

## Notes to the unaudited interim financial report

### 1. Activities and corporate affiliation

The Bank, through its branches and subsidiaries, provides a range of banking, financial and related services.

The ultimate holding company of the Bank is Arab Banking Corporation (B.S.C.) which is incorporated in the State of Bahrain and operates as an offshore bank.

### 2. Basis of preparation

This interim financial report is unaudited, but has been reviewed by KPMG in accordance with Statement of Auditing Standards 700 *“Engagements to Review Interim Financial Reports”*, issued by the Hong Kong Society of Accountants (*“HKSA”*). KPMG’s independent review report to the board of directors is included on page 12.

The interim financial report has been prepared in accordance with the requirements of the Main Board Listing Rules of The Stock Exchange of Hong Kong Limited, including compliance with Statement of Standard Accounting Practice (*“SSAAP”*) 25 *“Interim Financial Reporting”* issued by the HKSA. In addition, the interim financial report complies with the module on the *“Interim Financial Disclosure by Locally Incorporated Authorised Institutions”* under the Supervisory Policy Manual issued by the HKMA.

The financial information relating to the financial year ended 31 December 2001 included in the interim financial report does not constitute the Bank’s statutory accounts for that financial year but is derived from those accounts. Statutory accounts for the year ended 31 December 2001 are available from the Bank’s registered office. The auditors have expressed an unqualified opinion on those accounts in their report dated 7 February 2002.

The same accounting policies adopted in the 2001 annual accounts have been applied in the preparation of the interim financial report except that with effect from 1 January 2002, the Bank adopted the revised SSAP 1 *“Presentation of Financial Statements”* and revised SSAP15 *“Cash Flow Statements”*. As a result, a Consolidated Statement of Changes in Equity was prepared in accordance with the revised SSAP 1 to replace the Consolidated Statement of Recognised Gains and Losses that was previously prepared. The format of the Cash Flow Statement

was changed in accordance with the revised SSAP 15. In addition, cash equivalents under the revised SSAP15 do not include short term bank deposits which are not repayable on demand. The comparative figures were restated to conform with current period presentation.

The notes on the interim financial report include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Group since the 2001 annual accounts.

### 3. Other operating income

	Six months ended	
	30 June 2002 HK\$'000	30 June 2001 HK\$'000
Fee and commission income	68,358	54,359
Less: Fee and commission expense	(15,453)	(12,529)
Net fee and commission income	52,905	41,830
Dividend income from listed investments	656	522
Dividend income from unlisted investments	2,278	1,045
Rental income less outgoings	5,979	5,560
Gain on foreign exchange trading	3,911	5,692
Others	15,011	17,692
	<b>80,740</b>	<b>72,341</b>

### 4. Operating expenses

Operating expenses included depreciation amounting to HK\$28,003,000 (2001: HK\$22,231,000).

### 5. Gains less losses from disposal, redemption or transfer of investments in securities

	Six months ended	
	30 June 2002 HK\$'000	30 June 2001 HK\$'000
Net realised gain on disposal or redemption of investments in securities	60,992	40,357
Net unrealised gains from transfer of held-to-maturity securities to non-trading securities	0	28,628
	<b>60,992</b>	<b>68,985</b>

**6. Taxation**

Hong Kong Profits Tax has been provided at the rate of 16% (2001: 16%) on the estimated assessable profits for the period. The amounts of unprovided deferred tax liability as at 30 June 2002 and 31 December 2001 were not material.

**7. Earnings per share**

The earnings per share is calculated on earnings of HK\$100,838,000 (2001: HK\$162,388,000) and on the weighted average of 1,172,160,000 (2001: 1,172,160,000) shares in issue during the period. There were no convertible loan capital, options or warrants outstanding which would cause a dilution effect on the earnings per share.

**8. Segment reporting**

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is more relevant to the Group's internal financial reporting.

The Bank and its subsidiaries are principally engaged in the provision of banking and related financial services. Consumer Finance mainly comprises of the banks retail banking, credit card and hire purchase businesses. Retail banking mainly comprises of deposit account services, residential mortgage and other consumer lendings. Hire purchase lending includes both personal and corporate equipment, auto and other consumer leasing contracts and lending. Credit card business comprises of merchant acquiring and provisioning of credit card advances. Corporate Banking business covers trade financing, syndicated loans and other corporate lending. Investment Banking activities mainly comprise of private banking activities, securities brokerage, unit trusts and insurance services. Treasury activities are mainly the provision of foreign exchange services and centralised cash management for deposit taking and lending, management of trading securities and the overall funding of the Group. Unallocated items mainly comprise of the central management unit, management in investments in securities, investments on premises and property investment and other activities which cannot be reasonably allocated to specific business segments.

	<b>As at 30 June 2002 HK\$'000</b>	As at 30 June 2001 HK\$'000
<b>(a) Operating Income</b>		
Consumer Finance	328,597	328,870
Corporate Banking	40,392	39,507
Investment Banking	36,896	28,891
Treasury	19,824	4,301
Unallocated	29,405	40,123
	<u>455,114</u>	<u>441,692</u>
<b>(b) Profit before taxation</b>		
Consumer Finance	983	112,937
Corporate Banking	5,643	11,486
Investment Banking	17,239	12,258
Treasury	29,403	4,265
Unallocated	54,049	54,381
	<u>107,317</u>	<u>195,327</u>

### Geographical segments

The geographical segment is analysed based on the locations of the principal operations of the subsidiaries or on the location of the branches of the Bank responsible for reporting the results or booking the assets, the location of customers and the location of the assets. For the periods ended 30 June 2002 and 2001, all of the Group's operating income and profit before taxation were generated by assets booked by the principal operations of the branches and subsidiaries of the Bank located in Hong Kong. More than 90% of assets were either located in Hong Kong or were extended to companies and individuals domiciled in Hong Kong. The balance of the assets were extended to companies and individuals domiciled outside Hong Kong, mainly in China.

## 9. Short term funds

	As at 30 June 2002 HK'000	31 December 2001 HK'000
Balances with banks and other financial institutions	190,203	51,729
Money at call and short notice*	4,622,093	5,147,202
Treasury bills (including Exchange Fund Bills)	<u>894,404</u>	<u>0</u>
	<u><u>5,706,700</u></u>	<u><u>5,198,931</u></u>

\* Money at call and short notice represents deposits of up to a maximum of 1-month in maturity.

Treasury bills are issued by central governments and central banks and are unlisted. The analysis of treasury bills is as follows:

	As at 30 June 2002 HK'000	31 December 2001 HK'000
Treasury bills		
– Trading	593,400	0
– Non-trading	<u>301,004</u>	<u>0</u>
	<u><u>894,404</u></u>	<u><u>0</u></u>

The maturity profile of treasury bills included above and analysed by the remaining period at the balance sheet date to the contractual maturity date is as follows:

	As at 30 June 2002 HK'000	31 December 2001 HK'000
3 months or less but not repayable on demand	301,004	0
1 year or less but over 3 months	<u>593,400</u>	<u>0</u>
	<u><u>894,404</u></u>	<u><u>0</u></u>

**10. Placements with banks maturing between one and twelve months**

The maturity profile analysed by the remaining period at the balance sheet date to the contractual maturity date is as follows:

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
3 months or less but over 1 month	268,402	710,475
1 year or less but over 3 months	56,991	0
	<u>325,393</u>	<u>710,475</u>

**11. Trade bills less reserves and certificates of deposit**

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
Trade bills	16,089	9,538
Less: General reserves	(55)	(61)
	<u>16,034</u>	<u>9,477</u>
Certificates of deposit – unlisted, non-trading	<u>273,205</u>	<u>345,499</u>
	<u>289,239</u>	<u>354,976</u>

The maturity profile analysed by the remaining period at the balance sheet date to the contractual maturity date is as follows:

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
Repayable on demand	790	910
3 months or less but not repayable on demand	35,319	28,859
1 year or less but over 3 months	184,135	19,980
5 years or less but over 1 year	69,050	305,288
	<u>289,294</u>	<u>355,037</u>

## 12. Advances to customers less reserves

	As at 30 June 2002 <i>HK'000</i>	As at 31 December 2001 <i>HK'000</i>
Advances to customers	15,747,142	16,730,081
Reserves for doubtful debts		
– General	(144,412)	(167,301)
– Specific	(117,758)	(178,620)
	<u>15,484,972</u>	<u>16,384,160</u>

The specific reserves were made after taking into account the value of collateral in respect of doubtful debts totalling HK\$362,389,668 (2001: HK\$535,531,125).

The maturity profile analysed by the remaining period at the balance sheet date to the contractual maturity date is as follows:

	As at 30 June 2002 <i>HK'000</i>	As at 31 December 2001 <i>HK'000</i>
Repayable on demand	1,043,143	1,175,839
3 months or less but not repayable on demand	1,304,798	1,237,410
1 year or less but over 3 months	2,153,221	1,798,476
5 years or less but over 1 year	4,831,572	5,399,406
Over 5 years	5,835,747	6,225,127
Undated	578,661	893,823
	<u>15,747,142</u>	<u>16,730,081</u>

Total advances on which interest is being placed in suspense or on which interest accrual has ceased (“Non-performing advances”):

The non-performing advances, together with the aggregate amount of specific reserves made and amount of collateral held in respect of such advances are as follows:

	As at 30 June 2002		As at 31 December 2001	
	HK\$'000	<sup>1</sup> %	HK\$'000	<sup>1</sup> %
Non-performing advances <sup>2</sup>				
– Rescheduled	21,408	0.14	33,550	0.20
– Others	497,133	3.16	804,218	4.81
	<u>518,541</u>	3.30	<u>837,768</u>	5.01
Amount of specific reserves made against non-performing advances	103,921		164,379	
Amount of collateral held in respect of non-performing advances <sup>3</sup>	349,723		529,647	
	<u>453,644</u>		<u>694,026</u>	
Amount of interest suspended	<u>103,777</u>		<u>93,497</u>	

<sup>1</sup> As a percentage of gross advances to customers.

<sup>2</sup> Net of suspended interest.

<sup>3</sup> Including expected recoveries of HK\$16.76 million (2001: HK\$16.76 million) from companies in liquidation.



### 13. Investments

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
<b>Investments in securities</b>		
<b>Non-trading securities at fair value</b>		
Listed in Hong Kong		
– debt	3,281,469	2,544,670
– equity	39,364	44,091
Unlisted		
– debt	1,394,861	753,298
– equity	22,527	22,384
Sub-total	<u>4,738,221</u>	<u>3,364,443</u>
<b>Trading securities at fair value</b>		
– debt	<u>2,336</u>	<u>0</u>
Sub-total	<u>2,336</u>	<u>0</u>
Total	<u><u>4,740,557</u></u>	<u><u>3,364,443</u></u>
<b>Market value</b>		
Listed in Hong Kong		
– debt securities	<u>3,281,469</u>	<u>2,544,670</u>
– equity securities	<u>39,364</u>	<u>44,091</u>

\* Trading securities are all unlisted and are issued by public sector entities maturing less than 5 years but are over 1 year.

The non-trading securities are issued by:

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
Central governments and central banks	3,615,628	2,739,620
Public sector entities	544,548	0
Banks and other financial institutions	236,804	155,459
Corporate entities	<u>341,241</u>	<u>469,364</u>
Total	<u><u>4,738,221</u></u>	<u><u>3,364,443</u></u>

The maturity profile of debt securities analysed by the remaining period at the balance sheet date to the contractual maturity date is as follows:

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
3 months or less but not repayable on demand	0	50,185
1 year or less but over 3 months	100,410	404,775
5 years or less but over 1 year	4,304,566	2,808,181
Over 5 years	238,852	2,000
Undated	34,838	32,827
	<u>4,678,666</u>	<u>3,297,968</u>

#### 14. Investments in associated company

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
Unlisted shares, at cost	5,761	5,761
Advances	11,284	11,749
Less: Provision for diminution in value	<u>(5,761)</u>	<u>(5,761)</u>
	<u>11,284</u>	<u>11,749</u>

The Bank owns 40% (2001: 40%) of the issued share capital of IBA Finance Corporation, which is incorporated in the Philippines. The principal activity of the associated company is the provision of financing and leasing services in the Philippines. The Bank has not equity accounted for the investments in the associated company in view of the immaterial amount involved.

## 15. Premises and equipment

### THE GROUP

	Premises HK\$'000	Equipment HK\$'000	Other HK\$'000	Total HK\$'000
<b>Cost or valuation</b>				
At 1 January 2002	1,189,615	305,626	2,845	1,498,086
Additions	23	24,124	0	24,147
Disposals	0	(6,208)	0	(6,208)
	<u>1,189,638</u>	<u>323,542</u>	<u>2,845</u>	<u>1,516,025</u>
At 30 June 2002				
<b>Accumulated depreciation</b>				
At 1 January 2002	67,419	147,985	2,845	218,249
Charge for the period	6,796	21,207	0	28,003
Released on disposal	0	(6,208)	0	(6,208)
	<u>74,215</u>	<u>162,984</u>	<u>2,845</u>	<u>240,044</u>
At 30 June 2002				
<b>Net book value</b>				
At 30 June 2002	<u>1,115,423</u>	<u>160,558</u>	<u>0</u>	<u>1,275,981</u>
At 31 December 2001	<u>1,122,196</u>	<u>157,641</u>	<u>0</u>	<u>1,279,837</u>

## 16. Deposits and balances of other banks

The maturity profile analysed by the remaining period at the balance sheet date to the contractual maturity date is as follows:

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
Repayable on demand	1,545	36,253
3 months or less but not repayable on demand	<u>24,369</u>	<u>342,314</u>
	<u>25,914</u>	<u>378,567</u>

**17. Current, fixed and other deposits of customers**

The maturity profile analysed by the remaining period at the balance sheet date to the contractual maturity date is as follows:

	As at 30 June 2002 <i>HK'000</i>	As at 31 December 2001 <i>HK'000</i>
Repayable on demand	4,059,483	2,383,895
3 months or less but not repayable on demand	17,213,725	18,341,969
1 year or less but over 3 months	1,155,873	1,495,350
5 years or less but over 1 year	<u>16,877</u>	<u>24,703</u>
	<u><u>22,445,958</u></u>	<u><u>22,245,917</u></u>

**18. Certificates of deposit issued**

The maturity profile analysed by the remaining period at the balance sheet date to the contractual maturity date is as follows:

	As at 30 June 2002 <i>HK'000</i>	As at 31 December 2001 <i>HK'000</i>
3 months or less but not repayable on demand	0	310,000
1 year or less but over 3 months	405,000	505,000
5 years or less but over 1 year	<u>1,327,100</u>	<u>800,000</u>
	<u><u>1,732,100</u></u>	<u><u>1,615,000</u></u>

## 19. Reserves

	Capital redemption reserve HK\$'000	Investment revaluation reserve HK\$'000	Retained earnings HK\$'000	Total HK\$'000
At 1 January 2001	372,000	(4,280)	1,189,709	1,577,429
Profit after tax for the year	0	0	295,338	295,338
Net change in fair value of non-trading securities	0	(13,945)	0	(13,945)
Dividends approved in respect of the previous financial year	0	0	(58,608)	(58,608)
Interim dividend paid	0	0	(46,886)	(46,886)
	<u>372,000</u>	<u>(18,225)</u>	<u>1,379,553</u>	<u>1,733,328</u>
At 31 December 2001	<u>372,000</u>	<u>(18,225)</u>	<u>1,379,553</u>	<u>1,733,328</u>
At 1 January 2002	372,000	(18,225)	1,379,553	1,733,328
Profit after tax for the six months	0	0	100,838	100,838
Net change in fair value of non-trading securities	0	2,519	0	2,519
Dividends approved in respect of the previous financial year	0	0	(82,051)	(82,051)
	<u>372,000</u>	<u>(15,706)</u>	<u>1,398,340</u>	<u>1,754,634</u>
At 30 June 2002	<u>372,000</u>	<u>(15,706)</u>	<u>1,398,340</u>	<u>1,754,634</u>

- (a) The capital redemption reserve arose from the redemption of the Bank's "A" and "B" preference shares in 1991 and 1992 out of its retained earnings. The capital redemption reserve is undistributable under the Hong Kong Companies Ordinance section 79 C(2) but may be applied by the Bank in paying up its unissued shares to be allotted to its members as fully paid bonus shares.

After the balance sheet date the directors declared an interim dividend of 4 Hong Kong cents per share (2001: 4 Hong Kong cents per share) amounting to HK\$46,886,400 (2001: HK\$46,886,400). This dividend has not been recognised as a liability at the balance sheet date.

## 20. Material related parties transactions

During the period the Group entered into a number of transactions with its ultimate holding company and another major shareholder, China Everbright Limited and its subsidiaries, in the ordinary course of its banking business including, inter alia, lending, the acceptance and placement of interbank deposits, participation in loan syndicates, correspondent banking transactions and foreign exchange transactions. The contracts were priced based on relevant market rates at the time of each transaction, and were under the same terms as those available to other counterparties and customers of the Group. In the opinion of the Directors these transactions were conducted on normal commercial terms.

Information relating to income and expense from related party transactions during the period and balances outstanding as at the balance sheet date is set out below:

	<b>Six months ended</b>	
	<b>30 June 2002 HK\$'000</b>	30 June 2001 HK\$'000
(a) Income/(expense)		
Interest income	2,417	6,154
Interest expenses	(2,814)	(16,296)
	<b>As at 30 June 2002 HK'000</b>	<b>As at 31 December 2001 HK'000</b>
(b) Assets		
<i>Ultimate holding company</i>		
Short term funds	201,999	0
Accrued interest and other accounts	<u>1,813</u>	<u>1,163</u>
Due from ultimate holding company	<u>203,812</u>	<u>1,163</u>
<i>Other related parties</i>		
Loans and advances to customers	20,000	38,000
Accrued interest and other accounts	<u>15</u>	<u>5</u>
Due from other related parties	<u>20,015</u>	<u>38,005</u>
Total receivable	<u><u>223,827</u></u>	<u><u>39,168</u></u>

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
(c) Liabilities		
<i>Ultimate holding company</i>		
Deposits and balances with other banks	0	118,970
Other accounts and provisions	0	22
	<u>0</u>	<u>118,992</u>
Due to ultimate holding company	0	118,992
	<u>0</u>	<u>118,992</u>
<i>Other related parties</i>		
Current, fixed and other deposits of customers	0	103,215
Other accounts and provisions	0	60
	<u>0</u>	<u>103,275</u>
Due to other related parties	0	103,275
	<u>0</u>	<u>103,275</u>
Total payable	<u>0</u>	<u>222,267</u>

## 21. Outstanding commitments

- (a) Capital commitments outstanding at the balance sheet date not provided for in the accounts are as follows:

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
Contracted for	40,672	54,863
	<u>40,672</u>	<u>54,863</u>

- (b) The total future minimum lease payments under non-cancellable operating leases are payable as follows:

	As at 30 June 2002 HK'000	As at 31 December 2001 HK'000
Within one year	13,999	13,834
After one year but within five years	20,746	10,667
	<u>34,745</u>	<u>24,501</u>

## 22. Off-balance sheet exposures

### (a) *Contingent liabilities and commitments*

The following is a summary of the contractual and risk-weighted amounts of each significant class of contingent liabilities and commitments:

	As at 30 June 2002		As at 31 December 2001	
	Contractual Amounts HK\$'000	Risk Weighted Amounts HK\$'000	Contractual Amounts HK\$'000	Risk Weighted Amounts HK\$'000
Direct credit substitutes	58,514	58,514	62,920	62,920
Transaction-related contingencies	396,552	198,276	17,260	8,630
Trade-related contingencies	120,333	24,067	74,232	14,804
Trade bills for collection and shipping guarantees	220,763	0	295,828	0
Undrawn loan facilities				
– with an original maturity of under 1 year or which are unconditionally cancellable	5,650,335	0	6,029,268	0
– with an original maturity of 1 year or over	688,454	344,227	957,662	478,831
Forward forward deposits placed	697,394	139,479	263,884	52,777
	<u>7,832,345</u>	<u>764,563</u>	<u>7,701,054</u>	<u>617,962</u>

### (b) *Derivatives*

Derivatives refer to financial contracts whose value depends on the value of one or more underlying assets or indices.

	As at 30 June 2002		
	Contractual Amounts HK\$'000	Risk Weighted Amounts HK\$'000	Replacement Costs HK\$'000
Exchange rate contracts	2,670,664	12,477	28,685
Interest rate contracts	365,753	651	1,619
	<u>3,036,417</u>	<u>13,128</u>	<u>30,304</u>



	As at 31 December 2001		
	Contractual	Risk	Replacement
	Amounts	Weighted	Costs
	HK\$'000	Amounts	HK\$'000
	HK\$'000	HK\$'000	HK\$'000
Exchange rate contracts	1,113,206	2,398	14,717
	<u>1,113,206</u>	<u>2,398</u>	<u>14,717</u>

The replacement costs and credit risk-weighted amounts of the off-balance sheet exposures disclosed in parts (a) and (b) of this note to account do not take into account the effects of bilateral netting arrangements. The tables above gives the contractual amounts, replacement cost and credit risk-weighted amounts of off-balance sheet transactions. These are assessed in accordance with the HKMA's guidelines which implement the Basle agreement on capital adequacy and depend on the status of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% for contingent liabilities and commitments, and from 0% to 50% for exchange rate and interest rate contracts. Replacement cost represents the cost of replacing all contracts which have a positive value when marked to market. The credit risk-weighted amount refers to the amount as computed in accordance with the Third Schedule to the Hong Kong Banking Ordinance. Off-balance sheet financial instruments arise from forward and swap transactions undertaken by the Group in the foreign exchange and interest rate markets. The contractual amounts of these instruments indicate the volume of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

The above financial instruments represent transactions that are substantially all initiated in response to customer demands and no significant positions are maintained by the Group.