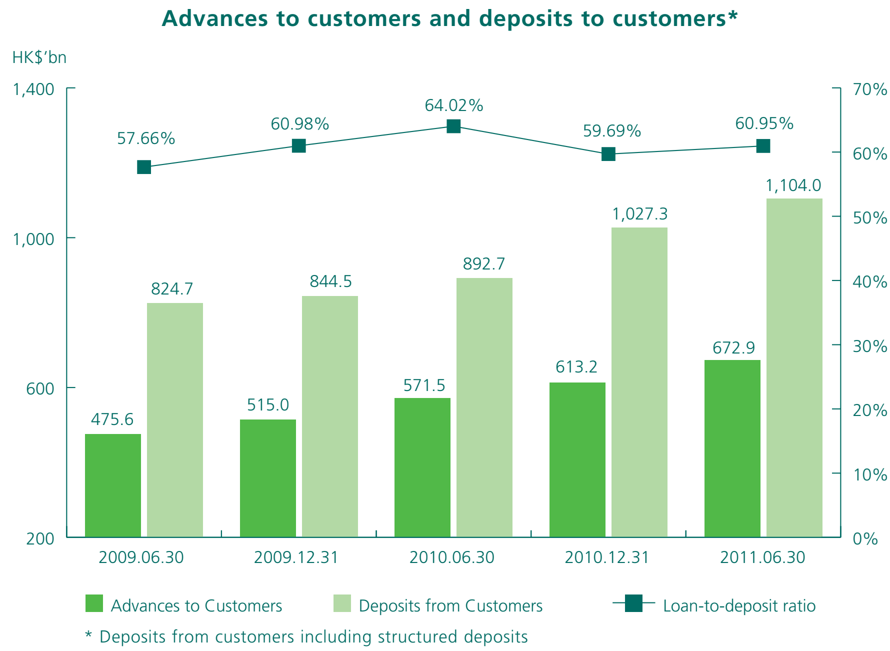
- Placements with banks and other financial institutions maturing between one and twelve months increased by HK$50,119 million, or 126.9%, mainly due to the growth in RMB placements with banks and other financial institutions.

- Securities investments increased by HK$11,913 million or 2.8%, mainly due to the increase in investments in government-related securities as well as high-quality financial institutions and corporate debts.

- Advances and other accounts rose by HK$74,076 million or 11.5%, which was mainly attributable to the growth in advances to customers by HK$59,639 million or 9.7%.

- Other assets grew by HK$15,959 million or 38.1%, which was mainly led by the increase in derivative financial instruments and accounts receivable.

- Deposits and balances from banks and other financial institutions increased by HK$73,120 million or 23.3%, led by the growth in interbank borrowing as well as RMB deposits from banks.




### *Advances to Customers*

| HK$'m, except percentage amounts | At 30 June 2011 | % | At 31 December 2010 | % |
|---|---|---|---|---|
| Loans for use in Hong Kong | **434,636** | **64.6** | 387,087 | 63.1 |
| Industrial, commercial and financial | **231,812** | **34.5** | 206,947 | 33.7 |
| Individuals | **202,824** | **30.1** | 180,140 | 29.4 |
| Trade finance | **59,840** | **8.9** | 53,396 | 8.7 |
| Loans for use outside Hong Kong | **178,382** | **26.5** | 172,736 | 28.2 |
| Total advances to customers | **672,858** | **100.0** | 613,219 | 100.0 |

The Group had adhered to a balanced growth strategy with regard to its loan book. It also strived to optimise the loan portfolio structure and improve its pricing. As a result, the Group recorded a healthy loan growth of HK$59,639 million or 9.7% to HK$672,858 million in the first half of 2011.

Loans for use in Hong Kong grew by HK$47,549 million or 12.3%.

- Lending to the industrial, commercial and financial sectors increased by HK$24,865 million, or 12.0%, to HK$231,812 million, covering a wide range of industries. Notable growth was recorded in the lending to wholesale and retail trade, property investment as well as transport and transport equipment.

- Residential mortgage loans (excluding those under the Government-sponsored Home Ownership Scheme) were up by HK$20,660 million, or 14.0%, to HK$168,084 million, as a result of the Group's effective marketing efforts in an active property market particularly in the first quarter of the year. The proportion of total new drawdown in HIBOR-based residential mortgage loans increased as customers were more inclined to take advantage of low interbank rates.

Trade finance rose by HK$6,444 million or 12.1%. Meanwhile, loans for use outside Hong Kong grew by HK$5,646 million or 3.3%.

### *Deposits from Customers**

| HK$'m, except percentage amounts | At 30 June 2011 | % | At 31 December 2010 | % |
|---|---|---|---|---|
| Demand deposits and current accounts | **70,619** | **6.4** | 70,453 | 6.9 |
| Savings deposits | **522,972** | **47.4** | 528,035 | 51.4 |
| Time, call and notice deposits | **509,844** | **46.2** | 428,545 | 41.7 |
| | **1,103,435** | **100.0** | 1,027,033 | 100.0 |
| Structured deposits designated at fair value through profit or loss | **569** | **0.0** | 234 | 0.0 |
| Deposits from customers | **1,104,004** | **100.0** | 1,027,267 | 100.0 |

* including structured deposits

In the first half of 2011, the Group's deposits from customers increased by HK$76,737 million, or 7.5%, to HK$1,104,004 million. Customers were inclined to shift their funds towards fixed deposits for higher interest rates amid the competition among banks in Hong Kong. Time, call and notice deposits rose by HK$81,299 million or 19.0% to HK$509,844 million. Savings deposits recorded a drop of HK$5,063 million or 1.0%. The Group's loan-to-deposit ratio was up 1.26 percentage points to 60.95% at the end of June 2011.

### *Loan Quality*

| HK$'m, except percentage amounts | At 30 June 2011 | At 31 December 2010 |
|---|---|---|
| Advances to customers | **672,858** | 613,219 |
| Classified or impaired loan ratio[1] | **0.10%** | 0.14% |
| | | |
| Impairment allowances | **2,470** | 2,311 |
| Regulatory reserve for general banking risks | **6,595** | 5,076 |
| Total allowances and regulatory reserve | **9,065** | 7,387 |
| | | |
| Total allowances as a percentage of advances to customers | **0.37%** | 0.38% |
| Impairment allowances[2] on classified or impaired loan ratio | **38.53%** | 40.02% |
| | | |
| Residential mortgage loans[3] – delinquency and rescheduled loan ratio[4] | **0.01%** | 0.02% |
| Card advances – delinquency ratio[4,5] | **0.15%** | 0.15% |

| | Half-year ended 30 June 2011 | Half-year ended 30 June 2010 |
|---|---|---|
| Card advances – charge-off ratio[5,6] | **1.07%** | 1.56% |

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.
2 Referring to 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.
6 Charge-off ratio is measured by a ratio of total write-offs made during the period to average card receivables during the period.

The Group's loan quality remained sound, with the classified or impaired loan ratio falling by 0.04 percentage point to 0.10%. Classified or impaired loans decreased by HK$161 million, or 18.6%, to HK$706 million mainly due to collections and fewer new classified loans. New classified loans in the first half of 2011 represented approximately 0.03% of total loans outstanding.

Total impairment allowances, including both individual assessment and collective assessment, amounted to HK$2,470 million. Total impairment allowances in respect of the classified or impaired loans as a percentage of total classified or impaired loans accounted for 38.53%.

The quality of the Group's residential mortgage loans remained sound with the combined delinquency and rescheduled loan ratio standing at a low level of 0.01% at the end of June 2011. As compared to the first half of 2010, the charge-off ratio of card advances dropped by 0.49 percentage points to 1.07%, mainly due to the cardholders' improved debt servicing capability as economic conditions improved.

### *Capital and Liquidity Ratios*

| HK$'m, except percentage amounts | **At 30 June 2011** | At 31 December 2010 |
|---|---|---|
| Core capital | **83,563** | 78,275 |
| Deductions | **(791)** | (332) |
| Core capital after deductions | **82,772** | 77,943 |
| Supplementary capital | **31,347** | 33,876 |
| Deductions | **(791)** | (332) |
| Supplementary capital after deductions | **30,556** | 33,544 |
| Total capital base after deductions | **113,328** | 111,487 |
| Risk-weighted assets | | |
| Credit risk | **561,273** | 648,236 |
| Market risk | **21,722** | 18,328 |
| Operational risk | **48,789** | 47,895 |
| Capital floor adjustment | **41,768** | – |
| Deductions | **(30,230)** | (23,862) |
| Total risk-weighted assets | **643,322** | 690,597 |
| Capital adequacy ratios (consolidated basis) | | |
| Core capital ratio | **12.87%** | 11.29% |
| Capital adequacy ratio | **17.62%** | 16.14% |

| | **Half-year ended 30 June 2011** | Half-year ended 30 June 2010 |
|---|---|---|
| Average liquidity ratio | **36.38%** | 37.81% |

The Group adopted the foundation internal ratings-based ("FIRB") approach to calculate credit risk and standardised (credit risk) ("STC") approach for certain credit exposures being exempted from FIRB effective from 1 January 2011. The market risk of the Group mainly sourced from BOCHK. BOCHK adopted the internal models approach ("IMM") to calculate general market risk for interest rate and exchange rate exposures effective from 1 April 2011 while the Group continued to adopt the standardised (market risk) ("STM") approach to calculate the remaining market risk. In addition, the Group continued to adopt the standardised (operational risk) ("STO") approach for operational risk. The Group's capital adequacy ratio was calculated based on the various risk measurement approaches above.

The Group adopted the STC approach and STM approach to calculate credit risk and market risk respectively as at 31 December 2010. As a result of the change in the basis used, the amounts shown above are not directly comparable.

Consolidated capital adequacy ratio of the banking group at 30 June 2011 was 17.62%. The Group's total capital base expanded by 1.7% to HK$113,328 million mainly due to the increase in retained earnings.

The average liquidity ratio in the first half of 2011 remained strong at 36.38%.

## BUSINESS REVIEW

### PERSONAL BANKING

| HK$'m | **Half-year ended 30 June 2011** | Half-year ended 30 June 2010 |
|---|---|---|
| Net interest income | **2,843** | 2,932 |
| Other operating income | **2,720** | 2,384 |
| Operating income | **5,563** | 5,316 |
| Operating expenses | **(2,754)** | (3,044) |
| Operating profit before impairment allowances | **2,809** | 2,272 |
| Net charge of loan impairment allowances | **(77)** | (37) |
| Others | **(9)** | (5) |
| Profit before taxation | **2,723** | 2,230 |

| | **At 30 June 2011** | At 31 December 2010 |
|---|---|---|
| Segment assets | **237,746** | 210,978 |
| Segment liabilities | **656,172** | 657,605 |

Note: For additional segmental information, see Note 40 to the Interim Financial Information.

**Financial Results**

In the first half of 2011, the Group's Personal Banking business recorded a profit before taxation of HK$2,723 million, up HK$493 million or 22.1% year-on-year. Operating income rose by 4.6%, driven mainly by the increase in net fee and commission income. The increase was, however, partially offset by a drop in net interest income. Operating profit before impairment allowances was HK$2,809 million, up 23.6%.

Net interest income decreased by 3.0% mainly because of higher deposit costs despite a growth in average balance of loans and advances. Other operating income rose by 14.1% on account of the strong growth in fee income from insurance and fund distribution.

During the period, a more detailed and comprehensive cost allocation mechanism was adopted. No change has been made to the comparative figures. If the same cost allocation mechanism is applied for the same period last year, it is estimated that operating expenses in the first half of 2011 would have increased by HK$179 million year-on-year. The increase was mainly due to higher business-related expenses such as marketing and promotional expenses.

Net charge of loan impairment allowances was HK$77 million, mainly due to impairment allowances made on collective assessment. The increase was in line with the expansion of loan balances.

Advances and other accounts, including mortgage loans and card advances, increased by 12.3% to HK$220,649 million, while deposits from customers dropped by 0.3% to HK$626,172 million.

**Business operation**

The Group managed to achieve solid growth in major Personal Banking businesses in the first half of 2011. It registered satisfactory growth in its residential mortgage business with improved pricing of new HIBOR-based mortgage loans. It also continued to enhance its securities business platform with the newly established mobile banking channel. Meanwhile, the Group strived to provide more differentiated services to its wealth management customers. The credit card business grew steadily in terms of card issuance and merchant acquiring volume. To meet customers' demand for RMB banking products and services, the Group expanded its product spectrum substantially, thus reinforcing its premier position in Hong Kong's RMB banking business as a whole.

***Robust growth of residential mortgages***

The Group maintained its steady growth in the first half of 2011. It launched the "First-year HIBOR-based and Prime-based afterwards" mortgage plan to meet customers' needs. Meanwhile, the Group continued to strengthen its strategic partnership with major property developers and participated in joint promotions in most of the prime property development projects. The Group's outstanding residential mortgage loans grew by 14.0% from the end of 2010. In view of higher funding costs, the Group raised the pricing of new HIBOR-based mortgage loans. The credit quality of residential mortgages remained sound under the Group's rigorous risk assessment and control over the mortgage business.

***Further development of investment and insurance businesses***

The Group expanded its stock brokerage service spectrum and embarked on a number of promotion and marketing campaigns. With the support of the new mobile banking service, stock brokerage volume through this channel increased satisfactorily. As for the fund distribution business, more RMB funds were introduced. The phenomenal 237.1% growth in the Group's retail fund distribution volume was partly accounted for by the professional consultation service on retail funds jointly offered by the sales staff and the newly formed Investment Product Specialist Team.

Regarding its Bancassurance business, the Group maintained its competitive advantages by enhancing its sales model, launching effective marketing campaigns and implementing a multi-channel distribution strategy. The financial planning model continued to expand with encouraging results. There was robust growth in the sales of insurance products. Meanwhile, more RMB insurance products were introduced to meet the market's demand. The Group further improved its service quality. New initiatives such as the customer satisfaction survey were taken for the purpose of service enhancement.

***Decent growth in credit card business***

The Group's card business sustained its growth momentum. The total number of cards issued increased by 6.4% from the end of 2010, while cardholder spending and merchant acquiring volume rose by 26.2% and 38.4% respectively year-on-year. The Group maintained its leadership in the China UnionPay ("CUP") merchant acquiring business and CUP card issuing business, with merchant acquiring and cardholder spending volume surging by 56.1% and 85.6% respectively compared to the first half of 2010.

Riding on the success of "BOC CUP Dual Currency Credit Card", the Group introduced "BOC CUP Dual Currency Commercial Card", which is the first of its kind in Hong Kong to use both RMB and HKD as the settlement currencies for corporate customers. The Group's success in credit card business gained extensive market recognition, as evidenced by a total of 30 awards received from VISA International, MasterCard and China UnionPay respectively.

The credit quality of the Group's card advances remained sound with the annualised charge-off ratio for the six months period to 30 June 2011 standing at 1.07%.

***Maintaining sound relationship with high potential customers***

To further expand its high net-worth customer base, the Group strived to maintain long-term relationship with its wealth management customers by providing differentiated services and customising wealth management solutions through different service channels. It organised a range of marketing activities and provided various market information to wealth management customers. Under the "Customer Referral Programme" and "New Customer Relationship Building Programme", the Group broadened its customer base by cross-selling with bundled promotional offers. At the end of June 2011, the total number of wealth management customers and their assets maintained with the Group grew by 9.7% and 4.0% respectively from the end of 2010.

***Optimising distribution channels and enhancing e-platform services***

The Group continuously optimised its distribution channels to meet cross-border and local customer needs. At the end of June 2011, the Group's service network in Hong Kong comprised 266 branches, including 132 wealth management centres and 21 dedicated Mainland customer service centres. Furthermore, a new hotline was set up specifically for providing enquiry services to Mainland customers.

The Group further invested in the automated banking service network to facilitate customers in using banking services beyond normal banking hours. This included installing newly designed ATM's as well as cash and cheque deposit machines with enhanced functions. To strengthen its multi-currency deposit and withdrawal services, the Group upgraded the cheque deposit machines to accept RMB and USD cheques in addition to HKD ones. This is the first of its kind in Hong Kong. The Group also enhanced the functions of its e-Banking platform, including the extension of FX and Bullion Margin trading hours. Moreover, the internet functions were extended to the mobile banking platform with good response. The number of mobile banking users increased significantly from the end of 2010.

In recognition of its well accepted electronic platform and outstanding services, the Group was honoured with the "Best Internet Banking" and "Best Mobile Telephone Banking" awards of the Capital Weekly Service Awards 2011.

## CORPORATE BANKING

| HK$'m | **Half-year ended 30 June 2011** | Half-year ended 30 June 2010 |
|---|---|---|
| Net interest income | **4,163** | 2,995 |
| Other operating income | **1,622** | 1,464 |
| Operating income | **5,785** | 4,459 |
| Operating expenses* | **(1,371)** | (1,232) |
| Operating profit before impairment allowances | **4,414** | 3,227 |
| Net reversal of loan impairment allowances | **40** | 131 |
| Others | **(1)** | – |
| Profit before taxation | **4,453** | 3,358 |

| | **At 30 June 2011** | At 31 December 2010 |
|---|---|---|
| Segment assets | **508,613** | 458,928 |
| Segment liabilities | **487,944** | 407,328 |

Note: For additional segmental information, see Note 40 to the Interim Financial Information.

* During the period, a more detailed and comprehensive cost allocation mechanism was adopted. No change has been made to the comparative figures.

**Financial Results**

Corporate Banking achieved a strong growth of HK$1,095 million or 32.6% in profit before taxation, which stood at HK$4,453 million. Operating profit before impairment allowances increased by 36.8% to HK$4,414 million. The increase was mainly driven by the growth in net interest income.

Net interest income increased by 39.0%, which was mainly attributable to the increase in the average balance of loans and deposits, and improved loan pricing. Other operating income increased by 10.8%, led by the growth in fee income from payment services and currency exchange, as well as bills commission.

Operating expenses* would have increased by HK$135 million year-on-year, if the same cost allocation mechanism is applied for the same period last year. The increase was mainly due to higher business-related expenses and staff costs.

Net reversal of loan impairment allowances decreased as recoveries were lower.

Advances and other accounts increased by 10.9% to HK$506,317 million, while deposits from customers grew by 20.2% to HK$482,304 million.

* During the period, a more detailed and comprehensive cost allocation mechanism was adopted. No change has been made to the comparative figures.

**Business Operation**

The Group's Corporate Banking business continued with a balanced growth strategy in the first half of 2011. Corporate loans registered steady growth with improvement in loan pricing. Besides, the Group focused on providing a full range of financial services, including cross-border financial services, to its core corporate clients.

The Group's RMB corporate banking business marked solid development as a result of the introduction of a broader range of relevant products and services as well as aggressive marketing and promotion. The Group's service platform was further improved. Alert to clients' needs, the Group succeeded in reaching out to new clients and capturing cross-selling opportunities for higher revenue.

At the same time, the Group adhered to its vigilant risk management policy to ensure well-balanced and sustainable growth.

***Quality growth in corporate lending business***

The demand for corporate loans continued to rise in the first half of the year. The Group grasped the market opportunity to grow its credit portfolio in a well-balanced manner. It remained cautious in securing new loans and focused more attention on the pricing of loans. The effectiveness of this strategy is reflected in the healthy growth of 8.5% in corporate lending and the improved loan pricing and loan quality in the first six months. The Group also maintained close collaboration with BOC through the "Global Relationship Manager Programme" and "Global United Facilities Arrangement" to better serve its customers. In the first half of 2011, the Group remained the top mandated arranger in the Hong Kong-Macau syndicated loan market.

***SME business registered steady development***

The Group further grew its SME banking business by participating in the "SME Financing Guarantee Scheme" launched by the Hong Kong Mortgage Corporation Limited as well as by enhancing its service model, improving its product features and offering total solution services to SME customers. Through closer collaboration with BOC and NCB (China) and cooperation with major trade associations, the Group continued to explore new targeted customers. In May 2011, BOCHK received for the fourth consecutive year the "SME's Best Partner Award" presented by the Hong Kong Chamber of Small and Medium Business Limited.

***Steady growth in trade finance and trade settlement business***

The flourishing of global trade fuelled the growth of the Group's trade finance business. The Group also collaborated with BOC to offer cross-border trade finance, such as the RMB agency payment services, to corporate customers in both Hong Kong and the Mainland. In the first half of 2011, the Group's balance of trade finance grew by 12.1% versus the end of 2010. Cross-border trade settlement volume recorded a notable growth of 138% year-on-year.

***Custody services making good progress***

The custody business continued to expand in the first half of 2011. The Group stepped up its sales efforts and had successfully secured mandates to provide global custody services to various Qualified Domestic Institutional Investors and other institutions including major banks, fund houses as well as insurance and securities companies inside and outside Mainland. Custody of RMB investment instruments was on the increase, and the Group continued to provide escrow services to large corporate entities. It also strengthened its relationship with its corporate customers and actively sought business opportunities in custody services. At the end of June 2011, excluding the RMB fiduciary account, total assets under the Group's custody were valued at HK$481.7 billion, increasing by 4.7% over the end of 2010.

***Expanding service spectrum in cash management***

The Group made further progress in developing its cash management business. New services were introduced to drive growth and to enhance the Group's competitiveness. In conjunction with the implementation of the local interbank RMB autopay system by the Hong Kong Interbank Clearing Limited in March 2011, the Group rolled out a wide range of RMB payment and receivable products. The Group also launched the cross-border RMB bill payment service which allows merchants in Shenzhen to collect RMB bill payments from bank accounts in Hong Kong. At the same time, the Group strengthened the linkage of its cash management service platform with those of BOC and its overseas branches. With effective marketing, the number of Corporate Banking Services Online ("CBS Online") customers increased by 12.4% over the end of 2010.

***Proactive measures in risk management***

The Group remained persistently vigilant over risk management. Stringent credit control was in place to safeguard asset quality. The Group closely monitored those corporate customers who could be adversely affected by rising production costs in the Mainland, RMB appreciation, upsurge in commodity prices, and emerging risks in Japan and the European region.

## MAINLAND BUSINESS

***Steady growth of Mainland business***

The Group's Mainland business recorded satisfactory growth in the first half of 2011. During the period, the Group focused on strengthening its deposit base to support long-term development. Customer deposits grew by 34.9% while advances to customers registered a 1.2% drop, thus resulting in an improvement in its loan-to-deposit ratio. The Group also strived to enlarge its customer base by strengthening its customer service capability and enriching its range of RMB wealth management products for Mainland customers.

***Further development in distribution channels and branch network***

The expansion of the Group's network in the Mainland continued. NCB (China)'s Beijing Zhongguancun sub-branch commenced operation on 1 March 2011. The Group's total number of branches and sub-branches in the Mainland increased to 26 at the end of June 2011. Meanwhile, NCB (China) has been approved by the China Banking Regulatory Commission ("CBRC") to establish the Foshan sub-branch and the Qingdao Development Zone sub-branch. Furthermore, the Group upgraded the platform and functionality of its internet banking channel to enhance customer experience. The improved corporate internet banking was launched during the interim period, while the new personal internet banking would commence in the second half of 2011.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## TREASURY

| HK$'m | **Half-year ended 30 June 2011** | Half-year ended 30 June 2010 |
|---|---|---|
| Net interest income | **2,393** | 2,341 |
| Other operating income | **752** | 35 |
| Operating income | **3,145** | 2,376 |
| Operating expenses* | **(323)** | (330) |
| Operating profit before impairment allowances | **2,822** | 2,046 |
| Net reversal of impairment allowances on securities investments | **43** | 72 |
| Profit before taxation | **2,865** | 2,118 |

| | **At 30 June 2011** | At 31 December 2010 |
|---|---|---|
| Segment assets | **992,322** | 910,772 |
| Segment liabilities | **509,338** | 437,174 |

Note: For additional segmental information, see Note 40 to the Interim Financial Information.

### Financial Results

The Treasury segment's profit before taxation rose by 35.3% year-on-year to HK$2,865 million in the first half of 2011. Operating profit before impairment allowances increased by 37.9% to HK$2,822 million, driven by improvements in both net interest income and other operating income.

Net interest income rose by 2.2%, which was mainly attributable to the growth of RMB business with improved asset yield. The substantial rise in other operating income resulted mainly from higher net trading gain from foreign exchange and related products and mark-to-market change of certain interest rate instruments.

Operating expenses* would have decreased by HK$57 million, if the same cost allocation mechanism is applied for the same period last year.

* During the period, a more detailed and comprehensive cost allocation mechanism was adopted. No change has been made to the comparative figures.

### Business Operation

***Enhancing investment portfolio management***

In the face of various uncertainties in the financial market, the Group proactively managed its banking book. The Group took advantage of the steepening yield curve and continued to invest in fixed rate debt securities, in particular government-related securities as well as high-quality financial institution and corporate bonds. The Group disposed of lower-yielding securities to improve the asset-liability structure. Furthermore, in order to capture the opportunities arising from the expansion of the RMB investment market, the Group took initiative to develop the RMB bond business in the Mainland.

The Group remained vigilant in managing its portfolio. In respect of the exposure to the European countries affected by the debt crisis, namely Portugal, Ireland, Italy, Greece and Spain, the Group only had exposure to debt securities issued by financial institutions of Ireland and Italy amounting to a total of HK$1,002 million as at the end of June 2011 (versus HK$1,238 million at the end of 2010).

***Growing traditional and RMB-related businesses***

The Group continued to strengthen its traditional product offering by improving its customer service quality and optimising the Investment Product Specialist Team for the high net-worth customer group. In addition, the Group's strategy of focusing on RMB-related business continued to yield promising results. The Group recorded robust growth in foreign exchange income. With regard to the RMB clearing bank business in Hong Kong, a major development was that the RMB Fiduciary Account Service was introduced to help Participating Banks to better manage their credit exposure to the Clearing Bank. The Group also launched securities sale and repurchase facilities (RMB Repo Facilities) through the Central Moneymarkets Unit to facilitate intraday liquidity management of Participating Banks. Meanwhile, following the establishment of the asset management platform towards the end of last year, the Group launched the "BOCHK RMB Bond Fund" targeting high net-worth customers. The Group also cooperated with BOC's overseas branches to build up a global RMB banknote network while providing product support and price-quoting services to those branches.

## INSURANCE

| HK$'m | **Half-year ended 30 June 2011** | Half-year ended 30 June 2010 |
|---|---|---|
| Net interest income | **847** | 724 |
| Gross earned premiums | **6,530** | 2,813 |
| Gross earned premiums ceded to reinsurers | **(3,133)** | (11) |
| Other operating income | **399** | 559 |
| Operating income | **4,643** | 4,085 |
| Net insurance benefits and claims | **(4,220)** | (3,875) |
| Net operating income | **423** | 210 |
| Operating expenses | **(101)** | (104) |
| Operating profit before impairment allowances | **322** | 106 |
| Net charge of impairment allowances on securities investments | **(31)** | – |
| Profit before taxation | **291** | 106 |

| | **At 30 June 2011** | At 31 December 2010 |
|---|---|---|
| Segment assets | **53,186** | 48,195 |
| Segment liabilities | **49,850** | 45,149 |

Note: For additional segmental information, see Note 40 to the Interim Financial Information.

**Financial Results**

The Group's Insurance segment recorded strong financial results in the first half of 2011. Profit before taxation grew by 174.5% to HK$291 million. The increase was mainly attributable to the improved underwriting profit and the success of the RMB product strategy.

Net interest income rose by 17.0% mainly due to the increase in debt securities investments made for the new premiums received. Gross insurance premium income rose considerably by 132.1% of which regular premium income accounted for a significant part. Net insurance benefits and claims, which reflect changes in policy reserves, rose by 8.9%. The increase was mainly caused by the overall growth of the insurance business.

Assets in the insurance segment grew by 10.4% with the increase in both debt and equity securities investments made for the new premiums. Liabilities rose by 10.4%, which reflected the corresponding increase in insurance contractual liabilities.

**Business Operation**

***Further enhancement in product mix, service quality and market share***

The Group maintained its growth momentum in the insurance business. The Group continued to focus on its regular-premium products. The flagship products – "Target 5 Years Insurance Plan Series" and "Multi-Plus Savings Insurance Plan" – registered strong sales. New products such as "Tactics Investment Insurance Plan" and "Well-Assure Refundable Accident Insurance Plan" were launched during the first half of 2011. The Group also enhanced its service by strengthening the quality and speed of the compensation and underwriting process. Through the optimisation of product mix and service quality, the Group further reinforced its market position and expanded its market share.

***Maintaining leading position in RMB insurance products***

In response to the strong market demand, the Group developed and introduced more RMB insurance products in the interim period, including the new RMB series of its popular plans, such as the "Target 5 Years Insurance Plan Series" and "Multi-Plus Savings Insurance Plan", which were well-received by customers. This further solidified the Group's leadership role in the RMB insurance market.

## 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 credit risk, interest rate risk, market risk, liquidity risk, operational risk, reputation risk, legal and compliance risk, and strategic risk. The Group's risk management objective is to enhance shareholder value by maintaining risk exposures within acceptable limits. The Group has a defined risk appetite statement approved by the Board, which is an expression of the types and level of risk that the Group is willing to take in order to achieve its business goals and to meet the expectations of its stakeholders under a controllable risk level.

**Risk Management Governance Structure**

The Group's risk 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 its committees, 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 Audit Committee 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 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.

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, NCB (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 of loss that a customer or counterparty will be unable to or unwilling to meet its contractual obligations. Credit risk exists in the trading book and banking book, on– and off-balance sheet exposures of a bank. It arises principally from the lending, trade finance and treasury businesses, and covers inter-bank transactions, foreign exchange and derivative transactions as well as investments in bonds and securities. The Chief Credit Officer, who reports directly to the CRO, takes charge of credit risk management and is also responsible for the control of credit risk exposure of subsidiaries in line with the credit risk management principles and requirements set by the Group. The Chief Analytics Officer, who also reports directly to the CRO, is responsible for the development and maintenance of internal rating models and rating criteria. For loans and advances to customers, different credit approval and control procedures are adopted according to the level of risk associated with the customer, counterparty or transaction. 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. Corporate and financial institution credit applications are independently reviewed and objectively assessed by risk management units. Obligor ratings and facility grades are assigned to these portfolios. Retail internal rating systems are deployed in the risk assessment of retail credit transactions, including small business retail exposures, residential mortgage loans, personal loans and credit cards. Obligor ratings as well as loss estimates (if applicable) are used to support credit approval.

The Group identifies credit concentration risk by industry, geography, customer and counterparty risk. The Group monitors changes to counterparties' credit risk, the quality of the credit portfolio and risk concentrations, and reports regularly to the Group's management

The Group uses loan grades, obligor ratings and loss estimates (if applicable) to support credit monitoring, analysis and reporting. For corporate and financial institutions, more frequent rating review and closer monitoring are required for riskier customers. For retail exposures, monthly updated ratings and loss estimates are used for credit monitoring on a portfolio basis. More comprehensive review is required for obligors being identified under high-risk pools. The Group has established a master scale for internal credit rating purpose, which is in compliance with the Banking (Capital) Rules on rating structure. In addition to obligor ratings, the Group adopts a facility rating system to assess the risk in the facility structure during credit approval. This two-dimensional rating approach to evaluate credit risk complies with the HKMA's requirement on IRB.

As of 30 June 2011, the Group continues to adopt loan grading criteria which divide credit assets into 5 categories with reference to HKMA's guidelines. The Risk Management Department ("RMD") provides regular credit management information reports and ad hoc reports to the Management Committee, RC and Board of Directors to facilitate their continuous monitoring of credit risk.

For investments in debt securities and securitisation assets, the obligor ratings or external credit ratings, assessment of the underlying assets and credit limits setting on customer/security issuer basis are used for managing credit risk associated with the investment. For derivatives, the Group sets customer limits to manage the credit risk involved and follows the same approval and control processes as applied for loans and advances. Ongoing monitoring and stop-loss 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 take into consideration not only the mark-to-market (MTM) price of the issue and its external credit rating, but also additional factors such as 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. Furthermore, 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.

**Interest Rate Risk Management**

Interest rate risk means the risk to a bank's earnings and economic value arising from adverse movements in interest rate and term structures of the bank's asset and liability positions. 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 that may affect net interest income;
- Basis risk – different pricing basis for different transactions so that the yield on assets and cost of liabilities may change by different amounts within the same repricing period;
- Yield curve risk – non-parallel shifts in the yield curve that may have an adverse impact on net interest income or economic value;
- Option risk – exercise of the options embedded in assets, liabilities or off-balance sheet items that can cause a change in the cashflows of assets and liabilities.

The Group has set out interest rate risk indicators and limits to identify, measure, monitor and control interest rate risk. The indicators and limits include, but are not limited to, re-pricing gap limits, basis risk, duration, price value of a basis point (PVBP), Greeks, net interest income sensitivity ratio, economic value sensitivity ratio (including sub-limit for AFS securities), etc.

The indicators and limits are classified into two levels, which are approved by the RC and ALCO respectively. Risk-taking business units are required to conduct their business within the boundary of the interest rate risk limits. Before launching a new product or business in the banking book, relevant departments are required to go through a risk assessment process, which includes assessment of underlying interest rate risk and consideration of the adequacy of current risk monitoring mechanism. Any material impact on interest rate risk noted during the risk assessment process will be reported to both the CFO and CRO and submitted to the RC for approval.

Net interest income (NII) sensitivity ratio and economic value (EV) sensitivity ratio assess the impact of interest rate movement on the Group's net interest income and capital base. They are the Group's key interest rate risk indicators. The former assesses the impact of interest rate movement on net interest income as a percentage to budgeted net interest income for the year. The latter assesses the impact of interest rate movement on economic value (i.e. the present value of cash-flows of assets, liabilities and off-balance-sheet items discounted using market interest rate) as a percentage to the latest capital base. Limits are set by RC on these two indicators to monitor and control the Group's banking book interest rate risk.

The Group uses scenario analysis and stress test to assess the banking book interest rate risk the Group would face under adverse circumstances. Scenario analysis and stress test are also devised to assess the impact on net interest income and economic value as well as capital base arising from the optionality of demand and savings deposits, the prepayment of mortgage loans and the prepayment of ABS/MBS due to extension/contraction of weighted average life.

**Market Risk Management**

Market risk refers to the risk of losses arising from adverse movements in the value of foreign exchange and commodity positions and the trading book interest rate and equity positions held by the Group due to the volatility of financial market prices (debt security price/interest rate, foreign exchange rate, equity price, commodity price). The Group adopts robust market risk appetite to achieve balance between risk and return. The Group's objective in managing market risk is to secure healthy growth of the treasury business, by effective management of potential market risk in the Group's business, according to the Group's overall risk appetite and strategy of the treasury business and based on well-established risk management regime and measures.

With regard to the corporate governance of risk management, the Board and Risk Committee, senior management and functional departments/units perform their respective duties and responsibilities to manage the Group's market risk. The Risk Management Department (Market Risk Management) is mainly responsible for managing market risk, assisting senior management to perform their day-to-day duties, independently monitoring the market risk profile and compliance of management policies and limits of the Group and BOCHK, and ensuring that the aggregate and individual market risks are within acceptable level.

The Group's market risk management framework covers the Group's subsidiaries. The Group establishes uniform market risk management policies to regulate the Group's and subsidiaries' market risk management work; meanwhile, the Group sets up the Group VAR limit, which is allocated and monitored across the Group, according to subsidiaries' business requirements and risk tolerance level. In line with the requirements set in the Group policy, subsidiaries should formulate detailed regulations (subject to prior consent by BOCHK) and must bear the responsibility of managing the daily market risk of the institution. Subsidiaries set up independent risk monitoring teams to monitor daily market risk and limit compliance, and submit management information and reports to BOCHK on a regular basis.

The Group sets up market risk indicators and limits to identify, measure, monitor and control market risk. Major risk indicators and limits include but are not limited to VAR, Stop Loss, Open Position, Stress Testing and Sensitivity Analysis (Basis Point Value, Greeks), etc. To meet management requirements, major risk indicators and limits are classified into three levels, and approved by the Risk Committee, Management Committee or CRO and Deputy Chief Executive (DCE) in charge of treasury business respectively. The treasury business units of BOCHK and other subsidiaries (as for Group Limit) are required to conduct their business within approved market risk indicators and limits.

VAR refers to the core indicator used in managing the Group's market risk. It is a statistical method used to measure the maximum loss of trading book positions held by the bank over a target horizon with a given level of confidence. The Group adopts a uniform VAR calculation model, using the historical simulation approach and two years' historical data, to calculate VAR of the Group and subsidiaries over a one-day holding period with a 99% confidence level, and set up VAR limit of the Group and subsidiaries.

The predictive power of the VAR measure is monitored by back-testing, 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, such as fee and commission. If back-testing revenues are negative and exceeding the VAR, a "back-testing exception" is noted. Generally speaking, the number of back-testing exceptions in a rolling 12-month period will not exceed four times. Back-testing results are reported to the Group's senior management, including the CE and CRO. BOCHK conducts backtesting of VAR measures on a monthly basis.

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 intraday exposures.

The Group recognises these limitations by formulating stress test indicators and limits to assess and manage the market risk uncovered by VAR. 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, the 2001 September 11 incidents and the 2008 Global Financial Crisis, etc.

HKMA has approved BOCHK to adopt an internal model to calculate general market risk capital charge for the risk categories of interest rates and exchange rates. The approval has become effective on 1 April 2011.

**Liquidity Risk Management**

Liquidity risk is the risk that banks fail to provide sufficient funds to grow assets or pay due obligations, and so need to bear an unacceptable loss. The Group adopts a sound liquidity risk appetite to provide stable, reliable and adequate sources of cash to meet liquidity needs under normal circumstances or stressed scenarios; and survive with net positive cumulative cash flow in extreme scenarios without requesting HKMA to act as the lender of last resort.

The Group's liquidity risk management objective is to effectively manage the liquidity of on-balance sheet and off-balance sheet items with reasonable cost based on the liquidity risk appetite to achieve sound operation and sustainable profitability. According to different term maturities and the results of funding needs estimated from stressed scenarios, the Group adjusts its asset structure (including loans, bond investments, interbank placements, etc.) to maintain sufficient liquid assets in support of normal business needs and ensure its ability to raise enough funds at reasonable costs to serve external claims in case of emergency. The Group is committed to diversifying the source of funds and the use of funds to avoid excessive concentration of assets and liabilities and prevent triggering liquidity risk due to the break of funding strand when problems occur in one concentrated funding source. The Group also pays attention to liquidity risk created by off-balance sheet activities, such as loan commitments, derivatives, options and other complex structured products. The Group has an overall liquidity risk management strategy to cover the liquidity management of foreign currency assets and liabilities, intraday liquidity, intra-group liquidity, the liquidity risk arising from others' risk, etc., and has formulated a corresponding funding contingency plan.

The Group establishes liquidity risk management indicators and limits to identify, measure, monitor and control liquidity risk. Such indicators and limits include (but are not limited to) liquidity ratio, deposit stability ratio, loan-to-deposit ratio, Maximum Cumulative Outflow ("MCO") and liquidity buffer asset portfolio. The Group applies cash flow analysis (under normal and stress conditions) and liquidity stress test (including institution-specific and worldwide crisis) to assess the Group's capability to withstand various severe liquidity crises. Also, the Assets and Liabilities Management System ("ALM") is developed to provide data support for facilitating the liquidity risk management duties.

The Group's liquidity risk management also covers new product or business development. Before launching a new product or business, the relevant departments are required to go through a risk assessment process, which includes the 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 to RC for approval.

The Group has established a set of uniform liquidity risk management policies which serve as standards and guidance to all the Group's members for liquidity risk management. On the basis of the Group's uniform policy, each of the subsidiaries formulates its own liquidity management policies according to its own characteristics (subject to prior consent by BOCHK), and assumes its own liquidity risk management responsibility. Subsidiaries are required to report their respective liquidity positions on a regular basis to the Risk Management Department (Market Risk Management) of BOCHK which consolidates such information and monitors group-wide liquidity risk.

**Operational Risk Management**

Operational risk is the risk of loss resulting from inadequate or failed internal process, staff and information technology system, or from external events. The risk is inherent in every aspect of business operations and confronted by the Bank in its day-to-day operational activities.

The Group has put in place an effective internal control process which requires the establishment of policies and control procedures for all the key activities. Proper segregation of duties and authorisation is the fundamental principle followed by the Group. Corporate-level policy and procedure on operational risk management are formulated by the Operational Risk & Compliance Department ("OR&CD") and approved by RC.

The Group has adopted the "Three Lines of Defence" model for its operational risk management governance structure: all departments as the first line of defence are the owner of operational risk and are responsible for carrying out the duties and functions of self-risk control in the process of business operation through self-assessment, self-checking and self-correction. OR&CD together with certain specialist functional units in relation to operational risk management within the Group are the second line of defence, which is responsible for assessing and monitoring the operational risk condition of the first line of defence, and providing them with guidance. In addition to formulating the operational risk management policy and procedure, OR&CD, being independent from business units, is the central management unit of the Group's operational risk management and also responsible for designing the operational risk assessment methodologies, tools and the reporting mechanism (including the capturing of data on operational risk events loss), monitoring the implementation status of policies and operational procedures in the departments of the first line of defence through operational risk management tools, and assessing and reporting the overall operational risk position to Management and RC. Certain specialist functional units, including the Human Resources Department, Information Technology Department, Corporate Services Department, OR&CD, Financial Management Department and General Accounting & Accounting Policy Department, are required to carry out their managerial duties of the second line of defence with respect to some specific aspects of operational risk. Besides taking charge of operational risk management in their own units, these units are also required to provide other units with professional advice/training in respect of certain operational risk categories and to lead the corporate-level operational risk management. Audit Department is the third line of defence which provides independent assessment with respect to the operational risk management framework and is required to conduct periodic audit of the operational risk management activities of various departments/business units within the Group regarding their compliance and effectiveness and to put forward recommendations for corrective actions.

The Group adopts the tools or methodologies such as key risk indicators, self-assessment, operational risk events reporting and review to identify, assess, monitor and control the risks inherent in business activities and products, as well as takes out insurance to mitigate unforeseeable operational risks. Business continuity plans are in place to support business operations in the event of an 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. Since reputation risk is often caused by various types of operational and strategic issues that may have a negative impact on the trust in and perception of the company, all operational and key risks identified are assessed through the established KCSA framework to evaluate the severity of their impact on the Group, including the damage to reputation. In addition, the Group has put in place a framework including system support to achieve continuous monitoring of external reputation risk incidents and published failures of risk incidents in the financial industry.

**Legal and Compliance Risk Management**

Legal risk is the risk that unenforceable contracts, lawsuits or adverse judgments may disrupt or otherwise negatively affect the Group's operation or financial condition. Compliance risk is the risk of legal or regulatory sanctions, financial loss, or loss to reputation that the Group may suffer as a result of any failure to comply with all applicable laws and regulations. Legal and compliance risks are managed by OR&CD, which reports directly to the CRO. All legal matters are handled by the Legal Services Centre ("LSC"), which reports to the Chief Operating Officer. OR&CD is responsible for legal risk management of the Group with support rendered by LSC. As part of the Group's corporate governance framework, policy for the management of legal and compliance risk is approved by the Risk Committee.

**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 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. ALCO monitors the Group's capital adequacy. The Group has complied with all the statutory capital standards for the reported period.

To comply with HKMA's requirements as stated in the Supervisory Policy Manual "Supervisory Review Process", the Group has established the Internal Capital Adequacy Assessment Process (ICAAP) and reviews it annually. Using the statutory minimum CAR, 8%, as a starting point, extra capital (capital add-on) needed to cover the risks not captured under Pillar I is assessed. A Scorecard approach based on HKMA's compliance guidance on Pillar II has been used to evaluate the Group's risk profile in order to assess the add-on capital in Pillar II to the regulatory capital under Pillar I to 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 response to the core capital requirements under Basel III Accord, minimum common equity CAR and minimum core CAR are introduced in 2011's ICAAP. As the Group has adopted Foundation Internal Ratings-Based ("FIRB") approach in its calculation of credit risk since 2011, all capital adequacy targets are determined based on FIRB approach.

**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 by various risk management units and ALCO monitors the results against limits approved by RC. The Financial Management Department reports the combined stress test results 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, unit-linked long-term business and retirement scheme management in Hong Kong. Major types of risk arising from the BOC Life's insurance business are insurance risk, interest rate risk, liquidity risk and credit risk. BOC Life closely monitors these risks independently and reports to its RC on a regular basis. The key risks of its insurance business and related risk control processes 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 to 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 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, BOC Life has a retention limit on any single life insured. BOC Life cedes the excess of the insured benefit over the limit for standard risks (from a medical point of view) to reinsurer under an excess of loss reinsurance arrangement.

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.

**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 framework that has been developed to achieve investment returns that match its obligations under insurance contracts.

**Liquidity Risk Management**

Liquidity risk is the risk of not being able to fund increases in assets or meet obligations as they fall due without incurring unacceptable loss. BOC Life's asset liability matching framework includes cash flow management 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.

**Credit Risk Management**

BOC Life has exposure to credit risk, which is the risk that a customer or counterparty will be unable to or unwilling to meet a commitment that it has entered into. 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)
- Re-insurers' 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 credit risk management, BOC Life has strengthened its communication with the Investment Management 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.

# CONDENSED CONSOLIDATED INCOME STATEMENT

| | Notes | (Unaudited) Half-year ended 30 June 2011 HK$'m | (Restated) (Unaudited) Half-year ended 30 June 2010 HK$'m |
|---|---|---|---|
| Interest income | | **15,156** | 10,671 |
| Interest expense | | **(4,951)** | (1,707) |
| **Net interest income** | 4 | **10,205** | 8,964 |
| Fee and commission income | | **5,432** | 4,481 |
| Fee and commission expense | | **(1,446)** | (1,084) |
| **Net fee and commission income** | 5 | **3,986** | 3,397 |
| Gross earned premiums | | **6,524** | 2,809 |
| Gross earned premiums ceded to reinsurers | | **(3,133)** | (11) |
| **Net insurance premium income** | | **3,391** | 2,798 |
| Net trading gain/(loss) | 6 | **761** | (36) |
| Net gain on financial instruments designated at fair value through profit or loss | | **398** | 640 |
| Net gain on investment in securities | 7 | **360** | 404 |
| Other operating income | 8 | **245** | 249 |
| **Total operating income** | | **19,346** | 16,416 |
| Gross insurance benefits and claims | 9 | **(7,100)** | (3,880) |
| Reinsurers' share of benefits and claims | | **2,880** | 5 |
| **Net insurance benefits and claims** | | **(4,220)** | (3,875) |
| **Net operating income before impairment allowances** | | **15,126** | 12,541 |
| Net (charge)/reversal of impairment allowances | 10 | **(30)** | 161 |
| **Net operating income** | | **15,096** | 12,702 |
| Operating expenses | 11 | **(1,993)** | (4,534) |
| **Operating profit** | | **13,103** | 8,168 |
| Net gain from disposal of/fair value adjustments on investment properties | 12 | **1,486** | 601 |
| Net loss from disposal/revaluation of properties, plant and equipment | 13 | **(5)** | (1) |
| Share of profits less losses after tax of associates | | **3** | (1) |
| **Profit before taxation** | | **14,587** | 8,767 |
| Taxation | 14 | **(2,233)** | (1,412) |
| **Profit for the period** | | **12,354** | 7,355 |
| **Profit attributable to:** | | | |
| Equity holders of the Company | | **11,993** | 7,192 |
| Non-controlling interests | | **361** | 163 |
| | | **12,354** | 7,355 |
| **Dividends** | 15 | **6,661** | 4,229 |
| | | **HK$** | HK$ |
| **Earnings per share for profit attributable to the equity holders of the Company** | | | |
| Basic and diluted | 16 | **1.1343** | 0.6802 |

The notes on pages 43 to 109 are an integral part of this interim financial information.

# CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| | Notes | (Unaudited) Half-year ended 30 June 2011 HK$'m | (Restated) (Unaudited) Half-year ended 30 June 2010 HK$'m |
|---|---|---|---|
| **Profit for the period** | | **12,354** | 7,355 |
| Change in fair value of available-for-sale securities | | **1,001** | 1,681 |
| Change in fair value of cash flow hedges | | **–** | (1) |
| Revaluation of premises | | **5,252** | 1,953 |
| Currency translation difference | | **170** | 25 |
| Change in fair value of hedging instruments under net investment hedges | | **(52)** | – |
| Net deferred tax effect | 31 | **(958)** | (566) |
| Reclassification adjustments | | | |
| Release upon disposal of available-for-sale securities | | **(318)** | (380) |
| Net reversal of impairment allowances on available-for-sale securities transferred to income statement | 10 | **(6)** | (40) |
| Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities | | **(17)** | (22) |
| **Other comprehensive income for the period, net of tax** | | **5,072** | 2,650 |
| **Total comprehensive income for the period** | | **17,426** | 10,005 |
| **Total comprehensive income attributable to:** | | | |
| Equity holders of the Company | | **17,030** | 9,839 |
| Non-controlling interests | | **396** | 166 |
| | | **17,426** | 10,005 |

The notes on pages 43 to 109 are an integral part of this interim financial information.

# CONDENSED CONSOLIDATED BALANCE SHEET

| | Notes | (Unaudited) At 30 June 2011 HK$'m | (Audited) At 31 December 2010 HK$'m |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances with banks and other financial institutions | 19 | **419,231** | 415,812 |
| Placements with banks and other financial institutions maturing between one and twelve months | | **89,618** | 39,499 |
| Financial assets at fair value through profit or loss | 20 | **48,337** | 69,876 |
| Derivative financial instruments | 21 | **27,554** | 23,854 |
| Hong Kong SAR Government certificates of indebtedness | | **54,460** | 46,990 |
| Advances and other accounts | 22 | **719,500** | 645,424 |
| Investment in securities | 23 | **393,636** | 360,184 |
| Interests in associates | | **214** | 212 |
| Investment properties | 24 | **11,664** | 10,342 |
| Properties, plant and equipment | 25 | **36,110** | 31,049 |
| Deferred tax assets | 31 | **147** | 157 |
| Other assets | 26 | **29,908** | 17,641 |
| Total assets | | **1,830,379** | 1,661,040 |
| **LIABILITIES** | | | |
| Hong Kong SAR currency notes in circulation | | **54,460** | 46,990 |
| Deposits and balances from banks and other financial institutions | | **386,904** | 313,784 |
| Financial liabilities at fair value through profit or loss | 27 | **4,875** | 25,493 |
| Derivative financial instruments | 21 | **23,940** | 21,355 |
| Deposits from customers | 28 | **1,103,435** | 1,027,033 |
| Debt securities in issue at amortised cost | | **5** | – |
| Other accounts and provisions | 29 | **47,842** | 35,480 |
| Current tax liabilities | | **3,334** | 1,726 |
| Deferred tax liabilities | 31 | **5,078** | 4,206 |
| Insurance contract liabilities | 32 | **43,045** | 39,807 |
| Subordinated liabilities | 33 | **27,838** | 26,877 |
| Total liabilities | | **1,700,756** | 1,542,751 |
| **EQUITY** | | | |
| Share capital | 34 | **52,864** | 52,864 |
| Reserves | 35 | **73,299** | 62,317 |
| Capital and reserves attributable to the equity holders of the Company | | **126,163** | 115,181 |
| Non-controlling interests | | **3,460** | 3,108 |
| Total equity | | **129,623** | 118,289 |
| Total liabilities and equity | | **1,830,379** | 1,661,040 |

The notes on pages 43 to 109 are an integral part of this interim financial information.

# CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

| | (Unaudited) | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Attributable to the 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$'m | Cash flow hedge reserve HK$'m | Regulatory reserve* HK$'m | Translation reserve HK$'m | Retained earnings HK$'m | Total HK$'m | Non-controlling interests HK$'m | Total equity HK$'m |
| At 1 January 2010, as previously reported | 52,864 | 11,559 | 1,880 | – | 4,040 | 225 | 32,334 | 102,902 | 2,733 | 105,635 |
| Effect of early adoption of HKAS 12 (Amendment) | – | 101 | – | – | – | – | 1,176 | 1,277 | 3 | 1,280 |
| At 1 January 2010, as restated | 52,864 | 11,660 | 1,880 | – | 4,040 | 225 | 33,510 | 104,179 | 2,736 | 106,915 |
| Comprehensive income | – | 1,629 | 974 | (1) | – | 66 | 7,171 | 9,839 | 166 | 10,005 |
| Release upon disposal of premises | – | (30) | – | – | – | – | 30 | – | – | – |
| Transfer from retained earnings | – | – | – | – | 571 | – | (571) | – | – | – |
| Dividend paid | – | – | – | – | – | – | (6,027) | (6,027) | (72) | (6,099) |
| At 30 June 2010 | 52,864 | 13,259 | 2,854 | (1) | 4,611 | 291 | 34,113 | 107,991 | 2,830 | 110,821 |
| Company and subsidiaries | 52,864 | 13,259 | 2,854 | (1) | 4,611 | 291 | 34,062 | 107,940 | | |
| Associates | – | – | – | – | – | – | 51 | 51 | | |
| | 52,864 | 13,259 | 2,854 | (1) | 4,611 | 291 | 34,113 | 107,991 | | |
| At 1 July 2010, as previously reported | 52,864 | 13,157 | 2,854 | (1) | 4,611 | 291 | 32,935 | 106,711 | 2,826 | 109,537 |
| Effect of early adoption of HKAS 12 (Amendment) | – | 102 | – | – | – | – | 1,178 | 1,280 | 4 | 1,284 |
| At 1 July 2010, as restated | 52,864 | 13,259 | 2,854 | (1) | 4,611 | 291 | 34,113 | 107,991 | 2,830 | 110,821 |
| Comprehensive income | – | 2,496 | (225) | 1 | – | 162 | 8,985 | 11,419 | 334 | 11,753 |
| Release upon disposal of premises | – | (5) | – | – | – | – | 5 | – | – | – |
| Transfer from retained earnings | – | – | – | – | 465 | – | (465) | – | – | – |
| Dividend paid | – | – | – | – | – | – | (4,229) | (4,229) | (56) | (4,285) |
| At 31 December 2010 | 52,864 | 15,750 | 2,629 | – | 5,076 | 453 | 38,409 | 115,181 | 3,108 | 118,289 |
| Company and subsidiaries | 52,864 | 15,750 | 2,629 | – | 5,076 | 453 | 38,359 | 115,131 | | |
| Associates | – | – | – | – | – | – | 50 | 50 | | |
| | 52,864 | 15,750 | 2,629 | – | 5,076 | 453 | 38,409 | 115,181 | | |
| At 1 January 2011 | **52,864** | **15,750** | **2,629** | **–** | **5,076** | **453** | **38,409** | **115,181** | **3,108** | **118,289** |
| Comprehensive income | **–** | **4,369** | **588** | **–** | **–** | **97** | **11,976** | **17,030** | **396** | **17,426** |
| Release upon disposal of premises | **–** | **(19)** | **–** | **–** | **–** | **–** | **19** | **–** | **–** | **–** |
| Transfer from retained earnings | **–** | **–** | **–** | **–** | **1,519** | **–** | **(1,519)** | **–** | **–** | **–** |
| Dividend paid | **–** | **–** | **–** | **–** | **–** | **–** | **(6,048)** | **(6,048)** | **(44)** | **(6,092)** |
| At 30 June 2011 | **52,864** | **20,100** | **3,217** | **–** | **6,595** | **550** | **42,837** | **126,163** | **3,460** | **129,623** |
| Company and subsidiaries | **52,864** | **20,100** | **3,217** | **–** | **6,595** | **550** | **42,785** | **126,111** | | |
| Associates | **–** | **–** | **–** | **–** | **–** | **–** | **52** | **52** | | |
| | **52,864** | **20,100** | **3,217** | **–** | **6,595** | **550** | **42,837** | **126,163** | | |
| Representing: | | | | | | | | | | |
| 2011 interim dividend (Note 15) | | | | | | | **6,661** | | | |
| Others | | | | | | | **36,176** | | | |
| Retained earnings as at 30 June 2011 | | | | | | | **42,837** | | | |

* 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 43 to 109 are an integral part of this interim financial information.

# CONDENSED CONSOLIDATED CASH FLOW STATEMENT

| | Notes | **(Unaudited) Half-year ended 30 June 2011 HK$'m** | (Unaudited) Half-year ended 30 June 2010 HK$'m |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Operating cash inflow before taxation | 36(a) | **7,166** | 21,742 |
| Hong Kong profits tax paid | | **(583)** | (325) |
| Overseas profits tax paid | | **(118)** | (32) |
| **Net cash inflow from operating activities** | | **6,465** | 21,385 |
| **Cash flows from investing activities** | | | |
| Purchase of properties, plant and equipment | | **(255)** | (162) |
| Purchase of investment properties | | **(12)** | (2) |
| Proceeds from disposal of properties, plant and equipment | | **5** | 93 |
| Proceeds from disposal of investment properties | | **6** | 163 |
| Dividend received from associates | | **1** | 3 |
| **Net cash (outflow)/inflow from investing activities** | | **(255)** | 95 |
| **Cash flows from financing activities** | | | |
| Dividend paid to the equity holders of the Company | | **(6,048)** | (6,027) |
| Dividend paid to non-controlling interests | | **(44)** | (72) |
| Proceeds from issuance of subordinated notes | | **–** | 19,261 |
| Repayment of subordinated loans | | **–** | (19,418) |
| Interest paid for subordinated liabilities | | **(296)** | (156) |
| **Net cash outflow from financing activities** | | **(6,388)** | (6,412) |
| (Decrease)/increase in cash and cash equivalents | | **(178)** | 15,068 |
| Cash and cash equivalents at 1 January | | **446,679** | 182,708 |
| **Cash and cash equivalents at 30 June** | 36(b) | **446,501** | 197,776 |

The notes on pages 43 to 109 are an integral part of this interim financial information.

# NOTES TO THE INTERIM FINANCIAL INFORMATION

## 1. Basis of preparation and significant accounting policies

### *Basis of preparation*

The unaudited interim financial information has been prepared in accordance with HKAS 34 'Interim Financial Reporting' issued by the HKICPA.

### *Significant accounting policies*

Except as described below, the significant accounting policies adopted and methods of computation used in the preparation of the unaudited interim financial information are consistent with those adopted and used in the Group's annual financial statements for the year ended 31 December 2010 and should be read in conjunction with the Group's Annual Report for 2010.

**Revised standards and amendments to standards that are mandatory for the first time for the financial year beginning on 1 January 2011**

- HKAS 24 (Revised), 'Related Party Disclosures'. The Group early adopted the partial exemption regarding disclosure requirements for transactions with government-related entities in its annual financial statements for the year ended 31 December 2009. The application of the remainder of the revised standard this year which amends the definition of related parties does not have significant impact on the Group.

- HKAS 34 (Amendment), 'Interim Financial Reporting'. The amendment, which is part of 'Improvements to HKFRSs in 2010', emphasises the existing disclosure principles in HKAS 34 and adds further guidance to illustrate the application of these principles. Greater emphasis has been placed on the disclosure principles for significant events and transactions. Additional requirements cover disclosure of changes to fair value measurement (if significant), and the need to update relevant information from the most recent annual report. The adoption of this amendment will only affect the presentation of the Group's financial statements.

- Other improvements to HKFRSs contain numerous amendments to HKFRSs which the HKICPA consider non-urgent but necessary. It comprises amendments that result in accounting changes for presentation, recognition or measurement purpose as well as terminology or editorial amendments related to a variety of individual HKFRS. For amendments that are effective for the financial year beginning on 1 January 2011, no material changes to accounting policies are expected.

**Standards and amendments issued that are relevant to the Group but not yet effective and have not been early adopted by the Group in 2011**

| Standard | Content | Applicable for financial year beginning on/after |
|---|---|---|
| HKAS 27 (2011) | Separate Financial Statements | 1 January 2013 |
| HKAS 28 (2011) | Investments in Associates and Joint Ventures | 1 January 2013 |
| HKFRS 9 | Financial Instruments | 1 January 2013 |
| HKFRS 10 | Consolidated Financial Statements | 1 January 2013 |
| HKFRS 11 | Joint Arrangements | 1 January 2013 |
| HKFRS 12 | Disclosure of Interests in Other Entities | 1 January 2013 |
| HKFRS 13 | Fair Value Measurement | 1 January 2013 |

## 1. Basis of preparation and significant accounting policies (continued)

### *Significant accounting policies (continued)*

**Standards and amendments issued that are relevant to the Group but not yet effective and have not been early adopted by the Group in 2011 (continued)**

Newly pronounced standards in the first half of 2011 that are relevant to the Group:

- HKFRS 10, 'Consolidated Financial Statements'. HKFRS 10 replaces all of the guidance on control and consolidation stipulated in HKAS 27 (Revised), 'Consolidated and Separate Financial Statements' and HK(SIC)-Int 12, 'Consolidation – Special Purpose Entities'. The remainder of HKAS 27 (Revised) is renamed HKAS 27 (2011), 'Separate Financial Statements' as a standard dealing solely with separate financial statements without changing the existing guidance for separate financial statements.

- HKFRS 11, 'Joint Arrangements'. Changes in the definitions stipulated in HKFRS 11 have reduced the 'types' of joint arrangements to two: joint operations and joint ventures. A joint operation is a joint arrangement that gives parties to the arrangement direct rights to the assets and obligations for the liabilities. The 'jointly controlled assets' classification in HKAS 31, 'Interests in Joint Ventures', has been merged into joint operations, as both types of arrangements generally result in the same accounting outcome. A joint venture, in contrast, gives the parties rights to the net assets or outcome of the arrangement. Joint ventures are accounted for using the equity method in accordance with HKAS 28, 'Investments in Associates' which is renamed as HKAS 28 (2011), 'Investments in Associates and Joint Ventures' to include the scope of joint ventures and merge with HK(SIC)-Int 13, 'Jointly Controlled Entities – Non-Monetary Contributions by Venturers'. After the application of the standard, entities can no longer account for an interest in a joint venture using the proportionate consolidation method.

- HKFRS 12, 'Disclosure of Interests in Other Entities'. The standard sets out the required disclosures for entities reporting under the two new standards, HKFRS 10 and HKFRS 11, and the revised standard HKAS 28 (2011). The existing guidance and disclosure requirements for separate financial statements stipulated in HKAS 27 (Revised) are unchanged. HKFRS 12, requires entities to disclose information that helps financial statement readers to evaluate the nature, risks and financial effects associated with the entity's interests in subsidiaries, associates, joint arrangements and unconsolidated structured entities.

The above HKFRS 10, HKFRS 11, HKFRS 12, HKAS 27 (2011) and HKAS 28 (2011) issued in June 2011 are a group of five new standards that address the scope of reporting entity and will supersede HKAS 27 (Revised), HKAS 28, HKAS 31, HK(SIC)-Int 12 and HK(SIC)-Int 13. Earlier application of these standards are permitted but only when they are applied at the same time. The Group is still considering the financial impact of the above standards on consolidated financial statements.

- HKFRS 13, 'Fair Value Measurement'. The new standard which was issued in June 2011 replaces the fair value measurement guidance contained in individual HKFRSs by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across HKFRSs. The requirements do not extend the use of fair value accounting, but provide guidance on how it should be applied when its use is already required or permitted by other standards within HKFRSs. The Group is still considering the financial impact on the application of this standard.

## 1. Basis of preparation and significant accounting policies (continued)

### *Significant accounting policies (continued)*

**Amendment issued that is not yet mandatorily effective but has been early adopted by the Group**

| Standard | Content | Applicable for financial year beginning on/after | Currently relevant to the Group | Year of early adoption |
|---|---|---|---|---|
| HKAS 12 (Amendment) | Income Taxes | 1 January 2012 | Yes | 2010 |

- HKAS 12 (Amendment), 'Income Taxes'. The standard which was revised in December 2010 will be effective for reporting period beginning on or after 1 January 2012. Earlier application is permitted. The Group considers that the required treatment under the revised standard better reflects the tax position of the investment properties of the Group, and have early adopted the amended standard retrospectively since the year ended 31 December 2010.

Upon early adoption, deferred tax liabilities for the revaluation of investment properties would be calculated subject to a nil tax rate retrospectively. The effect of the adoption of this amended standard on 30 June 2010 is set out below:

| | At 30 June 2010 HK$'m |
|---|---|
| **Items in Condensed Consolidated Balance Sheet:** | |
| Increase in deferred tax assets | 3 |
| Net increase in assets | 3 |
| Decrease in deferred tax liabilities | (1,281) |
| Net decrease in liabilities | (1,281) |
| Increase in premises revaluation reserve | 102 |
| Increase in retained earnings | 1,178 |
| Increase in non-controlling interests | 4 |
| Net increase in equity | 1,284 |

| | Half-year ended 30 June 2010 HK$'m |
|---|---|
| **Item in Condensed Consolidated Income Statement:** | |
| Decrease in taxation | (2) |

| | Half-year ended 30 June 2010 HK$ |
|---|---|
| **Increase in earnings per share, basic and diluted** | 0.0002 |

## 2. Critical accounting estimates and judgements in applying accounting policies

Except as described below, the nature and assumptions related to the Group's accounting estimates are consistent with those used in the Group's financial statements for the year ended 31 December 2010.

On 15 June 2011, the Group jointly announced with thirteen other distributing banks of Lehman Brothers minibonds ("Minibonds") the final resolution of certain series of Minibonds ("Final Resolution"). As part of this Final Resolution, the distributing banks made a voluntary offer to pay ex gratia payments to eligible customers and agreed to provide further funding to the trustee of the Minibonds ("Trustee") to pay for expenses which may be incurred in connection with the recovery of the underlying collateral of the Minibonds and the Trustee's role in respect of the Minibonds. The net amount recovered by the Group from the underlying collateral of the Minibonds, after deducting the ex gratia payments and provision for trustee expenses, was credited to operating expenses in the condensed consolidated income statement for the six months period ended 30 June 2011 (Note 11).

## 3. 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.

### *3.1 Credit Risk*

#### (A) Gross advances and other accounts

*(a) Impaired advances*

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.

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

#### (A) Gross advances and other accounts (continued)

*(a) Impaired advances (continued)*

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.

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Gross impaired advances to customers | **345** | 455 |
| Individually assessed loan impairment allowances made in respect of such advances | **249** | 326 |
| Current market value of collateral held against the covered portion of such advances to customers | **63** | 109 |
| Covered portion of such advances to customers | **51** | 80 |
| Uncovered portion of such advances to customers | **294** | 375 |
| Gross impaired advances to customers as a percentage of gross advances to customers | **0.05%** | 0.07% |

The loan impairment allowances were made after taking into account the value of collateral in respect of impaired advances.

Classified or impaired advances to customers are analysed as follows:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Gross classified or impaired advances to customers | **706** | 867 |
| Gross classified or impaired advances to customers as a percentage of gross advances to customers | **0.10%** | 0.14% |

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.

## 3. Financial risk management (continued)

### 3.1 Credit Risk (continued)

#### (A) Gross advances and other accounts (continued)

*(b) Advances overdue for more than three months*

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.

The gross amount of advances overdue for more than three months is analysed as follows:

| | **At 30 June 2011** | | At 31 December 2010 | |
|---|---|---|---|---|
| | **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 | **63** | **0.01%** | 38 | 0.01% |
| – one year or less but over six months | **28** | **0.01%** | 38 | 0.01% |
| – over one year | **307** | **0.04%** | 359 | 0.05% |
| Advances overdue for over three months | **398** | **0.06%** | 435 | 0.07% |
| Individually assessed loan impairment allowances made in respect of such advances | **189** | | 194 | |

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Current market value of collateral held against the covered portion of such advances to customers | **518** | 558 |
| Covered portion of such advances to customers | **168** | 213 |
| Uncovered portion of such advances to customers | **230** | 222 |

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

#### (A) Gross advances and other accounts (continued)

*(b) Advances overdue for more than three months (continued)*

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 30 June 2011 and 31 December 2010, there were no advances to banks and other financial institutions overdue for more than three months.

*(c) Rescheduled advances*

| | **At 30 June 2011** | | At 31 December 2010 | |
|---|---|---|---|---|
| | **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 three months" | **115** | **0.02%** | 228 | 0.04% |

As at 30 June 2011 and 31 December 2010, 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. Rescheduled advances, which have been overdue for more than three months under the revised repayment terms, are included in overdue advances.

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

#### (A) Gross advances and other accounts (continued)

*(d) 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:

| | At 30 June 2011 | | | | | |
|---|---|---|---|---|---|---|
| | 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 | 30,767 | 39.34% | 3 | 3 | – | 105 |
| – Property investment | 70,522 | 86.63% | 87 | 197 | 6 | 397 |
| – Financial concerns | 9,720 | 29.75% | – | – | – | 57 |
| – Stockbrokers | 1,625 | 63.74% | – | – | – | 7 |
| – Wholesale and retail trade | 32,296 | 70.05% | 30 | 104 | 16 | 162 |
| – Manufacturing | 16,559 | 44.82% | 54 | 155 | 16 | 103 |
| – Transport and transport equipment | 26,535 | 37.60% | 70 | 4 | 1 | 95 |
| – Recreational activities | 593 | 15.50% | – | – | – | 2 |
| – Information technology | 14,994 | 0.67% | 2 | 5 | 1 | 51 |
| – Others | 28,201 | 38.54% | 43 | 150 | 20 | 115 |
| Individuals | | | | | | |
| – Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme | 11,643 | 99.96% | 54 | 321 | – | 10 |
| – Loans for purchase of other residential properties | 168,084 | 99.99% | 44 | 961 | – | 109 |
| – Credit card advances | 8,595 | – | 20 | 238 | – | 75 |
| – Others | 14,502 | 64.29% | 49 | 157 | 20 | 19 |
| Total loans for use in Hong Kong | 434,636 | 72.99% | 456 | 2,295 | 80 | 1,307 |
| Trade finance | 59,840 | 15.35% | 128 | 164 | 90 | 263 |
| Loans for use outside Hong Kong | 178,382 | 22.34% | 122 | 166 | 79 | 651 |
| Gross advances to customers | 672,858 | 54.44% | 706 | 2,625 | 249 | 2,221 |

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

#### (A) Gross advances and other accounts (continued)

*(d) Concentration of advances to customers (continued)*

(i) Sectoral analysis of gross advances to customers (continued)

| | At 31 December 2010 | | | | | |
|---|---|---|---|---|---|---|
| | 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 | 29,542 | 34.21% | 3 | 3 | – | 93 |
| – Property investment | 67,265 | 88.59% | 87 | 273 | 7 | 374 |
| – Financial concerns | 9,011 | 30.57% | – | 4 | – | 50 |
| – Stockbrokers | 556 | 69.32% | – | – | – | 2 |
| – Wholesale and retail trade | 24,300 | 67.23% | 29 | 127 | 12 | 131 |
| – Manufacturing | 15,125 | 44.57% | 70 | 118 | 22 | 83 |
| – Transport and transport equipment | 23,409 | 34.39% | 80 | 21 | 2 | 80 |
| – Recreational activities | 521 | 19.00% | – | – | – | 2 |
| – Information technology | 14,212 | 0.62% | 3 | 3 | 1 | 44 |
| – Others | 23,006 | 42.85% | 48 | 168 | 7 | 86 |
| Individuals | | | | | | |
| – Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme | 12,291 | 99.96% | 64 | 377 | – | 10 |
| – Loans for purchase of other residential properties | 147,424 | 99.99% | 75 | 1,199 | – | 84 |
| – Credit card advances | 8,230 | – | 18 | 217 | – | 75 |
| – Others | 12,195 | 63.44% | 44 | 179 | 20 | 15 |
| Total loans for use in Hong Kong | 387,087 | 72.71% | 521 | 2,689 | 71 | 1,129 |
| Trade finance | 53,396 | 16.73% | 95 | 141 | 57 | 228 |
| Loans for use outside Hong Kong | 172,736 | 24.45% | 251 | 153 | 198 | 628 |
| Gross advances to customers | 613,219 | 54.24% | 867 | 2,983 | 326 | 1,985 |

* Advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid.

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

**(A) Gross advances and other accounts (continued)**

*(d) Concentration of advances to customers (continued)*

(ii) Geographical analysis of gross advances to customers

The following geographical analysis of advances to customers is based on the location of the counterparties, after taking into account the transfer of risk. In general, such transfer of risk takes place if the advances to customers are guaranteed by a party in a country which is different from that of the customer.

**Gross advances to customers**

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Hong Kong | **487,844** | 447,494 |
| Mainland China | **144,794** | 127,436 |
| Others | **40,220** | 38,289 |
| | **672,858** | 613,219 |
| **Collectively assessed loan impairment allowances in respect of the gross advances to customers** | | |
| Hong Kong | **1,514** | 1,375 |
| Mainland China | **554** | 478 |
| Others | **153** | 132 |
| | **2,221** | 1,985 |

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

**(A) Gross advances and other accounts (continued)**

*(d) Concentration of advances to customers (continued)*

(ii) Geographical analysis of gross advances to customers (continued)

**Overdue advances**

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Hong Kong | **2,379** | 2,761 |
| Mainland China | **145** | 207 |
| Others | **101** | 15 |
| | **2,625** | 2,983 |
| **Individually assessed loan impairment allowances in respect of the overdue advances** | | |
| Hong Kong | **154** | 137 |
| Mainland China | **42** | 64 |
| Others | **37** | 2 |
| | **233** | 203 |
| **Collectively assessed loan impairment allowances in respect of the overdue advances** | | |
| Hong Kong | **61** | 51 |
| Mainland China | **5** | 5 |
| Others | **2** | – |
| | **68** | 56 |

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

**(A) Gross advances and other accounts (continued)**

*(d) Concentration of advances to customers (continued)*

(ii) Geographical analysis of gross advances to customers (continued)

**Classified or impaired advances**

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Hong Kong | **582** | 656 |
| Mainland China | **74** | 113 |
| Others | **50** | 98 |
| | **706** | 867 |
| **Individually assessed loan impairment allowances in respect of the classified or impaired advances** | | |
| Hong Kong | **170** | 163 |
| Mainland China | **42** | 65 |
| Others | **37** | 98 |
| | **249** | 326 |
| **Collectively assessed loan impairment allowances in respect of the classified or impaired advances** | | |
| Hong Kong | **20** | 19 |
| Mainland China | **2** | 2 |
| Others | **1** | – |
| | **23** | 21 |

**(B) Repossessed assets**

The estimated market value of repossessed assets held by the Group as at 30 June 2011 amounted to HK$288 million (31 December 2010: HK$280 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.

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

#### (C) Debt securities

The tables below represent 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.

| | At 30 June 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | 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 | Others HK$'m | Total HK$'m |
| **Investment in securities** | | | | | | | | |
| US non-agency residential mortgage-backed | | | | | | | | |
| – Subprime | 174 | 37 | 102 | – | – | – | – | 313 |
| – Alt-A | 26 | 21 | – | 94 | – | – | – | 141 |
| – Prime | 90 | 46 | 110 | 93 | – | – | – | 339 |
| Fannie Mae | | | | | | | | |
| – mortgage-backed securities | – | – | – | – | – | 10 | – | 10 |
| Freddie Mac | | | | | | | | |
| – issued debt securities | 79 | – | – | – | – | – | – | 79 |
| – mortgage-backed securities | – | – | – | – | – | 454 | – | 454 |
| Other MBS/ABS | 2,094 | 201 | – | – | – | 9,721 | – | 12,016 |
| Other debt securities | 92,470 | 71,737 | 49,801 | 5,462 | 36,736 | 49,133 | 71,405 | 376,744 |
| Subtotal | 94,933 | 72,042 | 50,013 | 5,649 | 36,736 | 59,318 | 71,405 | 390,096 |
| **Financial assets at fair value through profit or loss** | | | | | | | | |
| Other MBS/ABS | 19 | – | – | – | – | – | – | 19 |
| Other debt securities | 3,141 | 6,862 | 17,019 | 1,483 | 11,358 | 15 | 2,791 | 42,669 |
| Subtotal | 3,160 | 6,862 | 17,019 | 1,483 | 11,358 | 15 | 2,791 | 42,688 |
| Total | 98,093 | 78,904 | 67,032 | 7,132 | 48,094 | 59,333 | 74,196 | 432,784 |

## 3. Financial risk management (continued)

### 3.1 Credit Risk (continued)

#### (C) Debt securities (continued)

| | At 31 December 2010 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | | 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 | Others HK$'m | Total HK$'m |
| **Investment in securities** | | | | | | | | |
| US non-agency residential mortgage-backed | | | | | | | | |
| – Subprime | 351 | 1 | 5 | – | – | – | – | 357 |
| – Alt-A | 90 | 112 | 40 | – | – | – | – | 242 |
| – Prime | 391 | 64 | 87 | 53 | – | – | – | 595 |
| Fannie Mae | | | | | | | | |
| – mortgage-backed securities | – | – | – | – | – | 15 | – | 15 |
| Freddie Mac | | | | | | | | |
| – issued debt securities | 79 | 158 | – | – | – | – | – | 237 |
| – mortgage-backed securities | – | – | – | – | – | 602 | – | 602 |
| Other MBS/ABS | 2,490 | 282 | – | – | – | 7,334 | – | 10,106 |
| Other debt securities | 99,456 | 79,249 | 45,852 | 6,885 | 15,989 | 49,260 | 47,812 | 344,503 |
| Subtotal | 102,857 | 79,866 | 45,984 | 6,938 | 15,989 | 57,211 | 47,812 | 356,657 |
| **Financial assets at fair value through profit or loss** | | | | | | | | |
| Other MBS/ABS | 19 | – | – | – | – | – | – | 19 |
| Other debt securities | 1,303 | 7,958 | 17,037 | 1,682 | 33,486 | – | 3,306 | 64,772 |
| Subtotal | 1,322 | 7,958 | 17,037 | 1,682 | 33,486 | – | 3,306 | 64,791 |
| Total | 104,179 | 87,824 | 63,021 | 8,620 | 49,475 | 57,211 | 51,118 | 421,448 |

The total amount of unrated issues amounted to HK$181,623 million (31 December 2010: HK$157,804 million) as at 30 June 2011, of which only HK$13,956 million (31 December 2010: HK$6,697 million) were without issuer ratings. For details, please refer to page 57.

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

#### (C) Debt securities (continued)

For the above debt securities with no issue rating, their issuer ratings are analysed as follows:

| | **At 30 June 2011** | | | | | |
|---|---|---|---|---|---|---|
| | **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 | **37,055** | **61,452** | **12,603** | **6,263** | **12,445** | **129,818** |
| Held-to-maturity securities | **431** | **20,517** | **700** | **100** | **512** | **22,260** |
| Loans and receivables | **–** | **14,089** | **1,292** | **–** | **–** | **15,381** |
| Financial assets at fair value through profit or loss | **–** | **11,443** | **1,722** | **–** | **999** | **14,164** |
| Total | **37,486** | **107,501** | **16,317** | **6,363** | **13,956** | **181,623** |

| | At 31 December 2010 | | | | | |
|---|---|---|---|---|---|---|
| | 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 | 39,825 | 34,342 | 8,321 | 4,833 | 5,638 | 92,959 |
| Held-to-maturity securities | 668 | 10,910 | 1,119 | – | – | 12,697 |
| Loans and receivables | – | 11,187 | 4,169 | – | – | 15,356 |
| Financial assets at fair value through profit or loss | – | 33,581 | 2,152 | – | 1,059 | 36,792 |
| Total | 40,493 | 90,020 | 15,761 | 4,833 | 6,697 | 157,804 |

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

#### (C) Debt securities (continued)

The impaired debt securities by credit rating are analysed as follows:

| | At 30 June 2011 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Carrying values | | | | | | Of which accumulated impairment allowances |
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m | HK$'m |
| **Investment in securities** | | | | | | | |
| US non-agency residential mortgage-backed | | | | | | | |
| – Subprime | 174 | 37 | 94 | – | – | 305 | 30 |
| – Prime | – | – | 16 | 13 | – | 29 | 3 |
| Other debt securities | – | – | – | 36 | – | 36 | 3 |
| Total | 174 | 37 | 110 | 49 | – | 370 | 36 |
| Of which accumulated impairment allowances | 19 | 5 | 8 | 4 | – | 36 | |

| | At 31 December 2010 | | | | | | |
|---|---|---|---|---|---|---|---|
| | Carrying values | | | | | | Of which accumulated impairment allowances |
| | Aaa HK$'m | Aa1 to Aa3 HK$'m | A1 to A3 HK$'m | Lower than A3 HK$'m | Unrated HK$'m | Total HK$'m | HK$'m |
| **Investment in securities** | | | | | | | |
| US non-agency residential mortgage-backed | | | | | | | |
| – Subprime | 345 | 1 | – | – | – | 346 | 36 |
| – Alt-A | – | 36 | 40 | – | – | 76 | 30 |
| – Prime | 48 | – | 45 | 12 | – | 105 | 26 |
| Other MBS/ABS | – | 15 | – | – | – | 15 | – |
| Other debt securities | – | – | – | 271 | – | 271 | 56 |
| Total | 393 | 52 | 85 | 283 | – | 813 | 148 |
| Of which accumulated impairment allowances | 53 | 14 | 21 | 60 | – | 148 | |

As at 30 June 2011 and 31 December 2010, there were no overdue debt securities.

## 3. Financial risk management (continued)

### 3.1 Credit Risk (continued)

#### (C) Debt securities (continued)

*MBS/ABS*

The tables below represent an analysis of the Group's exposure to MBS/ABS by geographical location.

| | At 30 June 2011 | | |
|---|---|---|---|
| | Carrying values | | Of which accumulated impairment allowances |
| | Total HK$'m | Impaired securities HK$'m | HK$'m |
| **US MBS/ABS** | | | |
| Non-agency residential mortgage-backed | | | |
| – Subprime | **313** | **305** | **30** |
| – Alt-A | **141** | **–** | **–** |
| – Prime | **339** | **29** | **3** |
| Ginnie Mae | **9,721** | **–** | **–** |
| Fannie Mae | **10** | **–** | **–** |
| Freddie Mac | **454** | **–** | **–** |
| Others | **623** | **–** | **–** |
| | **11,601** | **334** | **33** |
| **Other countries MBS/ABS** | | | |
| Residential mortgage-backed | **1,672** | **–** | **–** |
| Commercial mortgage-backed | **19** | **–** | **–** |
| | **1,691** | **–** | **–** |
| Total MBS/ABS | **13,292** | **334** | **33** |

## 3. Financial risk management (continued)

### *3.1 Credit Risk (continued)*

**(C) Debt securities (continued)**

*MBS/ABS (continued)*

| | At 31 December 2010 | | |
|---|---|---|---|
| | Carrying values | | Of which accumulated impairment allowances |
| | Total HK$'m | Impaired securities HK$'m | HK$'m |
| **US MBS/ABS** | | | |
| Non-agency residential mortgage-backed | | | |
| – Subprime | 357 | 346 | 36 |
| – Alt-A | 242 | 76 | 30 |
| – Prime | 595 | 105 | 26 |
| Ginnie Mae | 7,334 | – | – |
| Fannie Mae | 15 | – | – |
| Freddie Mac | 602 | – | – |
| Others | 850 | – | – |
| | 9,995 | 527 | 92 |
| **Other countries MBS/ABS** | | | |
| Residential mortgage-backed | 1,860 | 15 | – |
| Commercial mortgage-backed | 81 | – | – |
| | 1,941 | 15 | – |
| Total MBS/ABS | 11,936 | 542 | 92 |

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Increase in fair value taken to available-for-sale securities reserve on MBS/ABS for the period/year (net of reversal of impairment allowances taken to income statement excluding deferred tax impact) | **68** | 53 |
| Closing balance of available-for-sale securities reserve relating to MBS/ABS (excluding deferred tax impact) | **31** | (37) |

## 3. Financial risk management (continued)

### 3.1 Credit Risk (continued)

#### (C) Debt securities (continued)

*MBS/ABS (continued)*

The tables below represent an analysis of net (reversal)/charge of impairment allowances for the period/year for MBS/ABS held as at 30 June 2011 and 31 December 2010.

| | At 30 June 2011 | | | | | |
|---|---|---|---|---|---|---|
| | 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 | **(4)** | **–** | **(1)** | **–** | **–** | **(5)** |
| – Prime | **–** | **–** | **(1)** | **(2)** | **–** | **(3)** |
| Total MBS/ABS | **(4)** | **–** | **(2)** | **(2)** | **–** | **(8)** |

| | At 31 December 2010 | | | | | |
|---|---|---|---|---|---|---|
| | 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 | (16) | (2) | – | – | – | (18) |
| – Alt-A | – | (2) | (4) | – | – | (6) |
| – Prime | (4) | – | 5 | (2) | – | (1) |
| | (20) | (4) | 1 | (2) | – | (25) |
| **Other countries MBS/ABS** | | | | | | |
| Residential mortgage-backed | – | (4) | – | – | – | (4) |
| Total MBS/ABS | (20) | (8) | 1 | (2) | – | (29) |

Note: The net (reversal)/charge of impairment allowances for MBS/ABS disposed during the period/year is excluded.

## 3. Financial risk management (continued)

### *3.2 Market Risk*

#### (A) VAR

VAR refers to the core indicator used in managing the Group's market risk. It is a statistical method used to measure the maximum loss of trading book positions held by the bank over a target horizon with a given level of confidence. The Group adopts a uniform VAR calculation model, using the historical simulation approach and two years' historical data, to calculate VAR of the Group and subsidiaries over a one-day holding period with a 99% confidence level, and set up VAR limit of the Group and subsidiaries.

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

| | Year | At 30 June HK$'m | Minimum for the first half of year HK$'m | Maximum for the first half of year HK$'m | Average for the first half of year HK$'m |
|---|---|---|---|---|---|
| VAR for all market risk | 2011 | 13.0 | 6.8 | 14.6 | 9.6 |
| | 2010 | 7.4 | 6.9 | 15.7 | 10.5 |
| VAR for foreign exchange | 2011 | 9.6 | 1.9 | 12.8 | 6.3 |
| risk products | 2010 | 5.6 | 2.3 | 11.2 | 5.2 |
| VAR for interest rate risk | 2011 | 7.5 | 5.1 | 9.4 | 7.5 |
| products | 2010 | 6.0 | 5.1 | 13.6 | 8.7 |
| VAR for equity risk products | 2011 | 0.1 | 0.0 | 0.4 | 0.1 |
| | 2010 | 0.0 | 0.0 | 1.7 | 0.3 |
| VAR for commodity risk | 2011 | 0.2 | 0.0 | 0.6 | 0.1 |
| products | 2010 | 0.0 | 0.0 | 0.2 | 0.0 |

In the first half of 2011, the average daily revenue[2] of BOCHK earned from market risk-related trading activities was HK$7.2 million (first half of 2010: HK$4.5 million).

Notes:

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 back-testing, 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, such as fee and commission. If back-testing revenues are negative and exceeding the VAR, a "back-testing exception" is noted. Generally speaking, the number of back-testing exceptions in a rolling 12-month period will not exceed four times. Back-testing results are reported to the Group's senior management, including the CE and CRO. BOCHK conducts back-testing of VAR measures on a monthly basis.

#### (B) Currency risk

The Group's assets and liabilities are denominated in major currencies, particularly the Hong Kong dollar, the US dollar and Renminbi. To ensure the currency risk exposure of the Group is kept to an acceptable level, risk limits (e.g. Position and VAR limit) are used to serve as a monitoring tool. Moreover, the Group seeks to minimise the gap between asset and liability in the same currency. Foreign exchange contracts (e.g. FX swap) are usually used to manage FX risk associated with foreign currency-denominated assets and liabilities.

## 3. Financial risk management (continued)

### *3.2 Market Risk (continued)*

**(B) Currency risk (continued)**

The tables below summarise the Group's exposure to foreign currency exchange rate risk as at 30 June 2011 and 31 December 2010. Included in the tables are the assets and liabilities at carrying amounts in HK$ equivalent, categorised by the original currency.

| | At 30 June 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 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 | 378,135 | 20,430 | 17,168 | 1,139 | 142 | 1,021 | 1,196 | 419,231 |
| Placements with banks and other financial institutions maturing between one and twelve months | 71,445 | 14,040 | 3,675 | 30 | 13 | 150 | 265 | 89,618 |
| Financial assets at fair value through profit or loss | 1,571 | 13,881 | 32,676 | 129 | – | – | 80 | 48,337 |
| Derivative financial instruments | 301 | 2,834 | 24,387 | 10 | – | – | 22 | 27,554 |
| Hong Kong SAR Government certificates of indebtedness | – | – | 54,460 | – | – | – | – | 54,460 |
| Advances and other accounts | 29,774 | 217,736 | 454,658 | 5,997 | 2,137 | 63 | 9,135 | 719,500 |
| Investment in securities | | | | | | | | |
| – Available-for-sale securities | 24,628 | 160,954 | 77,546 | 17,099 | 1,333 | 272 | 33,231 | 315,063 |
| – Held-to-maturity securities | 17,795 | 23,877 | 10,911 | 1,706 | 2,055 | 8 | 6,840 | 63,192 |
| – Loans and receivables | – | – | 4,004 | 1,431 | – | 9,688 | 258 | 15,381 |
| Interests in associates | – | – | 214 | – | – | – | – | 214 |
| Investment properties | 102 | – | 11,562 | – | – | – | – | 11,664 |
| Properties, plant and equipment | 436 | 1 | 35,673 | – | – | – | – | 36,110 |
| Other assets (including deferred tax assets) | 5,199 | 3,800 | 19,757 | 520 | 218 | 151 | 410 | 30,055 |
| **Total assets** | 529,386 | 457,553 | 746,691 | 28,061 | 5,898 | 11,353 | 51,437 | 1,830,379 |
| **Liabilities** | | | | | | | | |
| Hong Kong SAR currency notes in circulation | – | – | 54,460 | – | – | – | – | 54,460 |
| Deposits and balances from banks and other financial institutions | 272,183 | 70,045 | 35,043 | 578 | 170 | 34 | 8,851 | 386,904 |
| Financial liabilities at fair value through profit or loss | 28 | 192 | 4,436 | – | – | – | 219 | 4,875 |
| Derivative financial instruments | 282 | 3,328 | 19,707 | 485 | 1 | – | 137 | 23,940 |
| Deposits from customers | 218,795 | 208,140 | 608,788 | 15,086 | 1,427 | 15,798 | 35,401 | 1,103,435 |
| Debt securities in issue at amortised cost | – | – | 5 | – | – | – | – | 5 |
| Other accounts and provisions (including current and deferred tax liabilities) | 3,896 | 14,009 | 35,255 | 1,128 | 441 | 726 | 799 | 56,254 |
| Insurance contract liabilities | 6,181 | 6,646 | 30,218 | – | – | – | – | 43,045 |
| Subordinated liabilities | – | 20,399 | – | 7,439 | – | – | – | 27,838 |
| **Total liabilities** | 501,365 | 322,759 | 787,912 | 24,716 | 2,039 | 16,558 | 45,407 | 1,700,756 |
| Net on-balance sheet position | 28,021 | 134,794 | (41,221) | 3,345 | 3,859 | (5,205) | 6,030 | 129,623 |
| Off-balance sheet net notional position* | (15,970) | (127,470) | 156,177 | (3,353) | (3,867) | 5,245 | (5,944) | 4,818 |
| Contingent liabilities and commitments | 19,756 | 99,615 | 241,458 | 4,779 | 1,197 | 793 | 3,295 | 370,893 |

## 3. Financial risk management (continued)

### 3.2 Market Risk (continued)

#### (B) Currency risk (continued)

| | At 31 December 2010 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 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 | 369,368 | 18,084 | 22,058 | 2,762 | 657 | 1,884 | 999 | 415,812 |
| Placements with banks and other financial institutions maturing between one and twelve months | 8,886 | 22,840 | 6,279 | 42 | – | 144 | 1,308 | 39,499 |
| Financial assets at fair value through profit or loss | 1,560 | 16,413 | 51,716 | 112 | – | – | 75 | 69,876 |
| Derivative financial instruments | 122 | 2,540 | 21,144 | 18 | – | – | 30 | 23,854 |
| Hong Kong SAR Government certificates of indebtedness | – | – | 46,990 | – | – | – | – | 46,990 |
| Advances and other accounts | 25,299 | 190,935 | 413,767 | 5,447 | 1,260 | 53 | 8,663 | 645,424 |
| Investment in securities | | | | | | | | |
| – Available-for-sale securities | 15,279 | 155,583 | 46,438 | 22,876 | 4,421 | 1,767 | 40,080 | 286,444 |
| – Held-to-maturity securities | 6,577 | 28,811 | 11,567 | 1,743 | 2,028 | 15 | 7,643 | 58,384 |
| – Loans and receivables | – | 5,791 | 9,565 | – | – | – | – | 15,356 |
| Interests in associates | – | – | 212 | – | – | – | – | 212 |
| Investment properties | 96 | – | 10,246 | – | – | – | – | 10,342 |
| Properties, plant and equipment | 420 | – | 30,629 | – | – | – | – | 31,049 |
| Other assets (including deferred tax assets) | 2,200 | 404 | 14,916 | 77 | 89 | 40 | 72 | 17,798 |
| **Total assets** | 429,807 | 441,401 | 685,527 | 33,077 | 8,455 | 3,903 | 58,870 | 1,661,040 |
| **Liabilities** | | | | | | | | |
| Hong Kong SAR currency notes in circulation | – | – | 46,990 | – | – | – | – | 46,990 |
| Deposits and balances from banks and other financial institutions | 241,539 | 42,496 | 13,393 | 99 | 252 | 15 | 15,990 | 313,784 |
| Financial liabilities at fair value through profit or loss | – | 76 | 25,280 | – | – | – | 137 | 25,493 |
| Derivative financial instruments | 130 | 3,599 | 16,863 | 681 | 2 | – | 80 | 21,355 |
| Deposits from customers | 156,391 | 184,993 | 612,360 | 15,764 | 1,921 | 16,745 | 38,859 | 1,027,033 |
| Other accounts and provisions (including current and deferred tax liabilities) | 4,430 | 10,799 | 24,267 | 535 | 48 | 642 | 691 | 41,412 |
| Insurance contract liabilities | 2,761 | 6,963 | 30,083 | – | – | – | – | 39,807 |
| Subordinated liabilities | – | 20,029 | – | 6,848 | – | – | – | 26,877 |
| **Total liabilities** | 405,251 | 268,955 | 769,236 | 23,927 | 2,223 | 17,402 | 55,757 | 1,542,751 |
| Net on-balance sheet position | 24,556 | 172,446 | (83,709) | 9,150 | 6,232 | (13,499) | 3,113 | 118,289 |
| Off-balance sheet net notional position* | (17,769) | (165,279) | 192,604 | (9,078) | (6,290) | 13,368 | (3,256) | 4,300 |
| Contingent liabilities and commitments | 11,813 | 85,973 | 227,256 | 5,720 | 1,559 | 1,076 | 3,313 | 336,710 |

* 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.

## 3. Financial risk management (continued)

### *3.2 Market Risk (continued)*

#### (C) Interest rate risk

The tables below summarise the Group's exposure to interest rate risk as at 30 June 2011 and 31 December 2010. Included in the tables are the assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

| | At 30 June 2011 | | | | | | |
|---|---|---|---|---|---|---|---|
| | 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 | 413,624 | – | – | – | – | 5,607 | 419,231 |
| Placements with banks and other financial institutions maturing between one and twelve months | – | 34,369 | 55,249 | – | – | – | 89,618 |
| Financial assets at fair value through profit or loss | 6,741 | 6,986 | 2,452 | 12,984 | 13,525 | 5,649 | 48,337 |
| Derivative financial instruments | – | – | – | – | – | 27,554 | 27,554 |
| Hong Kong SAR Government certificates of indebtedness | – | – | – | – | – | 54,460 | 54,460 |
| Advances and other accounts | 531,932 | 128,908 | 41,466 | 12,418 | 111 | 4,665 | 719,500 |
| Investment in securities | | | | | | | |
| – Available-for-sale securities | 37,814 | 57,696 | 50,270 | 120,427 | 45,316 | 3,540 | 315,063 |
| – Held-to-maturity securities | 7,997 | 15,636 | 10,633 | 20,047 | 8,879 | – | 63,192 |
| – Loans and receivables | 2,856 | 1,206 | 11,319 | – | – | – | 15,381 |
| Interests in associates | – | – | – | – | – | 214 | 214 |
| Investment properties | – | – | – | – | – | 11,664 | 11,664 |
| Properties, plant and equipment | – | – | – | – | – | 36,110 | 36,110 |
| Other assets (including deferred tax assets) | – | – | – | – | – | 30,055 | 30,055 |
| **Total assets** | 1,000,964 | 244,801 | 171,389 | 165,876 | 67,831 | 179,518 | 1,830,379 |
| **Liabilities** | | | | | | | |
| Hong Kong SAR currency notes in circulation | – | – | – | – | – | 54,460 | 54,460 |
| Deposits and balances from banks and other financial institutions | 357,801 | 11,371 | 2,452 | – | – | 15,280 | 386,904 |
| Financial liabilities at fair value through profit or loss | 1,392 | 2,562 | 679 | 221 | 21 | – | 4,875 |
| Derivative financial instruments | – | – | – | – | – | 23,940 | 23,940 |
| Deposits from customers | 820,643 | 138,094 | 80,202 | 9,544 | – | 54,952 | 1,103,435 |
| Debt securities in issue at amortised cost | – | – | 5 | – | – | – | 5 |
| Other accounts and provisions (including current and deferred tax liabilities) | 11,824 | 648 | 1,832 | 479 | – | 41,471 | 56,254 |
| Insurance contract liabilities | – | – | – | – | – | 43,045 | 43,045 |
| Subordinated liabilities | – | – | 7,439 | – | 20,399 | – | 27,838 |
| **Total liabilities** | 1,191,660 | 152,675 | 92,609 | 10,244 | 20,420 | 233,148 | 1,700,756 |
| Interest sensitivity gap | (190,696) | 92,126 | 78,780 | 155,632 | 47,411 | (53,630) | 129,623 |

## 3. Financial risk management (continued)

### *3.2 Market Risk (continued)*

#### (C) Interest rate risk (continued)

| | At 31 December 2010 | | | | | | |
|---|---|---|---|---|---|---|---|
| | 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 | 409,210 | – | – | – | – | 6,602 | 415,812 |
| Placements with banks and other financial institutions maturing between one and twelve months | – | 19,346 | 20,153 | – | – | – | 39,499 |
| Financial assets at fair value through profit or loss | 3,439 | 30,225 | 3,638 | 14,214 | 13,275 | 5,085 | 69,876 |
| Derivative financial instruments | – | – | – | – | – | 23,854 | 23,854 |
| Hong Kong SAR Government certificates of indebtedness | – | – | – | – | – | 46,990 | 46,990 |
| Advances and other accounts | 513,018 | 92,528 | 27,356 | 7,659 | 119 | 4,744 | 645,424 |
| Investment in securities | | | | | | | |
| – Available-for-sale securities | 34,227 | 41,732 | 49,471 | 125,084 | 32,403 | 3,527 | 286,444 |
| – Held-to-maturity securities | 7,142 | 16,570 | 9,808 | 16,132 | 8,732 | – | 58,384 |
| – Loans and receivables | 5,791 | 3,402 | 6,163 | – | – | – | 15,356 |
| Interests in associates | – | – | – | – | – | 212 | 212 |
| Investment properties | – | – | – | – | – | 10,342 | 10,342 |
| Properties, plant and equipment | – | – | – | – | – | 31,049 | 31,049 |
| Other assets (including deferred tax assets) | – | – | – | – | – | 17,798 | 17,798 |
| **Total assets** | 972,827 | 203,803 | 116,589 | 163,089 | 54,529 | 150,203 | 1,661,040 |
| **Liabilities** | | | | | | | |
| Hong Kong SAR currency notes in circulation | – | – | – | – | – | 46,990 | 46,990 |
| Deposits and balances from banks and other financial institutions | 298,078 | 8,729 | 969 | – | – | 6,008 | 313,784 |
| Financial liabilities at fair value through profit or loss | 4,996 | 16,993 | 3,316 | 168 | 20 | – | 25,493 |
| Derivative financial instruments | – | – | – | – | – | 21,355 | 21,355 |
| Deposits from customers | 787,316 | 107,409 | 73,421 | 5,010 | – | 53,877 | 1,027,033 |
| Other accounts and provisions (including current and deferred tax liabilities) | 11,005 | 1,070 | 2,163 | 394 | – | 26,780 | 41,412 |
| Insurance contract liabilities | – | – | – | – | – | 39,807 | 39,807 |
| Subordinated liabilities | – | – | 6,848 | – | 20,029 | – | 26,877 |
| **Total liabilities** | 1,101,395 | 134,201 | 86,717 | 5,572 | 20,049 | 194,817 | 1,542,751 |
| Interest sensitivity gap | (128,568) | 69,602 | 29,872 | 157,517 | 34,480 | (44,614) | 118,289 |

## 3. Financial risk management (continued)

### *3.3 Liquidity Risk*

#### (A) Liquidity ratio

| | **Half-year ended 30 June 2011** | Half-year ended 30 June 2010 |
|---|---|---|
| Average liquidity ratio | **36.38%** | 37.81% |

The average liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio of BOCHK for the period.

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.

## 3. Financial risk management (continued)

### *3.3 Liquidity Risk (continued)*

#### (B) Maturity analysis

Tables below analyse assets and liabilities of the Group as at 30 June 2011 and 31 December 2010 into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

| | At 30 June 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 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 | 366,804 | 52,427 | – | – | – | – | – | 419,231 |
| Placements with banks and other financial institutions maturing between one and twelve months | – | – | 34,369 | 55,249 | – | – | – | 89,618 |
| Financial assets at fair value through profit or loss | | | | | | | | |
| – debt securities held for trading | | | | | | | | |
| – certificates of deposit held | – | 200 | 1,179 | – | 2 | – | – | 1,381 |
| – others | – | 6,550 | 5,011 | 1,029 | 2,880 | 5,003 | – | 20,473 |
| – debt securities designated at fair value through profit or loss | | | | | | | | |
| – certificates of deposit held | – | – | 430 | 22 | 1,312 | 490 | – | 2,254 |
| – others | – | 50 | 112 | 1,583 | 9,052 | 7,783 | – | 18,580 |
| – fund and equity securities | – | – | – | – | – | – | 5,649 | 5,649 |
| Derivative financial instruments | 22,709 | 552 | 471 | 684 | 1,433 | 1,705 | – | 27,554 |
| Hong Kong SAR Government certificates of indebtedness | 54,460 | – | – | – | – | – | – | 54,460 |
| Advances and other accounts | | | | | | | | |
| – advances to customers | 55,889 | 13,123 | 49,886 | 116,556 | 249,499 | 184,812 | 623 | 670,388 |
| – trade bills | 33 | 13,629 | 17,848 | 15,316 | 37 | – | – | 46,863 |
| – advances to banks and other financial institutions | – | 1 | 73 | 1,320 | 855 | – | – | 2,249 |
| Investment in securities | | | | | | | | |
| – debt securities held for available-for-sale | | | | | | | | |
| – certificates of deposit held | – | 1,450 | 4,591 | 11,807 | 15,316 | – | – | 33,164 |
| – others | – | 20,496 | 29,473 | 49,139 | 129,676 | 49,515 | 60 | 278,359 |
| – debt securities held for held-to-maturity | | | | | | | | |
| – certificates of deposit held | – | 444 | 1 | 804 | 2,675 | 161 | – | 4,085 |
| – others | – | 3,320 | 4,709 | 12,075 | 28,300 | 10,393 | 310 | 59,107 |
| – debt securities held for loans and receivables | – | 2,856 | 1,206 | 11,319 | – | – | – | 15,381 |
| – equity securities | – | – | – | – | – | – | 3,540 | 3,540 |
| Interests in associates | – | – | – | – | – | – | 214 | 214 |
| Investment properties | – | – | – | – | – | – | 11,664 | 11,664 |
| Properties, plant and equipment | – | – | – | – | – | – | 36,110 | 36,110 |
| Other assets (including deferred tax assets) | 6,862 | 17,730 | 28 | 253 | 4,200 | 888 | 94 | 30,055 |
| **Total assets** | 506,757 | 132,828 | 149,387 | 277,156 | 445,237 | 260,750 | 58,264 | 1,830,379 |

## 3. Financial risk management (continued)

### *3.3 Liquidity Risk (continued)*

#### (B) Maturity analysis (continued)

| | At 30 June 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 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 |
| **Liabilities** | | | | | | | | |
| Hong Kong SAR currency notes in circulation | 54,460 | – | – | – | – | – | – | 54,460 |
| Deposits and balances from banks and other financial institutions | 313,144 | 59,937 | 11,371 | 2,452 | – | – | – | 386,904 |
| Financial liabilities at fair value through profit or loss | | | | | | | | |
| – certificates of deposit issued | – | – | – | – | – | – | – | – |
| – others | – | 1,392 | 2,562 | 679 | 221 | 21 | – | 4,875 |
| Derivative financial instruments | 17,490 | 702 | 525 | 794 | 3,470 | 959 | – | 23,940 |
| Deposits from customers | 594,576 | 278,395 | 137,054 | 82,568 | 10,842 | – | – | 1,103,435 |
| Debt securities in issue at amortised cost | – | – | – | 5 | – | – | – | 5 |
| Other accounts and provisions (including current and deferred tax liabilities) | 28,102 | 16,254 | 778 | 5,247 | 5,873 | – | – | 56,254 |
| Insurance contract liabilities | 980 | 419 | 30 | 3,424 | 27,050 | 11,142 | – | 43,045 |
| Subordinated liabilities | – | – | 420 | 1 | – | 27,417 | – | 27,838 |
| **Total liabilities** | 1,008,752 | 357,099 | 152,740 | 95,170 | 47,456 | 39,539 | – | 1,700,756 |
| Net liquidity gap | (501,995) | (224,271) | (3,353) | 181,986 | 397,781 | 221,211 | 58,264 | 129,623 |

## 3. Financial risk management (continued)

### 3.3 Liquidity Risk (continued)

#### (B) Maturity analysis (continued)

| | At 31 December 2010 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 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 | 374,818 | 40,994 | – | – | – | – | – | 415,812 |
| Placements with banks and other financial institutions maturing between one and twelve months | – | – | 19,346 | 20,153 | – | – | – | 39,499 |
| Financial assets at fair value through profit or loss | | | | | | | | |
| – debt securities held for trading | | | | | | | | |
| – certificates of deposit held | – | – | 568 | 1,678 | 2 | – | – | 2,248 |
| – others | – | 3,209 | 27,603 | 2,628 | 3,179 | 5,054 | – | 41,673 |
| – debt securities designated at fair value through profit or loss | | | | | | | | |
| – certificates of deposit held | – | – | 118 | 422 | 1,316 | 474 | – | 2,330 |
| – others | – | 63 | 180 | 722 | 9,964 | 7,611 | – | 18,540 |
| – fund and equity securities | – | – | – | – | – | – | 5,085 | 5,085 |
| Derivative financial instruments | 19,539 | 507 | 509 | 1,080 | 1,167 | 1,052 | – | 23,854 |
| Hong Kong SAR Government certificates of indebtedness | 46,990 | – | – | – | – | – | – | 46,990 |
| Advances and other accounts | | | | | | | | |
| – advances to customers | 43,572 | 17,031 | 43,051 | 107,513 | 232,575 | 166,473 | 693 | 610,908 |
| – trade bills | 53 | 10,109 | 16,190 | 5,253 | – | – | – | 31,605 |
| – advances to banks and other financial institutions | – | 1 | 147 | 1,209 | 1,554 | – | – | 2,911 |
| Investment in securities | | | | | | | | |
| – debt securities held for available-for-sale | | | | | | | | |
| – certificates of deposit held | – | 303 | 501 | 11,577 | 11,248 | – | – | 23,629 |
| – others | – | 18,164 | 12,873 | 48,637 | 142,051 | 37,144 | 419 | 259,288 |
| – debt securities held for held-to-maturity | | | | | | | | |
| – certificates of deposit held | – | 3 | 41 | 1,280 | 2,910 | 366 | – | 4,600 |
| – others | – | 1,054 | 3,743 | 11,637 | 26,645 | 10,311 | 394 | 53,784 |
| – debt securities held for loans and receivables | – | 5,791 | 3,402 | 6,163 | – | – | – | 15,356 |
| – equity securities | – | – | – | – | – | – | 3,527 | 3,527 |
| Interests in associates | – | – | – | – | – | – | 212 | 212 |
| Investment properties | – | – | – | – | – | – | 10,342 | 10,342 |
| Properties, plant and equipment | – | – | – | – | – | – | 31,049 | 31,049 |
| Other assets (including deferred tax assets) | 4,609 | 10,744 | 6 | 211 | 2,125 | – | 103 | 17,798 |
| **Total assets** | 489,581 | 107,973 | 128,278 | 220,163 | 434,736 | 228,485 | 51,824 | 1,661,040 |

## 3. Financial risk management (continued)

### *3.3 Liquidity Risk (continued)*

#### (B) Maturity analysis (continued)

| | At 31 December 2010 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 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 |
| **Liabilities** | | | | | | | | |
| Hong Kong SAR currency notes in circulation | 46,990 | – | – | – | – | – | – | 46,990 |
| Deposits and balances from banks and other financial institutions | 260,453 | 43,633 | 8,729 | 969 | – | – | – | 313,784 |
| Financial liabilities at fair value through profit or loss | | | | | | | | |
| – certificates of deposit issued | – | – | – | – | – | – | – | – |
| – others | – | 4,996 | 16,994 | 3,316 | 167 | 20 | – | 25,493 |
| Derivative financial instruments | 14,706 | 1,040 | 495 | 1,287 | 3,082 | 745 | – | 21,355 |
| Deposits from customers | 599,586 | 239,253 | 107,982 | 74,014 | 6,198 | – | – | 1,027,033 |
| Other accounts and provisions (including current and deferred tax liabilities) | 22,967 | 8,579 | 1,829 | 3,237 | 4,800 | – | – | 41,412 |
| Insurance contract liabilities | 1,407 | 1,131 | 55 | 3,413 | 25,351 | 8,450 | – | 39,807 |
| Subordinated liabilities | – | – | 419 | 1 | – | 26,457 | – | 26,877 |
| **Total liabilities** | 946,109 | 298,632 | 136,503 | 86,237 | 39,598 | 35,672 | – | 1,542,751 |
| Net liquidity gap | (456,528) | (190,659) | (8,225) | 133,926 | 395,138 | 192,813 | 51,824 | 118,289 |

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 30 June 2011 and 31 December 2010.

# 3. Financial risk management (continued)

## *3.4 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 insurance products. For most of the insurance policies issued, the Group has a retention limit on any single life insured. The Group cedes the excess of the insured benefit over the limit for standard risks (from a medical point of view) to reinsurers under an excess of loss reinsurance arrangement. For some of the insurance liabilities dominated in Renminbi, the Group's insurance subsidiary has entered into another reinsurance arrangement that reinsures most of insurance 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, 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.

## *3.5 Capital Management*

The Group adopted the foundation internal ratings-based ("FIRB") approach to calculate credit risk and standardised (credit risk) ("STC") approach for certain credit exposures being exempted from FIRB effective from 1 January 2011. The market risk of the Group mainly sourced from BOCHK. BOCHK adopted the internal models approach ("IMM") to calculate general market risk for interest rate and exchange rate exposures effective from 1 April 2011 while the Group continued to adopt the standardised (market risk) ("STM") approach to calculate the remaining market risk. In addition, the Group continued to adopt the standardised (operational risk) ("STO") approach for operational risk. The Group's capital adequacy ratio was calculated based on the various risk measurement approaches above.

The Group adopted the STC approach and STM approach to calculate credit risk and market risk respectively as at 31 December 2010. As a result of the change in the basis used, the amounts shown below are not directly comparable.

### (A) Capital adequacy ratio

| | **At 30 June 2011** | At 31 December 2010 |
|---|---|---|
| Capital adequacy ratio | **17.62%** | 16.14% |
| Core capital ratio | **12.87%** | 11.29% |

## 3. Financial risk management (continued)

### *3.5 Capital Management (continued)*

**(A) Capital adequacy ratio (continued)**

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 122.

**(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 30 June 2011 and 31 December 2010 and reported to the HKMA is analysed as follows:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Core capital: | | |
| Paid up ordinary share capital | **43,043** | 43,043 |
| Reserves | **32,509** | 28,475 |
| Profit and loss account | **6,401** | 5,332 |
| Non-controlling interests | **1,610** | 1,425 |
| | **83,563** | 78,275 |
| Deductions from core capital | **(791)** | (332) |
| Core capital | **82,772** | 77,943 |
| Supplementary capital: | | |
| Fair value gains arising from holdings of available-for-sale securities | **931** | 588 |
| Fair value gains arising from holdings of securities designated at fair value through profit or loss | **35** | 29 |
| Collective loan impairment allowances | **92** | 1,985 |
| Regulatory reserve | **247** | 5,076 |
| Surplus provisions | **3,232** | – |
| Term subordinated debt | **26,810** | 26,198 |
| | **31,347** | 33,876 |
| Deductions from supplementary capital | **(791)** | (332) |
| Supplementary capital | **30,556** | 33,544 |
| Total capital base after deductions | **113,328** | 111,487 |

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 pages 119 to 122. Investment costs in such subsidiaries are deducted from the capital base.

Term subordinated debt represents subordinated liabilities qualified as Tier 2 Capital of BOCHK pursuant to the regulatory requirements of the HKMA.

## 4. Net interest income

| | Half-year ended 30 June 2011 HK$'m | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| **Interest income** | | |
| Due from banks and other financial institutions | **3,760** | 996 |
| Advances to customers | **6,306** | 5,419 |
| Listed investments | **2,240** | 1,934 |
| Unlisted investments | **2,708** | 2,233 |
| Others | **142** | 89 |
| | **15,156** | 10,671 |
| **Interest expense** | | |
| Due to banks and other financial institutions | **(1,949)** | (303) |
| Deposits from customers | **(2,636)** | (1,068) |
| Subordinated liabilities | **(283)** | (275) |
| Others | **(83)** | (61) |
| | **(4,951)** | (1,707) |
| **Net interest income** | **10,205** | 8,964 |

Included within interest income is HK$1 million (first half of 2010: HK$5 million) of interest with respect to income recognised on advances classified as impaired for the first half of 2011. Interest income accrued on impaired investment in securities amounted to HK$10 million (first half of 2010: HK$50 million).

Included within interest income and interest expense are HK$15,113 million (first half of 2010: HK$10,593 million) and HK$5,253 million (first half of 2010: HK$1,906 million), before hedging effect, for financial assets and financial liabilities that are not recognised at fair value through profit or loss respectively.

## 5. Net fee and commission income

| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| **Fee and commission income** | | |
| Securities brokerage | **1,485** | 1,509 |
| Credit cards | **1,189** | 903 |
| Insurance | **610** | 220 |
| Loan commissions | **588** | 623 |
| Bills commissions | **418** | 371 |
| Payment services | **303** | 272 |
| Currency exchange | **224** | 125 |
| Funds distribution | **176** | 67 |
| Trust services | **123** | 98 |
| Safe deposit box | **107** | 103 |
| Others | **209** | 190 |
| | **5,432** | 4,481 |
| **Fee and commission expense** | | |
| Credit cards | **(950)** | (668) |
| Securities brokerage | **(234)** | (234) |
| Payment services | **(44)** | (42) |
| Others | **(218)** | (140) |
| | **(1,446)** | (1,084) |
| **Net fee and commission income** | **3,986** | 3,397 |
| Of which arise from | | |
| – financial assets or financial liabilities not at fair value through profit or loss | | |
| – Fee and commission income | **690** | 725 |
| – Fee and commission expense | **(1)** | (4) |
| | **689** | 721 |
| – trust and other fiduciary activities | | |
| – Fee and commission income | **249** | 213 |
| – Fee and commission expense | **(3)** | (3) |
| | **246** | 210 |

## 6. Net trading gain/(loss)

| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Net gain/(loss) from: | | |
| – foreign exchange and foreign exchange products | **662** | 350 |
| – interest rate instruments and items under fair value hedge | **(4)** | (424) |
| – equity instruments | **32** | (20) |
| – commodities | **71** | 58 |
| | **761** | (36) |

## 7. Net gain on investment in securities

| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Net gain from disposal of available-for-sale securities | **359** | 404 |
| Net gain from redemption of held-to-maturity securities | **1** | – |
| | **360** | 404 |

## 8. Other operating income

| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Dividend income from investment in securities | | |
| – listed investments | **48** | 41 |
| – unlisted investments | **14** | 13 |
| Gross rental income from investment properties | **184** | 164 |
| Less: Outgoings in respect of investment properties | **(41)** | (30) |
| Others | **40** | 61 |
| | **245** | 249 |

Included in the "Outgoings in respect of investment properties" is HK$4 million (first half of 2010: HK$7 million) of direct operating expenses related to investment properties that were not let during the period.

## 9. Gross insurance benefits and claims

| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Claims, benefits and surrenders paid | **3,866** | 2,239 |
| Movement in liabilities | **3,234** | 1,641 |
| | **7,100** | 3,880 |

## 10. Net (charge)/reversal of impairment allowances

| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| **Advances to customers** | | |
| Individually assessed | | |
| – new allowances | **(79)** | (46) |
| – releases | **121** | 102 |
| – recoveries | **204** | 277 |
| Net reversal of individually assessed loan impairment allowances | **246** | 333 |
| Collectively assessed | | |
| – new allowances | **(357)** | (265) |
| – releases | **62** | 9 |
| – recoveries | **12** | 17 |
| Net charge of collectively assessed loan impairment allowances | **(283)** | (239) |
| Net (charge)/reversal of loan impairment allowances | **(37)** | 94 |
| **Available-for-sale securities** | | |
| Net reversal of impairment allowances on available-for-sale securities | | |
| – Individually assessed | **6** | 40 |
| **Held-to-maturity securities** | | |
| Net reversal of impairment allowances on held-to-maturity securities | | |
| – Individually assessed | **6** | 32 |
| **Others** | **(5)** | (5) |
| **Net (charge)/reversal of impairment allowances** | **(30)** | 161 |

## 11. Operating expenses

| | Half-year ended 30 June 2011 HK$'m | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Staff costs (including directors' emoluments) | | |
| – salaries and other costs | **2,529** | 2,332 |
| – pension cost | **211** | 194 |
| | **2,740** | 2,526 |
| Premises and equipment expenses (excluding depreciation) | | |
| – rental of premises | **286** | 249 |
| – information technology | **178** | 183 |
| – others | **146** | 142 |
| | **610** | 574 |
| Depreciation | **614** | 556 |
| Auditor's remuneration | | |
| – audit services | **4** | 4 |
| – non-audit services | **2** | 6 |
| Lehman Brothers related products* | **(2,835)** | 77 |
| Other operating expenses | **858** | 791 |
| | **1,993** | 4,534 |

* Including the net amount of HK$2,854 million recovered by the Group from the underlying collateral of the Minibonds, after deducting the ex gratia payments and provision for trustee expenses (Note 2).

## 12. Net gain from disposal of/fair value adjustments on investment properties

| | Half-year ended 30 June 2011 HK$'m | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Net gain on fair value adjustments on investment properties | **1,486** | 601 |

## 13. Net loss from disposal/revaluation of properties, plant and equipment

| | Half-year ended 30 June 2011 HK$'m | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Net loss on disposal of other fixed assets | **(7)** | (2) |
| Net gain on revaluation of premises | **2** | 1 |
| | **(5)** | (1) |

## 14. Taxation

Taxation in the condensed consolidated income statement represents:

| | **Half-year ended 30 June 2011 HK$'m** | (Restated) Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Hong Kong profits tax | | |
| Current tax | | |
| – current period taxation | **2,168** | 1,341 |
| Deferred tax (credit)/charge | **(76)** | 18 |
| Hong Kong profits tax | **2,092** | 1,359 |
| Overseas taxation | **141** | 53 |
| | **2,233** | 1,412 |

Hong Kong profits tax has been provided at the rate of 16.5% (2010: 16.5%) on the estimated assessable profits arising in Hong Kong for the first half of 2011. Taxation on overseas profits has been calculated on the estimated assessable profits for the first half of 2011 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:

| | **Half-year ended 30 June 2011 HK$'m** | (Restated) Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Profit before taxation | **14,587** | 8,767 |
| Calculated at a taxation rate of 16.5% (2010: 16.5%) | **2,407** | 1,447 |
| Effect of different taxation rates in other countries | **17** | 14 |
| Income not subject to taxation | **(269)** | (99) |
| Expenses not deductible for taxation purposes | **108** | 47 |
| Tax losses not recognised | **2** | 3 |
| Utilisation of previously unrecognised tax losses | **(32)** | – |
| Taxation charge | **2,233** | 1,412 |
| Effective tax rate | **15.3%** | 16.1% |

## 15. Dividends

| | Half-year ended 30 June 2011 | | Half-year ended 30 June 2010 | |
|---|---|---|---|---|
| | **Per share HK$** | **Total HK$'m** | Per share HK$ | Total HK$'m |
| Interim dividend | **0.63** | **6,661** | 0.40 | 4,229 |

At a meeting held on 24 August 2011, the Board declared an interim dividend of HK$0.63 per ordinary share for the first half of 2011 amounting to approximately HK$6,661 million. This declared dividend is not reflected as a dividend payable in this interim financial information, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2011.

## 16. 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 first half of 2011 of approximately HK$11,993 million (first half of 2010: HK$7,192 million) and on the ordinary shares in issue of 10,572,780,266 shares (2010: 10,572,780,266 ordinary shares).

There was no dilution of earnings per share as no potential ordinary shares were in issue for the first half of 2011 (first half of 2010: Nil).

## 17. 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 10 years of service, or at a scale ranging from 30% to 90% for employees who have completed between 3 to 10 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 first half of 2011 amounted to approximately HK$161 million (first half of 2010: approximately HK$155 million), after a deduction of forfeited contributions of approximately HK$2.5 million (first half of 2010: approximately HK$5.9 million). For the MPF Scheme, the Group contributed approximately HK$25 million (first half of 2010: approximately HK$22 million) for the first half of 2011.

## 18. 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 first half of 2011 (first half of 2010: 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.

## 18. Share option schemes (continued)

### *(b) Pre-Listing Share Option Scheme (continued)*

Details of the share options outstanding as at 30 June 2011 and 31 December 2010 are disclosed as follows:

| | Directors | Senior management | Total number of share options | Average exercise price (HK$ per share) |
|---|---|---|---|---|
| At 1 January 2011 and at 30 June 2011 | **3,976,500** | **247,300** | **4,223,800** | **8.5** |
| Exercisable at 30 June 2011 | **3,976,500** | **247,300** | **4,223,800** | **8.5** |
| At 1 January 2010 | 3,976,500 | 1,074,300 | 5,050,800 | 8.5 |
| Less: Share options exercised during the year | – | (827,000) | (827,000) | 8.5 |
| At 31 December 2010 | 3,976,500 | 247,300 | 4,223,800 | 8.5 |
| Exercisable at 31 December 2010 | 3,976,500 | 247,300 | 4,223,800 | 8.5 |

No share options were exercised during the period. Share options were exercised on a regular basis throughout the year of 2010 and its weighted average share price was HK$22.73.

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.

## 19. Cash and balances with banks and other financial institutions

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Cash | **4,558** | 4,571 |
| Balances with central banks | **321,945** | 336,923 |
| Balances with banks and other financial institutions | **40,301** | 33,324 |
| Placements with banks and other financial institutions maturing within one month | **52,427** | 40,994 |
| | **419,231** | 415,812 |

## 20. Financial assets at fair value through profit or loss

| | Trading securities | | Financial assets designated at fair value through profit or loss | | Total | |
|---|---|---|---|---|---|---|
| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
| At fair value | | | | | | |
| Debt securities | | | | | | |
| – Listed in Hong Kong | **2,030** | 1,398 | **794** | 829 | **2,824** | 2,227 |
| – Listed outside Hong Kong | **5,185** | 5,188 | **2,897** | 3,253 | **8,082** | 8,441 |
| | **7,215** | 6,586 | **3,691** | 4,082 | **10,906** | 10,668 |
| – Unlisted | **14,639** | 37,335 | **17,143** | 16,788 | **31,782** | 54,123 |
| | **21,854** | 43,921 | **20,834** | 20,870 | **42,688** | 64,791 |
| Fund | | | | | | |
| – Unlisted | **–** | – | **2,958** | 3,028 | **2,958** | 3,028 |
| Equity securities | | | | | | |
| – Listed in Hong Kong | **31** | 38 | **2,329** | 1,810 | **2,360** | 1,848 |
| – Listed outside Hong Kong | **–** | – | **200** | 112 | **200** | 112 |
| – Unlisted | **131** | 97 | **–** | – | **131** | 97 |
| | **162** | 135 | **2,529** | 1,922 | **2,691** | 2,057 |
| Total | **22,016** | 44,056 | **26,321** | 25,820 | **48,337** | 69,876 |

Financial assets at fair value through profit or loss are analysed by type of issuer as follows:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Sovereigns | **14,322** | 35,223 |
| Public sector entities* | **281** | 302 |
| Banks and other financial institutions | **24,003** | 25,135 |
| Corporate entities | **9,731** | 9,216 |
| | **48,337** | 69,876 |

* Included financial assets at fair value through profit or loss of HK$237 million (31 December 2010: HK$258 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

## 20. Financial assets at fair value through profit or loss (continued)

Financial assets at fair value through profit or loss are analysed as follows:

| | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|
| Treasury bills | **11,378** | 32,840 |
| Certificates of deposit held | **3,635** | 4,578 |
| Other financial assets at fair value through profit or loss | **33,324** | 32,458 |
| | **48,337** | 69,876 |

## 21. Derivative financial instruments

The Group enters into the following foreign exchange, interest rate, precious metal and equity related derivative financial instrument contracts 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 (for example, cross-currency interest rate swaps). Except for certain currency swap contracts, no exchange of principal takes place.

Foreign currency, interest rate, precious metal and equity 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 condensed 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 foreign exchange rates, market interest rates, metal prices or equity prices relative to their terms. The aggregate fair values of derivative financial instruments assets and liabilities can fluctuate significantly from time to time.

## 21. Derivative financial instruments (continued)

The following tables summarise the contract/notional amounts of each significant type of derivative financial instrument as at 30 June 2011 and 31 December 2010:

| | At 30 June 2011 | | | |
|---|---|---|---|---|
| | Trading HK$'m | Hedging HK$'m | Not qualified for hedge accounting* HK$'m | Total HK$'m |
| Exchange rate contracts | | | | |
| Spot and forwards | 333,433 | – | 321 | 333,754 |
| Swaps | 310,258 | 4,442 | 4,086 | 318,786 |
| Foreign currency options | | | | |
| – Options purchased | 3,006 | – | – | 3,006 |
| – Options written | 3,227 | – | – | 3,227 |
| | 649,924 | 4,442 | 4,407 | 658,773 |
| Interest rate contracts | | | | |
| Futures | 4,047 | – | – | 4,047 |
| Swaps | 344,942 | 12,313 | 3,432 | 360,687 |
| Interest rate options | | | | |
| – Swaptions purchased | 1,006 | – | – | 1,006 |
| – Swaptions written | 506 | – | – | 506 |
| | 350,501 | 12,313 | 3,432 | 366,246 |
| Bullion contracts | 13,585 | – | – | 13,585 |
| Equity contracts | 112 | – | – | 112 |
| Other contracts | 89 | – | – | 89 |
| Total | 1,014,211 | 16,755 | 7,839 | 1,038,805 |

* 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.

## 21. Derivative financial instruments (continued)

| | At 31 December 2010 | | | |
|---|---|---|---|---|
| | Trading HK$'m | Hedging HK$'m | Not qualified for hedge accounting HK$'m | Total HK$'m |
| Exchange rate contracts | | | | |
| Spot and forwards | 332,032 | – | 111 | 332,143 |
| Swaps | 310,451 | 4,437 | 2,993 | 317,881 |
| Foreign currency options | | | | |
| – Options purchased | 1,543 | – | – | 1,543 |
| – Options written | 2,601 | – | – | 2,601 |
| | 646,627 | 4,437 | 3,104 | 654,168 |
| Interest rate contracts | | | | |
| Futures | 7,735 | – | – | 7,735 |
| Swaps | 266,326 | 46,345 | 3,144 | 315,815 |
| | 274,061 | 46,345 | 3,144 | 323,550 |
| Bullion contracts | 13,761 | – | – | 13,761 |
| Equity contracts | 145 | – | – | 145 |
| Other contracts | 99 | – | – | 99 |
| Total | 934,693 | 50,782 | 6,248 | 991,723 |

## 21. Derivative financial instruments (continued)

The following tables summarise the fair values of each class of derivative financial instrument as at 30 June 2011 and 31 December 2010:

| | At 30 June 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 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 | 22,386 | – | 2 | 22,388 | (17,400) | – | (1) | (17,401) |
| Swaps | 739 | 68 | 78 | 885 | (960) | (72) | (79) | (1,111) |
| Foreign currency options | | | | | | | | |
| – Options purchased | 10 | – | – | 10 | – | – | – | – |
| – Options written | – | – | – | – | (12) | – | – | (12) |
| | 23,135 | 68 | 80 | 23,283 | (18,372) | (72) | (80) | (18,524) |
| Interest rate contracts | | | | | | | | |
| Futures | 1 | – | – | 1 | (3) | – | – | (3) |
| Swaps | 3,227 | 3 | 1 | 3,231 | (4,027) | (535) | (108) | (4,670) |
| Interest rate options | | | | | | | | |
| – Swaptions purchased | 10 | – | – | 10 | – | – | – | – |
| – Swaptions written | – | – | – | – | (14) | – | – | (14) |
| | 3,238 | 3 | 1 | 3,242 | (4,044) | (535) | (108) | (4,687) |
| Bullion contracts | 1,027 | – | – | 1,027 | (728) | – | – | (728) |
| Equity contracts | 2 | – | – | 2 | (1) | – | – | (1) |
| Total | 27,402 | 71 | 81 | 27,554 | (23,145) | (607) | (188) | (23,940) |

## 21. Derivative financial instruments (continued)

| | At 31 December 2010 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 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 | 19,376 | – | 1 | 19,377 | (14,673) | – | – | (14,673) |
| Swaps | 843 | 56 | 63 | 962 | (1,315) | (74) | (83) | (1,472) |
| Foreign currency options | | | | | | | | |
| – Options purchased | 11 | – | – | 11 | – | – | – | – |
| – Options written | – | – | – | – | (12) | – | – | (12) |
| | 20,230 | 56 | 64 | 20,350 | (16,000) | (74) | (83) | (16,157) |
| Interest rate contracts | | | | | | | | |
| Futures | – | – | – | – | (3) | – | – | (3) |
| Swaps | 1,592 | 869 | 1 | 2,462 | (2,339) | (1,842) | (114) | (4,295) |
| | 1,592 | 869 | 1 | 2,462 | (2,342) | (1,842) | (114) | (4,298) |
| Bullion contracts | 1,040 | – | – | 1,040 | (899) | – | – | (899) |
| Equity contracts | 2 | – | – | 2 | (1) | – | – | (1) |
| Total | 22,864 | 925 | 65 | 23,854 | (19,242) | (1,916) | (197) | (21,355) |

The credit risk weighted amounts of the above derivative financial instruments are as follows:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Exchange rate contracts | | |
| Forwards | **2,069** | 1,938 |
| Swaps | **975** | 1,365 |
| Foreign currency options | | |
| – Options purchased | **1** | – |
| Interest rate contracts | | |
| Swaps | **1,071** | 1,165 |
| Interest rate options | | |
| – Swaptions purchased | **3** | – |
| Bullion contracts | **25** | 2 |
| | **4,144** | 4,470 |

## 21. Derivative financial instruments (continued)

The credit risk weighted amounts are calculated in accordance with the Banking (Capital) Rules. The amounts are dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

The Group adopted the FIRB approach to calculate credit risk as at 30 June 2011, as opposed to the STC approach that was used as at 31 December 2010. As a result of the change in the basis used, the risk weighted amounts shown above are not directly comparable.

There is no effect of valid bilateral netting agreement on the fair values or the credit risk weighted amounts of the derivative financial instruments.

## 22. Advances and other accounts

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Personal loans and advances | **210,458** | 187,000 |
| Corporate loans and advances | **462,400** | 426,219 |
| Advances to customers* | **672,858** | 613,219 |
| Loan impairment allowances | | |
| – Individually assessed | **(249)** | (326) |
| – Collectively assessed | **(2,221)** | (1,985) |
| | **670,388** | 610,908 |
| Trade bills | **46,863** | 31,605 |
| Advances to banks and other financial institutions | **2,249** | 2,911 |
| Total | **719,500** | 645,424 |

As at 30 June 2011, advances to customers included accrued interest of HK$1,066 million (31 December 2010: HK$886 million).

As at 30 June 2011 and 31 December 2010, no impairment allowance was made in respect of trade bills and advances to banks and other financial institutions.

* Included advances to customers denominated in HK dollars of HK$453,703 million (31 December 2010: HK$415,585 million) and US dollars equivalent to HK$177,471 million (31 December 2010: HK$159,766 million).

## 23. Investment in securities

| | | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|---|
| **(a)** | **Available-for-sale securities** | | |
| | Debt securities, at fair value | | |
| | – Listed in Hong Kong | **10,990** | 10,176 |
| | – Listed outside Hong Kong | **112,934** | 111,966 |
| | | **123,924** | 122,142 |
| | – Unlisted | **187,599** | 160,775 |
| | | **311,523** | 282,917 |
| | Equity securities, at fair value | | |
| | – Listed in Hong Kong | **2,909** | 2,971 |
| | – Unlisted | **631** | 556 |
| | | **3,540** | 3,527 |
| | | **315,063** | 286,444 |
| **(b)** | **Held-to-maturity securities** | | |
| | Listed, at amortised cost | | |
| | – in Hong Kong | **1,167** | 1,121 |
| | – outside Hong Kong | **16,947** | 19,296 |
| | | **18,114** | 20,417 |
| | Unlisted, at amortised cost | **45,110** | 38,016 |
| | | **63,224** | 58,433 |
| | Impairment allowances | **(32)** | (49) |
| | | **63,192** | 58,384 |
| **(c)** | **Loans and receivables** | | |
| | Unlisted, at amortised cost | **15,381** | 15,356 |
| **Total** | | **393,636** | 360,184 |
| Market value of listed held-to-maturity securities | | **18,269** | 20,414 |

## 23. Investment in securities (continued)

Investment in securities is analysed by type of issuer as follows:

| | At 30 June 2011 | | | |
|---|---|---|---|---|
| | **Available-for-sale securities HK$'m** | **Held-to-maturity securities HK$'m** | **Loans and receivables HK$'m** | **Total HK$'m** |
| Sovereigns | **80,206** | **21,248** | **–** | **101,454** |
| Public sector entities* | **39,341** | **8,611** | **–** | **47,952** |
| Banks and other financial institutions | **173,926** | **29,155** | **15,381** | **218,462** |
| Corporate entities | **21,590** | **4,178** | **–** | **25,768** |
| | **315,063** | **63,192** | **15,381** | **393,636** |

| | At 31 December 2010 | | | |
|---|---|---|---|---|
| | Available-for-sale securities HK$'m | Held-to-maturity securities HK$'m | Loans and receivables HK$'m | Total HK$'m |
| Sovereigns | 73,394 | 10,507 | – | 83,901 |
| Public sector entities* | 32,975 | 7,741 | – | 40,716 |
| Banks and other financial institutions | 165,201 | 34,647 | 15,356 | 215,204 |
| Corporate entities | 14,874 | 5,489 | – | 20,363 |
| | 286,444 | 58,384 | 15,356 | 360,184 |

* Included available-for-sale securities of HK$24,201 million (31 December 2010: HK$15,973 million) and held-to-maturity securities of HK$1,971 million (31 December 2010: HK$822 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

Available-for-sale and held-to-maturity securities are analysed as follows:

| | **Available-for-sale securities** | | **Held-to-maturity securities** | |
|---|---|---|---|---|
| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
| Treasury bills | **39,956** | 23,847 | **9,681** | 5,037 |
| Certificates of deposit held | **33,164** | 23,629 | **4,085** | 4,600 |
| Others | **241,943** | 238,968 | **49,426** | 48,747 |
| | **315,063** | 286,444 | **63,192** | 58,384 |

## 24. Investment properties

| | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|
| At 1 January | **10,342** | 9,364 |
| Additions | **12** | 2 |
| Disposals | **(6)** | (171) |
| Fair value gains | **1,486** | 1,511 |
| Reclassification to properties, plant and equipment (Note 25) | **(171)** | (365) |
| Exchange difference | **1** | 1 |
| At period/year end | **11,664** | 10,342 |

## 25. Properties, plant and equipment

| | Premises HK$'m | Equipment, fixtures and fittings HK$'m | Total HK$'m |
|---|---|---|---|
| Net book value at 1 January 2011 | **28,581** | **2,468** | **31,049** |
| Additions | **24** | **231** | **255** |
| Disposals | **(4)** | **(8)** | **(12)** |
| Revaluation | **5,254** | **–** | **5,254** |
| Depreciation for the period (Note 11) | **(283)** | **(331)** | **(614)** |
| Reclassification from investment properties (Note 24) | **171** | **–** | **171** |
| Exchange difference | **4** | **3** | **7** |
| Net book value at 30 June 2011 | **33,747** | **2,363** | **36,110** |
| At 30 June 2011 | | | |
| Cost or valuation | **33,747** | **7,019** | **40,766** |
| Accumulated depreciation and impairment | **–** | **(4,656)** | **(4,656)** |
| Net book value at 30 June 2011 | **33,747** | **2,363** | **36,110** |
| Net book value at 1 January 2010 | 23,701 | 2,585 | 26,286 |
| Additions | 92 | 596 | 688 |
| Disposals | (106) | (11) | (117) |
| Revaluation | 4,946 | – | 4,946 |
| Depreciation for the year | (484) | (647) | (1,131) |
| Reclassification from/(to) investment properties (Note 24) | 378 | (13) | 365 |
| Transfer | 47 | (47) | – |
| Exchange difference | 7 | 5 | 12 |
| Net book value at 31 December 2010 | 28,581 | 2,468 | 31,049 |
| At 31 December 2010 | | | |
| Cost or valuation | 28,581 | 6,859 | 35,440 |
| Accumulated depreciation and impairment | – | (4,391) | (4,391) |
| Net book value at 31 December 2010 | 28,581 | 2,468 | 31,049 |

## 25. Properties, plant and equipment (continued)

The analysis of cost or valuation of the above assets is as follows:

| | Premises HK$'m | Equipment, fixtures and fittings HK$'m | Total HK$'m |
|---|---|---|---|
| At 30 June 2011 | | | |
| At cost | **–** | **7,019** | **7,019** |
| At valuation | **33,747** | **–** | **33,747** |
| | **33,747** | **7,019** | **40,766** |
| At 31 December 2010 | | | |
| At cost | – | 6,859 | 6,859 |
| At valuation | 28,581 | – | 28,581 |
| | 28,581 | 6,859 | 35,440 |

## 26. Other assets

| | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|
| Repossessed assets | **71** | 81 |
| Precious metals | **4,617** | 3,664 |
| Reinsurance assets | **4,988** | 2,158 |
| Accounts receivable and prepayments | **20,232** | 11,738 |
| | **29,908** | 17,641 |

## 27. Financial liabilities at fair value through profit or loss

| | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|
| Trading liabilities | | |
| – Short positions in Exchange Fund Bills and Notes | **4,306** | 25,259 |
| Financial liabilities designated at fair value through profit or loss | | |
| – Structured deposits (Note 28) | **569** | 234 |
| | **4,875** | 25,493 |

The carrying amount of financial liabilities designated at fair value through profit or loss as at 30 June 2011 is more than the amount that the Group would be contractually required to pay at maturity to the holders by HK$2 million (31 December 2010: HK$2 million). The amount of change in the fair values of financial liabilities at fair value through profit or loss, during the period and cumulatively, attributable to changes in credit risk is insignificant.

## 28. Deposits from customers

| | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|
| Current, savings and other deposit accounts (per condensed consolidated balance sheet) | **1,103,435** | 1,027,033 |
| Structured deposits reported as financial liabilities at fair value through profit or loss (Note 27) | **569** | 234 |
| | **1,104,004** | 1,027,267 |
| Analysed by: | | |
| Demand deposits and current accounts | | |
| – corporate | **55,726** | 54,660 |
| – personal | **14,893** | 15,793 |
| | **70,619** | 70,453 |
| Savings deposits | | |
| – corporate | **168,111** | 158,284 |
| – personal | **354,861** | 369,751 |
| | **522,972** | 528,035 |
| Time, call and notice deposits | | |
| – corporate | **303,714** | 235,283 |
| – personal | **206,699** | 193,496 |
| | **510,413** | 428,779 |
| | **1,104,004** | 1,027,267 |

## 29. Other accounts and provisions

| | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|
| Other accounts payable | **47,505** | 35,284 |
| Provisions | **337** | 196 |
| | **47,842** | 35,480 |

## 30. Assets pledged as security

As at 30 June 2011, liabilities of the Group amounting to HK$5,450 million (31 December 2010: HK$23,832 million) were secured by assets deposited with central depositories to facilitate settlement operations. In addition, the liabilities of the Group amounting to HK$42,621 million (31 December 2010: HK$14,071 million) were secured by debt securities related to sale and repurchase arrangements. The amount of assets pledged by the Group to secure these liabilities was HK$48,338 million (31 December 2010: HK$37,932 million) included in "Trading securities" and "Available-for-sale securities".

## 31. 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 this interim financial information in accordance with HKAS 12 "Income Taxes".

The major components of deferred tax (assets)/liabilities recorded in the condensed consolidated balance sheet, and the movements during the first half of 2011 and the year ended 31 December 2010 which have shown the impact of the early adoption of HKAS 12 (Amendment) "Income Taxes", are as follows:

| | **At 30 June 2011** | | | | | |
|---|---|---|---|---|---|---|
| | **Accelerated tax depreciation HK$'m** | **Property revaluation HK$'m** | **Losses HK$'m** | **Impairment allowance HK$'m** | **Other temporary differences HK$'m** | **Total HK$'m** |
| At 1 January 2011 | **535** | **3,881** | **(124)** | **(333)** | **90** | **4,049** |
| (Credited)/charged to condensed income statement (Note 14) | **(15)** | **3** | **–** | **(44)** | **(20)** | **(76)** |
| Charged to other comprehensive income | **–** | **855** | **–** | **–** | **103** | **958** |
| Exchange difference | **–** | **1** | **–** | **(1)** | **–** | **–** |
| At 30 June 2011 | **520** | **4,740** | **(124)** | **(378)** | **173** | **4,931** |

| | At 31 December 2010 | | | | | |
|---|---|---|---|---|---|---|
| | Accelerated tax depreciation HK$'m | Property revaluation HK$'m | Losses HK$'m | Impairment allowance HK$'m | Other temporary differences HK$'m | Total HK$'m |
| At 1 January 2010, as previously reported | 540 | 4,359 | (139) | (274) | (44) | 4,442 |
| Effect of early adoption of HKAS 12 (Amendment) | (11) | (1,269) | – | – | – | (1,280) |
| At 1 January 2010, as restated | 529 | 3,090 | (139) | (274) | (44) | 3,162 |
| Charged/(credited) to income statement | 6 | 1 | 15 | (57) | 5 | (30) |
| Charged to other comprehensive income | – | 788 | – | – | 129 | 917 |
| Exchange difference | – | 2 | – | (2) | – | – |
| At 31 December 2010 | 535 | 3,881 | (124) | (333) | 90 | 4,049 |

## 31. 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 condensed consolidated balance sheet:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Deferred tax assets | **(147)** | (157) |
| Deferred tax liabilities | **5,078** | 4,206 |
| | **4,931** | 4,049 |

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Deferred tax assets to be recovered after more than twelve months | **(119)** | (106) |
| Deferred tax liabilities to be settled after more than twelve months | **4,878** | 4,085 |
| | **4,759** | 3,979 |

The deferred tax charged for each component of other comprehensive income during the period is as follows:

| | **Half-year ended 30 June 2011 HK$'m** | (Restated) Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Fair value changes of available-for-sale securities | **103** | 253 |
| Revaluation of premises | **849** | 313 |
| Non-controlling interests | **6** | – |
| | **958** | 566 |

## 32. Insurance contract liabilities

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| At 1 January | **39,807** | 33,408 |
| Benefits paid | **(3,689)** | (3,366) |
| Claims incurred and movement in liabilities | **6,927** | 9,765 |
| At period/year end | **43,045** | 39,807 |

The insurance contract liabilities that are covered by reinsurance arrangements amounted to HK$4,922 million (31 December 2010: HK$2,053 million) and the associated reinsurance assets of HK$4,988 million (31 December 2010: HK$2,158 million) are included in "Other assets" (Note 26).

## 33. Subordinated liabilities

| | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|
| **Subordinated loans, at amortised cost** | | |
| EUR 660m* | **7,439** | 6,848 |
| **Subordinated notes, at amortised cost with fair value hedge adjustment** | | |
| USD2,500m** | **20,399** | 20,029 |
| Total | **27,838** | 26,877 |

In 2008, BOCHK obtained floating-rate subordinated loans from BOC, the intermediate holding company of the Group. The subordinated loans are repayable prior to maturity after the first 5-year tenure at the option of the borrower. In 2010, BOCHK issued listed subordinated notes with an aggregate amount of USD2,500 million.

Amounts qualified as supplementary capital for regulatory purposes are shown in Note 3.5(B).

* Interest rate at 6-month EURIBOR plus 0.85% for the first 5 years, 6-month EURIBOR plus 1.35% for the remaining tenure payable semi-annually, due June 2018.

** Interest rate at 5.55% per annum payable semi-annually, due February 2020.

## 34. Share capital

| | At 30 June 2011 HK$'m | At 31 December 2010 HK$'m |
|---|---|---|
| Authorised: | | |
| 20,000,000,000 ordinary shares of HK$5 each | **100,000** | 100,000 |
| Issued and fully paid: | | |
| 10,572,780,266 ordinary shares of HK$5 each | **52,864** | 52,864 |

## 35. Reserves

The Group's reserves and the movements therein for the current and prior periods are presented in the condensed consolidated statement of changes in equity on page 41.

## 36. Notes to condensed consolidated cash flow statement

### *(a) Reconciliation of operating profit to operating cash inflow before taxation*

| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Operating profit | **13,103** | 8,168 |
| Depreciation | **614** | 556 |
| Net charge/(reversal) of impairment allowances | **30** | (161) |
| Unwind of discount on impairment allowances | **(1)** | (5) |
| Advances written off net of recoveries | **118** | 115 |
| Change in subordinated liabilities | **1,257** | 729 |
| Change in balances with banks and other financial institutions with original maturity over three months | **(230)** | 5,726 |
| Change in placements with banks and other financial institutions with original maturity over three months | **(50,019)** | 21,741 |
| Change in financial assets at fair value through profit or loss | **16,782** | (17,019) |
| Change in derivative financial instruments | **(1,115)** | 247 |
| Change in advances and other accounts | **(74,235)** | (70,191) |
| Change in investment in securities | **(31,490)** | (3,771) |
| Change in other assets | **(12,272)** | (2,438) |
| Change in deposits and balances from banks and other financial institutions | **73,120** | 11,139 |
| Change in financial liabilities at fair value through profit or loss | **(20,618)** | 10,588 |
| Change in deposits from customers | **76,402** | 49,890 |
| Change in debt securities in issue at amortised cost | **5** | – |
| Change in other accounts and provisions | **12,362** | 4,760 |
| Change in insurance contract liabilities | **3,238** | 1,642 |
| Exchange difference | **115** | 26 |
| Operating cash inflow before taxation | **7,166** | 21,742 |
| Cash flows from operating activities included: | | |
| – Interest received | **14,178** | 10,135 |
| – Interest paid* | **4,034** | 1,296 |
| – Dividend received | **62** | 54 |

* The comparative amount has been revised to conform with the current period's presentation.

### *(b) Analysis of the balances of cash and cash equivalents*

| | **At 30 June 2011 HK$'m** | At 30 June 2010 HK$'m |
|---|---|---|
| Cash and balances with banks and other financial institutions with original maturity within three months | **412,673** | 158,378 |
| Placements with banks and other financial institutions with original maturity within three months | **13,651** | 12,769 |
| Treasury bills with original maturity within three months | **20,177** | 26,629 |
| | **446,501** | 197,776 |

## 37. 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:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Direct credit substitutes | **6,377** | 5,619 |
| Transaction-related contingencies | **12,397** | 7,262 |
| Trade-related contingencies | **49,081** | 42,691 |
| Commitments that are unconditionally cancellable without prior notice | **242,833** | 216,626 |
| Other commitments with an original maturity of | | |
| – up to one year | **12,686** | 15,470 |
| – over one year | **47,519** | 49,042 |
| | **370,893** | 336,710 |
| Credit risk weighted amount | **44,182** | 38,282 |

The credit risk weighted amount is calculated in accordance with the Banking (Capital) Rules. The amount is dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

The Group adopted the FIRB approach to calculate credit risk as at 30 June 2011, as opposed to the STC approach that was used as at 31 December 2010. As a result of the change in the basis used, the risk weighted amounts shown above are not directly comparable.

## 38. Capital commitments

The Group has the following outstanding capital commitments not provided for in this interim financial information:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Authorised and contracted for but not provided for | **322** | 169 |
| Authorised but not contracted for | **23** | 12 |
| | **345** | 181 |

The above capital commitments mainly relate to commitments to purchase computer equipment and software, and to renovate the Group's premises.

## 39. Operating lease commitments

### *(a) As lessee*

The Group has commitments to make the following future minimum lease payments under non-cancellable operating leases:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Land and buildings | | |
| – not later than one year | **543** | 474 |
| – later than one year but not later than five years | **861** | 547 |
| – later than five years | **307** | 22 |
| | **1,711** | 1,043 |

Certain non-cancellable operating leases included in the table above were subject to renegotiation and rent adjustment with reference to market rates prevailing at specified agreed dates.

### *(b) As lessor*

The Group has contracted with tenants for the following future minimum lease receivables under non-cancellable operating leases:

| | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
|---|---|---|
| Land and buildings | | |
| – not later than one year | **356** | 309 |
| – later than one year but not later than five years | **504** | 594 |
| | **860** | 903 |

The Group leases its investment properties (Note 24) 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 include contingent rentals.

## 40. 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. The classification of the Group's operating segments is based on customer segment and product type, which is aligned with the RPC (relationship, product and channel) management model of the Group.

As the Group's major revenue is derived from interest and the senior management relies primarily on net interest revenue to assess the performance of the segment, the total interest income and expense for all reportable segments will be presented on a net basis.

Both Personal Banking and Corporate Banking segments provide general banking services. Personal Banking mainly serves individual customers while Corporate Banking mainly 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 long-term life insurance products, including traditional and linked individual life insurance and group life insurance products, and the senior management relies primarily on net insurance premium income and benefits and claims to assess the performance of the segment. "Others" refers to those items related to the Group as a whole rather than directly attributable to 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. Inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group. 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. In this period, a more detailed and comprehensive cost allocation mechanism was adopted. No change has been made to the comparative figures. However, if the same mechanism is applied for the same period last year, it is estimated that the operating expenses of Personal Banking, Corporate Banking, Treasury and Others will be decreased by HK$469 million and increased by HK$4 million, HK$50 million and HK$88 million respectively.

## 40. Segmental reporting (continued)

| | Personal Banking HK$'m | Corporate Banking HK$'m | Treasury HK$'m | Insurance HK$'m | Others HK$'m | Subtotal HK$'m | Eliminations HK$'m | Consolidated HK$'m |
|---|---|---|---|---|---|---|---|---|
| **Half-year ended 30 June 2011** | | | | | | | | |
| Net interest income/(expense) | | | | | | | | |
| – external | 820 | 3,287 | 5,262 | 847 | (11) | 10,205 | – | 10,205 |
| – inter-segment | 2,023 | 876 | (2,869) | – | (30) | – | – | – |
| | 2,843 | 4,163 | 2,393 | 847 | (41) | 10,205 | – | 10,205 |
| Net fee and commission income | 2,407 | 1,483 | 57 | 19 | 66 | 4,032 | (46) | 3,986 |
| Net insurance premium income | – | – | – | 3,397 | – | 3,397 | (6) | 3,391 |
| Net trading gain/(loss) | 301 | 139 | 352 | (2) | (29) | 761 | – | 761 |
| Net gain on financial instruments designated at fair value through profit or loss | – | – | 18 | 380 | – | 398 | – | 398 |
| Net gain on investment in securities | – | – | 324 | – | 36 | 360 | – | 360 |
| Other operating income | 12 | – | 1 | 2 | 663 | 678 | (433) | 245 |
| **Total operating income** | 5,563 | 5,785 | 3,145 | 4,643 | 695 | 19,831 | (485) | 19,346 |
| Net insurance benefits and claims | – | – | – | (4,220) | – | (4,220) | – | (4,220) |
| **Net operating income before impairment allowances** | 5,563 | 5,785 | 3,145 | 423 | 695 | 15,611 | (485) | 15,126 |
| Net (charge)/reversal of impairment allowances | (82) | 40 | 43 | (31) | – | (30) | – | (30) |
| **Net operating income** | 5,481 | 5,825 | 3,188 | 392 | 695 | 15,581 | (485) | 15,096 |
| Operating expenses | (2,754) | (1,371) | (323) | (101) | 2,071 | (2,478) | 485 | (1,993) |
| **Operating profit** | 2,727 | 4,454 | 2,865 | 291 | 2,766 | 13,103 | – | 13,103 |
| Net gain from disposal of/fair value adjustments on investment properties | – | – | – | – | 1,486 | 1,486 | – | 1,486 |
| Net loss from disposal/revaluation of properties, plant and equipment | (4) | (1) | – | – | – | (5) | – | (5) |
| Share of profits less losses after tax of associates | – | – | – | – | 3 | 3 | – | 3 |
| **Profit before taxation** | 2,723 | 4,453 | 2,865 | 291 | 4,255 | 14,587 | – | 14,587 |
| **At 30 June 2011** | | | | | | | | |
| **Assets** | | | | | | | | |
| Segment assets | 237,746 | 508,613 | 992,322 | 53,186 | 56,310 | 1,848,177 | (18,012) | 1,830,165 |
| Interests in associates | – | – | – | – | 214 | 214 | – | 214 |
| | 237,746 | 508,613 | 992,322 | 53,186 | 56,524 | 1,848,391 | (18,012) | 1,830,379 |
| **Liabilities** | | | | | | | | |
| Segment liabilities | 656,172 | 487,944 | 509,338 | 49,850 | 15,464 | 1,718,768 | (18,012) | 1,700,756 |
| **Half-year ended 30 June 2011** | | | | | | | | |
| **Other information** | | | | | | | | |
| Capital expenditure | 6 | – | – | – | 261 | 267 | – | 267 |
| Depreciation | 164 | 75 | 25 | 2 | 348 | 614 | – | 614 |
| Amortisation of securities | – | – | (23) | 34 | – | 11 | – | 11 |

## 40. Segmental reporting (continued)

| | Personal Banking HK$'m | Corporate Banking HK$'m | Treasury HK$'m | Insurance HK$'m | Others HK$'m | Subtotal HK$'m | Eliminations HK$'m | Consolidated HK$'m |
|---|---|---|---|---|---|---|---|---|
| **Half-year ended 30 June 2010** | | | | | | | | |
| Net interest income/(expense) | | | | | | | | |
| – external | 1,358 | 3,235 | 3,647 | 724 | – | 8,964 | – | 8,964 |
| – inter-segment | 1,574 | (240) | (1,306) | – | (28) | – | – | – |
| | 2,932 | 2,995 | 2,341 | 724 | (28) | 8,964 | – | 8,964 |
| Net fee and commission income/(expense) | 2,160 | 1,382 | (4) | (154) | 67 | 3,451 | (54) | 3,397 |
| Net insurance premium income | – | – | – | 2,802 | – | 2,802 | (4) | 2,798 |
| Net trading gain/(loss) | 205 | 81 | (296) | (4) | (18) | (32) | (4) | (36) |
| Net gain on financial instruments designated at fair value through profit or loss | – | – | 49 | 591 | – | 640 | – | 640 |
| Net gain on investment in securities | – | – | 286 | 118 | – | 404 | – | 404 |
| Other operating income | 19 | 1 | – | 8 | 968 | 996 | (747) | 249 |
| **Total operating income** | 5,316 | 4,459 | 2,376 | 4,085 | 989 | 17,225 | (809) | 16,416 |
| Net insurance benefits and claims | – | – | – | (3,875) | – | (3,875) | – | (3,875) |
| **Net operating income before impairment allowances** | 5,316 | 4,459 | 2,376 | 210 | 989 | 13,350 | (809) | 12,541 |
| Net (charge)/reversal of impairment allowances | (42) | 131 | 72 | – | – | 161 | – | 161 |
| **Net operating income** | 5,274 | 4,590 | 2,448 | 210 | 989 | 13,511 | (809) | 12,702 |
| Operating expenses | (3,044) | (1,232) | (330) | (104) | (633) | (5,343) | 809 | (4,534) |
| **Operating profit** | 2,230 | 3,358 | 2,118 | 106 | 356 | 8,168 | – | 8,168 |
| Net gain from disposal of/fair value adjustments on investment properties | – | – | – | – | 601 | 601 | – | 601 |
| Net loss from disposal/revaluation of properties, plant and equipment | – | – | – | – | (1) | (1) | – | (1) |
| Share of profits less losses after tax of associates | – | – | – | – | (1) | (1) | – | (1) |
| **Profit before taxation** | 2,230 | 3,358 | 2,118 | 106 | 955 | 8,767 | – | 8,767 |
| **At 31 December 2010** | | | | | | | | |
| **Assets** | | | | | | | | |
| Segment assets | 210,978 | 458,928 | 910,772 | 48,195 | 50,650 | 1,679,523 | (18,695) | 1,660,828 |
| Interests in associates | – | – | – | – | 212 | 212 | – | 212 |
| | 210,978 | 458,928 | 910,772 | 48,195 | 50,862 | 1,679,735 | (18,695) | 1,661,040 |
| **Liabilities** | | | | | | | | |
| Segment liabilities | 657,605 | 407,328 | 437,174 | 45,149 | 14,190 | 1,561,446 | (18,695) | 1,542,751 |
| **Half-year ended 30 June 2010** | | | | | | | | |
| **Other information** | | | | | | | | |
| Capital expenditure | 1 | 1 | – | – | 162 | 164 | – | 164 |
| Depreciation | 154 | 78 | 36 | 2 | 286 | 556 | – | 556 |
| Amortisation of securities | – | – | 25 | 47 | – | 72 | – | 72 |

## 41. Significant related party transactions

The Group is subject to the control of the State Council of the PRC Government through China Investment Corporation ("CIC"), its wholly-owned subsidiary Central Huijin Investment Ltd. ("Central Huijin"), and BOC in which Central Huijin has controlling equity interests.

### *(a) Transactions with the parent companies and the other companies controlled by the parent companies*

**General information of the parent companies:**

The Group is controlled by BOC. Central Huijin is the controlling entity of BOC, and it is a wholly-owned subsidiary of CIC which is a wholly state-owned company engaging in foreign currency investment and management.

Central Huijin has controlling equity interests in certain other entities in the PRC.

The Group enters into banking and other transactions with these companies in the normal course of business. These include loans, investment securities, money market and reinsurance transactions.

### *(b) Transactions with government authorities, agencies, affiliates and other state controlled entities*

The Group is subject to the control of the State Council of the PRC Government through CIC and Central Huijin, which also directly and indirectly controls a significant number of entities through its government authorities, agencies, affiliates and other state controlled entities. The Group enters into banking transactions with government authorities, agencies, affiliates and other state controlled entities in the normal course of business and commercial terms.

These transactions include, but are not limited to, the following:

– lending, provision of credits and guarantees, and deposit taking;

– inter-bank balance taking and placing;

– sales, purchase, underwriting and redemption of bonds issued by other state-controlled entities;

– rendering of foreign exchange, remittance and investment related services;

– provision of fiduciary activities; and

– purchase of utilities, transport, telecommunication and postage services.

## 41. Significant related party transactions (continued)

### (c) *Summary of transactions entered into during the ordinary course of business with associates and other related parties*

The aggregate income and expenses arising from related party transactions with associates and other related parties of the Group are summarised as follows:

| | **Half-year ended 30 June 2011** | | Half-year ended 30 June 2010 | |
|---|---|---|---|---|
| | **Associates HK$'m** | **Other related parties HK$'m** | Associates HK$'m | Other related parties HK$'m |
| Income statement items: | | | | |
| Administrative services fees received/receivable | **–** | **4** | – | 4 |

| | **At 30 June 2011** | | At 31 December 2010 | |
|---|---|---|---|---|
| | **Associates HK$'m** | **Other related parties HK$'m** | Associates HK$'m | Other related parties HK$'m |
| Balance sheet items: | | | | |
| Deposits from customers | **166** | **–** | 157 | – |

### (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 periods, no material transaction was conducted with key management personnel of BOCHK, its holding companies and parties related to them.

The key management compensation is detailed as follows:

| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m |
|---|---|---|
| Salaries and other short-term employee benefits | **21** | 23 |
| Post-employment benefits | **1** | 1 |
| | **22** | 24 |

## 42. Currency concentrations

The following is a summary of the major foreign currency exposures arising from trading, non-trading and structural positions and is prepared with reference to the Completion Instructions for the prudential return "Foreign Currency Position of an Authorized Institution" issued by the HKMA. The net options position is calculated based on the basis of delta-weighted positions of all foreign exchange options contracts.

| | At 30 June 2011 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Equivalent in million of HK$ | | | | | | | |
| | US Dollars | Japanese Yen | Euro | Australian Dollars | Pound Sterling | Renminbi | Other foreign currencies | Total foreign currencies |
| Spot assets | **476,409** | **6,041** | **28,395** | **38,501** | **11,777** | **538,097** | **17,000** | **1,116,220** |
| Spot liabilities | **(341,308)** | **(2,181)** | **(24,808)** | **(30,859)** | **(16,982)** | **(514,418)** | **(18,560)** | **(949,116)** |
| Forward purchases | **264,114** | **28,875** | **29,491** | **25,919** | **21,609** | **103,611** | **31,189** | **504,808** |
| Forward sales | **(391,984)** | **(32,739)** | **(33,087)** | **(33,514)** | **(16,369)** | **(119,572)** | **(29,534)** | **(656,799)** |
| Net options position | **154** | **(1)** | **5** | **(21)** | **(8)** | **(1)** | **14** | **142** |
| Net long/(short) position | **7,385** | **(5)** | **(4)** | **26** | **27** | **7,717** | **109** | **15,255** |
| Net structural position | **316** | **–** | **–** | **–** | **–** | **5,135** | **–** | **5,451** |

| | At 31 December 2010 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Equivalent in million of HK$ | | | | | | | |
| | US Dollars | Japanese Yen | Euro | Australian Dollars | Pound Sterling | Renminbi | Other foreign currencies | Total foreign currencies |
| Spot assets | 454,733 | 8,486 | 33,414 | 46,818 | 4,366 | 434,077 | 15,517 | 997,411 |
| Spot liabilities | (281,774) | (2,250) | (23,881) | (37,113) | (17,865) | (412,948) | (22,109) | (797,940) |
| Forward purchases | 250,546 | 28,083 | 20,996 | 22,732 | 32,637 | 91,295 | 34,530 | 480,819 |
| Forward sales | (417,632) | (34,375) | (30,466) | (32,549) | (19,273) | (109,072) | (27,925) | (671,292) |
| Net options position | 262 | 1 | 3 | (19) | (7) | – | 15 | 255 |
| Net long/(short) position | 6,135 | (55) | 66 | (131) | (142) | 3,352 | 28 | 9,253 |
| Net structural position | 296 | – | – | – | – | 3,309 | – | 3,605 |

## 43. 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 30 June 2011** | | | | |
| Asia, other than Hong Kong | | | | |
| – Mainland China | 233,460 | 337,664 | 110,728 | 681,852 |
| – Others | 53,613 | 7,039 | 29,488 | 90,140 |
| | 287,073 | 344,703 | 140,216 | 771,992 |
| North America | | | | |
| – United States | 5,887 | 49,115 | 34,761 | 89,763 |
| – Others | 7,748 | 2,941 | 208 | 10,897 |
| | 13,635 | 52,056 | 34,969 | 100,660 |
| Western Europe | | | | |
| – United Kingdom | 31,511 | 1,916 | 3,022 | 36,449 |
| – Others | 42,673 | 18,878 | 5,502 | 67,053 |
| | 74,184 | 20,794 | 8,524 | 103,502 |
| Total | 374,892 | 417,553 | 183,709 | 976,154 |

## 43. Cross-border claims (continued)

| | Banks HK$'m | Public sector entities* HK$'m | Others HK$'m | Total HK$'m |
|---|---|---|---|---|
| At 31 December 2010 | | | | |
| Asia, other than Hong Kong | | | | |
| – Mainland China | 155,935 | 347,683 | 87,066 | 590,684 |
| – Others | 51,481 | 12,405 | 27,333 | 91,219 |
| | 207,416 | 360,088 | 114,399 | 681,903 |
| North America | | | | |
| – United States | 5,653 | 51,303 | 30,968 | 87,924 |
| – Others | 8,761 | 3,438 | 125 | 12,324 |
| | 14,414 | 54,741 | 31,093 | 100,248 |
| Western Europe | | | | |
| – United Kingdom | 29,834 | 2,722 | 1,246 | 33,802 |
| – Others | 56,616 | 14,083 | 4,989 | 75,688 |
| | 86,450 | 16,805 | 6,235 | 109,490 |
| Total | 308,280 | 431,634 | 151,727 | 891,641 |

* Included United States of HK$9,721 million (31 December 2010: HK$7,334 million), other countries in North America of HK$2,906 million (31 December 2010: HK$3,405 million) and other countries in Western Europe of HK$11,582 million (31 December 2010: HK$5,026 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

## 44. 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 are summarised as follows:

| | **At 30 June 2011** | | | |
|---|---|---|---|---|
| | **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 | **207,821** | **59,196** | **267,017** | **30** |
| Companies and individuals outside Mainland China where the credit is granted for use in Mainland China | **34,365** | **15,270** | **49,635** | **18** |
| Other non-bank Mainland China exposures | **35,814** | **1,544** | **37,358** | **45** |
| | **278,000** | **76,010** | **354,010** | **93** |

## 44. Non-bank Mainland China exposures (continued)

| | At 31 December 2010 | | | |
|---|---|---|---|---|
| | 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 | 185,309 | 48,278 | 233,587 | 59 |
| Companies and individuals outside Mainland China where the credit is granted for use in Mainland China | 25,600 | 11,827 | 37,427 | 18 |
| Other non-bank Mainland China exposures | 30,170 | 3,838 | 34,008 | 44 |
| | 241,079 | 63,943 | 305,022 | 121 |

## 45. Compliance with HKAS 34

The unaudited interim financial information for the first half of 2011 complies with HKAS 34 "Interim Financial Reporting" issued by the HKICPA.

## 46. Statutory accounts

The information in this interim report is unaudited and does not constitute statutory accounts. The statutory accounts for the year ended 31 December 2010 have been delivered to the Registrar of Companies and the HKMA. The auditor expressed an unqualified opinion on those statutory accounts in their report dated 24 March 2011.

# ADDITIONAL INFORMATION

## 1. Corporate information

### *Board of Directors*

| | |
|---|---|
| **Chairman** | XIAO Gang# |
| **Vice Chairmen** | LI Lihui#<br>HE Guangbei |
| **Directors** | LI Zaohang#<br>ZHOU Zaiqun#<br>ZHANG Yanling#<br>GAO Yingxin<br>FUNG Victor Kwok King*<br>KOH Beng Seng*<br>SHAN Weijian*<br>TUNG Chee Chen*<br>TUNG Savio Wai-Hok* |

\# Non-executive Directors

* Independent Non-executive Directors

### *Senior Management*

| | |
|---|---|
| **Chief Executive** | HE Guangbei |
| **Deputy Chief Executive** | GAO Yingxin |
| **Chief Financial Officer** | ZHUO Chengwen |
| **Deputy Chief Executive** | WONG David See Hong |
| **Deputy Chief Executive** | YEUNG Jason Chi Wai (appointed on 1 April 2011)<br>LAM Yim Nam (retired from 1 April 2011) |
| **Chief Risk Officer** | LI Jiuzhong |
| **Chief Operating Officer** | LEE Alex Wing Kwai |
| **Assistant Chief Executive** | ZHU Yan Lai |

### *Company Secretary*

CHAN Chun Ying
(appointed on 1 April 2011)
YEUNG Jason Chi Wai
(ceased to act with effect from 1 April 2011)

### *Registered Office*

52nd Floor
Bank of China Tower
1 Garden Road
Hong Kong

### *Auditor*

PricewaterhouseCoopers

### *Share Registrar*

Computershare Hong Kong Investor Services Limited
17M Floor
Hopewell Centre
183 Queen's Road East
Wan Chai
Hong Kong

### *ADR Depositary Bank*

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

### *Credit Ratings (Long Term)*

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

### *Index Constituent*

The Company is a constituent of the following indices:
Hang Seng Index
Hang Seng Corporate Sustainability Index
Hang Seng (Mainland and Hong Kong) Corporate Sustainability Index
MSCI Index
FTSE Index Series

### *Stock Codes*

Ordinary shares:

| | |
|---|---|
| The Stock Exchange of Hong Kong Limited | 2388 |
| Reuters | 2388.HK |
| Bloomberg | 2388 HK |

Level 1 ADR Programme:

| | |
|---|---|
| CUSIP No. | 096813209 |
| OTC Symbol | BHKLY |

### *Website*

www.bochk.com

## 2. Dividend and closure of register of members

The Board declared an interim dividend of HK$0.63 per share (2010: HK$0.40), payable on Friday, 23 September 2011 to shareholders whose names appear on the Register of Members of the Company on Thursday, 15 September 2011.

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to the interim dividend, from Monday, 12 September 2011 to Thursday, 15 September 2011 (both days inclusive), during which period no transfer of shares will be registered. In order to qualify for the interim dividend, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are 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, Wan Chai, Hong Kong, not later than 4:30 p.m. on Friday, 9 September 2011. Shares of the Company will be traded ex-dividend as from Thursday, 8 September 2011.

## 3. Substantial interests in share capital

The register maintained by the Company pursuant to section 336 of the SFO recorded that, as at 30 June 2011, 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$5.00 each in the Company (% of total issued shares) | |
|---|---|---|
| Central Huijin | 6,984,274,213 | (66.06%) |
| BOC | 6,984,274,213 | (66.06%) |
| BOCHKG | 6,984,175,056 | (66.06%) |
| BOC (BVI) | 6,984,175,056 | (66.06%) |

Notes:

1. Following the reorganisation of BOC in August 2004, Central Huijin holds the controlling equity capital of BOC on behalf of the State. Accordingly, for the purpose of the SFO, Central Huijin 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 6,984,175,056 shares of the Company.

3. 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 24,479 shares of the Company and an interest in 72,000 shares held under physically settled equity derivatives while BOCI Financial Products Limited had an interest in 2,678 shares of the Company.

All the interests stated above represented long positions. Save as disclosed above, as at 30 June 2011, BOCI Financial Products Limited had an interest in 143,522 shares which represented short positions. BOC and Central Huijin are deemed to be interested in such amount of shares for the purpose of the SFO. Save as disclosed, no other interests or short positions were recorded in the register maintained by the Company under section 336 of the SFO as at 30 June 2011.

## 4. 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 30 June 2011 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 2011 | Exercised during the period | Surrendered during the period | Lapsed during the period | Balances as at 30 June 2011 |
| 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 | 1,084,500 | – | – | – | 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 | | | | 4,338,000 | 3,976,500 | – | – | – | 3,976,500 |

Save as disclosed above, at no time during the period 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.

## 5. Directors' and Chief Executive's interests in shares, underlying shares and debentures

As at 30 June 2011, 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 |
| HE Guangbei | 100,000 | – | – | – | 100,000 | 0.001% |
| LI Zaohang | 1,446,000 [Note] | – | – | – | 1,446,000 | 0.014% |
| ZHOU Zaiqun | 1,084,500 [Note] | – | – | – | 1,084,500 | 0.010% |
| ZHANG Yanling | 1,446,000 [Note] | – | – | – | 1,446,000 | 0.014% |
| Total | 4,076,500 | – | – | – | 4,076,500 | 0.039% |

Note: 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.

## 5. Directors' and Chief Executive's interests in shares, underlying shares and debentures (continued)

Save as disclosed above, as at 30 June 2011, 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.

## 6. Changes of information in respect of Directors

In accordance with Rule 13.51B(1) of the Listing Rules, the changes in information required to be disclosed by Directors pursuant to paragraphs (a) to (e) and (g) of Rule 13.51(2) of the Listing Rules after the publication of the Company's Annual Report 2010 on 24 March 2011 up to 24 August 2011 (being the approval date of this Interim Report) are set out below:

### *Experience including other directorships and major appointments*

(a) Mr. ZHOU Zaiqun, a Non-executive Director of the Company, resigned as an executive director, member of the board's special committees and executive vice president of BOC, a company listed on the Stock Exchange of Hong Kong and the Shanghai Stock Exchange and a controlling shareholder of the Company, effective from 28 May 2011.

(b) Dr. FUNG Victor Kwok King, an Independent Non-executive Director of the Company, was appointed an independent non-executive director of Koc Holding A.S., a company listed on the Istanbul Stock Exchange, effective from 7 April 2011.

(c) Mr. SHAN Weijian, an Independent Non-executive Director of the Company, was appointed a governor of China Venture Capital and Private Equity Association Limited effective from 7 June 2011.

(d) Mr. TUNG Chee Chen, an Independent Non-executive Director of the Company, retired as an independent non-executive director of PetroChina Company Limited, a company listed on the Stock Exchange of Hong Kong, the Shanghai Stock Exchange and the New York Stock Exchange, effective from 18 May 2011.

(e) Mr. TUNG Savio Wai-Hok, an Independent Non-executive Director of the Company, was appointed the chief executive, North America, overseeing the private equity, real estate, hedge fund and technology investment activities of Investcorp (a company incorporated in Luxembourg), effective from 1 July 2011.

## 7. Purchase, sale or redemption of the Company's shares

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

# ADDITIONAL INFORMATION

## 8. Audit Committee

The Audit Committee consists only of Non-executive Directors, the majority of whom are Independent Non-executive Directors. It is chaired by Independent Non-executive Director Mr. SHAN Weijian. Other members include Mr. ZHOU Zaiqun, Dr. FUNG Victor Kwok King, Mr. TUNG Chee Chen, Mr. TUNG Savio Wai-Hok and Mr. KOH Beng Seng.

Based on the principle of independence, the Audit Committee assists the Board in monitoring the financial reports, internal control, internal audit and external audit of the Group.

At the request of the Audit Committee of the Company, the Group's external auditor has carried out a review of the interim financial information in accordance with the Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the HKICPA. The Audit Committee has reviewed with management the accounting principles and practices adopted by the Group and discussed auditing, internal control and financial reporting matters including the review of the unaudited interim financial reports.

## 9. Compliance with "Code on Corporate Governance Practices"

The Company is committed to embrace and enhance good corporate governance principles and practices. The Company has been in full compliance with all the code provisions of the "Code on Corporate Governance Practices" contained in Appendix 14 of the Listing Rules (the "CG Code") and that it has also complied with nearly all the recommended best practices set out in the CG Code throughout the period under review. For further details, please refer to the section titled "Corporate Governance" contained in the Annual Report 2010 of the Company.

## 10. Compliance with the Codes for Securities Transactions by Directors

The Company has adopted the "Code for Securities Transactions by Directors" (the "Company's Code") to govern securities transactions by Directors. The terms of the Company's 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 (the "Model Code"). Apart from the securities of the Company, the Company's 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 Model Code throughout the period under review. The Company had undertaken a review of the Company's Code in December 2010. There were no fundamental amendments to the Company's Code and changes were in adaptive nature mainly to refine the Company's Code.

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

The unaudited interim report complies 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.

## 12. Interim Report

This Interim Report is available in both English and Chinese. The Chinese version of this Interim Report will be provided by writing to the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong or email to bochk.ecom@computershare.com.hk.

This Interim Report is also available (in both English and Chinese) on the Company's website at www.bochk.com and the website of Hong Kong Exchanges and Clearing Limited at www.hkexnews.hk. You are encouraged to access the Interim Report and other 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.

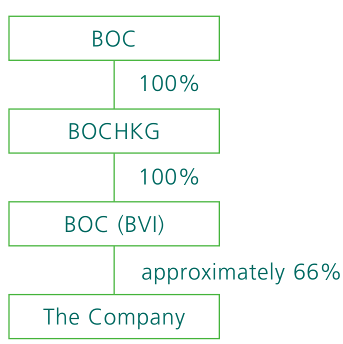
If you have any queries about how to obtain copies of this Interim Report or how to access those documents on the Company's website, please call the Company's hotline at (852) 2846 2700.

## 13. 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 interim financial information. 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 interim financial information 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.



## 13. Reconciliation between HKFRSs vs IFRS/CAS (continued)

Second, the Group has prepared its interim financial information 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 interim financial information 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.

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;

– deferred taxation impact arising from the above different measurement basis; and

– early adoption of the amendment to HKAS 12.

### (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 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.

## 13. Reconciliation between HKFRSs vs IFRS/CAS (continued)

### *(d) Early adoption of the amendment to HKAS 12*

The Company has early adopted the amendment to HKAS 12 while BOC has not elected to early adopt the amendment under IFRS and CAS. Therefore, adjustments have been made to remove the effects from the early adoption of the amendment to HKAS 12.

***Profit after tax/net assets reconciliation***

**HKFRSs vs IFRS/CAS**

| | Profit after tax | | Net assets | |
|---|---|---|---|---|
| | **Half-year ended 30 June 2011 HK$'m** | Half-year ended 30 June 2010 HK$'m | **At 30 June 2011 HK$'m** | At 31 December 2010 HK$'m |
| **Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under HKFRSs** | **12,354** | 7,355 | **129,623** | 118,289 |
| Add: IFRS/CAS adjustments | | | | |
| Re-measurement of carrying value of treasury products | **(14)** | (17) | **–** | (3) |
| Restatement of carrying value of bank premises | **181** | 172 | **(22,757)** | (17,726) |
| Deferred tax adjustments | **8** | (40) | **3,779** | 2,931 |
| Effect of early adoption of HKAS 12 (Amendment) | **(214)** | (2) | **(1,658)** | (1,449) |
| **Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under IFRS/CAS** | **12,315** | 7,468 | **108,987** | 102,042 |

# INDEPENDENT REVIEW REPORT

**REPORT ON REVIEW OF INTERIM FINANCIAL INFORMATION**
**TO THE BOARD OF DIRECTORS OF BOC HONG KONG (HOLDINGS) LIMITED**
(incorporated in Hong Kong with limited liability)

## Introduction

We have reviewed the interim financial information set out on pages 38 to 109, which comprises the condensed consolidated balance sheet of BOC Hong Kong (Holdings) Limited (the "Company") and its subsidiaries (together, the "Group") as at 30 June 2011 and the related condensed consolidated income statement, the condensed consolidated statement of comprehensive income, the condensed consolidated statement of changes in equity and the condensed consolidated cash flow statement for the six-month period then ended, and a summary of significant accounting policies and other explanatory notes. The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and Hong Kong Accounting Standard 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants. The directors of the Company are responsible for the preparation and presentation of this interim financial information in accordance with Hong Kong Accounting Standard 34 "Interim Financial Reporting". Our responsibility is to express a conclusion on this interim financial information based on our review and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

## Scope of Review

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

## Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the interim financial information is not prepared, in all material respects, in accordance with Hong Kong Accounting Standard 34 "Interim Financial Reporting".

**PricewaterhouseCoopers**
*Certified Public Accountants*
Hong Kong, 24 August 2011

# 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<br>16 October 1964 | Ordinary shares<br>HK$43,042,840,858 | 100.00% | Banking business |
| BOC Group Life Assurance Company Limited* | Hong Kong<br>12 March 1997 | Ordinary shares<br>HK$2,868,000,000 | 51.00% | Life insurance business |
| BOCHK Asset Management (Cayman) Limited* | Cayman Islands<br>7 October 2010 | Ordinary shares<br>HK$30,000,000 | 100.00% | Investment holding |
| **Indirectly held:** | | | | |
| Nanyang Commercial Bank, Limited | Hong Kong<br>2 February 1948 | Ordinary shares<br>HK$700,000,000 | 100.00% | Banking business |
| Chiyu Banking Corporation Limited | Hong Kong<br>24 April 1947 | Ordinary shares<br>HK$300,000,000 | 70.49% | Banking business |
| BOC Credit Card (International) Limited | Hong Kong<br>9 September 1980 | Ordinary shares<br>HK$480,000,000 | 100.00% | Credit card services |
| Bank of China (Hong Kong) Nominees Limited* | Hong Kong<br>1 October 1985 | Ordinary shares<br>HK$2 | 100.00% | Nominee services |
| Bank of China (Hong Kong) Trustees Limited* | Hong Kong<br>6 November 1987 | Ordinary shares<br>HK$3,000,000 | 100.00% | Trustee and agency services |
| BOC Group Trustee Company Limited* | Hong Kong<br>1 December 1997 | Ordinary shares<br>HK$200,000,000 | 64.20% | Trustee services |
| BOC Travel Services Limited* | Hong Kong<br>24 August 1982 | Ordinary shares<br>HK$2,000,000 | 100.00% | Travel services |
| BOCHK Asset Management Limited* | Hong Kong<br>28 October 2010 | Ordinary shares<br>HK$29,500,000 | 100.00% | Asset management |
| BOCHK Financial Products (Cayman) Limited | Cayman Islands<br>10 November 2006 | Ordinary shares<br>US$50,000 | 100.00% | Note issuing |
| BOCHK Information Technology (Shenzhen) Co., Ltd.* | PRC<br>16 April 1990 | Registered capital<br>HK$70,000,000 | 100.00% | Property holding and investment |
| BOCHK Information Technology Services (Shenzhen) Ltd.* | PRC<br>26 May 1993 | Registered capital<br>HK$40,000,000 | 100.00% | Information technology services |

# APPENDIX

## 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 |
|---|---|---|---|---|
| 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 |
| Glister Company Limited* | Hong Kong 26 March 2001 | Ordinary shares HK$2 | 70.49% | Investment holding |
| Glory Cardinal Limited* | Hong Kong 4 May 2001 | Ordinary shares HK$2 | 70.49% | Investment holding |
| Grace Charter Limited* | Hong Kong 4 May 2001 | Ordinary shares HK$2 | 70.49% | Investment holding |
| G.Z.Y. Microfilm Technology (Shenzhen) Co., Ltd.* | PRC 24 September 1993 | Registered capital HK$40,000,000 | 100.00% | Property holding and investment |
| Kincheng Finance (H.K.) Limited | Hong Kong 30 March 1979 | Ordinary shares HK$100 | 100.00% | Loan financing |
| Kincheng Investments & Developments (H.K.) Limited | Hong Kong 15 May 1981 | Ordinary shares HK$6,000 | 100.00% | Property holding and investment |
| Kincheng (Nominees) Limited* | Hong Kong 12 December 1980 | Ordinary shares HK$100,000 | 100.00% | Nominee services |
| Kiu Nam Investment Corporation Limited | Hong Kong 9 November 1963 | Ordinary shares HK$2,000,000 | 100.00% | Property holding and investment |
| Kwong Li Nam Investment Agency Limited* | Hong Kong 25 May 1984 | Ordinary shares HK$3,050,000 | 100.00% | Investment agency |

## 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 |
|---|---|---|---|---|
| Nan Song Company, Limited* | Hong Kong 13 April 1965 | Ordinary shares HK$1,000,000 | 100.00% | Property investment and investment holding |
| Nanyang Commercial Bank (China), Limited | PRC 14 December 2007 | Registered capital RMB4,100,000,000 | 100.00% | Banking business |
| Nanyang Commercial Bank (Nominees) Limited* | Hong Kong 22 August 1980 | Ordinary shares HK$50,000 | 100.00% | Nominee services |
| Nanyang Commercial Bank Trustee Limited* | Hong Kong 22 October 1976 | Ordinary shares HK$3,000,000 | 100.00% | Trustee services |
| Nanyang Finance Company Limited | Hong Kong 16 March 1979 | Ordinary shares HK$50,000,000 | 100.00% | Financial services |
| Pacific Trend Profits Corporation* | British Virgin Islands 20 April 2001 | Registered shares US$1 | 70.49% | Investment holding |
| Patson (HK) Limited* | Hong Kong 18 August 1970 | Ordinary shares HK$1,000,000 | 100.00% | Property investment |
| Perento Limited | Hong Kong 27 September 1983 | Ordinary shares HK$10,000 | 100.00% | Property holding and investment |
| Po Hay Enterprises Limited | Hong Kong 2 October 1979 | Ordinary shares HK$100,000 | 100.00% | Property holding and investment |
| Po Sang Financial Investment Services Company Limited* | Hong Kong 23 September 1980 | Ordinary shares HK$25,000,000 | 100.00% | Gold trading and investment holding |
| Po Sang Futures Limited* | Hong Kong 19 October 1993 | Ordinary shares HK$25,000,000 | 100.00% | Commodities brokerage |
| 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 |

## 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 |
|---|---|---|---|---|
| Sin Mei (Nominee) Limited* | Hong Kong<br>27 April 1982 | Ordinary shares<br>HK$100,000 | 100.00% | Nominee services |
| Sin Yeh Shing Company Limited | Hong Kong<br>28 November 1980 | Ordinary shares<br>HK$100,000 | 100.00% | Property holding and investment |
| Sino Information Services Company Limited* | Hong Kong<br>11 February 1993 | Ordinary shares<br>HK$7,000,000 | 100.00% | Information services |
| The China-South Sea (Nominees) Services Limited* | Hong Kong<br>13 February 1981 | Ordinary shares<br>HK$100,000 | 100.00% | Nominee services |
| Track Link Investment Limited | Hong Kong<br>8 February 1994 | Ordinary shares<br>HK$2 | 100.00% | Property holding and investment |

Glory Cardinal Limited has been deregistered on 7 January 2011.

Nanyang Finance Company Limited, Patson (HK) Limited and Nan Song Company Limited commenced members' voluntary winding up on 23 March 2011.

Dwell Bay Limited, Perento Limited and Shenstone Limited commenced members' voluntary winding up on 30 June 2011.

Glister Company Limited disposed of its entire equities to a third party on 18 March 2011.

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 Interim Report, unless the context otherwise requires, the following terms shall have the meanings set out below:

| Terms | Meanings |
|---|---|
| "ABS" | Asset-backed securities |
| "ADR" | American Depositary Receipt |
| "ALCO" | the Asset and Liability Management Committee |
| "ATM" | Automated Teller Machine |
| "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 |
| "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 |
| "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 |
| "CAS" | China Accounting Standards |
| "CB" | Clearing Bank |

# DEFINITIONS

| Terms | Meanings |
|---|---|
| "CBRC" | China Banking Regulatory Commission |
| "CE" | Chief Executive |
| "CFO" | Chief Financial Officer |
| "CIC" | China Investment Corporation |
| "CRO" | Chief Risk Officer |
| "Central Huijin" | Central Huijin Investment Ltd. (formerly known as "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% |
| "the Company" | BOC Hong Kong (Holdings) Limited, a company incorporated under the laws of Hong Kong |
| "DCE" | Deputy Chief Executive |
| "EURIBOR" | Euro Interbank Offered Rate |
| "FIRB" | Foundation Internal Ratings-Based |
| "GDP" | Gross Domestic Product |
| "the 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) |
| "HKFRS(s)" | Hong Kong Financial Reporting Standard(s) |
| "HKICPA" | Hong Kong Institute of Certified Public Accountants |
| "HKMA" | Hong Kong Monetary Authority |
| "HK(SIC)-Int" | Hong Kong (SIC) Interpretation |
| "Hong Kong" or "Hong Kong SAR" | Hong Kong Special Administrative Region |
| "ICAAP" | Internal Capital Adequacy Assessment Process |
| "IFRS" | International Financial Reporting Standards |
| "IMM" | Internal Models Approach |
| "Listing Rules" | the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited |
| "LSC" | Legal Services Centre |

| Terms | Meanings |
|---|---|
| "Mainland" or "Mainland China" | the mainland of the PRC |
| "MBS" | Mortgage-backed securities |
| "MPF" | Mandatory Provident Fund |
| "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 |
| "NCB (China)" | Nanyang Commercial Bank (China), Limited, a company incorporated under the laws of the PRC and a wholly owned subsidiary of Nanyang |
| "OR&CD" | the Operational Risk & Compliance Department |
| "ORSO schemes" | the Occupational Retirement Schemes under Occupational Retirement Schemes Ordinance, Chapter 426 of the Laws of Hong Kong |
| "PBs" | Participating Banks |
| "PRC" | the People's Republic of China |
| "QDIIs" | Qualified Domestic Institutional Investors |
| "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" | Standardised (Credit Risk) |
| "STM" | Standardised (Market Risk) |
| "STO" | Standardised (Operational Risk) |
| "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 |

# DEFINITIONS

| Terms | Meanings |
|---|---|
| "Stock Exchange" or "Hong Kong Stock Exchange" or "Stock Exchange of Hong Kong" | The Stock Exchange of Hong Kong Limited |
| "US" | the United States of America |
| "VAR" | Value at Risk |

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