THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION

If you are in any doubt as to any aspect of this circular or as to the action to be taken, you should consult your licensed securities dealer, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold or transferred all your shares in CITIC International Financial Holdings Limited, you should at once hand this circular, together with the enclosed form of proxy, to the purchaser or transferee or the bank, licensed securities dealer or other agent through whom the sale or transfer was effected for transmission to the purchaser.

中信國際金融控股有限公司
CITIC INTERNATIONAL FINANCIAL HOLDINGS LIMITED

(Incorporated in Hong Kong with limited liability under the Companies Ordinance)

(Stock Code: 183)

SUBSCRIPTION OF SHARES BY BBVA AND STRATEGIC COOPERATION

VERY SUBSTANTIAL ACQUISITION AND CONNECTED TRANSACTION IN RELATION TO THE PROPOSED ACQUISITION OF FURTHER INTEREST IN CHINA CITIC BANK

Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders

SOMERLEY LIMITED

A letter from the Independent Board Committee containing its recommendation to the Independent Shareholders in relation to the proposed acquisition of an interest in China CITIC Bank is set out on page 29 of this circular. A letter from Somerley Limited, the Independent Financial Adviser, containing its advice to the Independent Board Committee and the Independent Shareholders is set out on pages 30 to 54 of this circular.

A notice convening the EGM to be held on 9 February 2007 at 10:00 a.m. at Salon 5, Level 3, JW Marriott Hotel Hong Kong, Pacific Place, 88 Queensway, Hong Kong is set out on pages 373 to 377 of this circular. If you are not able to attend the EGM, you are requested to complete and return the enclosed form of proxy in accordance with the instructions printed thereon to the Company's share registrar, Computershare Hong Kong Investor Services Limited at 46th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong as soon as possible but in any event not less than 48 hours before the time appointed for holding the EGM. Completion and return of the form of proxy will not preclude you from attending and voting in person at the EGM or any adjournment of it should you so wish.

29 December 2006

CONTENTS

In this circular, the following expressions have the following meanings unless the context requires otherwise:

"Affiliate"	as applied to any person, any other person directly or indirectly controlling, controlled by or under common control with such person and for such purposes, "control" with respect to any person, is to have the ability to direct the management and affairs of such person, whether through the ownership of voting securities or by contract, and such ability is deemed to exist when any person holds a majority of the outstanding voting securities, or the economic rights and benefits, of such person;
"Announcement"	the announcement of the Company dated 23 November 2006;
"Anti-Dilution Top Up Right"	the top up right granted to BBVA by the Company under the Subscription Agreement in relation to the issue of new Shares by the Company, further details of which are set out in the section headed "Anti-Dilution Top Up Right" in this circular;
"Approved State Valuation"	the valuation of net assets of CNCB required to be prepared pursuant to requirements under PRC laws and to be approved by the PRC Ministry of Finance;
"Asia"	Greater China, Japan, North Korea, South Korea, Malaysia, Thailand, Cambodia, Indonesia, Singapore, Laos, Vietnam, Australia and New Zealand;
"Associate"	has the meaning ascribed thereto under the Listing Rules;
"Banking Ordinance"	the Banking Ordinance (Cap. 155 of the Laws of Hong Kong);
"BBVA"	Banco Bilbao Vizcaya Argentaria, S.A., a company incorporated in the Kingdom of Spain;
"Board"	the board of Directors;
"CIAM"	CITIC International Assets Management Limited;
"CITIC Group"	CITIC Group, a state-owned enterprise incorporated in the PRC;
"CITIC Group Agreement"	the share purchase agreement dated 22 November 2006 between CITIC Group and BBVA in relation to, among other things, the sale and purchase of the Sale Shares;

"CITIC Group Shares"	the number of Shares issued to CITIC Group pursuant to the Original Agreement;
"CKWB"	CITIC Ka Wah Bank Limited;
"CNCB"	China CITIC Bank;
"CNCB Cooperation Agreement"	the agreement to be entered into among CITIC Group, CNCB and the Company pursuant to the CNCB Cooperation MOU;
"CNCB Cooperation MOU"	the memorandum of understanding entered into among CITIC Group, CNCB and the Company on 22 November 2006;
"CNCB Top Up"	the subscription of the Top Up Shares by the Company in CNCB (or its successor, the Joint Stock Company) pursuant to the Top Up Agreement;
"Company"	CITIC International Financial Holdings Limited (stock code: 183), a company incorporated in Hong Kong and the Shares of which are listed on the Stock Exchange;
"Cooperation MOU"	the memorandum of understanding entered into between the Company and BBVA on 22 November 2006;
"Directors"	the directors of the Company;
"EGM"	the extraordinary general meeting of the Company to be convened on 9 February 2007 to consider and, if thought fit, approve, amongst other things, the Top Up Agreement, the CNCB Cooperation MOU (including the CNCB Cooperation Agreement), the Subscription Agreement, the Cooperation MOU and the transactions contemplated therein;
"Greater China"	the PRC (including without limitation Hong Kong and Macau);
"Greenshoe Shares Allotment Right"	the option to be granted by the Joint Stock Company to the underwriters of the global offering in respect of the shares of the Joint Stock Company, exercisable by the underwriters or their representative, to require the Joint Stock Company to issue additional shares of the Joint Stock Company as part of the global offering;

"Group"	the Company and its subsidiaries;
"HK$"	Hong Kong dollars, the lawful currency of Hong Kong;
"HKMA"	The Hong Kong Monetary Authority;
"Hong Kong"	the Hong Kong Special Administrative Region of the PRC;
"IFRS"	International Financial Reporting Standards issued by the International Accounting Standards Board;
"Independent Board Committee"	the independent board committee of the Company comprising of Mr. Rafael Gil-Tienda, Mr. Lam Kwong Siu and Mr. Tsang Yiu Keung Paul;
"Independent Financial Adviser"	Somerley Limited which has been appointed to make recommendations to the Independent Board Committee and the Independent Shareholders;
"Independent Shareholders"	Shareholders other than CITIC Group and its Associates;
"Joint Stock Company"	the joint stock company to be restructured from CNCB;
"Latest Practicable Date"	22 December 2006, being the latest practicable date prior to the printing of this circular for ascertaining certain information contained in this circular;
"Listing Rules"	the Rules Governing the Listing of Securities on the Stock Exchange;
"Lock-up Period"	the period in which BBVA is restricted from disposing or encumbering any Shares if the effect would be that BBVA and its Affiliates in aggregate hold less than the Locked-up Shares;
"Locked-up Shares"	the aggregate of the Subscription Shares and the Sale Shares;
"Original Agreement"	the sale and purchase agreement entered into between the Company and CITIC Group dated 13 April 2006, further details of which are set out in the Original Circular;
"Original Circular"	the circular of the Company dated 30 June 2006;

"Original Investment"	the acquisition of the equity interest in CNCB pursuant to the Original Agreement, further details of which are set out in the Original Circular;
"PRC"	the People's Republic of China;
"Relevant Period"	any period during which BBVA is a strategic investor in CNCB (and which period shall include, for the avoidance of doubt, any period during which: (i) BBVA holds 5% or more of the total number of issued and outstanding shares in CNCB; or (ii) BBVA holds less than 5% of the total number of issued and outstanding shares in CNCB as a result of: (a) a dilution due to any exercise of any over-allotment option (or similar arrangement) for the issue of securities in respect of a public offering; or (b) a dilution due to an issue of shares in respect of which BBVA was not legally or contractually permitted to participate);
"Sale Shares"	167,143,593 Shares to be acquired by BBVA from CITIC Group pursuant to the CITIC Group Agreement;
"SFO"	the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong);
"Shareholder(s)"	holder(s) of the Shares;
"Shares"	ordinary shares of HK$1.00 each in the share capital of the Company;
"Stock Exchange"	The Stock Exchange of Hong Kong Limited;
"Subscriber Directors"	the persons nominated by BBVA to the Board as non-executive Directors;
"Subscription"	the subscription of the Subscription Shares by BBVA under the Subscription Agreement;
"Subscription Agreement"	the subscription agreement entered into between the Company and BBVA dated 22 November 2006;
"Subscription Completion Date"	the 10th business day after the conditions are fulfilled or such other date as the Company and BBVA agree in writing;
"Subscription Consideration"	HK$3,897,788,600;

"Subscription Price"	HK$5.83 per Subscription Share;
"Subscription Shares"	668,574,374 Shares;
"Top Up Agreement"	the subscription agreement entered into among CNCB, CITIC Group and the Company dated 22 November 2006;
"Top Up Completion Date"	the date on which the CNCB Top Up under the Top Up Agreement is completed, which shall occur on the same date when the subscription for global offering of H-shares and A-shares (if applicable) of the Joint Stock Company is completed;
"Top Up Consideration"	the Top Up Shares multiplied by the Top Up Price, provided that the Top Up Consideration (on the basis that this is not aggregated to the Original Investment) shall not result in any of the Company's "percentage ratios" under Rule 14.07 of the Listing Rules to exceed 25%;
"Top Up Price"	the subscription price for each Top Up Share equivalent to the final Hong Kong dollar price per H-share of the Joint Stock Company at which the H-shares of the Joint Stock Company are to be offered to the public; and
"Top Up Shares"	the H-shares to be subscribed by the Company in accordance with the Top Up Agreement such that upon the Top Up Completion Date, the percentage of equity interests to be held by the Company in the Joint Stock Company shall be no less than 15% of the total equity interests in the Joint Stock Company, subject to a maximum cap amount.

中信國際金融控股有限公司
CITIC INTERNATIONAL FINANCIAL HOLDINGS LIMITED
(Incorporated in Hong Kong with limited liability under the Companies Ordinance)
(Stock Code: 183)

Chairman:
Mr. Kong Dan

Vice Chairman:
Mr. Chang Zhenming

Executive Directors:
Mr. Dou Jianzhong
Mrs. Chan Hui Dor Lam Doreen
Mr. Lo Wing Yat Kelvin
Mr. Roger Clark Spyer
Mr. Zhao Shengbiao

Non-executive Directors:
Mr. Chen Xiaoxian
Mr. Feng Xiaozeng
Mr. Ju Weimin
Mr. Liu Jifu
Mr. Wang Dongming

Independent Non-executive Directors:
Mr. Rafael Gil-Tienda
Mr. Lam Kwong Siu
Mr. Tsang Yiu Keung Paul

Registered Office:
Suites 1801-2
Bank of America Tower
12 Harcourt Road
Central
Hong Kong

29 December 2006

To the Shareholders

Dear Sir/Madam,

**SUBSCRIPTION OF SHARES BY BBVA
AND
STRATEGIC COOPERATION**

**VERY SUBSTANTIAL ACQUISITION
AND CONNECTED TRANSACTION
IN RELATION TO THE PROPOSED ACQUISITION OF
FURTHER INTEREST IN CHINA CITIC BANK**

INTRODUCTION

AGREEMENTS WITH BBVA

Subscription Agreement

As part of the Company's strategic vision to expand its regional capabilities, the Company has on 22 November 2006 entered into the Subscription Agreement with BBVA.

Pursuant to the Subscription Agreement, BBVA, as a strategic investor, has agreed to subscribe for, and the Company has agreed to allot, 668,574,374 Shares at a price of HK$5.83 each. The Subscription Consideration is HK$3,897,788,600 and will be payable in cash on completion.

The Company has been informed by CITIC Group that CITIC Group has on 22 November 2006 entered into the CITIC Group Agreement with BBVA pursuant to which CITIC Group has agreed to sell and BBVA has agreed to purchase 167,143,593 Sale Shares at a consideration of HK$974,447,147.

Business Cooperation with BBVA

With the introduction of BBVA as a strategic partner of the Group, the Company has on 22 November 2006 entered into the Cooperation MOU with BBVA confirming the intention of the parties to pursue discussions in relation to business cooperation, merger or acquisition by the Company and/or CKWB of BBVA's existing wholesale banking business in Asia and an increase by BBVA of its shareholding interest in the Company and/or a subscription for CKWB shares. Further information in relation to the Cooperation MOU is set out below.

AGREEMENTS WITH CITIC GROUP AND CNCB

CNCB Top Up

On 13 April 2006, the Company entered into the Original Agreement with CITIC Group pursuant to which the Company agreed to purchase approximately 19.9% of the entire equity interests of CNCB from CITIC Group. On 30 June 2006, CITIC Group contributed RMB5 billion cash to the registered capital of CNCB. In addition, CITIC Group increased the capital of CNCB by retaining profits of RMB2.4 billion in CNCB. As a result of these capital contributions, upon receiving the relevant governmental approvals and completing the relevant registration procedures, the percentage equity interest of the Joint Stock Company (upon its establishment) to be held by the Company will be approximately 15.17%.

CITIC Group has undertaken to the Company that if CNCB decides to increase its capital prior to an investment by a strategic investor and/or the listing of CNCB, such capital injection shall be the responsibility of CITIC Group and any such capital injection shall not result in the value of the Company's equity interest in CNCB falling below a lower equity value to that accorded to the Company on the date and that the Company's interest will not be less than 15%.

To ensure that the Company's interest in CNCB will not be less than 15%, the Company entered into the Top Up Agreement with CNCB and CITIC Group on 22 November 2006, pursuant to which the Company agreed to subscribe for, and CNCB (or, its successor, the Joint Stock Company) agreed to issue the Top Up Shares such that upon the Top Up Completion Date, the percentage of equity interests to be held by the Company in the Joint Stock Company is expected to be no less than 15% of the total equity interests in the Joint Stock Company, subject to the maximum cap amount as further set out below. CITIC Group has undertaken to procure CNCB or the Joint Stock Company to complete the CNCB Top Up. The consideration for the Top Up Shares is to be satisfied by cash and will be calculated by multiplying the Top Up Price by the Top Up Shares provided that the total consideration (calculated on the basis that the CNCB Top Up is not aggregated with the Original Investment) shall not result in any of the Company's "percentage ratios" under Rule 14.07 of the Listing Rules in respect of the CNCB Top Up to exceed 25%. The CNCB Top Up is subject to certain conditions as described below.

CNCB Cooperation MOU

In order to set out a clearer framework for cooperation between the Company, CNCB and CITIC Group, on 22 November 2006, the Company has also entered into the CNCB Cooperation MOU with CITIC Group and CNCB pursuant to which, after obtaining Independent Shareholders' approval for the CNCB Cooperation MOU, the parties to the CNCB Cooperation MOU will execute the CNCB Cooperation Agreement (subject to such amendments as may be required by the relevant regulatory authorities of the PRC and Hong Kong including the relevant stock exchanges in the PRC and in Hong Kong).

Very substantial acquisition

As the Top Up Agreement was entered into within 12 months from the Original Agreement, in accordance with Rule 14.22 of the Listing Rules, the transaction contemplated under the Top Up Agreement is aggregated with the Original Agreement for the purposes of calculating the percentage ratios under the Listing Rules. As certain of the percentage ratios calculated under the Listing Rules in respect of the Top Up Agreement (aggregated with the Original Investment) exceed 100%, the CNCB Top Up constitutes a very substantial acquisition by the Company and requires Independent Shareholders' approval under Rule 14.49 of the Listing Rules.

Connected transaction

In addition, as CITIC Group is the controlling shareholder of the Company and CNCB is a subsidiary of CITIC Group, the CNCB Top Up, the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transaction contemplated therein constitute connected transactions of the Company. Given the size of the CNCB Top Up, the transaction contemplated under the Top Up Agreement falls under Rule 14A.16(5) of the Listing Rules and are subject to the reporting, announcement and Independent Shareholders' approval requirements of the Listing Rules pursuant to Rule 14A.17. The CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transactions contemplated therein will also be brought forward in the EGM for Independent Shareholders' approval.

The purpose of this circular is to provide you with information on amongst other things, the Top Up Agreement, the CNCB Cooperation Agreement, the Subscription Agreement, the recommendation of the Independent Board Committee and the letter of advice from Somerley Limited in respect of the Top Up Agreement and the CNCB Cooperation Agreement and to give you notice of the EGM.

AGREEMENTS WITH BBVA

Subscription Agreement

As part of the Company's strategic vision to expand the Company's regional capabilities, the Company has on 22 November 2006 entered into the Subscription Agreement with BBVA as a strategic investor for the Shares of the Company.

Date

22 November 2006

Parties

(a) the Company (as issuer)

(b) BBVA (as subscriber), a party independent of and not connected with the Company nor with the directors, chief executive or substantial shareholder of the Company, and any of their subsidiaries or any of their respective associates. BBVA has confirmed to the Company that it has not held any interests in the Shares of the Company prior to the date of the Subscription Agreement.

Description of the Subscription

Pursuant to the Subscription Agreement, BBVA has agreed to subscribe for, and the Company has agreed to allot, 668,574,374 Shares at a price of HK$5.83 each. The Subscription Consideration is HK$3,897,788,600 and will be payable in cash on completion.

The Subscription Shares

The number of Subscription Shares is 668,574,374, represent approximately 19.8% of the issued share capital of the Company of 3,378,515,405 Shares as at the date of the Subscription Agreement, approximately 19.3% of the issued share capital of the Company of 3,468,912,372 Shares as at the Latest Practicable Date and approximately 16.2% of the Company's issued share capital as enlarged by the Subscription. Assuming the completion of the Original Agreement and on the basis that approximately 1,562 million consideration Shares are issued by the Company under the Original Agreement and there are no other changes to the issued share capital of the Company, the Subscription Shares of BBVA will represent approximately 12% of the Company's issued share capital as enlarged by the Subscription Shares and the 1,562 million consideration Shares. The net proceeds from the Subscription of approximately HK$3,890 million will be used to strengthen the Company's capital base and support its future development, including financing the additional funding requirements of the Company in respect of the CNCB Top Up. A specific mandate is proposed at the EGM for the issuance of the Subscription Shares.

Subscription Price

The subscription price is HK$5.83 per Subscription Share. This price was agreed after arm's length negotiations and represents (i) a premium of approximately 0.3% to the closing price of HK$5.81 per Share as quoted on the Stock Exchange on 21 November 2006; (ii) a premium of approximately 2.5% to the average closing price per Share of approximately HK$5.69 per Share as quoted on the Stock Exchange from 8 November 2006 to 21 November 2006 both dates inclusive, being the last ten trading days of the Shares immediately before the date on which the trading in the Shares of the Company has been suspended pending the issue of the Announcement; and (iii) a premium of approximately 9.2% to the average closing price per Share of approximately HK$5.34 per share as quoted on the Stock Exchange from 10 October 2006 to 21 November 2006 both dates inclusive, being the last thirty trading days of the Shares immediately before the date on which the trading in the Shares of the Company has been suspended pending the issue of the Announcement; and (iv) a discount of 9.2% to the closing price per Share of HK$6.42 as quoted on the Stock Exchange on the Latest Practicable Date.

Conditions precedent

Completion of the Subscription is conditional upon:

(a) the Listing Committee of the Stock Exchange agreeing to grant the listing of, and permission to deal in, the Subscription Shares (and such listing and permission not subsequently be revoked prior to the delivery of definitive share certificates representing the Subscription Shares);

(b) certain conditions precedent under the CITIC Group Agreement having been fulfilled in accordance with the terms of that agreement or waived;

(c) BBVA having been approved, or not objected to within the relevant period, by the HKMA as a minority shareholder controller (as such expression is defined in Section 2 of the Banking Ordinance) of each of the Company, CKWB and HKCB Finance Limited (as applicable) under Section 70 of the Banking Ordinance;

(d) the approval of the Bank of Spain for BBVA to enter into and perform the Subscription Agreement having been obtained;

(e) all consents, waivers, approvals, authorisations and clearances (if any) of any governmental authority or any other relevant third party necessary for the parties to proceed to completion of the Subscription Agreement having been obtained;

(f) the approval by the shareholders of the Company approving the entering into and performance of the Subscription Agreement by the Company having been obtained;

(g) no governmental or regulatory action or limitation will be placed on either party that would deprive such party of the expected benefit of the transaction contemplated under the Subscription Agreement; and

(h) (i) the execution by CITIC Group of a confirmation relating to matters in the Cooperation MOU; or (ii) the execution of certain agreements pursuant to the Cooperation MOU.

In the event any of the conditions set out above have not been fulfilled on or before 15 March 2007 (or such other date agreed by the parties in writing), the Subscription Agreement shall automatically terminate and neither party shall have any claim against the other party, except in relation to any breach caused by a party's failure to take actions within its control that it was obliged to undertake as a result of its obligation to use reasonable endeavours to procure fulfilment of a relevant condition.

Rights of the Subscription Shares

The Subscription Shares will, when issued, rank equally with the existing Shares.

Use of proceeds

The net proceeds from the Subscription of approximately HK$3,890 million will be used to strengthen the Company's capital base and support its future development, including financing the additional funding requirements of the Company in respect of the CNCB Top Up.

Completion

The Subscription is to be completed on the Subscription Completion Date.

Application for listing

Application will be made by the Company to the Stock Exchange for the grant of the listing of and permission to deal in the Subscription Shares.

Termination

BBVA may terminate the Subscription Agreement at any time prior to 8:00 a.m. (Hong Kong time) on the Subscription Completion Date if at any time prior to Completion:

(i) there occurs any suspension of dealings in the Shares for any consecutive period of 7 consecutive trading days (other than as a result of the Subscription);

(ii) any breach of any of the warranties and undertakings by the Company which comes to the knowledge of BBVA or any event occurs or any matter arises on or after the date of the Subscription Agreement and prior to the Subscription Completion Date which if it had occurred or arisen before the date of the Subscription Agreement would have rendered any of the warranties and undertakings untrue or incorrect in any respect and any such breach or failure is material or (in the reasonable opinion of BBVA) is or would materially and adversely affect the financial position or business of the Group; or

(iii) there is any adverse change, or development involving a prospective adverse change in the general affairs, condition, results of operations or prospects, management, business, stockholders' equity or in the financial or trading position of the Group as a whole which would reasonably be expected to cause a reduction in the consolidated net asset value of the Company by 10% or more from that in the Company's pro forma accounts in appendix 3 of the Circular or, if published later than the Circular, the most recently published audited consolidated accounts of the Company.

Other terms

Lock-up Period

BBVA has undertaken to the Company that unless otherwise agreed by BBVA and the Company in writing, BBVA and its relevant Affiliate shall not, at any time during the period commencing from the Subscription Completion Date and ending on:

(i) if the Cooperation MOU is not terminated but the necessary agreements required under the Cooperation MOU have not been entered into, the expiration of 36 months from the Subscription Completion Date;

(ii) if the Cooperation MOU is not terminated and the necessary agreements required under the Cooperation MOU have been entered into, the expiration of 36 months from the completion of the shareholding increase by BBVA of interest in the Company and/or CKWB contemplated under the Cooperation MOU; or

(iii) if the Cooperation MOU is terminated, the expiration of six months from the termination of the Cooperation MOU,

transfer, dispose or encumber any Shares if the effect would be that BBVA and its Affiliates in aggregate hold less than the Locked-up Shares. After the expiry of the Lock-up Period, if BBVA disposes of Shares held by it, BBVA will consult with the Company with a view to ensuring orderly market in such Shares including by way of block trades or sales on the open market.

Maintenance of public float

BBVA has undertaken to the Company that BBVA and its Affiliates will not, at any time, acquire any Shares which, in aggregate, would result in the Company not being able to maintain the minimum public float requirement pursuant to Rule 8.08(1)(a) of the Listing Rules.

Appointment of Directors

Subject to the provisions of the articles of association of the Company, the Company will convene a meeting of the Board to appoint two Subscriber Directors nominated by BBVA to the Board as non-executive Directors upon Completion.

During the Lock-up Period, in the event that any of the Subscriber Directors is removed from the Board, the Company will, as soon as practicable convene a meeting of the Board to appoint a replacement Subscriber Director to the Board such that the total number of Subscriber Directors on the Board shall be two.

Restriction from issuance of Shares

The Company has undertaken to BBVA that for the period of six months from the date of the Subscription Agreement, the Company will not enter into any agreements or do anything or acts in respect of the issue of any Shares, or any options, warrants or other rights to acquire, or securities convertible into or exchangeable for Shares other than (i) for the purposes of implementation of the transactions contemplated under the Subscription Agreement, (ii) the issue of new Shares pursuant to the exercise of the conversion rights in respect of any outstanding convertible bonds of the Company, (iii) the issue of new Shares pursuant to the exercise of the share options which have been granted or which may fall to be granted under the share option scheme of the Company, or (iv) the issue of new Shares to institutional investors (other than certain competitors of BBVA) for the purposes of raising proceeds to acquire further interests in CNCB so as to enable the Company to maintain at least 15% and not more than 16% shareholding in CNCB.

Convertible bond top up right

The Company has granted a top up right to BBVA to subscribe for new Shares at HK$5.83 per Share where the Company issues or may issue new Shares upon the exercise of the conversion rights in relation to the outstanding convertible bonds of the Company exercised after 14 November 2006. The top up right is exercisable in whole or in part and from time to time during the period commencing on the Subscription Completion Date and ending on the earlier of 10 business days after 31 December 2007 and 10 business days after such date when no convertible bonds are outstanding. The number of Shares which may be issued to BBVA under the top up right shall not exceed 17.6471% of the aggregate number of Shares issued and which may fall to be issued by the Company upon exercise of the convertible bonds (less any number of Shares issued to BBVA as a result of any prior exercise of the top up right). The expiration date of the convertible bonds is 8 November 2008. As at 14 November 2006, the total number of Shares which may fall to be issued upon the full conversion of the outstanding convertible bonds of the Company was 189,003,224 Shares. Accordingly, the maximum number of Shares which may be issued to BBVA in relation to the top up right is 33,353,587 Shares. A specific mandate will be proposed at the EGM for the issuance of the new Shares under this top up right.

Anti-Dilution Top Up Right

The Company has further granted an Anti-Dilution Top Up Right to BBVA to subscribe for new Shares at a price equivalent to the average closing price of the Company for the twenty trading days immediately before the date of the notice of exercise by BBVA of such Anti-Dilution Top Up Right where the Company issues any new Shares (other than upon conversion of the outstanding convertible bonds of the Company, the issue of new Shares pursuant to the exercise of the share options which have been granted or which may fall to be granted under the share option scheme of the Company, the issue of the CITIC Group Shares, the issue of the Subscription Shares and any issue of Shares pro rata to all Shareholders) provided that the number of new Shares issued under this top-up right would not exceed 112,984,900 Shares (being 17.6471% of the number of Shares which could be issued under the general mandate of the Company at the date of the Subscription Agreement). The Anti-Dilution Top Up Right is exercisable in whole or in part and from time to time during the period commencing on the Subscription Completion Date and ending on the 10th business day after the expiry of six months after the Subscription Completion Date. A specific mandate will be proposed at the EGM for the issuance of new Shares under the Anti-Dilution Top Up Right.

The Stock Exchange has indicated that the issue of Shares pursuant to the exercise of the Anti-Dilution Top Up Right will be subject to the following conditions:

(a) the pricing of any new Shares in respect of which BBVA is entitled to exercise its Anti-Dilution Top Up Right must be approved by the Directors (including the independent non-executive Directors) who do not have a direct interest in the transaction and who are not connected with BBVA or its associates;

(b) where the Shares to be issued pursuant to the exercise of the Anti-Dilution Top Up Right is at a discount of more than 10% to the bench mark price, being the higher of:

  (i) the closing price on the date of exercise relating to the proposed issue of Shares in respect of the Anti-Dilution Top Up Right; and

  (ii) the average closing price in the five trading days immediately prior to the earlier of:

    (1) the date of the announcement in respect of the proposed issuance of Shares in respect of the Anti-Dilution Top Up Right (if any);

    (2) the date of the relevant exercise of the Anti-Dilution Top Up Right; and

(3) the date on which the subscription price in respect of the exercise of the Anti-Dilution Top Up Right is fixed,

an independent financial adviser's opinion on the fairness of the price or value at which new Shares are to be issued to BBVA will be required, in addition to the approval of the Directors described above, and the Company will be required to include reference to this opinion in any announcement to be issued by the Company in relation to the issue of new Shares pursuant to the exercise of the Anti-Dilution Top Up Right by BBVA;

(c) where the new Shares to be issued pursuant to the exercise of the Anti-Dilution Top Up Right by BBVA is at a discount of 20% or more to the benchmark price (described above), the approval of the independent Shareholders will be required in advance of such issue; and

(d) the issue price to BBVA upon the exercise of the Anti-Dilution Top Up Right should be no less than the price offered to independent third parties.

The Company has also undertaken to BBVA that (other than the exceptions from the restrictions to issue new Shares as described above), the Company will not issue any new Shares during the period commencing on the date of the Subscription Agreement and ending ten business days after the expiry of six months after the Subscription Completion Date to the extent that the total number of such new Shares issued by the Company after the date of the Subscription Agreement, when aggregated with the number of Shares issued (or to be issued) to BBVA as a result of the exercise of this top-up right will exceed 640,246,275 Shares (being the number of Shares which could be issued under the general mandate of the Company at the date of the Subscription Agreement). For the avoidance of doubt, unless the relevant Stock Exchange and/or shareholders' approval of the Company (if required) have been obtained in respect of the Anti-Dilution Top Up Right, the Company has undertaken not issue any Shares (other than the exceptions from the restrictions to issue new Shares as described above) before the expiry of the period in which BBVA has Anti-Dilution Top Up Right.

Declaration of dividends

The Company has undertaken to BBVA that the Company shall not declare any dividends after the date of the Subscription Agreement unless the book close for the record date for the entitlement to such dividends is after the Subscription Completion Date and BBVA is entitled to such dividends in respect of the Locked-up Shares held by BBVA at that time.

Pre-emption rights

The Company has granted to BBVA from the date of the Subscription Agreement to the end of the Relevant Period, a first right of offer to acquire or procure third party (provided that BBVA retains control of the voting rights attached to the shares in CNCB which such third party proposes to acquire and provided further that the transfer is not made to certain competitors of CNCB) to acquire the shares the Company holds in CNCB in the event that the Company wishes to transfer them to any person other than its Affiliates.

The Company has further granted to BBVA from the date of the Subscription Agreement to the end of the Relevant Period, a first right of offer to acquire or procure third party (provided that BBVA retains control of the voting rights attached to the shares in CNCB which such third party proposes to acquire and provided further that the transfer is not made to certain competitors of CNCB) to acquire the shares the Company holds in CNCB in the event that the Company wishes to transfer them to its Affiliates and the number of shares in CNCB which will be offered will be the attributable interest held by BBVA in CNCB through the Company.

Business Cooperation with BBVA

With the introduction of BBVA as a strategic investor of the Group, the Company has on 22 November 2006 entered into the Cooperation MOU with BBVA confirming the intention of the parties to pursue discussions in relation to business cooperation and proposed merger or acquisition by the Company and/or CKWB of BBVA's existing wholesale banking business in Asia and an increase by BBVA of its shareholding interest in the Company and/or a subscription for CKWB shares. The Cooperation MOU provides that in the six-month period after the signing of the Cooperation MOU, the parties shall conclude discussions with a view to the signing of agreements containing the material terms relating to the proposed business transfer, business cooperation and a further increase in shareholding in the Company and/or CKWB by BBVA. In the period commencing six months after the date of the Cooperation MOU and ending nine months after the date of the Cooperation MOU, BBVA and the Company intend to discuss and agree any outstanding issues in respect of the above that are not agreed in the initial six-month period.

Exclusive strategic cooperation

Under the Cooperation MOU, for the nine-month period commencing on the date of the Cooperation MOU (or such longer period as the Company and BBVA may agree in writing), BBVA will be the sole and exclusive strategic investor in the Company (other than CITIC Group and its Affiliates). The expected areas of business cooperation are wholesale banking, treasury and capital markets, retails and others.

Non-competition

If at any time following the signing of the agreements containing the material terms relating to the proposed business transfer, business cooperation and a further increase in shareholding in the Company and/or CKWB by BBVA, BBVA and its Affiliates hold, in aggregate, a number of Shares greater than or equal to the number of Locked-up Shares, then (for the duration of any period that BBVA and its Affiliates hold, in aggregate, such a number of Shares) BBVA will not (and will procure that its Affiliates will not), whether as principal or agent, whether undertaken directly or indirectly (including through any associate, body corporate, partnership, joint venture or contractual arrangement), carry on, engage, invest, participate or otherwise be interested in any business which competes with the business of the Company and/or its subsidiaries in respect of:

(a) wholesale banking business in Asia (save for those in Greater China); and

(b) retail and wholesale banking in Greater China.

In the event that following the signing of the agreements containing the material terms relating to the proposed business transfer, business cooperation and a further increase in shareholding in the Company and/or CKWB by BBVA, there are further opportunities to acquire interests in other relevant wholesale banking businesses in Asia (except to the extent otherwise agreed by BBVA and CITIC Group in relation to the Mainland China), BBVA shall pursue such business opportunities through the alliance between BBVA and the Company and to the extent the Company or its subsidiaries do not pursue such opportunity, BBVA may pursue such opportunities provided that it complies with the non-compete principles set out above.

In the event that the Cooperation MOU is terminated after nine months from the date of the Cooperation MOU, then for the duration of six months after the date of termination, BBVA will not, and will procure that its Affiliates will not, whether as principal or agent, whether undertaken directly or indirectly (including through any associate, body corporate, partnership, joint venture or contractual arrangement), carry on, engage, invest, participate or otherwise be interested in any business which competes with the business of the Company and/or its subsidiaries in respect of wholesale and retail banking business in Hong Kong and Macau (other than in the form of, and in line with the current scale of, its operations in Hong Kong as at the date of the Cooperation MOU including organic growth). However, BBVA is not restricted from undertaking activities in respect of: (a) any passive equity investment of less than 3% of the total number of issued and outstanding shares of a publicly traded company whose principal business is financial business to the extent such activities are in the ordinary and usual course of the investment business of BBVA and its Affiliates; and (b) any equity investment in a company (other than certain agreed companies) whose principal business is not in financial business.

CITIC Group Agreement

The Company has been informed by CITIC Group that CITIC Group has on 22 November 2006 entered into the CITIC Group Agreement with BBVA pursuant to which CITIC Group has agreed to sell and BBVA has agreed to purchase 167,143,593 Sale Shares at a consideration of HK$5.83. The completion of the CITIC Group Agreement will be conditional on the simultaneous completion of the Subscription Agreement. Consequently, upon completion of both the Subscription Agreement and the CITIC Group Agreement, BBVA is expected to hold an aggregate of 835,717,967 Shares which represent approximately 24.1% of the issued share capital of the Company as at the Latest Practicable Date and approximately 20.2% of the Company's issued share capital as enlarged by the Subscription.

Information on the Company and BBVA

The Company is an investment holding company and is the holding company of CKWB, a Hong Kong licensed bank, and CIAM, an asset management company which specializes in distressed assets management, direct investment and financial advisory services. The Company also holds 50% of CITIC Capital Holdings Limited, which focuses on China-related merchant financing and investment management services.

BBVA, headquartered in Spain, is one of the leading global banks with business operations span across retail, wholesale and investment banking in 32 countries. As of 31 December 2005, BBVA achieved total assets of approximately Euro 392 billion (or approximately HK$3,930 billion), net profit of approximately Euro 3.8 billion (or approximately HK$38 billion), non-performing loan ratio of 0.94% and return on equity of 37%. BBVA is the largest bank by assets in Spain and it also has a strong presence in the European and Latin American markets. The Company also notes an announcement by BBVA dated 22 November 2006 which states that it has entered into an agreement with CITIC Group to acquire a 5% equity stake in CNCB.

Reasons and Benefits of the Subscription and the Cooperation MOU

The entering into of the Subscription will strengthen the Company's capital base and support its future development, including financing the additional funding requirements of the Company in respect of the CNCB Top Up (although the exact amount of the CNCB Top Up has not been confirmed at the Latest Practicable Date). However, with the certainty of available funding as a result of the Subscription (assuming that the Subscription Agreement will be approved by the Shareholders at the EGM), the Company will be able to significantly meet its funding needs.

Strategically, the entering into of the Subscription indicates the willingness and intention of forming a strategic partnership between the Company and BBVA. The partnership will help the Company to realize its vision of building an international bank with presence in the PRC by providing a global platform, enlarging its customer base, bringing in product expertise in areas such as wholesale banking, treasury and capital markets business and retail banking, as well as presenting new training opportunities for employees. The entering into of the Cooperation MOU further strengthens the strategic partnership, increases the level of commitment from both parties through increasing the shareholding for the strategic partner.

AGREEMENTS WITH CITIC GROUP AND CNCB

Update on the Original Agreement

On 13 April 2006, the Company entered into the Original Agreement with CITIC Group pursuant to which the Company agreed to purchase approximately 19.9% of the entire equity interests of CNCB from CITIC Group. On 30 June 2006, CITIC Group contributed RMB5 billion cash to the registered capital of CNCB. In addition, CITIC Group increased the capital of CNCB by retaining profits of RMB2.4 billion in CNCB. As a result of these capital contributions, upon receiving the relevant governmental approvals and completing the relevant registration procedures, the percentage equity interest of the Joint Stock Company (upon its establishment) to be held by the Company will be approximately 15.17%.

CITIC Group has undertaken to the Company that if CNCB decides to increase its capital prior to an investment by a strategic investor and/or the listing of CNCB, such capital injection shall be the responsibility of CITIC Group and any such capital injection shall not result in the value of the Company's equity interest in CNCB falling below a lower equity value to that accorded to the Company on the date and that the Company's interest will not be less than 15%. In the ordinary course, it is anticipated that CITIC Group may reinvest profits into CNCB. However, the Company anticipates that notwithstanding this, it would be able to maintain above 15% equity interest in CNCB.

On 22 November 2006, the Company has also been informed that the Approved State Valuation has been issued and the maximum number of Shares to be issued pursuant to the Original Agreement (assuming the maximum increase in relation to any appreciation in the RMB against the HK$) is 1,562,349,676 Shares.

To ensure that the Company's interest in CNCB will not be less than 15%, on 22 November 2006, the Company entered into the Top Up Agreement with CNCB and CITIC Group.

The Top Up Agreement

Date

22 November 2006

Parties

(a) the Company (as subscriber)

(b) CNCB

(c) CITIC Group, a state-owned enterprise incorporated in the PRC. CITIC Group is also the controlling shareholder of the Company and, as at the Latest Practicable Date, owns approximately 52% of the Shares in issue.

Summary of the CNCB Top Up

Subject to fulfillment of the conditions precedent described below, the Company agreed to subscribe for, and CNCB (or its successor, the Joint Stock Company) agreed to issue the Top Up Shares. CITIC Group has undertaken to procure CNCB or its successor, the Joint Stock Company, to complete the CNCB Top Up.

Top Up Shares

The number of Top Up Shares to be subscribed for by the Company is determined as follows:

(1) upon the CNCB Top Up Completion Date, the percentage of equity interests to be held by the Company in the Joint Stock Company as of the Top Up Completion Date shall be no less than 15% of the total equity interests in CNCB (or its successor, the Joint Stock Company), as enlarged by the issue of the Top Up Shares, on a fully diluted basis.

(2) if the Top Up Consideration required to be paid by the Company for the Top Up Shares in accordance with the principle set out in paragraph (1) above will result in any of the Company's "five tests" under Rule 14.07 of the Listing Rules exceeding 25%, then the amount of Top Up Shares to be subscribed by the Company shall be the maximum whole number of Top Up Shares that would not result in Company's "five tests" exceeding 25% under Rule 14.07 of the Listing Rules.

Consideration

The Top Up Consideration is to be satisfied by cash and will be calculated by multiplying the Top Up Price and the Top Up Shares, provided that the Top Up Consideration (on the basis that this is not aggregated to the Original Investment) shall not result in any of the Company's "percentage ratios" under Rule 14.07 of the Listing Rules exceeding 25%. Assuming the "consideration test" under Rule 14.07(4) is the most relevant to determining the Top Up Consideration, this translates to a maximum of approximately HK$7,196 million (based on the market capitalisation of the Company as at 22 November 2006 as enlarged by the issue of 1,562,349,676 Shares under the Original Agreement).

In calculating the percentage ratios, the parties agree that this will be on the basis that the Original Agreement has completed and the consideration ratio will be calculated based on the average closing price of the Shares as quoted on the Stock Exchange the five trading days immediately before the date of the Top Up Agreement.

Basis of the Consideration

The CNCB Top Up Consideration was determined after arm's length negotiations between the Company and CNCB and will be based on the Top Up Price as the Top Up Price represents the final Hong Kong dollar price per H-share of the Joint Stock Company at which the H-shares of the Joint Stock Company will be offered to the public.

Conditions precedent

Completion of CNCB Top Up is conditional upon the satisfaction or waiver of the following conditions precedent:

(a) the Stock Exchange approving the listing of, and permission to deal in, the H-shares of the Joint Stock Company to be listed in the Stock Exchange (including the Top Up Shares);

(b) all requisite authorizations and approvals required for CNCB, the Joint Stock Company and/or CITIC Group for the CNCB Top Up having been obtained (except for the updated change in the business license in respect of the CNCB Top Up);

(c) all requisite consents, authorizations and approvals (including but not limited to approvals from the Stock Exchange and The Shanghai Stock Exchange) required for the Company for the CNCB Top Up having been obtained;

(d) the CNCB Cooperation Agreement with form and substance substantially the same as set out in the CNCB Cooperation MOU having been executed by all parties subject to amendments required by the relevant PRC or Hong Kong governmental and regulatory authorities;

(e) the approval at the shareholders meeting of the Joint Stock Company and approval by the Independent Shareholders of the Top Up Agreement, the CNCB Top Up and all transactions thereunder having been obtained; and

(f) the representations and warranties given under the Top Up Agreement by the parties remaining true, correct, accurate and not misleading up to the Top Up Completion Date.

If any of the conditions set out above has not been fulfilled (or waived) on or before 31 December 2007, or such later date as all the parties may agree in writing, the Top Up Agreement will automatically terminate and no party shall have any claim of any nature whatsoever against any other party (save in respect of any rights and liabilities of the parties which have accrued prior to termination).

Completion

Completion shall take place on the Top Up Completion Date, being the date on which the CNCB Top Up under the Top Up Agreement is completed, which shall occur on the same date when the subscription for global offering of H-shares and A-shares (if applicable) of the Joint Stock Company is completed.

Other Terms

CNCB and CITIC Group have undertaken jointly and severally and on behalf of the Joint Stock Company that after the date on which the Greenshoe Shares Allotment Right expires, in the event that CNCB decides to increase its equity interest, the Joint Stock Company and CITIC Group will support the Company to acquire more equity interests (by way of subscribing existing equity interest or new equity interest), so as to ensure that, under all circumstances, the shareholding of the Company, after the said acquisition, will not be less than 15% of the total amount of capital stock of the Joint Stock Company on a fully diluted basis. The parties also agree that such acquisition shall comply with the relevant consents, requirements of law and relevant governmental rules in all circumstances and the subscription price should be the lowest price as allowed under the relevant consents, requirements of law and governmental rules. Should the undertaking given by CNCB and CITIC Group be in breach of any consents or governmental rules or cause the Joint Stock Company unable to satisfy the requirements of the Stock Exchange, the rights and obligations of the parties pursuant to this undertaking will cease to have any effect. In the event that any additional acquisition of interest in CNCB is required to be made from CNCB or CITIC Group, this will constitute a connected transaction of the Company and the Company will comply with the relevant requirements of the Listing Rules as appropriate.

The CNCB Cooperation MOU

In order to set out a clearer framework of cooperation between the Company, CNCB and CITIC Group, on 22 November 2006, the Company has also entered into the CNCB Cooperation MOU with CITIC Group and CNCB pursuant to which, after obtaining Independent Shareholders' approval, the parties to the CNCB Cooperation MOU will execute the CNCB Cooperation Agreement (subject to such amendments as may be required by the relevant regulatory authorities of the PRC and Hong Kong including the relevant stock exchanges in the PRC and in Hong Kong).

Under the CNCB Cooperation Agreement, the parties will form the basis of avoiding simple competition. CNCB will confirm that it has no intention to compete with the Company in Hong Kong by establishing any rival branches or commercial banking network but will continue the development of its current operations in Hong Kong and will only establish new operations in Hong Kong after having non-binding consultation with the Company. On the other hand, the Company will confirm that neither the Company nor CKWB will have any intention to compete with CNCB in the Mainland by establishing any rival branches or commercial banking network and will procure that CKWB will not establish any additional branches in the Mainland. However, the development of the current operations in the Mainland will be continued.

The CNCB Cooperation MOU and the framework of the CNCB Cooperation Agreement is subject to Independent Shareholders' approval and the CNCB Cooperation Agreement will also be subject to further amendments as required by the relevant regulatory authorities.

Information on CNCB and CITIC Group

CNCB is principally engaged in the business of provision of banking and financing services in the PRC. CITIC Group is the controlling shareholder of CNCB.

The following table shows the audited, consolidated financial information of CNCB for the years ended 31 December 2004 and 31 December 2005 (both prepared in accordance with IFRS):

	Audited, consolidated financial information for the year ended 31 December 2004	Audited, consolidated financial information for the year ended 31 December 2005
Net profit before taxation and extraordinary items	RMB4,061 million (approximately HK$3,942 million)	RMB5,453 million (approximately HK$5,293 million)
Net profit after taxation and extraordinary items	RMB2,428 million (approximately HK$2,357 million)	RMB3,089 million (approximately HK$2,993 million)

The audited consolidated net book value of CNCB as at 31 December 2005 was RMB23,225 million (approximately HK$22,543 million).

CITIC Group was approved by the PRC's State Council and established in 1979. CITIC Group operates a wide range of businesses in the financial, services and industrial investment sectors. One of its main focuses is the development of financial businesses, with substantial interests in two commercial banks and non-banking financial institutions including securities firms, an insurance company, as well as a trust company. CITIC Group is the controlling shareholder of the Company and therefore, is a connected person of the Company.

Rule 4.10 Waiver

Rule 4.10 of the Listing Rules requires that the information to be disclosed in respect of Rules 4.04 to 4.09 of the Listing Rules must be in accordance with best practice which is at least that required to be disclosed in respect of those specific matters in the accounts of a company under the Companies Ordinance and Hong Kong Financial Reporting Standards or IFRS and, in the case of banking companies, the Financial Disclosure by Locally Incorporated Authorised Institutions issued by the HKMA ("HKMA guidelines").

The Company is currently unable to provide certain disclosures in respect of the accounts of CNCB as required under Supervisory Policy Manual FD-1 "Financial Disclosure by Locally Incorporated Authorised Institutions" issued by the HKMA. The Company has applied to the Stock Exchange for a waiver from strict compliance with the requirement under Rule 4.10 of the Listing Rules to the extent that the disclosure does not fully comply with the HKMA guidelines.

The HKMA guidelines require a separate disclosure in relation to movements in the allowance for loan impairment losses for individually assessed loans and for collectively assessed loans. The breakdown of such movements is not available from the systems of CNCB and therefore could not be provided. However, in lieu of this information, disclosure on the movements on an aggregated basis has been disclosed in Note 16(b) to the accountants' report of CNCB in Appendix III of this circular.

In addition, the HKMA guidelines require a separate disclosure in relation to the amount of new provisions charged to the income statement and the amount of provisions released back to the income statement in the movement of allowance for loan impairment losses. Similarly, the systems of CNCB did not contain information in relation to the amount of new provisions charged to the income statement and the amount of provisions released back to the income statement in the movement of allowance for loan impairment losses. However, in lieu of that, disclosure of these two amounts on a net basis has been made in Note 16(b) to the accountants' report of CNCB in Appendix III of this circular.

Reasons for and Effects / Benefits of the CNCB Top Up, the CNCB Cooperation MOU and the CNCB Cooperation Agreement

As the CNCB Top Up will enable the Company to maintain its 15% equity interest in CNCB which, together with the ability of the Company to exercise significant influence over CNCB through board representation, provide the basis on which the Group intends to equity account for its investment in CNCB, the Directors believe that the CNCB Top Up is beneficial to the Company.

The Directors including the Independent Non-executive Directors (whose views are subject to the advice of the Independent Financial Adviser) consider the CNCB Top Up and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) to be in the interests of the Company and the Shareholders as a whole and the terms of the CNCB Top Up and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) to be fair and reasonable.

Effect on Earnings and Assets and Liabilities of the Company

Based on the unaudited pro forma combined consolidated balance sheet of the Group as set out in Appendix IV, the net asset value of the Group (taking into account the CNCB Top Up, the Original Investment and the Subscription and on the basis of the assumptions of the preparation of the unaudited pro forma financial information set out in Appendix IV), as at 30 June 2006, would be approximately HK$18,992 million and based on the unaudited pro forma combined consolidated income statement of the Group (taking into account the CNCB Top Up, the Original Investment and the Subscription and on the basis of the assumptions of the preparation of the unaudited pro forma financial information set out in Appendix IV), as at 30 June 2006, the net profit after tax of the Group for the six months ended 30 June 2006 would be approximately HK$748 million.

The pro forma financial information set out in Appendix IV are prepared in accordance with Rule 4.26 of the Listing Rules for the purpose of providing investors information on the effect of the CNCB Top Up, the Original Investment and the Subscription (on the assumption that the maximum Top Up Consideration of HK$7,196 million was used in the preparation of the pro forma financial information). The statements are prepared for illustrative purpose only and because of their nature, they do not purport to present a picture of the actual financial performance of the Company (taking into account the CNCB Top Up, the Original Investment and the Subscription) (the "Combined Group") has the CNCB Top Up, the Original Investment and the Subscription actually been completed as at the relevant dates as set out on the basis stated. The unaudited pro forma financial information of the Combined Group does not purport to predict the Combined Group's future financial position or results of operations.

INCREASE IN AUTHORISED SHARE CAPITAL OF THE COMPANY

The Directors further propose that the existing authorised share capital of the Company be increased from HK$6,000,000,000 to HK$8,000,000,000 by creation of additional 2,000,000,000 Shares (the "Proposal").

GENERAL

As the Top Up Agreement was entered into within twelve months from the Original Agreement, in accordance with Rule 14.22 of the Listing Rules, the transaction contemplated under the Top Up Agreement is aggregated with the Original Agreement for the purposes of calculating the percentage ratios under the Listing Rules. As certain of the percentage ratios calculated under the Listing Rules in respect of the Top Up Agreement (aggregated with the Original Investment) exceed 100%, the CNCB Top Up constitutes a very substantial acquisition by the Company and requires Independent Shareholders' approval under Rule 14.49 of the Listing Rules. In addition, as CITIC Group is the controlling shareholder of the Company and CNCB is a subsidiary of CITIC Group, the CNCB Top Up, the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transactions contemplated therein constitute connected transactions of the Company. Given the size of the CNCB Top Up, the transaction contemplated under the Top Up Agreement falls under Rule 14A.16(5) of the Listing Rules and are subject to the reporting, announcement and Independent Shareholders' approval requirements of the Listing Rules pursuant to Rule 14A.17 of the Listing Rules. The CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transactions contemplated therein will also be brought forward in the EGM for Independent Shareholders' approval.

To the best of the Directors' knowledge, information and belief, having made all reasonable enquiries, apart from CITIC Group and its associates, no other Shareholder has a material interest in the CNCB Top Up and accordingly, only CITIC Group and its

Associates are required to abstain from voting on the resolution to approve the Top Up Agreement, the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transactions contemplated therein at the EGM.

The Subscription Agreement, the Cooperation MOU and the transactions contemplated therein will also be brought to the Shareholders for their approval at the EGM.

EGM

A notice convening an EGM of the Company to be held on 9 February 2007 at 10:00 a.m. at Salon 5, Level 3, JW Marriott Hotel Hong Kong, Pacific Place, 88 Queensway, Hong Kong is set out on pages 373 to 377 of this circular. Whether or not you are able to attend the meeting in person, you are requested to complete and return the accompanying form of proxy in accordance with the instructions printed thereon to the Company's share registrar, Computershare Hong Kong Investor Services Limited, at 46th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong as soon as practicable but in any event not later than 48 hours before the time appointed for the holding of the meeting or the adjourned meeting (as the case may be). Completion and return of the form of proxy will not preclude you from attending and voting at the meeting or any adjourned meeting thereof (as the case may be) should you so desire.

PROCEDURE FOR DEMANDING A POLL AT A GENERAL MEETING OF THE COMPANY

Article 69 of the articles of association of the Company sets out the procedure by which the Shareholders may demand a poll:

At any general meeting, a resolution put to the vote of the meeting shall be decided on a show of hands unless (before or on the declaration of the result of the show of hands or on the withdrawal of any other demand for a poll) a poll is demanded by:

(i) the Chairman of the meeting; or

(ii) at least three members present in person (or in the case of a member being a corporation, by its duly authorized representative) or by proxy and entitled to vote at the meeting; or

(iii) any member or members present in person (or in the case of a member being a corporation, by its duly authorised representative) or by proxy and representing in the aggregate not less than one-tenth of the total voting rights of all members having the right to attend and vote at the meeting; or

(iv) any member or members present in person (or in the case of a member being a corporation, by its duly authorised representative) or by proxy and holding shares conferring a right to attend and vote at the meeting on which there have been paid up sums in the aggregate equal to not less than one-tenth of the total sum paid up on all shares conferring that right.

Unless a poll is so demanded and the demand is not withdrawn, a declaration by the Chairman that a resolution has, on a show of hands, been carried unanimously or by a particular majority or lost shall be final and conclusive, and an entry to that effect in the minute book of the Company shall be conclusive evidence of the fact without proof of the number or proportion of the votes recorded for or against such resolution.

INDEPENDENT BOARD COMMITTEE

An Independent Board Committee comprising of Mr. Rafael Gil-Tienda, Mr. Lam Kwong Siu and Mr. Tsang Yiu Keung Paul has been formed to advise the Independent Shareholders as to whether the terms of the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) are fair and reasonable and whether such transaction is in the interest of the Company and its Shareholders as a whole and to advise the Independent Shareholders on how to vote in respect of the resolution to be proposed at the EGM to approve the transactions contemplated under the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement). Somerley Limited has been appointed to make recommendations to the Independent Board Committee and the Independent Shareholders as to whether the terms of the Top Up Agreement, the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) are fair and reasonable and whether the transactions contemplated under the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) are in the interests of the Company and its shareholders as a whole and to advise the Independent Shareholders on how to vote in respect of the resolution to be proposed at the EGM to approve the Top Up Agreement, the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transactions contemplated therein.

Your attention is drawn to the recommendation of the Independent Board Committee set out in its letter on page 29 of this circular.

INDEPENDENT FINANCIAL ADVISER

Somerley Limited has been appointed to make recommendations to the Independent Board Committee and the Independent Shareholders as to whether the terms of the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) are fair and reasonable and whether the transactions contemplated under the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) are in the interest of the Company and its Shareholders as a whole and to advise the Independent Shareholders on how to vote in respect of the resolution to be proposed at the EGM to approve the Top Up Agreement, the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transactions contemplated therein. Your attention is drawn to its letter to the Independent Board Committee set out on pages 30 to 54 of this circular.

RECOMMENDATION

The Directors consider that the terms of the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) are fair and reasonable and the entering into of the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) is in the interests of the Company and the Shareholders as a whole and therefore recommend the Independent Shareholders to vote in favour of the ordinary resolution to be proposed at the EGM to approve the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement).

You are advised to read carefully the letter from the Independent Board Committee on page 29 of this circular. The Independent Board Committee, having taken into account the advice of Somerley Limited, the text of which is set out on pages 30 to 54 of this circular, considers that the terms of the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) are fair and reasonable and the entering into of the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) is in the interests of the Company and the Shareholders as a whole and accordingly, the Independent Board Committee recommends the Independent Shareholders to vote in favour of the ordinary resolution to approve the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transactions contemplated therein.

The Directors further consider that the terms of the Subscription Agreement are fair and reasonable and the entering into of the Subscription Agreement is in the interests of the Company and the Shareholders as a whole and therefore recommend the Shareholders to vote in favour of the ordinary resolution to be proposed at the EGM to approve the Subscription Agreement, the issue of the Subscription Shares and to approve the issue of Shares under the top up rights pursuant to the Subscription Agreement. In addition, the Directors also recommend that the Shareholders vote in favour of the ordinary resolution to be proposed at the EGM to increase the authorised share capital of the Company.

ADDITIONAL INFORMATION

Your attention is also drawn to the additional information set out in the appendices to this circular.

By Order of the Board of
CITIC International Financial Holdings Limited
Dou Jianzhong
Director and Chief Executive Officer

中信國際金融控股有限公司
CITIC INTERNATIONAL FINANCIAL HOLDINGS LIMITED
(Incorporated in Hong Kong with limited liability under the Companies Ordinance)
(Stock Code: 183)

29 December 2006

To the Independent Shareholders

Dear Sir or Madam,

We have been appointed by the Directors to advise you in connection with the Top Up Agreement, the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) and the transactions contemplated thereunder. Details of the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) are set out in the letter from the Board on pages 6 to 28 of the circular (the "Circular") dated 29 December 2006, of which this letter forms a part. Terms defined in the Circular shall have the same meanings in this letter.

We wish to draw your attention to the letter from the Board set out on pages 6 to 28 of the Circular and the letter of advice from Somerley Limited set out on pages 30 to 54 of the Circular. Having taken into account the advice and recommendation of Somerley Limited, we consider the terms of the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) to be fair and reasonable so far as the Independent Shareholders are concerned. Accordingly, we recommend the Independent Shareholders to vote in favour of the ordinary resolution set out in the notice convening the EGM to approve the Top Up Agreement and the CNCB Cooperation MOU (including the CNCB Cooperation Agreement) at the EGM.

Yours faithfully,
Independent Board Committee

Rafael Gil-Tienda	**Lam Kwong Siu**	**Tsang Yiu Keung Paul**
Independent Non-executive Director	*Independent Non-executive Director*	*Independent Non-executive Director*

Somerley Limited
Suite 2201, 22nd Floor
Two International Finance Centre
8 Finance Street
Central
Hong Kong

29 December 2006

To: The Independent Board Committee and
the Independent Shareholders

Dear Sirs,

VERY SUBSTANTIAL ACQUISITION
AND CONNECTED TRANSACTION
IN RELATION TO THE PROPOSED ACQUISITION OF
"TOP UP" INTERESTS IN CHINA CITIC BANK
AND
CNCB COOPERATION MOU

INTRODUCTION

We refer to our appointment to advise the Independent Board Committee and the Independent Shareholders in connection with the Group's proposed acquisition of further interests in CNCB pursuant to the Top Up Agreement between the Company, CNCB and CITIC Group and the CNCB Cooperation MOU (which forms the framework of the proposed CNCB Cooperation Agreement) entered into among the Company, CNCB and CITIC Group. Details are contained in the circular to the Shareholders dated 29 December 2006 (the "Second Circular"), of which this letter forms a part. Unless otherwise defined, terms used in this letter shall have the same meanings as defined in the Second Circular.

The CNCB Top Up, when aggregated with the Group's acquisition of an initial interest in CNCB pursuant to the Original Agreement entered into between the Company and CITIC Group on 13 April 2006, constitutes a very substantial acquisition of the Company. As CITIC Group is the controlling shareholder of the Company and CNCB is its subsidiary, the Top Up Agreement, the CNCB Cooperation MOU and the transactions contemplated therein constitute connected transactions of the Company and are subject to, among other things, the approval of the Independent Shareholders by way of poll at the EGM.

The Independent Board Committee comprising Messrs Rafael Gil-Tienda, Lam Kwong Siu and Tsang Yiu Keung Paul, the three independent non-executive Directors, has been formed to advise the Independent Shareholders in respect of the terms of the CNCB Top Up and the CNCB Cooperation MOU. We, Somerley Limited, have been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in this regard.

We are not connected with the Company, CITIC Group, CNCB or their respective substantial shareholders or associates and accordingly are considered suitable to give independent financial advice on the terms of the Top Up Agreement and the CNCB Cooperation MOU. Apart from normal professional fees payable to us in connection with this appointment and our previous appointment in relation to the Group's acquisition of the initial interest in CNCB pursuant to the Original Agreement, no arrangement exists whereby we will receive any fees or benefits from the Company, CITIC Group, CNCB or their respective substantial shareholders or associates.

In formulating our advice and recommendation, we have relied on the information and facts supplied, and the opinions expressed, by the Directors, which we have assumed to be true, accurate and complete. We have reviewed the financial information of the Group and the CNCB Group (as defined below), both for the three years ended 31 December 2005 and the six months ended 30 June 2006, and the unaudited pro forma financial information of the Group prepared on the assumption that the Original Agreement, the Top Up Agreement and the Subscription Agreement have been completed (the "Completion").

We have sought and received confirmation from the Directors that all material relevant information has been supplied to us and that, to the best knowledge of the Directors, no material facts have been omitted from the information supplied and opinions expressed by them. We consider that the information we have received is sufficient for us to reach our advice and recommendation as set out in this letter and to justify our reliance on such information. We have no reason to doubt the truth and accuracy of the information provided to us or to believe that any material information has been omitted or withheld. We have assumed that all information and representations contained or referred to in the Second Circular are true at the date of the Second Circular and will continue to be true up to the time of the EGM. However, we have not conducted any independent investigation into the business and affairs of the Group or of CNCB and its subsidiaries (the "CNCB Group").

PRINCIPAL FACTORS AND REASONS TAKEN INTO ACCOUNT

In arriving at our opinion as regards the CNCB Top Up and the CNCB Cooperation MOU (which forms the framework of the CNCB Cooperation Agreement), we have taken into account the following principal factors and reasons:

1. Background to and reasons for the Top Up Agreement

On 13 April 2006, the Company entered into the Original Agreement to acquire from the CITIC Group 19.9% of the then equity interest in CNCB.

The Group is developing as the CITIC Group's offshore financial services flagship. As stated in the annual report of the Company for the year ended 31 December 2005 (the "2005 Annual Report"), one of the Group's priorities for 2006 is to strengthen the collaboration between CKWB and CNCB and to build an integrated platform to promote their complementary competencies. The Original Agreement will allow CKWB and CNCB to deepen the collaborative efforts they have established in the past years and to break new ground in their partnership. The benefits of the acquisition pursuant to the Original Agreement will, in the opinion of the Board, include the following:

(i) to improve the Company's service capabilities and its ability to provide "one-stop" solutions to Greater China and overseas customers;

(ii) to create economies of scale for the Company and expand its capabilities in business and product development;

(iii) to better attract and retain top talent; and

(iv) to capture growth opportunities in the banking business in the PRC.

Completion of the Original Agreement is expected to take place after formal transformation of CNCB into the Joint Stock Company.

Subsequent to the signing of the Original Agreement, CITIC Group contributed an additional RMB5 billion in cash to the registered capital of CNCB. As a result, the percentage equity interest of the Joint Stock Company (upon its establishment) to be held by the Company on completion of the Original Agreement would have been diluted to approximately 16.4%. On 16 November 2006, CITIC Group and the Company signed a promoters' agreement in relation the establishment of the Joint Stock Company under which, among other things, CITIC Group's interest in the registered capital will also include retained profits of CNCB in the sum of RMB2.4 billion. On this basis, the Company's interest in CNCB will be diluted to approximately 15.2%. This percentage would be further diluted at the initial public offering ("IPO") of CNCB.

CITIC Group has undertaken to the Company, among other things, that the Company can maintain its interest in CNCB immediately after the IPO at not less than 15%. The Board believes a minimum of 15% interest is appropriate given the strategic nature of the investments and the benefits (summarised above) they expect it to generate. The CNCB Top Up will enable the Company to maintain its 15% equity interest in CNCB which, together with the ability of the Company to exercise significant influence over CNCB through board representation, provide the basis on which the Group intends to equity account for its investment in CNCB. This is the assumption adopted for the unaudited pro forma financial information of the Group after Completion as set out in appendix IV to the Second Circular.

Pursuant to the Top Up Agreement, the Company will subscribe such number of Top Up Shares so that its percentage of equity interest in the Joint Stock Company as of the Top Up Completion Date shall be no less than 15% of the then total equity interest in the Joint Stock Company, as enlarged by the issue of the Top Up Shares. However, this is subject to the condition that if the Top Up Consideration required to be paid by the Company for the Top Up Shares will result in any of the Company's "Five Tests" under Rule 14.07 of the Listing Rules exceeding 25%, then the amount of Top Up Shares to be subscribed by the Company shall be the maximum whole number of Top Up Shares that would not result in the ratios to be computed under the "Five Tests" exceeding 25% under Rule 14.07 of the Listing Rules.

The Top Up Consideration is to be satisfied by cash and therefore the relevant "Five Tests" are the profits test, revenue test, total assets test and consideration test. Assuming the "consideration test" under Rule 14.07(4) will be the most relevant, the maximum transaction value for the CNCB Top Up would be calculated with reference to the market capitalisation of the Company as at 22 November 2006 as enlarged by the consideration shares to be issued pursuant to the Original Agreement. Pursuant to the Original Agreement, the number of consideration shares to be issued is subject to adjustments for the Approved State Valuation and any appreciation of the RMB against the HK Dollar, subject to caps. The Company has been informed that the Approved State Valuation has been issued and the maximum number of Shares to be issued pursuant to the Original Agreement (assuming the maximum increase of 3% in relation to any appreciation of the RMB against the HK$) is approximately 1,562 million Shares. On this basis and applying the "consideration test", the maximum transaction size for the CNCB Top Up would amount to approximately HK$7 billion (based on the market capitalisation of the Company as at 22 November 2006 as enlarged by the assumed issue of approximately 1,562 million consideration shares under the Original Agreement).

Conditions precedent

Completion of the Top Up Agreement is conditional upon, among others, the satisfaction or waiver of the following conditions precedent:

(a) the Stock Exchange approving the listing of, and permission to deal in, the H-shares of the Joint Stock Company to be listed on the Stock Exchange (including the Top Up Shares);

(b) the CNCB Cooperation Agreement in a form and substance substantially the same as set out in the CNCB Cooperation MOU having been executed by all parties, subject to any amendments required by the relevant PRC or Hong Kong governmental and regulatory authorities; and

(c) approval by the Independent Shareholders of the Top Up Agreement, the CNCB Top Up and all transactions thereunder having been obtained.

2. Business of the Group

We set out below information on the businesses and results of the Group up to 30 June 2006. We regard these results as broadly satisfactory, but they show, in our opinion, some signs of the relative maturity, and therefore slower growth, of the Hong Kong banking market as opposed, for example, to the PRC market.

(a) Businesses of the Group

The Company, an investment holding company formed in November 2002 as the result of a reorganisation of CKWB, is the CITIC Group's offshore financial services flagship. The Group's business is by far principally based in Hong Kong. The Company is the holding company of CKWB which is a Hong Kong licensed bank. CKWB currently operates 31 branches in Hong Kong. It also has branches in Beijing, Shanghai, Macau, New York and Los Angeles. CKWB holds 100% of China International Finance Company Limited (Shenzhen) ("CIFC") which provides wholesale and retail banking services in the PRC. CKWB (through CIFC) was the first Hong Kong bank able to offer Renminbi services to its corporate clients and individual clients who are non-Mainland citizens; and they will also be able to extend such services to all Mainland citizens when the PRC opens up its banking sector at the end of 2006. The Shanghai branch of CKWB was granted its derivatives licence in April 2006 and successfully launched its first derivative product in early August 2006. The derivatives licence will allow CKWB to strengthen its collaboration with CNCB in the treasury services area and to develop relevant QDII products and services. Once the Group completes acquisition of equity interest in CNCB, CKWB expects to leverage its international business experience and expertise as well as its network in the PRC to provide services to its Hong Kong and cross-border clientele, and to cater to PRC customers with two-way business needs between China, Hong Kong and elsewhere.

The Company presently holds the entire interest in CIAM, which is an asset management company specialising in distressed assets (including non-performing loans) management, direct investments and advisory services. On 4 December 2006, the Company entered into an agreement to introduce three joint venture partners into CIAM. Upon completion of the above agreement, the Company will be interested in 40% of the enlarged issued share capital of CIAM and CIAM will no longer be a subsidiary of the Company.

The Company also holds 50% of CITIC Capital Holdings Limited ("CCHL") (formerly known as CITIC Capital Markets Holdings Limited), which is engaged in asset management, private equity and merchant banking. CCHL is accounted for as an associate of the Company.

For the six months ended 30 June 2006, the Group reported a profit attributable to Shareholders of approximately HK$491.6 million, of which approximately HK$364.0 million came from CKWB. As at 30 June 2006, the Group's total assets amounted to approximately HK$89.7 billion (of which approximately HK$86.3 billion was attributable to CKWB) and its total loans amounted to approximately HK$46.8 billion (of which approximately HK$46.4 billion was attributable to CKWB).

(b) Operating results of the Group

Set out below is the abridged income statement of the Group for the six months ended 30 June 2005 and 2006 and the year ended 31 December 2004 and 2005 as extracted from the Group's 2006 interim report (the "2006 Interim Report") and 2005 Annual Report respectively:

	For the six months ended 30 June		**For the year ended 31 December**	
	2006	**2005**	**2005**	**2004**
	HK$(million)	*HK$(million)*	*HK$(million)*	*HK$(million)*
Net interest income	498	565	1,099	1,473
Non-interest income	490	409	872	682
Operating income	988	974	1,971	2,155
Operating expenses	(530)	(500)	(1,095)	(1,117)
	458	474	876	1,038
Impairment allowances written back	2	93	58	–
(Charge) of bad and doubtful debts	–	–	–	(78)
Net profit on disposal of available-for-sale securities	18	–	–	–
Operating profit	478	567	934	960
Loss on disposal of associates	–	(6)	(6)	–
Net profit on disposal of fixed assets	59	251	240	12
Revaluation gain on investment properties	7	–	2	7
Share of profits less losses of associates	46	12	46	76
Profit before taxation	590	824	1,216	1,055
Tax	(99)	(101)	(113)	(151)
Profit attributable to Shareholders	491	723	1,103	904
Earnings per Share (basic)	HK$0.1537	HK$0.2262	HK$0.3451	HK$0.2832

Based on the 2006 Interim Report, the operating profit of the Group (before impairment allowances, provision of bad and doubtful debts and net profit on disposal of available-for- sale securities) for the six months ended 30 June 2006 is relatively stable and just slightly decreased by 3.4% compared to the same period in 2005 to HK$458 million. Such decrease was resulted from the increase in funding cost of the Group during the period which led to a fall in net interest income of the Group by 11.9% to HK$498 million for the six months ended 30 June 2006 and also offset the Group's growth in non-interest income. The operating profit of the Group (before impairment allowances, provision of bad and doubtful debts and net profit on disposal of available-for-sale securities) for the year ended 31 December 2005 was HK$876 million which represent decreases of approximately 15.6% compared to the year ended 31 December 2004. The decline for the year ended 31 December 2005 was mainly attributable to the adverse impact of rising interest rates throughout the year. There was a sustained narrowing of the spread between the Prime Lending Rate and the Hong Kong Interbank Offered Rate, combined with a swing of core deposits to time deposits.

On the other hand, the non-interest income of the Group grew substantially from approximately HK$409 million in the first half of 2005 to approximately HK$490 million in the first half of 2006 and from approximately HK$682 million for 2004 to approximately HK$872 million for 2005. These represented growth of approximately 19.8% and 27.9% over the previous period and year, derived mainly from CKWB's strengthened business performance in loans, investment and treasury-related products for the six months ended 30 June 2006 and CKWB's retail banking and fund investment businesses for the year ended 31 December 2005.

The Group recorded HK$2 million and HK$58 million releases in impairment allowances for the six months ended 30 June 2006 and the year ended 31 December 2005 respectively. A charge of bad and doubtful debts of approximately HK$78 million was recorded in 2004.

The profit attributable to the Shareholders amounted to approximately HK$491 million for the six months ended 30 June 2006, representing an overall decrease of approximately 32.1% as compared to the same period in 2005, which was due to a net profit of approximately HK$251 million on disposal of fixed assets in 2005. The profit attributable to the Shareholders amounted to approximately HK$1,103 million for the year ended 31 December 2005, representing an overall increase of approximately 22.0% as compared to 2004.

(c) Financial position and key financial ratios of the Group

As at 30 June 2006, the Group's total assets amounted to approximately HK$89.7 billion, representing an approximately 5.5% increase from that of 2005. Total loans rose 8.0% from the end of 2005 to approximately HK$46.8 billion, with an increase in loans for use outside Hong Kong, financial sector related loans and trade finance. Total deposits also grew by 7.3% for the end of 2005 to approximately HK$66.4 billion as at 30 June 2006. Net asset value as at 30 June 2006 was approximately HK$9.8 billion, representing an approximately 3.3% increase from the 2005 year-end.

The following is the key financial ratios of the Group as set out in its 2006 Interim Report:

	As at 30 June 2006	**As at 31 December 2005**
Unadjusted capital adequacy	15.0%	16.0%
Loans to deposits	70.5%	70.1%
Loans to total assets	52.2%	51.0%
Coverage *(note)*	98.2%	92.7%

Note: Coverage is equal to the sum of individually assessed impairment allowances and collateral of impaired loans divided by the gross impaired loans.

During the six months ended 30 June 2006, the Group's unadjusted capital adequacy ratio decreased slightly from 16.0% as at 31 December 2005 to 15.0% as at 30 June 2006. Its coverage ratio increased from 92.7% as at 31 December 2005 to 98.2% as at 30 June 2006. As at 30 June 2006, the loans to deposits ratio and loans to total assets ratio stood at 70.5% and 52.2% respectively, a slight increase from the position as at 31 December 2005 of 70.1% and 51.0% respectively.

3. Business of CNCB

We set out below information on the business and results of CNCB up to 30 June 2006. In general, we consider these figures show an improving trend of profitability and a strengthened financial position. We also consider that these results outperform to a certain degree the results of the Company itself over the same period, on which basis, the growth prospects of CNCB may also be regarded as superior to those of the present Group in isolation.

CNCB was established in 1987 and is currently wholly owned by CITIC Group. It is principally engaged in the business of provision of banking and financial services in the PRC. It is one of the commercial banks in the PRC operating with a national licence and provides services to both corporates and consumers in 18 provinces, autonomous regions and municipalities in the PRC. CNCB has three small subsidiaries, which have principal activities of money lending and property holding in Hong Kong, and property management in the PRC respectively.

CNCB has a relatively small operation in Hong Kong. China Investment and Finance Limited ("CIFL"), a 95% owned subsidiary of CNCB, is engaged in money lending and investment holding in Hong Kong. The remaining 5% equity interest of CIFL is owned by CKWB.

As at 30 June 2006, the CNCB Group had total assets of approximately RMB647 billion, with RMB430 billion in loans and approximately RMB102 billion in investments. CNCB's main source of funding is customers deposits, which amounted to approximately RMB571 billion as at 30 June 2006.

The board of directors of CNCB currently has five members, of which two are also directors of the Company. After the establishment of the Joint Stock Company, the currently proposed board of directors would consist of 6 executive directors, 4 of which are also directors of the Company.

(a) Operating results of the CNCB Group

The following table summarises the audited consolidated financial results of the CNCB Group for the six months ended 30 June 2006 and the three years ended 31 December 2005 prepared in accordance with the IFRS as set out in the appendix III to the Second Circular:

	For the six months ended 30 June		For the year ended 31 December		
	2006	**2005**	**2005**	**2004**	**2003**
	RMB (million)	*RMB (million)*	*RMB (million)*	*RMB (million)*	*RMB (million)*
Interest income	13,327	10,676	22,511	17,795	12,967
Interest expense	(5,983)	(4,659)	(9,851)	(7,412)	(5,294)
Net interest income	7,344	6,017	12,660	10,383	7,673
Fee and commission income	402	266	608	449	353
Fee and commission expense	(76)	(96)	(190)	(131)	(88)
Net fee and commission income	326	170	418	318	265
Other gains, net	30	33	98	57	33
Net gain arising from foreign currency dealing	219	145	266	227	151
Other operating income	97	58	213	161	246
Operating income	8,016	6,423	13,655	11,146	8,368
General and administrative expenses	(3,943)	(3,282)	(7,104)	(5,451)	(3,940)
Impairment losses charge	(944)	(635)	(1,098)	(1,634)	(2,145)
Profit before taxation	3,129	2,506	5,453	4,061	2,283
Tax	(1,362)	(1,176)	(2,369)	(1,633)	(862)
Net profit	1,767	1,330	3,084	2,428	1,421

The operating result of the CNCB Group has made a satisfactory progress over the six months ended 30 June 2006. The net profit and operating income of the CNCB Group for the six months ended 30 June 2006 had increased by approximately 32.9% and 24.8% over the same period in 2005 respectively to about RMB1,767 million and RMB8,016 million respectively. The net profit of the CNCB Group for the two years ended 31 December 2005 were approximately RMB3,084 million and RMB2,428 million respectively, representing an increase of approximately 27.0% and 70.9% over 2004 and 2003 respectively. The increase in net profits for the six months ended 30 June 2006 was mainly attributable to (i) an increase in net interest income; and (ii) an increase in net fee and commission income.

Unlike the situation for CKWB in Hong Kong where non-interest income is becoming almost as important as interest income, the net interest income of the CNCB Group accounted for by far a significant portion of the total operating income of the CNCB Group, representing 91.6% and 92.7%, 93.2% and 91.7% of the total operating income of the CNCB Group for the six months ended 30 June 2006 and the years ended 31 December 2005, 2004 and 2003 respectively. For the six months ended 30 June 2006, net interest income increased by 22.1% to RMB7,344 million compared, to RMB6,017 million for the six months ended 30 June 2005. The increase in net interest income during the six months ended 30 June 2006 was mainly attributable to the continued growth in loans and advances to customers of the CNCB Group. For the six months ended 30 June 2006, the increase in loans and advances to customers was higher than the increase in customer deposits. Capital contribution of RMB5 billion from the CITIC Group and issue of RMB6 billion subordinated debt also contributed significantly to the funding of the CNCB Group during the above period. However, customer deposits remained the principal funding source for loans and advances to customers. The loans to deposits ratio of the CNCB Group increased from 69.8% as at 31 December 2005 to 77.2% as at 30 June 2006.

General and administrative expenses mainly comprise staff costs, property and equipment expenses, management fee payable to CITIC Group and business tax and surcharges. For the six months ended 30 June 2006, general and administrative expenses were about RMB3,943 million, as compared to RMB3,282 million for the same period in 2005. As a result of the increase in staff costs of the CNCB Group for expansion of its operations and in other expenses including management fees paid to CITIC Group, there were sharp increases in the general and administrative expenses of the CNCB Group over the three years ended 31 December 2005 which were approximately RMB3,940 million, RMB5,451 million and RMB7,104 million respectively.

The impairment losses charged over the six months ended 30 June 2006 and the three years ended 31 December 2005 mainly comprised provisions for loans and advances to customers. The gross impaired loans and advances as a percentage of total loans and advances decreased from about 9% in 2003 to about 3% in June 2006. This is discussed further in sub-section (b) below.

(b) Financial position and asset components of the CNCB Group

The audited consolidated balance sheets of the CNCB Group as at 30 June 2006, 31 December 2005, 2004 and 2003 have been prepared in accordance with the IFRS. Shareholders may refer to the full set of audited consolidated financial statements of the CNCB Group (including the notes) in appendix III to the Second Circular. A summary of the balance sheets is set out as follows:

	30 June	As at 31 December		
	2006	**2005**	**2004**	**2003**
	RMB (million)	*RMB (million)*	*RMB (million)*	*RMB (million)*
Assets				
Cash and balances with central bank	75,125	84,453	54,253	42,299
Amounts due from banks and other financial institutions	23,551	31,352	20,899	31,848
Loans and advances to customers	430,006	358,030	291,921	240,539
Investments	102,395	104,416	110,903	58,403
Property and equipment	8,444	8,614	8,090	6,826
Deferred tax assets	3,356	4,082	5,424	5,999
Other assets	4,320	3,955	3,655	3,903
Total assets	647,197	594,602	495,445	396,817
Liabilities				
Amounts due to central bank	160	240	300	3,921
Amounts due to banks and other financial institutions	27,291	28,021	38,190	37,600
Deposits from customers	570,995	530,573	435,020	345,356
Tax liabilities	721	1,203	1,052	988
Other liabilities and provisions	6,575	5,340	4,120	3,550
Subordinated debts/bonds issued	12,000	6,000	6,000	–
Total liabilities	617,742	571,377	484,682	391,415
Equity				
Share capital	31,661	26,661	17,790	14,032
Reserves	(2,211)	(3,441)	(7,031)	(8,633)
Minority interests	5	5	4	3
Total equity	29,455	23,225	10,763	5,402
Total equity and liabilities	647,197	594,602	495,445	396,817

Loans and advances to customers increased over the years from RMB241 billion as at 31 December 2003 to RMB430 billion as at 30 June 2006, due to organic growth in the business of the CNCB Group. The customer loans of RMB430 billion as at 30 June 2006 represented an increase of 20% from 31 December 2005.

Loans and advances to customers were mainly made up of corporate loans, representing approximately 80% of the total loans as at 30 June 2006. The table below sets out further information in respect of the corporate loan portfolio of the CNCB Group analysed by legal form of borrowers as at 30 June 2006, 31 December 2005, 2004 and 2003 respectively:

	As at 30 June		As at 31 December					
	2006		2005		2004		2003	
	RMB (million)		*RMB (million)*		*RMB (million)*		*RMB (million)*	
Joint-stock enterprises	162,525	47.1%	130,157	46.1%	119,369	46.6%	83,086	42.7%
State-owned enterprises	123,188	35.7%	100,738	35.7%	84,252	32.9%	64,826	33.3%
Others	59,361	17.2%	51,380	18.2%	52,801	20.5%	46,605	24.0%
	345,074	100.0%	282,275	100.0%	256,422	100.0%	194,517	100.0%

The CNCB Group has a diversified corporate loan portfolio, without a high concentration of loans in a particular industry. Set out below is a table of loans and advances to customers analysed by economic sectors as at 30 June 2006, 31 December 2005, 2004 and 2003 respectively:

	As at 30 June		As at 31 December					
	2006		2005		2004		2003	
	RMB (million)		*RMB (million)*		*RMB (million)*		*RMB (million)*	
Manufacturing	101,890	29.5%	81,537	28.9%	71,247	27.8%	51,860	26.7%
Wholesale and retail	35,009	10.1%	29,902	10.6%	26,023	10.1%	23,099	11.9%
Production and supply of electric power, gas and water	36,187	10.5%	26,559	9.4%	23,825	9.3%	9,857	5.1%
Others	171,988	49.9%	144,277	51.1%	135,327	52.8%	109,701	56.3%
	345,074	100.0%	282,275	100.0%	256,422	100.0%	194,517	100.0%

A majority of the loan portfolio of the CNCB Group was allocated to the more developed regions of the PRC as set out below:

	As at 30 June		As at 31 December					
	2006		2005		2004		2003	
	RMB (million)		*RMB (million)*		*RMB (million)*		*RMB (million)*	
Bohai Rim	129,081	29.3%	115,706	31.2%	100,195	32.6%	89,770	34.9%
Yangtze River Delta	144,761	32.8%	120,026	32.4%	91,672	29.9%	70,051	27.2%
Pearl River Delta and West Strait	62,181	14.1%	52,885	14.3%	49,491	16.1%	46,780	18.2%
Others	104,939	23.8%	81,643	22.1%	65,521	21.4%	50,712	19.7%
	440,962	100.0%	370,260	100.0%	306,879	100.0%	257,313	100.0%

Note: "Bohai Rim" refers to the following areas where tier-1 branches of the CNCB Group are located: Beijing, Tianjin, Dalian, Qingdao, Shijiazhuang and Jinan; "Yangtze River Delta" refers to the following areas where tier-1 branches of the CNCB Group are located: Shanghai, Nanjing, Suzhou, Hangzhou and Ningbo; "Pearl River Delta and West Strait" refers to the following areas where tier-1 branches of the CNCB Group are located: Guangzhou, Shenzhen, Dongguan and Fuzhou.

Although the loan portfolio of the CNCB Group has been expanding, the amount and the percentage of impaired loans and advances, which are graded substandard, doubtful or loss, has decreased. Set out below is the amount of impaired loans and advances as well as their percentage to the total balance of the loan portfolio:

	As at 30 June	As at 31 December		
	2006	2005	2004	2003
	RMB (million)	*RMB (million)*	*RMB (million)*	*RMB (million)*
Gross loans and advances to customers	440,962	370,260	306,879	257,313
Gross impaired loans and advances to customers	12,894	15,311	19,280	23,205
% of gross impaired loans and advances to customers to gross loans and advances to customers	2.9%	4.1%	6.3%	9.0%

The impairment allowances made by the CNCB Group as a percentage of gross impaired loans and advances to customers were relatively stable, as illustrated below:

	As at 30 June	As at 31 December		
	2006	**2005**	**2004**	**2003**
	RMB (million)	*RMB (million)*	*RMB (million)*	*RMB (million)*
Gross impaired loans and advances to customers	12,894	15,311	19,280	23,205
Impairment allowances against gross impaired loans	(8,216)	(9,847)	(12,698)	(14,929)
% of impairment allowances to gross impaired loans and advances to customers	63.7%	64.3%	65.9%	64.3%

An impaired loan may not be fully written off. The management of the Company understand that CNCB's impairment policy takes into account for example factors including the existence and value of security for a particular loan.

The CNCB Group has made loans and advances to related parties. Their outstanding balances as extracted from the financial information of the CNCB Group contained in appendix III to the Second Circular are set out as follows:

	As at 30 June	As at 31 December		
	2006	**2005**	**2004**	**2003**
	RMB (million)	*RMB (million)*	*RMB (million)*	*RMB (million)*
Gross loans and advances to related parties of the CNCB Group	2,308	5,468	6,379	6,486
Impairment allowances	–	(725)	(814)	(829)
% of impairment allowances to gross impaired loans and advances to CNCB's related parties	–	13.3%	12.8%	12.8%

The CNCB Group has, during the six months ended 30 June 2006, disposed of approximately RMB3 billion loans and advances to related parties. As a result, the gross amount of loans and advances to related parties has decreased by about 58% from RMB5,468 million as at 31 December 2005 to RMB2,308 million as at 30 June 2006.

The CNCB Group's lending business is mainly funded by deposits from corporate customers. As at 30 June 2006, 31 December 2005, 2004 and 2003, approximately 84.5%, 86.6%, 89.0% and 90.6% of the deposits came from corporates while the remaining balance was from individuals. The spilt between time deposits and demand deposits is quite stable over the three years ended 31 December 2005 and the six months ended 30 June 2006.

Majority of the deposits came from the more affluent areas in the PRC. Set out below is the geographical distribution of the customers placing deposits with the CNCB Group based on the value of their deposits:

	As at 30 June		As at 31 December					
	2006		**2005**		**2004**		**2003**	
	RMB (million)		*RMB (million)*		*RMB (million)*		*RMB (million)*	
Bohai Rim	203,276	35.6%	207,676	39.1%	167,713	38.6%	131,092	38.0%
Yangtze River Delta	167,804	29.4%	146,579	27.6%	127,269	29.3%	95,109	27.5%
Pearl River Delta and West Strait	82,486	14.4%	72,855	13.7%	59,003	13.5%	50,914	14.7%
Others	117,429	20.6%	103,463	19.6%	81,035	18.6%	68,241	19.8%
	570,995	100.0%	530,573	100.0%	435,020	100.0%	345,356	100.0%

Note: Please refer to the table above in relation to the geographical distribution of loan portfolio of the CNCB Group for detailed definitions of the geographical segments.

Similar to other banks in the industry, CNCB has to manage liquidity risk in its normal operation. This involves ensuring that the bank is able to meet deposit withdrawals either on demand or at contractual maturity, to repay borrowings in full when they mature, or to meet other obligations for payments, to comply with the statutory liquidity ratio, and to make new loans and investments as opportunities arise.

The following is the key financial ratios of the CNCB Group as extracted from the financial information of the CNCB Group contained in appendix III to the Second Circular:

	30 June 2006	**31 December 2005**
Capital adequacy ratio	9.5%	8.1%
Loans to deposits	77.2%	69.8%
Loans to total assets	68.1%	62.3%
Loan loss coverage	85.0%	79.9%

During the six months ended 30 June 2006, the CNCB Group's capital adequacy ratio increased from 8.1% as at 31 December 2005 to 9.5% as at 30 June 2006. Loan loss coverage ratio increased from 79.9% as at 31 December 2005 to 85.0% as at 30 June 2006. As at 30 June 2006, the loans to deposits ratio and loans to total assets ratio stood at 77.2% and 68.1% respectively, an increase from the position as at 31 December 2005 of 69.8% and 62.3% respectively.

Overall, no material difference in the types of loan portfolio or customer deposits since the signing of the Original Agreement is noted from the financial statements of CNCB for the six months ended 30 June 2006. Financial performance of the CNCB Group has been improving, as reflected in CNCB's consolidated income statement for the six months ended 30 June 2006.

4. The CNCB Cooperation MOU

In order to set out a framework of cooperation between the Company, CNCB and CITIC Group, on 22 November 2006, the Company entered into the CNCB Cooperation MOU with CITIC Group and CNCB. Pursuant to the CNCB Cooperation MOU, after obtaining Independent Shareholders' approval, the parties will execute the CNCB Cooperation Agreement which will largely follow the framework of cooperation set out in the CNCB Cooperation MOU, but will be subject to such amendments as may be required by the relevant regulatory authorities of the PRC and Hong Kong which include the relevant stock exchanges in the PRC and in Hong Kong.

The Group and CNCB are principally operated in Hong Kong and PRC respectively. Both groups have insignificant operations in the other party's major operating territory. Under the CNCB Cooperation Agreement, the parties will set out the basis on which they will avoid direct competition with each other. CNCB will confirm that it has no intention to compete with the Company in Hong Kong by establishing any rival branches or commercial banking network. It will continue its current operations in Hong Kong through CIFL, but will only establish new operations in Hong Kong after conducting non-binding consultations with the Company. On the other hand, the Company will confirm that neither the Company nor CKWB intends to compete with CNCB in the PRC by establishing any rival branches or commercial banking network. It will be agreed under the CNCB Cooperation Agreement that CKWB may continue its current operations, but will not establish any additional branches in the PRC. On this basis, there will be a clear delineation between the businesses of the Group and those of CNCB on a geographical basis.

In addition, leveraging on both parties' strengths within and outside the PRC, the Group and CNCB will further cooperate on business and product development so as to improve their capabilities in providing cross-border banking services to clients.

As the Directors have formed the view that it would be advantageous to develop the Company's PRC banking business through investment in and co-operation with CNCB, we agree with the Directors that it is in the interest of the Group to clarify the position by way of the CNCB Cooperation Agreement. The agreement also set out areas of future cooperation between the two groups, thus contributing to the future growth of the Group's cross-border banking business.

5. Basis of the Consideration

The Top Up Consideration was determined after arm's length negotiations between the Company and CNCB and will be the same as the final Hong Kong dollar per H-share of the Joint Stock Company offered to the public (the "H-Share Offer Price").

CNCB is in the process of being transformed into the Joint Stock Company in preparation for its listing on the Stock Exchange and in the PRC.

We have identified the following banks which were listed on the Stock Exchange since 1 January 2005 and have substantial operations in the PRC (the "Comparable Banks"). Their relevant price to book ("P/B") and price to earnings ("P/E") ratios as at IPOs and the Latest Practicable Date were as follows:

	At IPO		At Latest Practicable Date	
Name of the listed banks	**P/B ratio**	**P/E ratio**	**P/B ratio**	**P/E ratio**
Bank of Communications Co., Ltd.	1.79	15.63	4.67	38.47
China Construction Bank Corporation	2.04	13.06	3.63	19.35
Bank of China Limited	2.38	22.35	3.63	28.00
China Merchants Bank Co., Ltd.	2.49	23.11	7.03	53.39
Industrial & Commercial Bank of China Limited	2.40	19.19	4.29	29.49
Average	2.22	18.66	4.65	33.74

Source: Bloomberg and the announcements and prospectus of the respective companies.

Based on the table above, the P/B ratios of the Comparable Banks at IPOs ranged from 1.79 times to 2.49 times with an average of 2.22 times. The P/E ratios of the Comparable Banks at IPOs ranged from 13.06 times to 23.11 times with an average of 18.66 times. As at the Latest Practicable Date, the P/B ratios of the Comparable Banks ranged from 3.63 times to 7.03 times with an average of 4.65 times, while their P/E ratios ranged from 19.35 times to 53.39 times with an average of 33.74 times.

The final H-share Offer Price of the Joint Stock Company will be principally dependent on the reaction of investors to the information on CNCB presented to them and on the stock market conditions in Hong Kong and elsewhere, and is likely to be set with reference to the above market statistics. We also note an announcement by BBVA dated 22 November 2006 which states that it has entered into an agreement with CITIC Group to acquire a 5% equity stake in CNCB. Based on market information, we understand BBVA has agreed to pay approximately 3 times the estimated net book value of CNCB for the above acquisition.

6. Funding for the CNCB Top Up

The consideration for the CNCB Top Up will be based on the final H-Share Offer Price of the Joint Stock Company and the number of shares required to be subscribed by the Company in order to maintain an equity interest of at least 15% in CNCB. The percentage of equity interest in CNCB to be subscribed by the Company would depend on the number of new shares (including any over-allotment option) which the Joint Stock Company would issue at IPO, for which preparations are not yet finalised. The exact amount of Top Up Consideration cannot be determined at this stage, but it would in any case be subject to a cap of 25% of the Company's "Five Tests". As mentioned above, assuming the "consideration test" is the most relevant, the maximum Top Up Consideration would amount to approximately HK$7 billion. On the basis of the net book value of CNCB of RMB29.5 billion as at 30 June 2006 and with reference to the above market statistics of the Comparable Banks, it is unlikely that the final Top Up Consideration required to allow the Company to maintain an equity interest of at least 15% in CNCB would be as high as HK$7 billion, and may be estimated, in our opinion, for illustrative purposes only, at approximately HK$3 – 4 billion.

The Company has entered into the Subscription Agreement with BBVA to raise approximately HK$3.9 billion net proceeds by issuing new Shares which will represent approximately 12% of the Company's issued share capital as enlarged by the Subscription and the issue of consideration shares for the Original Agreement (assuming approximately 1,562 million consideration shares are to be issued) (the "Fully Enlarged Share Capital"). The net proceeds from the Subscription of approximately HK$3.9 billion will be applied to support the Group's future development, including financing the CNCB Top Up. On our estimation set out above, the net proceeds from the Subscription should be approximately sufficient to meet the funding needs for the Top Up Consideration. If further or alternative funding is required to finance the CNCB Top Up, on the basis of the Group's strong asset base and earnings and cashflow generating capabilities, the Directors do not anticipate significant difficulty in raising such capital. We agree with the Directors' view in this regard.

Completion of the Subscription is conditional upon:

(a) the Listing Committee of the Stock Exchange agreeing to grant the listing of, and permission to deal in, the Subscription Shares (and such listing and permission not subsequently revoked prior to the delivery of definitive share certificates representing the Subscription Shares);

(b) certain conditions precedent under the CITIC Group Agreement whereby BBVA would acquire from the CITIC Group approximately 3% of the Company's Fully Enlarged Shares Capital having been fulfilled in accordance with the terms of that agreement or waived;

(c) the shareholders of the Company approving the entering into of the Subscription Agreement by the Company; and

(d) (i) the execution by CITIC Group of a confirmation relating to matters in the Cooperation MOU entered into between the Company and BBVA; or (ii) the execution of certain agreements pursuant to the Cooperation MOU.

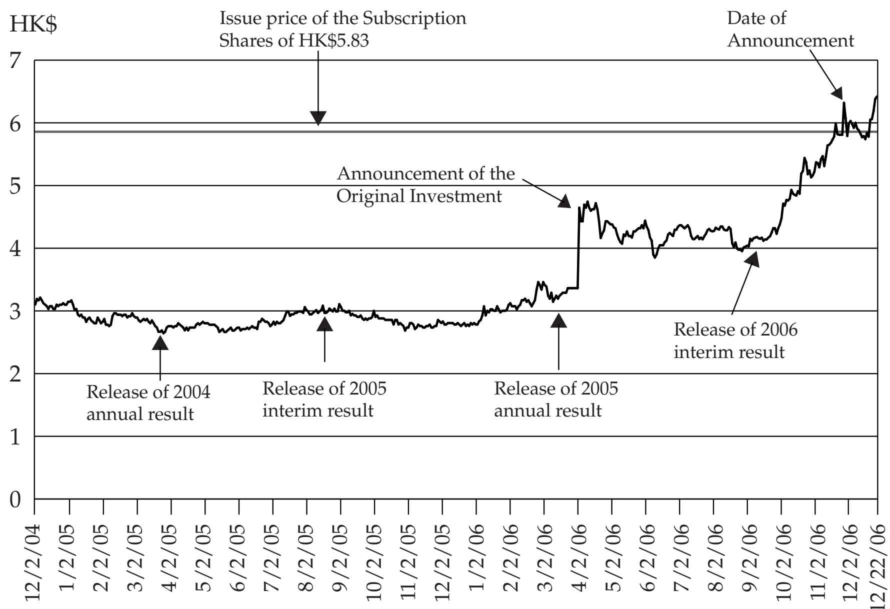
As CITIC Group holds approximately 52% interest in the Company and is eligible to vote, we regard Shareholders' approval of the Subscription a formality. The Directors also believe that the remaining conditions will be fulfilled before the long-stop date of the Subscription Agreement and we regard them as standard for a subscription of shares of this type. On this basis, the arrangements for the funding for the CNCB Top Up are in place.

The Subscription also serves to bring in BBVA as a strategic partner. The Company has on 22 November 2006 entered into the Cooperation MOU with BBVA confirming the intention of the parties to pursue discussions in relation to business cooperation and proposed merger or acquisition by the Company and/or CKWB of BBVA's existing wholesale banking business in Asia and an increase by BBVA of its shareholding interest in the Company and/or a subscription for CKWB shares. The Cooperation MOU provides that in the six-month period after the signing of the Cooperation MOU, the parties shall conclude discussions with a view to the signing of agreements containing the material terms relating to the proposed business transfer, business cooperation and a further increase in shareholding in the Company and/or CKWB by BBVA. In the period commencing six months after the date of the Cooperation MOU and ending nine months after the date of the Cooperation MOU, BBVA and the Company intend to discuss and agree any outstanding issues in respect of the above that are not agreed in the initial six-month period.

7. Share price performance and comparison with the Subscription Price of HK$5.83 per Subscription Share

(a) Share price

The chart below shows the closing prices of the Shares traded on the Stock Exchange during the 24 months preceding the date of the Announcement (the "Comparison Period") up to and including the Latest Practicable Date:



Source: Bloomberg

Before the issue of the Announcement, the Share price was trading close to the Subscription Price of HK$5.83 and closed at HK$5.81 on 21 November 2006 (being the last trading day immediately before the publication of the Announcement (the "Last Trading Day")). Upon the release of the Announcement, the market price of the Shares increased by approximately 8.8% from HK$5.81 as at the Last Trading Day to HK$6.32 per Share as at 24 November 2006 (being the first trading day immediately after the publication of the Announcement). Subsequently, the Share price fell, but remained higher than the Subscription Price. The initial price movement in the Shares represents, in our opinion, a positive response from the market to the Subscription and the CNCB Top Up and reflects the market's perception of the potential benefits to the Company upon completion of the Subscription Agreement and the CNCB Top Up. At the Latest Practicable Date, the closing price of the Shares was HK$6.42.

The issue price of HK$5.83 for the Subscription represents a premium of approximately 0.34% to the closing price of the Shares of HK$5.81 as at the Last Trading Day.

(b) Shareholding structure before and after the Subscription

The table below sets out the shareholding structure of the Company (i) prior to the Subscription Completion Date; and (ii) immediately after the Subscription Completion Date.

	Prior to the Subscription Completion Date *(note 1)*		**Immediately after the Subscription Completion Date** *(notes 1 and 2)*	
	Number of Shares *(million)*	%	**Number of Shares** *(million)*	%
CITIC Group	3,353	66.6	3,186	55.9
BBVA	–	–	835	14.7
Independent Shareholders	1,678	33.4	1,678	29.4
Total	5,031	100.0	5,699	100.0

Note:

(i) Assume the Original Agreement has been completed and approximately 1,562 million consideration shares have been issued pursuant to the Original Agreement.

(ii) Assuming the CITIC Group Agreement is completed concurrently with the Subscription Agreement.

Assuming the Original Agreement has been completed, the shareholdings of the Independent Shareholders will be approximately 33.4%. Immediately after completion of the Subscription Agreement, Independent Shareholders' shareholdings would be diluted from 33.4% to 29.4%.

(c) Net asset value

Pursuant to the Subscription, Subscription Shares would be issued at an unit price of HK$5.83, which represents 2.02 times the net asset value per Share of HK$2.89 (calculated based the latest published consolidated net asset value (unaudited) of the Company as at 30 June 2006 and the total issued share capital of the Company as at the date of the Subscription Agreement). On this basis, there would be an increase in net asset value per Share, as a result of the Subscription being priced at a premium over net asset value per Share.

8. Financial effects of the CNCB Top Up on the Group

(a) Earnings

We note that the PRC banking industry has seen rapid growth in line with the economic development of the PRC. Banks have historically been, and continue to be, a significant source of capital for the economy and the primary choice for domestic savings. On this basis, it is expected that CNCB would continue to achieve satisfactory growth and would contribute positively to the Group's future financial performance, once the Original Agreement is completed. The CNCB Top Up would enable the Company to maintain its 15% equity interest in the Joint Stock Company, on which basis and bearing in mind the Company shall be able to exercise significant influence over CNCB through representation on the board of the Joint Stock Company, the Group intends to equity account the financial results of the Joint Stock Company. The accounting polices as regards the Company's holding in the Joint Stock Company will be reviewed with the Company's auditors in due course.

Based on the unaudited pro forma financial information of the Group after Completion as set out in appendix IV to the Second Circular, the unaudited pro forma net profit after taxation of the Group (principally based on (i) the unaudited net profit after taxation of the Group of approximately HK$491 million for the six months ended 30 June 2006 and (ii) the sharing of 15% of the net profit after taxation of CNCB Group prepared in accordance with the IFRS of approximately RMB1,767 million for the six months ended 30 June 2006 assuming the Original Investment, the CNCB Top Up and the Subscription had taken place as at 1 January 2006) will be approximately HK$701 million, representing approximately HK$0.13 per Share. The unaudited pro forma net profit after taxation per Share following Completion of approximately HK$0.13 represents an approximately 13.3% decrease from the unaudited net profit after taxation per Share of approximately HK$0.15 for the six months ended 30 June 2006. We consider this level of immediate decrease in the pro forma earnings per Share acceptable in the context of the long-term expected benefits for the Company in being a strategic shareholder and commercial partner of CNCB.

(b) Goodwill and other intangible assets

Goodwill will arise if the consideration for the CNCB Top Up is in excess of the fair value of CNCB's tangible and intangible assets (such as trade name or customer relationships) attributable to the further interest in CNCB to be acquired by the Company pursuant to the Top Up Agreement. In the case of tangible assets, net book values are normally taken to be their fair values. By reference to the market statistics of the Comparable Banks, the Top Up Price, which would equal to the H-Share Offer Price of CNCB, is expected to be at a significant premium over CNCB's net asset value. In the unaudited pro forma financial information of the Group after Completion set out in appendix IV to the Second Circular, there is no reference to impairment on the interest in associates relating to the CNCB Top Up. However, the Company's investment into CNCB would be subject to impairment reviews. If intangible assets are recognised, they would also be subject to impairment reviews annually in addition to, in the case of intangible assets with a finite life, being amortised over their estimated useful life. Impairment charges and amortisation expenses, if any, will be charged to the profit and loss account of the Group. On the basis set out in the unaudited pro forma financial information of the Group after Completion as contained in appendix IV to the Second Circular, the effect of amortisation of acquired intangible assets is not expected to be material to the results of the Group.

DISCUSSION AND ANALYSIS

As set out in the Circular, the Company agreed in April 2006 to acquire a 19.9% of the equity interest in CNCB as at 31 December 2005. The reasons for this acquisition included improving the Company's service capabilities in China and other potential benefits of strengthened co-operation with CNCB. The consideration will be entirely satisfied by the issue of approximately 1.56 billion new Shares. Although Shareholders approved this acquisition on 19 July 2006, it had not yet been completed pending establishment of the Joint Stock Company and receipt of outstanding PRC approvals. Owing to the subsequent injection of RMB5 billion cash as new capital into CNCB by CITIC Group and the retention of profits in the sum of RMB2.4 billion by CNCB prior to completion which serves to increase capital attributable to CITIC Group, the Company's interest in CNCB when the acquisition under the Original Agreement is completed will be approximately 15.2%. Completion of the Original Agreement is expected to take place after formal transformation of CNCB into the Joint Stock Company.

The Directors have taken the view that the Company's holding in CNCB is a strategic one and should not be allowed to fall below 15%. Based on this percentage holding and the ability of the Company to exercise significant influence over CNCB through its representation on the board of the Joint Stock Company, the Company intends to equity account its interest. Apart from CITIC Group's injection of capital, dilution in the Company's interest will arise from the planned IPO, for which preparations are in hand. While the structure of the IPO is not yet finalised, we estimate that a further equity injection of approximately HK$3 – 4 billion of new capital (at the time of the IPO of the Joint Stock Company and at the H-Share Offer Price) will be sufficient to keep the Company's interest above 15%. The maximum amount of investment which the Company is asking Shareholders to sanction at the EGM is approximately HK$7 billion, which is just below the level at which the CNCB Top Up (in isolation) would be classified as a "major" transaction by reference to the "Five Tests". The Directors have informed us that they do not intend to subscribe more than necessary to maintain an approximately 15% interest.

We have reviewed the position of CNCB as at 30 June 2006 and the changes since 31 December 2005, the latest figures available when the Company signed the Original Agreement. Our analysis and comments are set out in section headed "Business of CNCB" above. Based on our financial analysis, we consider CNCB has made satisfactory progress in the meantime.

We consider the Directors' reasons for entering to the Original Investment as described in section headed "Background to and reasons for the Top Up Agreement" above were sound and agree with their rationale in maintaining, through the CNCB Top Up, a 15% strategic stake in CNCB, a level at which it is expected to be equity accounted. We also agree that it would not be sensible for the Company to try to develop its business in the PRC in competition with CNCB. For this reason, we believe it is justified for the Company to sign the CNCB Cooperation MOU (which contains restrictions for example on CKWB opening new branches in China). As the Group will be giving up some of its own potential expansion in the PRC, the maintenance of the strategic stake in and the relationship with CNCB will become still more important.

The additional investment in CNCB will be at the H-Share Offer Price, which is likely to be substantially higher than the price that the Company agreed to pay for its initial investment in CNCB, which was equivalent to approximately 1.2 times CNCB's book value as at 31 December 2005. The five most recent IPOs of Chinese banks had IPO pricing reflecting an average of 2.2 times book. In our view, a premium over the cost of the initial investment is justified in that the investment in the Joint Stock Company as its IPO is less risky and more liquid; in any event, we consider that if a top-up investment is to be made by the Company in CNCB as part of its IPO, as we agree it should be, the H-Share Offer Price is the only practical basis. The H-Share Offer Price will reflect and be based on market values and conditions at the time. The IPO pricing of the five Chinese banks referred to above has in the event given investors considerable upside. The subscription by BBVA of an about 12% interest of the Fully Enlarged Share Capital of the Company will provide substantially all the funds expected to be needed for the CNCB Top Up. Although the two subscriptions are not inter-conditional, we consider it highly likely that the Subscription Agreement will proceed, as the conditions to which it is subject are standard ones.

OPINION AND RECOMMENDATION

Based on the above principal factors and reasons and taking these factors and reasons as a whole as summarised in the section above headed "Discussion and analysis", we consider the terms of the Top Up Agreement and the CNCB Cooperation MOU (which forms the framework for the CNCB Cooperation Agreement) are fair and reasonable to the Independent Shareholders and the entering into of the Top Up Agreement and the CNCB Cooperation MOU, and subsequently the CNCB Cooperation Agreement, is in the interests of the Company and its Shareholders as a whole. We therefore advise the Independent Board Committee to recommend the Independent Shareholders, and we ourselves advise the Independent Shareholders, to vote in favour of the resolutions to approve the Top Up Agreement and the CNCB Cooperation MOU to be proposed at the EGM.

Yours faithfully,
for and on behalf of
SOMERLEY LIMITED
M.N. Sabine
Chairman

1. FINANCIAL SUMMARY

The following is a summary of the management unaudited financial information of the Group for each of the three years ended 31 December 2005 as extracted from the relevant annual reports of the Group.

Three-Year Financial Summary

	2005	**2004** (restated)	**2003**
Profit & Loss Items for The Year *(HK$ million)*			
Net interest income	1,099	1,473	1,562
Non-interest income	871	682	459
Operating expenses	1,095	1,117	1,015
Impairment losses written back on loans and advances	(58)	N/A	N/A
Charge for bad and doubtful debts	N/A	78	514
Profit before taxation	1,216	1,055	772
Taxation	112	151	115
Profit attributable to shareholders	1,103	904	657
Per Share *(HK$)*			
Basic earnings per share	0.345	0.283	0.210
Dividends per share	0.173	0.141	0.093
Book value at year-end	2.96	2.61	2.45
Market value at year-end	2.875	3.450	4.200
Balance Sheet Items at Year-End *(HK$ million)*			
Loans and advances	43,368	42,921	40,643
Impairment allowance	569	N/A	N/A
Loan loss provision	N/A	1,059	1,237
Total assets	85,037	83,577	79,917
Average interest earnings assets	70,384	70,297	73,472
Total deposits	61,883	62,411	61,559
Shareholders' funds	9,455	8,322	7,812
Financial Ratios			
Capital adequacy	16.0%	15.9%	18.4%
Loans to deposits	70.1%	68.8%	66.0%
Loans to total assets	51.0%	51.4%	50.9%
General provision coverage	N/A	1.2%	1.3%
Collective assessment coverage	0.7%	N/A	N/A
Cost to income			
– Before goodwill amortisation in respect of 2004 and 2003	55.6%	49.1%	47.3%
– After goodwill amortisation in respect of 2004 and 2003	55.6%	51.9%	50.3%
Dividend payout	50.1%	50.0%	45.1%
Return on assets	1.3%	1.1%	0.8%
Return on shareholders' funds	12.4%	11.2%	8.7%

The Hong Kong Institute of Certified Public Accountants has issued a number of new and revised Hong Kong Financial Reporting Standards ("HKFRS") that are effective or available for early adoption for accounting periods beginning on or after 1 January 2005. Information on the changes in accounting policies resulting from initial application of these new and revised HKFRSs is provided in note 3 on the Group's audited consolidated financial statements for the year ended 31 December 2005. Figures for 2004 and 2005 have been adjusted for these new and revised policies in accordance with the transitional provisions and as disclosed in note 3 on the Group's audited consolidated financial statements for the year ended 31 December 2005. Figures for 2003 have not been restated.

2. SUMMARY OF AUDITED FINANCIAL STATEMENTS

The following is the audited financial statements of the Group for the year ended 31 December 2005 together with the accompanying notes prepared in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, extracted from the Group's annual report for the year ended 31 December 2005.

Consolidated Income Statement
for the year ended 31 December 2005 (Expressed in Hong Kong dollars)

	Note	**2005** HK$'000	**2004** (restated) HK$'000
Interest income	4	3,007,372	2,241,410
Interest expense		(1,908,115)	(767,953)
Net interest income		1,099,257	1,473,457
Fee and commission income	5	439,662	461,307
Fee and commission expense		(12,837)	(26,880)
Net fee and commission income		426,825	434,427
Net trading income	6	343,466	177,944
Net income from financial instruments designated at fair value through profit or loss	7	22,481	–
Net hedging expense	8	(679)	–
Other operating income	9	79,301	69,198
Operating income		1,970,651	2,155,026
Operating expenses	10	(1,094,688)	(1,117,485)
		875,963	1,037,541
Impairment losses written back on loans and advances	13(a)	57,544	–
Charge for bad and doubtful debts	13(b)	–	(78,065)
Impairment losses written back on held-to-maturity investments		6,306	–
Impairment losses on available-for-sale securities		(7,817)	–
Provision written back on held-to-maturity investments		–	9,682
Impairment losses written back on properties	32	1,517	–
Impairment losses on goodwill	33	–	(9,502)
Impairment losses written back/(charged)		57,550	(77,885)

	Note	2005 HK$'000	2004 (restated) HK$'000
Operating profit		933,513	959,656
Loss on disposal of associates		(6,352)	–
Net profit on disposal of fixed assets		240,222	11,862
Revaluation gain on investment properties	32	2,140	7,555
Share of profits less losses of associates		46,123	75,659
Profit before taxation		1,215,646	1,054,732
Income tax	14	(112,206)	(151,177)
Profit for the year		1,103,440	903,555
Attributable to:			
Equity shareholders of the Company	15	1,103,395	903,925
Minority interests	46	45	(370)
Profit for the year		1,103,440	903,555
Dividends payable to equity shareholders of the Company attributable to the year:	16		
Interim dividend declared and paid during the year		361,358	210,759
Final dividend proposed after the balance sheet date		191,872	239,636
		553,230	450,395
Earnings per share	17		
Basic		34.51¢	28.32¢
Diluted		32.38¢	25.77¢

Consolidated Balance Sheet
at 31 December 2005 (Expressed in Hong Kong dollars)

	Note	2005 HK$'000	2004 (restated) HK$'000
Assets			
Cash and balances with banks and other financial institutions	19	1,161,309	1,488,919
Placements with banks and other financial institutions	20	5,265,044	6,822,355
Trade bills	21	406,364	246,081
Trading assets	22	6,473,029	–
Securities designated at fair value through profit or loss	23	1,139,908	–
Other investment in securities	24	–	4,043,467
Advances to customers and other accounts	25	44,108,183	43,323,300
Available-for-sale securities	27	5,945,960	–
Held-to-maturity investments	28	17,194,283	23,930,181
Investment securities	29	–	39,841
Interest in associates	31	1,291,180	1,334,442
Fixed assets	32		
– Investment property		64,994	64,850
– Other property and equipment		936,474	1,182,610
Goodwill	33	1,007,749	1,007,749
Deferred tax assets	38	42,201	93,562
Total assets		85,036,678	83,577,357
Equity and liabilities			
Deposits and balances of banks and other financial institutions	34	4,157,446	3,555,852
Deposits from customers	35	54,415,279	55,451,727
Trading liabilities	36	661,137	–
Certificates of deposit issued	37	7,467,961	6,959,690
Debt securities issued	40	2,245,435	2,322,798
Convertible bonds issued	41	1,289,817	1,399,384
Current taxation	38	50,478	6,446
Deferred tax liabilities	38	45,466	8
Other liabilities		895,455	1,283,553
Loan capital	47	4,352,351	4,275,896
Total liabilities		75,580,825	75,255,354

	Note	2005 HK$'000	2004 (restated) HK$'000
Equity			
Share capital	44	3,197,859	3,194,153
Reserves	45	6,257,458	5,127,850
Total equity attributable to equity shareholders of the Company		9,455,317	8,322,003
Minority interests	46	536	–
Total equity		9,455,853	8,322,003
Total equity and liabilities		85,036,678	83,577,357

Balance Sheet

at 31 December 2005 (Expressed in Hong Kong dollars)

		2005		2004 (restated)	
	Note	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Non-current assets					
Fixed assets	32				
– Other property and equipment			55,565		57,823
Investments in subsidiaries	30		6,245,247		6,239,934
			6,300,812		6,297,757
Current assets					
Trading assets	22	93,707		–	
Other investment in securities	24	–		86,074	
Advances to customers and other accounts	25	18,403		23,963	
Amounts due from subsidiaries	26	1,025,464		1,070,478	
		1,137,574		1,180,515	
Current liabilities					
Other liabilities		6,343		6,777	
Amounts due to subsidiaries	39	1,396,145		1,399,608	
		1,402,488		1,406,385	
Net current liabilities			(264,914)		(225,870)
Total assets less current liabilities			6,035,898		6,071,887
Capital and reserves					
Share capital	44		3,197,859		3,194,153
Reserves	45		2,838,039		2,877,734
Total equity			6,035,898		6,071,887

Consolidated Statement of Changes in Equity
for the year ended 31 December 2005 (Expressed in Hong Kong dollars)

		2005		2004 (restated)	
	Note	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Total equity at 1 January:					
As previously reported:					
– attributable to equity shareholders of the Company		8,310,355		7,811,770	
– minority interests	*46*	–		191	
		8,310,355		7,811,961	
Prior period adjustments arising from changes in accounting policies	*45*	11,648		4,754	
As restated, before opening balance adjustments		8,322,003		7,816,715	
Opening balance adjustments arising from changes in accounting policies	*45*	638,816		–	
At 1 January, after prior period and opening balance adjustments			8,960,819		7,816,715
Net income recognized directly in equity:					
Exchange differences on translation of:					
– financial statements of overseas branches, subsidiaries and associates	*45*	3,371		283	
– related borrowings	*45*	(329)		–	
– on disposal of an associate	*45*	627		–	
			3,669		283
Surplus on revaluation of other premises upon reclassification to investment properties, net of deferred tax	*45*		6,785		–
Cash flow hedge					
– effective portion of changes in fair value	*45*	9,364		–	
– transfer to deferred tax	*45*	(1,639)		–	
			7,725		–
Changes in fair value					
– of available-for-sale securities	*45*	(59,442)		–	
– transfer to deferred tax	*45*	10,403		–	
			(49,039)		–
Share of associates					
– share option reserve	*45*	6,500		–	
– fair value reserve	*45*	2,894		–	
			9,394		–

		2005		2004 (restated)	
	Note	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Net profit for the year:					
As previously reported					
– attributable to equity shareholders of the Company				901,339	
– minority interests	*46*			(370)	
				900,969	
Prior year adjustments arising from changes in accounting policies	*3(a)*			2,586	
Net profit for the year (2004: as restated)			1,103,440		903,555
Total recognized income and expense for the year (2004: as restated)			1,081,974		903,838
Attributable to:					
– equity shareholders of the Company		1,081,929		904,208	
– minority interests		45		(370)	
		1,081,974		903,838	
Dividends paid during the year	*16(c)*		(601,197)		(411,897)
Minority interests attributable to subsidiaries acquired/disposed during the year			491		179
Movements in equity arising from capital transactions:					
Shares issued under share option scheme	*44(a)*	3,706		4,318	
Net share premium received	*45*	4,264		4,542	
Equity settled share-based transactions, net of tax (2004: as restated)	*45*	5,796		4,308	
			13,766		13,168
Total equity at 31 December			9,455,853		8,322,003

Consolidated Cash Flow Statement
for the year ended 31 December 2005 (Expressed in Hong Kong dollars)

	2005	2004 (restated)
	HK$'000	*HK$'000*
OPERATING ACTIVITIES		
Profit for the year before taxation	1,215,646	1,054,732
Adjustments for non-cash items:		
Charge for bad and doubtful debts	–	78,065
Impairment losses written back on loans and advances	(57,544)	–
Share of profits less losses on associates	(46,123)	(75,659)
Revaluation gain on investment properties	(2,140)	(7,555)
Net profit on disposal of fixed assets	(240,222)	(11,862)
Impairment losses written back on held-to-maturity investments	(6,306)	–
Provision written back on held-to-maturity securities	–	(9,682)
Impairment loss written back on properties	(1,517)	–
Impairment loss on available-for-sale securities	7,817	–
Share-based payment	5,796	4,308
Amortization of deferred expenses	94,260	101,485
Amortization of discount on debt securities issued	–	(284)
Interest expenses on convertible bonds	37,731	3,495
Depreciation on tangible fixed assets	112,837	146,399
Dividend income from equity investment securities	(25,717)	(10,777)
Interest expenses on loan capital	355,262	355,877
Loss on disposal of associates	6,352	–
Profit on disposal of a subsidiary	–	(865)
Amortization of goodwill	–	60,336
Impairment loss on goodwill	–	9,502
Foreign exchange differences	(16,112)	7,937
	1,440,020	1,705,452

	2005	2004
		(restated)
	HK$'000	*HK$'000*
(Increase)/decrease in operating assets#		
Placements with banks and other financial institutions with original maturity beyond three months	(305,511)	82,153
Treasury bills with original maturity beyond three months	299,355	(398,823)
Certificates of deposit held with original maturity beyond three months	776,453	692,785
Trading assets	(2,677,493)	–
Securities designated at fair value through profit or loss	(70,110)	–
Other investments in securities	–	(1,455,248)
Advances to customers, banks and other financial institutions, trade bills and other accounts	(485,294)	(2,270,500)
Held-to-maturity investments	(494,513)	168,884
Investment securities	–	142
Available-for-sale securities	242,570	–
Increase/(decrease) in operating liabilities#		
Deposits and balances of banks and other financial institutions	601,594	69,773
Deposits from customers	(1,036,448)	(1,395,879)
Trading liabilities	661,137	–
Certificates of deposit issued	502,577	2,248,515
Debt securities issued	(65,515)	–
Other liabilities	(810,308)	(85,208)
NET CASH USED IN OPERATIONS	(1,421,486)	(637,954)
Income tax		
Hong Kong profits tax paid	(113,585)	(115,782)
Overseas profits tax paid	(1,034)	(1,568)
NET CASH USED IN OPERATING ACTIVITIES	(1,536,105)	(755,304)

The changes in these balances are quantified after taking into account the opening balance adjustments made at 1 January 2005. The opening balance adjustments result from the changes in accounting policies is described in note 3.

	Note	2005	2004 (restated)
		HK$'000	*HK$'000*
INVESTING ACTIVITIES			
Dividends received from equity investment securities		25,717	10,777
Purchase of fixed assets		(53,934)	(64,003)
Proceeds from disposal of fixed assets		439,065	241,875
Proceeds from disposal of associates		35,524	–
Increase in shareholding in an associate		–	(500,000)
Capital injection into an associate		–	(250,000)
Net cash outflow from disposal of a subsidiary	*52(b)*	–	(8,872)
Purchase of an associate		(39)	–
NET CASH GENERATED FROM/(USED IN) INVESTING ACTIVITIES		446,333	(570,223)
FINANCING ACTIVITIES			
Ordinary dividends paid		(601,197)	(411,897)
Interest paid on convertible bonds		(3,499)	(3,505)
Interest paid on loan capital		(355,733)	(355,602)
Proceeds from debt securities		–	2,323,082
Proceeds from shares issued		7,970	8,860
NET CASH (USED IN)/GENERATED FROM FINANCING ACTIVITIES		(952,459)	1,560,938
NET (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS		(2,042,231)	235,411
CASH AND CASH EQUIVALENTS AT 1 JANUARY		8,054,509	7,819,098
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	*48*	6,012,278	8,054,509
Cash flows from operating activities include:			
Interest received		3,102,761	3,072,324
Interest paid		(2,027,636)	(1,549,720)

Notes on the Financial Statements

(Expressed in Hong Kong dollars unless otherwise indicated)

1. Principal Activities

The principal activities of CITIC International Financial Holdings Limited (the "Company") and its subsidiaries (the "Group"), which materially affect the results or comprise the assets and liabilities of the Group, are the provision of banking and related financial services.

2. Significant Accounting Policies

(a) Statement of compliance

These financial statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("HKFRSs"), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs"), and Interpretations issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance. These financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

The HKICPA has issued a number of new and revised HKFRSs that are effective or available for early adoption for accounting periods beginning on or after 1 January 2005. Information on the changes in accounting policies resulting from initial application of these new and revised HKFRSs for the current and prior accounting periods reflected in these financial statements is provided in note 3.

(b) Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is historical cost except that the following assets and liabilities are stated at their fair value as explained in the accounting policies set out below:

– financial instruments classified as trading, designated at fair value through profit or loss and available-for-sale (see note 2(g)(ii)); and

– investment property (see note 2(j)).

The preparation of financial statements in conformity with HKFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of HKFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 61.

(c) Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognized in the income statement as follows:

(i) Interest income

Interest income for all interest-bearing financial instruments, except those classified as held for trading or designated at fair value through profit or loss, is recognized as interest income in the income statement using the effective interest method.

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

For impaired loans, the accrual of interest income based on the original terms of the loan is discontinued, but any increase in the present value of impaired loans due to the passage of time is reported as interest income.

Net income from financial instruments designated at fair value through profit or loss and net trading income comprises all gains and losses from changes in fair value (net of accrued coupon) of such financial assets and financial liabilities, together with interest income and expense and dividend income attributable to those financial instruments.

(ii) Fee and commission income

Fee and commission income is recognized when the corresponding service is provided, except where the fee is charged to cover the costs of a continuing service to, or risk borne for, the customer, or is interest in nature. In these cases, the fee is recognized as income in the accounting period in which the costs or risk is incurred or accounted for as interest income.

(iii) Finance income from finance lease and hire purchase contract

Finance income implicit in the finance lease and hire purchase payments is recognized as interest income over the period of the leases so as to produce an approximately constant periodic rate of return, on the outstanding net investment in the leases for each accounting period.

(iv) Rental income from operating lease

Rental income received under operating leases is recognized as other operating income in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives granted are recognized in the income statement as an integral part of the aggregate net lease payments receivable.

(v) Dividend income is recognized as follows:

- dividend income from listed investments is recognized when the share price of the investment is quoted ex-dividend; and

– dividend income from unlisted investments is recognized when the shareholder's right to receive payment is established.

(d) Subsidiaries and controlled entities

A subsidiary, in accordance with the Hong Kong Companies Ordinance, is a company in which the Group, directly or indirectly, holds more than half of the issued share capital or controls more than half of the voting power or controls the composition of the board of directors. Subsidiaries are considered to be controlled if the Company has the power, directly or indirectly, to govern the financial and operating policies, so as to obtain benefits from their activities.

An investment in a controlled subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases.

Intra-group balances and transactions and any unrealized profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial statements. Unrealized losses resulting from intra-group transactions are eliminated in the same way as unrealized gains but only to the extent that there is no evidence of impairment.

Minority interests at the balance sheet date, being the portion of the net assets of subsidiaries attributable to equity interests that are not owned by the Company, whether directly or indirectly through subsidiaries, are presented in the consolidated balance sheet and statement of changes in equity within equity, separately from equity attributable to the equity shareholders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated income statement as an allocation of the net profit or loss for the year between minority interests and the equity shareholders of the Company.

Where losses applicable to the minority exceed the minority's interests in the equity of a subsidiary, the excess, and any further losses applicable to the minority, are charged against the Group's interest except to the extent that the minority has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Group's interest is allocated all such profits until the minority's share of losses previously absorbed by the Group has been recovered.

In the Company's balance sheet, an investment in a subsidiary is stated at cost less impairment losses (see note 2(n)).

(e) Associates

An associate is an entity over which the Group or the Company has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

An investment in an associate is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of the associate's net assets. The consolidated income statement includes the Group's share of the post-acquisition, post-tax results of the associates for the year, including any impairment loss on goodwill relating to the investment in associates recognized for the year (see notes 2(f) and (n)).

When the Group's share of losses exceeds its interest in the associate, the Group's interest is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate. For these purposes, the Group's interest in the associate accounted for under equity method is the carrying amount of the investment under equity method together with the Group's other long-term interests that in substance form part of the Group's net investment in the associate.

Unrealized profits and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associate, except where unrealized losses provide evidence of an impairment of the asset transferred, in which case they are recognized immediately in profit or loss.

In the Company's balance sheet, its investments in associates are stated at cost less impairment losses (see note 2(n)).

(f) *Goodwill*

Goodwill represents the excess of the cost of a business combination or an investment in an associate over the Group's interest in the net fair value of the acquirer's identifiable assets, liabilities and contingent liabilities.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is tested annually for impairment (see note 2(n)). In respect of an associate, the carrying amount of goodwill is included in the carrying amount of the interest in the associate.

Any excess of the Group's interest in the net fair value of acquirer's identifiable assets, liabilities and contingent liabilities over the cost of a business combination or an investment in an associate is recognized immediately in profit or loss.

On disposal of a cash generating unit, or an associate during the year, any attributable amount of purchased goodwill is included in the calculation of the profit or loss on disposal.

(g) *Financial instruments*

(i) Initial recognition

The Group classifies its financial instruments into different categories at inception, depending on the purpose for which the assets were acquired or the liabilities were incurred. The categories are: fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets and other financial liabilities.

Financial instruments are measured initially at fair value, which normally will be equal to the transaction price, plus, in case of a financial asset or financial liability not held at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial assets or financial liabilities. Transaction costs on financial assets and financial liabilities at fair value through profit or loss are expensed immediately.

The Group recognizes financial assets and financial liabilities on the date it becomes a party to the contractual provisions of the instrument. A regular way purchase or sale of financial assets is recognized using trade date accounting. From this date, any gains and losses arising from changes in fair value of the financial assets or financial liabilities are recorded.

(ii) Categorization

Fair value through profit or loss

This category comprises financial assets and liabilities held for trading, and those designated at fair value through profit or loss upon initial recognition, but excludes those investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured.

Trading financial instruments are financial assets or financial liabilities which are acquired or incurred principally for the purpose of trading, or are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives that do not qualify for hedge accounting (note 2(i)) are accounted for as trading instruments.

Financial instruments designated at fair value through profit or loss primarily consist of securities with embedded derivatives where the characteristics and risks of the embedded derivatives are not closely related to the host contracts.

Financial assets and liabilities under this category are carried at fair value. Changes in the fair value are included in the income statement in the period in which they arise. Upon disposal or repurchase, the difference between the net sale proceeds or the net payment and the carrying value is included in the income statement.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than (a) those that the Group intends to sell immediately or in the near term, which will be classified as held for trading; (b) those that the Group, upon initial recognition, designates at fair value through profit or loss or as available-for-sale; or (c) those where the Group may not recover substantially all of its initial investment, other than because of credit deterioration, which will be classified as available-for-sale. Loans and receivables mainly comprise loans and advances to customer and placements with banks and financial institutions.

Loans and receivables are carried at amortized cost using the effective interest method, less impairment losses, if any (see note 2(n)).

Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity where the Group has the positive intention and ability to hold to maturity, other than those that the Group, upon initial recognition, designates as fair value through profit or loss or as available-for-sale.

Held-to-maturity investments are carried at amortized cost using the effective interest method less impairment losses, if any (see note 2(n)).

Available-for-sale securities

Available-for-sale securities are non-derivative financial assets that are designated as available-for-sale or are not classified in any of the other three categories above. They include financial assets intended to be held for an indefinite period of time, but which may be sold in response to needs for liquidity or changes in the market environment.

Investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured, and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments are carried at cost less impairment losses, if any (see note 2(n)).

Available-for-sale financial assets are carried at fair value. Unrealized gains and losses arising from changes in the fair value are recognized directly in the fair value reserve, except for foreign exchange gains and losses on monetary items such as debt securities which are recognized in the income statement.

When the available-for-sale financial assets are sold, the difference between the net sale proceeds and the carrying value, and the accumulated fair value adjustments in the equity are treated as gains or losses on disposal.

Other financial liabilities

Financial liabilities, other than trading liabilities and those designated at fair value through profit or loss, are measured at amortized cost using the effective interest method.

The fair value of the liability portion of a convertible bond is determined using a market interest rate for an equivalent non-convertible bond. This amount is recorded as a liability on an amortized cost basis until extinguished on conversion or maturity of the bonds. The remainder of the proceeds is allocated to the conversion option. This is recognized and included in shareholders' equity.

(iii) Fair value measurement principles

The fair value of financial instruments is based on their quoted market prices at the balance sheet date without any deduction for estimated future selling costs. Financial assets are priced at current bid prices, while financial liabilities are priced at current asking prices.

If a traded price or a quoted market price for exchange traded financial instrument is not available on a recognized stock exchange or a price from a broker/dealer for non-exchange-traded financial instrument is not available, or if the market for a financial instrument is not active, the fair value of the instrument is estimated using valuation techniques that provides a reasonable estimate of prices which could be obtained in actual market transactions.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate used is a market rate at the balance sheet date applicable for an instrument with similar terms and conditions. Where other pricing models are used, inputs are based on market data at the balance sheet date.

(iv) Derecognition

A financial asset is derecognized when the contractual rights to receive the cash flows from the financial asset expire, or where the financial asset together with substantially all the risks and rewards of ownership, have been transferred.

A financial liability is derecognized when the obligation specified in the contract is discharged, cancelled or expires.

(v) Offsetting

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

(vi) Embedded derivatives

An embedded derivative is a component of a hybrid (combined) instrument that includes both the derivative and a host contract with the effect that some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. The embedded derivatives are separated from the host contract and accounted for as a derivative when (a) the economic characteristics and risks of the embedded derivative are not closely related to the host contract; and (b) the hybrid (combined) instrument is not measured at fair value with changes in fair value recognized in the income statement.

When the embedded derivative is separated, the host contract is accounted for in accordance with the accounting policies for financial instruments.

(h) *Repurchase and reverse repurchase transactions*

Securities sold subject to a simultaneous agreement to repurchase these securities at a certain later date at a fixed price (repurchase agreements) are retained in the financial statements and measured in accordance with their original measurement principles. The proceeds from the sale are reported as liabilities and are carried at amortized cost.

Securities purchased under agreements to resell (reverse repurchase agreements) are reported not as purchases of the securities, but as receivables and are carried in the balance sheet at amortized cost.

Interest earned on reverse repurchase agreements and interest incurred on repurchase agreements are recognized as interest income and interest expense respectively, over the life of each agreement using the effective interest method.

(i) *Hedging*

Hedge accounting recognizes the offsetting effects on profit or loss of changes in the fair values of the hedging instrument and the hedged item. The Group assesses and documents whether the financial instruments that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items attributable to the hedged risks both at hedge inception and on an ongoing basis. The Group discontinues prospectively hedge accounting when (a) the hedging instrument expires or is sold, terminated or exercised; (b) the hedge no longer meets the criteria for hedge accounting; or (c) the Group revokes the designation.

(i) Fair value hedge

A fair value hedge seeks to offset risks of changes in the fair value of recognized asset or liability that will give rise to a gain or loss being recognized in the income statement.

The hedging instrument is measured at fair value, with fair value changes recognized in the income statement. The carrying amount of the hedged item is adjusted by the amount of the changes in fair value of the hedging instrument attributable to the risk being hedged. This adjustment is recognized in the income statement to offset the effect of the gain or loss on the hedging instrument.

(ii) Cash flow hedge

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognized asset or liability, or a highly probable forecast transaction, or the foreign currency risk of a committed future transaction, the effective part of any gain or loss on the derivative financial instrument in relation to the hedged risk is recognized directly in equity. The ineffective part of any gain or loss is recognized immediately in the income statement.

If a hedge of a forecast transaction subsequently results in the recognition of a financial asset or a financial liability, the associated gains or losses that were recognized directly in equity are reclassified in the income statement in the same period or periods during which the asset acquired or liability assumed affects the income statement. If the hedge of a forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, the associated cumulative gain or loss is removed from equity and included in the initial cost or other carrying amount of the non-financial asset or liability.

For cash flow hedges of a recognized asset or liability, the associated cumulative gain or loss is removed from equity and recognized in the income statement in the same period or periods during which the hedged cash flows affect the profit.

When a hedging instrument expires or is sold, terminated or exercised, or the Group revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognized in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, the cumulative unrealized gain or loss recognized in equity is recognized immediately in the income statement.

(iii) Hedge effectiveness testing

The Group expects the hedge to be highly effective (prospective effectiveness) at the inception of the hedge and throughout its life in order to qualify for hedge accounting. Actual effectiveness (retrospective effectiveness) also needs to be demonstrated on an ongoing basis.

The documentation of each hedging relationship sets out how the effectiveness of the hedge is assessed. The method which the Group adopts for assessing hedge effectiveness will depend on its risk management strategy.

For fair value hedge relationships, the Group utilizes the cumulative dollar offset method as effectiveness testing methodologies. For cash flow hedge relationships, the Group utilizes the cumulative dollar offset method using the hypothetical derivative approach.

For prospective effectiveness, the hedging instrument must be expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated. For actual effectiveness, the changes in fair value or cash flows must offset each other in the range of 80% to 125% for the hedge to be deemed effective.

(j) Investment property

Investment properties are land and buildings which are owned and/or held under a leasehold interest (see note 2(l)) to earn rental income and/or for capital appreciation. These include land and buildings held for a currently undetermined future use.

Investment properties are stated in the balance sheet at fair value. Any gain or loss arising from a change in fair value is recognized in the income statement. Rental income from investment property is accounted for as described in accounting policy 2(c)(iv).

(k) Other property and equipment

In preparing these financial statements, advantage has been taken of the transitional provisions set out in paragraph 80A of HKAS 16 "Property, plant and equipment", issued by the HKICPA, with effect that other premises which are carried at revalued amounts in financial statements relating to periods ended before 30 September 1995 have not been revalued to fair value at the balance sheet date.

The following items of property and equipment are stated in the balance sheet at cost less accumulated depreciation and impairment losses, if any (see note 2(n)):

– held under operating leases and buildings thereon, where the fair value of the leasehold interest in the land and buildings cannot be measured separately at the inception of the lease and the building is not clearly held under an operating lease (see note 2(l)).

– items of equipment.

Depreciation is calculated to write off the cost or valuation of items of property and equipment using the straight line method over the estimated useful lives as follows:

– freehold land is not depreciated.

– buildings – over 30 years or the unexpired terms of the land leases, whichever is the shorter.

– furniture, fixtures and equipment – 3 to 10 years.

Where parts of an item of property and equipment have different useful lives, the cost or valuation of the item is allocated on a reasonable basis between the parts and each part is depreciated separately. Both the useful life of an asset and its residual value, if any, are reviewed annually.

Gains or losses arising from the retirement or disposal of an item of property and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognized in the income statement on the date of retirement or disposal. Any related revaluation surplus is transferred from the revaluation reserve to retained profits.

(l) Leases and hire purchase contracts

(i) Classification of leased assets

Leases which transfer substantially all the risks and rewards of ownership to the lessee are classified as finance leases. Leases which do not transfer substantially all the risks and rewards of ownership to the lessee are classified as operating leases.

(ii) Assets held under finance leases

Where the Group is a lessor under finance leases, an amount representing the net investment in the lease is included in the balance sheet as loans and advances to customers. Hire purchase contracts having the characteristics of finance leases are accounted for in the same manner as finance leases. Impairment losses are accounted for in accordance with the accounting policy as set out in note 2(n).

(iii) Assets held for use in operating leases

Where the Group leases out assets under operating leases, the assets are included in the balance sheet according to their nature and, where applicable, are depreciated in accordance with the Group's depreciation policies, as set out in note 2(k). Impairment losses are accounted for in accordance with the accounting policy as set out in note 2(n).

Revenue arising from operating leases is recognized in accordance with the Group's revenue recognition policies, as set out in note 2(c)(iv).

(iv) Operating lease charges

Where the Group has the use of assets held under operating leases, payments made under the leases are charged to income statement in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognized in income statement as an integral part of the aggregate net lease payments made.

(m) Repossessed assets

In the recovery of impaired loans and advances, the Group may take repossession of the assets held as collateral through court proceedings or voluntary delivery of possession by the borrowers. Where it is intended to achieve an orderly realisation and the Group is no longer seeking repayment from the borrower, repossessed assets are reported in "other assets".

Repossessed assets are recognized at the lower of the amount of the related loans and advances and fair value less costs to sell at the date of exchange. They are not depreciated or amortized.

Impairment losses on initial classification and on subsequent remeasurement are recognized in the income statement.

(n) Impairment of assets

The carrying amount of the Group's assets are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, the carrying amount is reduced to the estimated recoverable amount by means of a charge to the income statement.

(i) Loans and receivables

Impairment losses of loans and receivables are measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Receivables with a short duration are not discounted if the effect of discounting is immaterial.

The total allowance for credit losses consists of two components: individual impairment allowances, and collective impairment allowances.

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

The individual impairment allowance is based upon management's best estimate of the present value of the cash flows which are expected to be received discounted at the original effective interest rate. In estimating these cash flows, management makes judgements about the borrower's financial situation and the net realizable value of any underlying collateral or guarantees in favor of the Group. Each impaired asset is assessed on its own merits.

In assessing the need for collective impairment allowances, management considers factors such as credit quality, portfolio size, concentrations, and economic factors. In order to estimate the required allowance, the Group makes assumptions both to define the way the Group models inherent losses and to determine the required input parameters, based on historical experience and current economic conditions.

The accuracy of the impairment allowances the Group makes depends on how well the Group can estimate future cash flows for individually assessed impairment allowances and the model assumptions and parameters used in determining collective impairment allowances. While this necessarily involves judgement, the Group believes that the impairment allowances on loans and advances to customers are reasonable and supportable.

Any subsequent changes to the amounts and timing of the expected future cash flows compared to the prior estimates that can be linked objectively to an event occurring after the write-down, will result in a change in the impairment allowances on loans and receivables and be charged or credited to the income statement.

When there is no reasonable prospect of recovery, the loan and the related interest receivables are written off.

(ii) Held-to-maturity investments

For held-to-maturity investments, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets) on an individual basis.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognized, the impairment loss is reversed through the income statement. A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognized in prior years.

(iii) Available-for-sale securities

When there is objective evidence that an available-for-sale financial asset is impaired, the cumulative loss that had been recognized directly in equity is removed from equity and is recognized in the income statement. The amount of the cumulative loss that is recognized in the income statement is the difference between the acquisition cost (net of any principal repayment and amortization) and current fair value, less any impairment loss on that asset previously recognized in the income statement.

For unquoted available-for-sale equity securities that are carried at cost, the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

Impairment losses recognized in the income statement in respect of available-for-sale equity securities are not reversed through the income statement. Any subsequent increase in the fair value of such assets is recognized directly in equity.

Impairment losses in respect of available-for-sale debt securities are reversed if the subsequent increase in fair value can be objectively related to an event occurring after the impairment loss was recognized. Reversals of impairment losses in such circumstances are recognized in the income statement.

(iv) Other assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognized no longer exists or may have decreased:

– property and equipment (other than properties carried at revalued amounts);

– investments in subsidiaries and associates; and

– goodwill.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill, the recoverable amount is estimated annually whether or not there is any indication of impairment.

– Calculation of recoverable amount

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

– Recognition of impairment losses

An impairment loss is recognized in the income statement whenever the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognized in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit (or group of units) and then, to reduce the carrying amount of the other assets in the unit (or group of units) on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

– Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a favorable change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is not reversed.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognized in prior years. Reversals of impairment losses are credited to the income statement in the year in which the reversals are recognized.

(o) Cash equivalents

Cash equivalents are short-term highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition.

(p) Employee benefits

(i) Short term employee benefits and contributions to defined contribution retirement plans

Salaries, annual bonuses, paid annual leave, contributions to defined contribution plans and the cost of non-monetary benefits are accrued in the year in which the associated services are rendered by employees. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) Share-based payments

Employee share option scheme

The fair value of share options granted to employees is recognized as an employee cost with a corresponding increase in a capital reserve within equity. The fair value is measured at grant date using the trinomial lattice model, taking into account the terms and conditions upon which the options were granted. Where the employees have to meet vesting conditions before becoming unconditionally entitled to those share options, the total estimated fair value of the share options is spread over the vesting period, taking into account the probability that the options will vest.

During the vesting period, the number of share options that is expected to vest is reviewed. Any adjustment to the cumulative fair value recognized in prior years is charged/credited to the income statement for the year of the review unless the original employee expenses qualify for recognition as an asset, with a corresponding adjustment to the capital reserve. On vesting date, the amount recognized as an expense is adjusted to reflect the actual number of share options that vest (with a corresponding adjustment to capital reserve) except where forfeiture is only due to not achieving vesting conditions that relate to the market price of the Company's shares.

The equity amount is recognized in equity until either the option is exercised (when it is transferred to share premium) or the option expires (when it is released directly to retained profits).

Employee Equity Linked Deferred Award Scheme ("ELDA")

Awards are granted to employees of the Group under ELDA. The fair value of the amount payable to the employee is recognized as an employee cost with a corresponding increase in liabilities. The fair value is initially measured at grant date and spread over the period during which the employees become unconditionally entitled to payment. The fair value of the award is measured based on the maximum payment of HK$3.00 per share. The liability is remeasured at each balance sheet date and at settlement date. Any changes in the fair value of the liability are recognized in the income statement.

(iii) Staff retirement scheme

The Group operates a defined contribution provident fund and a Mandatory Provident Fund scheme. Contributions are charged to the income statement as and when the contributions fall due.

(q) Income tax

(i) Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognized in the income statement except to the extent that they relate to items recognized directly in equity, in which case they are recognized in equity.

(ii) Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

(iii) Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilized, are recognized.

Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried back or forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilised.

The limited exceptions to recognition of deferred tax assets and liabilities are those temporary differences arising from goodwill not deductible for tax purposes, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit (provided they are not part of a business combination), and temporary differences relating to investments in subsidiaries to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, unless it is probable that they will reverse in the future.

The amount of deferred tax recognized is measured based on the expected manner of realization or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow the related tax benefit to be utilized. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profit will be available. Additional income taxes that arise from the distribution of dividends are recognized when the liability to pay the related dividends is recognized.

(iv) Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities if, and only if, the Group or the Company has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

– in the case of current tax assets and liabilities, the Group or the Company intends either to settle on a net basis, or to realize the asset and settle the liability simultaneously; or

– in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:

  – the same taxable entity; or

  – different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realize the current tax assets and settle the current tax liabilities on a net basis or realize and settle simultaneously.

(r) Translation of foreign currencies

Foreign currency transactions during the year are translated into Hong Kong dollars at the exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. Exchange gains and losses are dealt with in the income statement.

Exchange differences relating to investments at fair value through profit or loss and derivative financial instruments are included in gains and losses on investments and net gain/(loss) on derivatives, respectively. All other exchange differences relating to monetary items are presented separately in the income statement.

The results of foreign operations are translated into Hong Kong dollars at the average exchange rates for the year; balance sheet items are translated at the rates of exchange ruling at the balance sheet date. The resulting exchange differences are dealt with as a movement in reserves.

On disposal of a foreign enterprise, the cumulative amount of the exchange differences recognized in reserves which relate to that foreign operation is included in the calculation of the profit or loss on disposal.

(s) Provisions and contingent liabilities

Provisions are recognized for liabilities of uncertain timing or amount when the Group or the Company has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(t) Related parties

For the purpose of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals (being members of key management personnel, significant shareholders and/or their close family members) or other entities and include entities which are under the significant influence of related parties of the Group where those parties are individuals, and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group.

(u) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

The Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format for the purposes of these financial statements.

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. Segment revenue, expenses, assets, and liabilities are determined before intra-group balances and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between Group entities within a single segment.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets (both tangible and intangible) that are expected to be used for more than one period.

Unallocated items mainly comprise the bank premises and any items which cannot be reasonably allocated to specific business segments.

3. Changes in Accounting Policies

The HKICPA has issued a number of new and revised HKFRSs that are effective for accounting periods beginning on or after 1 January 2005.

The accounting policies of the Group and the Company after the adoption of these new and revised HKFRSs have been summarized in note 2. The following sets out information on the significant changes in accounting policies for the current and prior accounting periods reflected in these financial statements.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 62).

(a) Restatement of prior periods and opening balances

The following tables disclose the adjustments that have been made in accordance with the transitional provisions of the respective HKFRSs to each of the line items in the consolidated income statement and consolidated balance sheet and the Company's balance sheet and other significant related disclosure items as previously reported for the year ended 31 December 2004. The effects of the changes in accounting policies on the balances at 1 January 2004 and 2005 are disclosed in note 45.

Effect on the consolidated financial statements

Consolidated Income Statement for the year ended 31 December 2004

	2004 (as previously reported)	Effect of new policy (increase/(decrease) in profit for the year) HKAS 28 *(note 3(d))*	HKAS 1 & 30 *(note 3(i))*	2004 (as restated)
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Interest income	2,241,410	–	–	2,241,410
Interest expense	(767,953)	–	–	(767,953)
Net interest income	1,473,457	–	–	1,473,457
Fee and commission income	461,307	–	–	461,307
Fee and commission expense	(26,880)	–	–	(26,880)
Net fee and commission income	434,427	–	–	434,427
Net trading income	–	–	177,944	177,944
Other operating income	248,551	(1,409)	(177,944)	69,198
Operating income	2,156,435	(1,409)	–	2,155,026
Operating expenses	(1,117,485)	–	–	(1,117,485)
	1,038,950	(1,409)	–	1,037,541
Charge for bad and doubtful debts	(78,065)	–	–	(78,065)
Provision written back on held-to-maturity investments	9,682	–	–	9,682
Impairment losses on goodwill	(9,502)	–	–	(9,502)
Impairment losses	(77,885)	–	–	(77,885)
Operating profit	961,065	(1,409)	–	959,656
Net profit on disposal of fixed assets	11,862	–	–	11,862
Revaluation gain on investment properties	7,555	–	–	7,555
Share of profits less losses of associates	75,978	4,287	(4,606)	75,659
Profit before taxation	1,056,460	2,878	(4,606)	1,054,732
Income tax	(155,491)	(292)	4,606	(151,177)
Profit for the year	900,969	2,586	–	903,555
Attributable to:				
Equity shareholders of the Company	901,339	2,586	–	903,925
Minority interests	(370)	–	–	(370)
Profit for the year	900,969	2,586	–	903,555
Earnings per share				
Basic	28.24¢	0.08¢	–	28.32¢
Diluted	25.70¢	0.07¢	–	25.77¢

Consolidated Balance Sheet as at 31 December 2004

	2004 (as previously reported)	Effect of new policy (increase/(decrease) in total assets and total liabilities) HKFRS 2 (note 3(e))	HKAS 28 (note 3(d))	HKAS 1 & 30 (note 3(i))	Sub-total	2004 (as restated)
	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000	HK$'000
Assets						
Cash and short-term funds	8,345,790	–	–	(6,856,871)	(6,856,871)	1,488,919
Placements with banks and other financial institutions	364,307	–	–	6,458,048	6,458,048	6,822,355
Trade bills	246,081	–	–	–	–	246,081
Certificates of deposit held	1,366,315	–	–	(1,366,315)	(1,366,315)	–
Other investments in securities	3,968,263	–	(14,745)	89,949	75,204	4,043,467
Advances to customers and other accounts	43,323,300	–	–	–	–	43,323,300
Held-to-maturity investments	22,254,992	–	–	1,675,189	1,675,189	23,930,181
Investment securities	39,841	–	–	–	–	39,841
Interest in associates	1,312,357	–	22,085	–	22,085	1,334,442
Goodwill	1,007,749	–	–	–	–	1,007,749
Fixed assets	1,247,460	–	–	–	–	1,247,460
Deferred tax assets	93,562	–	–	–	–	93,562
Total assets	83,570,017	–	7,340	–	7,340	83,577,357
Equity and liabilities						
Deposits and balances of banks and other financial institutions	3,555,852	–	–	–	–	3,555,852
Deposits from customers	55,451,727	–	–	–	–	55,451,727
Certificates of deposit issued	6,959,690	–	–	–	–	6,959,690
Debt securities issued	2,322,798	–	–	–	–	2,322,798
Convertible bonds issued	1,399,384	–	–	–	–	1,399,384
Current taxation	6,446	–	–	–	–	6,446
Deferred tax liabilities	8	–	–	–	–	8
Other liabilities	1,287,861	(4,308)	–	–	(4,308)	1,283,553
Loan capital	4,275,896	–	–	–	–	4,275,896
Total liabilities	75,259,662	(4,308)	–	–	(4,308)	75,255,354
Equity						
Share capital	3,194,153	–	–	–	–	3,194,153
Reserves	5,116,202	4,308	7,340	–	11,648	5,127,850
Total equity attributable to equity shareholders of the Company	8,310,355	4,308	7,340	–	11,648	8,322,003
Minority interests	–	–	–	–	–	–
Total equity	8,310,355	4,308	7,340	–	11,648	8,322,003
Total equity and liabilities	83,570,017	–	7,340	–	7,340	83,577,357

Effect on the Company's balance sheet
Balance Sheet as at 31 December 2004

	2004 (as previously reported)	Effect of new policy (increase/(decrease) in total assets and liabilities) HKFRS 2 *(note 3(e))*	2004 (as restated)
	HK$'000	*HK$'000*	*HK$'000*
Non-current assets			
Fixed assets			
– Other property and equipment	57,823	–	57,823
Investments in subsidiaries	6,236,222	3,712	6,239,934
	6,294,045	3,712	6,297,757
Current assets			
Other investments in securities	86,074	–	86,074
Advances to customers and other accounts	23,963	–	23,963
Amounts due from subsidiaries	1,070,478	–	1,070,478
	1,180,515	–	1,180,515
Current liabilities			
Other liabilities	6,777	–	6,777
Amounts due to subsidiaries	1,399,608	–	1,399,608
	1,406,385	–	1,406,385
Net current liabilities	(225,870)	–	(225,870)
Total assets less current liabilities	6,068,175	3,712	6,071,887
Capital and reserves			
Share capital	3,194,153	–	3,194,153
Reserves	2,874,022	3,712	2,877,734
Total equity	6,068,175	3,712	6,071,887

(b) Estimated effect of changes in accounting policies on the current year

The following tables provide estimates of the extent to which each of the line items in the consolidated income statement, consolidated balance sheet and the Company's balance sheet for the year ended 31 December 2005 is higher or lower than it would have been had the previous policies still been applied in the year, where it is practicable to make such estimates.

Effect on the consolidated financial statements

Estimated effect on the Consolidated Income Statement for the year ended 31 December 2005

	Effect of new policy (increase/ (decrease) in profit for the year)			
	HKFRS 2	**HKFRS 3**	**HKAS 32 & 39***	**Total**
	(note 3(e))	*(note 3(f))*	*(note 3(c))*	
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Interest income	–	–	(186,677)	(186,677)
Interest expense	–	–	80,564	80,564
Net interest income	–	–	(106,113)	(106,113)
Net fee and commission income	–	–	10,161	10,161
Net trading income	–	–	64,524	64,524
Net income from financial instruments designated at fair value through profit or loss	–	–	52,447	52,447
Net hedging expense	–	–	(679)	(679)
Operating income	–	–	20,340	20,340
Operating expenses	(2,699)	59,280	–	56,581
Profit before taxation	(2,699)	59,280	20,340	76,921

* *In respect of the year ended 31 December 2005, it is not practicable to estimate the extent to which the profit for the year would have been higher or lower had the previous policy on impairment of financial assets still been applied.*

The effect of HKAS 28 is not material and not estimated in the above income statement.

Estimated effect on the Consolidated Balance Sheet as at 31 December 2005

	Effect of new policy (increase/(decrease) in total assets and total liabilities)				
	HKFRS 2	**HKFRS 3 & HKAS 36**	**HKAS 32 & 39***	**HKAS 40**	**Total**
	(note 3(e))	*(note 3(f))*	*(note 3(c))*	*(note 3(g))*	
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Assets					
Trading assets	–	–	4,300,413	–	4,300,413
Securities designated at fair value through profit or loss	–	–	1,042,277	–	1,042,277
Other investments in securities	–	–	(3,953,518)	–	(3,953,518)
Advances to customers and other accounts	–	–	(211,560)	–	(211,560)
Available-for-sale securities	–	–	6,017,754	–	6,017,754
Held-to-maturity investments	–	–	(6,309,110)	–	(6,309,110)
Investment securities	–	–	(39,841)	–	(39,841)
Interest in associates	–	–	(4,271)	–	(4,271)
Fixed assets					
– Investment property	–	–	–	7,939	7,939
Goodwill	–	59,280	–	–	59,280
Total	–	59,280	842,144	7,939	909,363
Equity and liabilities					
Trading liabilities	–	–	845,863	–	845,863
Certificates of deposit issued	–	–	(153,530)	–	(153,530)
Debt securities issued	–	–	(73,520)	–	(73,520)
Convertible bonds issued	–	–	(106,105)	–	(106,105)
Current taxation	–	–	38,291	–	38,291
Deferred tax liabilities	–	–	67,788	1,154	68,942
Other liabilities	(7,404)	–	(230,269)	–	(237,673)
Loan capital	–	–	87,033	–	87,033
Total	(7,404)	–	475,551	1,154	469,301
Equity					
Reserves	7,404	59,280	366,593	6,785	440,062
Total equity attributable to equity shareholders of the Company	7,404	59,280	366,593	6,785	440,062
Total	–	59,280	842,144	7,939	909,363

* *In respect of the year ended 31 December 2005, it is not practicable to estimate the extent to which the net assets would have been higher or lower had the previous policy on impairment of financial assets still been applied.*

The effect of HKAS 28 is not material and not estimated in the above balance sheet.

Estimated effect on net income recognized directly in consolidated equity for the year ended 31 December 2005:

	Effect of new policy (increase/(decrease) in equity)		
	HKAS 32 & 39	**HKAS 40**	**Total**
	(note 3(c))	*(note 3(g))*	
	HK$'000	*HK$'000*	*HK$'000*
Attributable to equity shareholders of the Company	(41,314)	6,785	(34,529)
Minority interests	–	–	–
Total equity	(41,314)	6,785	(34,529)

Estimated effect on amounts recognized as capital transactions with owners of the Group for the year ended 31 December 2005:

	Effect of new policy (increase/(decrease) in equity)
	HKFRS 2
	(note 3(e))
	HK$'000
Attributable to equity shareholders of the Company	5,796
Minority interests	–
Total equity	5,796

Effect on the Company's balance sheet

Estimated effect on the Company's Balance Sheet as at 31 December 2005

	Effect of new policy (increase/(decrease) in total assets and total liabilities)	
	HKFRS 2	**Total**
	(note 3(e))	
	HK$'000	*HK$'000*
Current assets		
Investments in subsidiaries	(5,313)	(5,313)
Total	(5,313)	(5,313)
Capital and reserves		
Reserves	5,313	5,313
Total	5,313	5,313

There is no estimated effect on net income recognized directly in the Company's equity for the year ended 31 December 2005.

Estimated effect on amounts recognized as capital transactions with owners of the Company for the year ended 31 December 2005:

	Effect of new policy (increase/(decrease) in equity) HKFRS 2 *(note 3(e))* *HK$'000*
Attributable to equity shareholders of the Company	5,796

(c) Financial instruments (HKAS 32, Financial instruments: Disclosure and presentation and HKAS 39, Financial instruments: Recognition and measurement)

With effect from 1 January 2005, in order to comply with HKAS 32, the Group has provided additional disclosures of terms, conditions, accounting policies, risk and fair values of financial instruments throughout the notes to the financial statements and the specific notes 55 and 56. In order to comply with HKAS 39, the Group has changed its accounting policies relating to financial instruments to those set out in notes 2(g) to (i), (c), (n) and (q). Further details of the changes are as follows:

(i) Financial instruments (see note 2(g))

In prior years, all financial assets were carried at cost or amortized cost net of impairment provisions for diminution in value, except for other investments (under Benchmark treatment of Statement of Standard Accounting Practice ("SSAP") 24) which were held at fair value. Gains and losses from change in fair value were recognized in the income statement in respect of other investments. Provisions were recognized as an expense in the income statement and written back to income statement when circumstances and events that led to the write-down cease to exist.

In prior years, all financial liabilities except for trading securities short positions were carried at cost or amortized cost. Trading securities short positions were carried at fair value and any changes in fair value were recognized through the income statement.

With effect from 1 January 2005, and in accordance with HKAS 39, financial instruments are recognized according to the following categories: (i) fair value through profit or loss, (ii) loans and receivables, (iii) held-to-maturity investments, (iv) available-for-sale securities and (v) other financial liabilities.

(ii) Derivatives and hedge accounting (see notes 2(g) and (i))

In prior years, derivatives mainly included derivatives arising from futures, forward, swap and option transactions undertaken by the Group in the foreign exchange, interest rate and equity markets. Netting was applied where a legal right of off-set existed.

The accounting for these instruments was dependent upon whether the transactions were undertaken for trading purposes or as part of the management of asset and liability portfolios.

Derivatives used for trading purposes

Trading transactions included transactions undertaken for market making, to service customers' needs and for proprietary purposes, as well as any related hedges.

Transactions undertaken for trading purposes were marked to market and the net present value of the gain or loss arising was recognized in the income statement as dealing gains/losses.

The fair value of derivatives that were not exchange-traded was estimated at the amount that the Group would receive or pay to terminate the contract at the balance sheet date taking into account current market conditions and the current creditworthiness of the counterparties.

Derivatives used for asset and liability management purposes

Derivatives used for this purpose were accounted for as hedges and were valued on an equivalent basis to the underlying assets, liabilities or net positions which they were hedging. Any profit or loss was recognized on the same basis as that arising from the related assets, liabilities or net positions.

Any gain or loss on termination of hedging derivatives was deferred and amortized to the income statement over the original life of the terminated contract. Where the underlying asset, liability or position was sold or terminated, the hedging derivative was immediately marked to market through the income statement.

With effect from 1 January 2005, in order to comply with HKAS 39, the Group has changed its accounting policies relating to derivative and hedge accounting set out in note 2(g) and (i) respectively.

(iii) Embedded derivatives (see note 2(g))

In prior years, embedded derivatives were not separately accounted for and they were carried accordingly to the classification of the host contracts.

With effect from 1 January 2005, embedded derivative that is not closely related to the host contract or where the hybrid (combined) instrument is not measured at fair value through profit or loss is accounted for separately from the host contract as equity, assets or liabilities.

(iv) Convertible bonds issued (see note 2(g))

In prior years, convertible bonds issued were recorded as a liability and stated at cost.

With effect from 1 January 2005, and in accordance with HKAS 32, the Group has provided additional disclosures of terms, conditions, accounting policies, risk and fair values of convertible bonds. In order to comply with HKAS 32 & 39, convertible bonds issued are split into their liability and equity components at initial recognition by recognizing the liability component at its fair value and attributing to the equity component the difference between the proceeds from the issue and the fair value of the liability component. The liability component is subsequently carried at amortized cost. The equity component is recognized in the convertible bond – equity component until the note is either converted (in which case it is transferred to share premium) or the note is redeemed (in which case it is released directly to retained profits). Further details of the new policy are set out in note 2(g).

(v) Impairment of financial assets (see note 2(n)(i), (ii) and (iii))

Loans and advances

In prior years, provisions were made against specific loans and advances as and when the directors had doubts on the ultimate recoverability of principal or interest in full.

Specific provisions represented the quantification of actual and expected losses from identified accounts and were deducted from loans and advances in the balance sheet.

Other than where provisions on smaller balance homogeneous advances were assessed on a portfolio basis, the amount of specific provision raised was assessed on a case by case basis. Specific provisions were made against the carrying amount of advances that were identified as being in doubt based on regular reviews of outstanding balances to reduce these advances, net of any collateral, to their recoverable amounts.

Where specific provisions were raised on a portfolio basis, the level of provisioning took into account management's assessment of the portfolio's structure, past and expected credit losses, business and economic conditions, and any other relevant factors. The principal portfolios evaluated on this basis were credit cards and certain unsecured personal advances.

General provisions augmented specific provisions and provided cover for loans which were impaired at the balance sheet date but would not be identified as such until some time in the future. The Group maintained a general provision which was determined taking into account the structure and risk characteristics of the Group's loan portfolio and the expected loss of the individual components of the loan portfolio based primarily on the historical loss experience. Historic levels of latent risk were regularly reviewed to determine that the level of general provisioning continues to be appropriate. General provisions were deducted from loans and advances to customers in the balance sheet.

In respect of the year ended 31 December 2005, it is not practicable to estimate the extent to which the profit for the year would have been higher or lower had the previous policy on impairment of financial assets still been applied.

With effect from 1 January 2005, in order to comply with HKAS39, the Group has changed its accounting policies relating to impairment on loans and advances to customers set out in note 2(n).

Other financial assets

For financial assets, other than loans and advances, were reviewed on each balance sheet date to determine whether there was any indication of impairment. If the recoverable amount of the asset was estimated to be less than its carrying amount, the carrying amount of the asset was reduced to its recoverable amount and the impairment loss was recognized in the income statement.

With effect from 1 January 2005, in order to comply with HKAS 39, the Group has changed its accounting policies relating to impairment of investments in debt and equity securities, and impairment of other financial assets set out in note 2(n).

(vi) Interest recognition on impaired loans

In prior years, loans were not reclassified as accruing until interest and principal payments were up-to-date and future payments were reasonably assured. Where the probability of receiving interest payments was remote, interest was no longer accrued. Where the loan had no reasonable prospect of recovery, the loan and related suspended interests were written off.

With effect from 1 January 2005, in order to comply with HKAS 39, the Group has changed its accounting policies relating to interest income recognition set out in note 2(c)(i).

(vii) Description of transitional provisions and effect of adjustments

The changes in accounting policies of the above items were adopted by way of opening balance adjustments to certain reserves and redesignation of financial instruments as at 1 January 2005 as disclosed in the respective notes. Comparative amounts have not been restated as this is prohibited by the transitional arrangements in HKAS 39.

The adjustments for each financial statement line item of the Group and of the Company affected for the year ended 31 December 2005 are set out in note 3(b).

(d) Interest in associates (HKAS 28, Investments in associates)

In prior years, investments held by the Group with 20% or more of the voting power of the investee that were acquired and held exclusively with a view to subsequent disposal in the near future were classified as other investments in securities and stated at fair value.

With effect from 1 January 2005, and in accordance with HKAS 28, such investments are reclassified as investment in associates and accounted for in the consolidated financial statements under the equity method. Further details of the new policy are set out in note 2(e).

The adjustments for each consolidated financial statement line item of the Group for the year ended 31 December 2004 are set out in note 3(a).

(e) Employee share option scheme (HKFRS 2, Share-based payment)

(i) Employee share option scheme

In prior years, no amounts were recognized when employees (which term includes directors) were granted share options over shares in the Company. If the employees chose to exercise the options, the nominal amount of share capital and share premium were credited only to the extent of the option's exercise price receivable.

With effect from 1 January 2005, in order to comply with HKFRS 2, the Group has adopted a new policy for employee share options. Under the new policy, the Group recognizes the fair value of such share options as an expense in the consolidated income statement with a corresponding increase recognized in a capital reserve within equity. Further details of the new policy are set out in note 2(p)(ii).

The new accounting policy has been applied retrospectively with comparatives restated, except that the Group has taken advantage of the transitional provisions set out in HKFRS 2, under which the new recognition and measurement policies have not been applied to the following grants of options:

(a) all options granted to employees on or before 7 November 2002; and

(b) all options granted to employees after 7 November 2002 but which had vested before 1 January 2005.

Details of the employee share option scheme are set out in note 43.

(ii) Employee Equity Linked Deferred Award Scheme ("ELDA")

In prior years, when employees (which term includes directors) were granted awards under ELDA, provision for the ELDA was made and recognized immediately as expenses in the year in which the awards were granted.

With effect from 1 January 2005, in order to comply with HKFRS 2, the fair value of the amount payable is recognized as an expense in the income statement over the relevant vesting period with a corresponding increase in liabilities. The liability is remeasured at each balance sheet date and at settlement date. Any changes in the fair value of the liability are recognized in the income statement. Further details of the new policy are set out in note 2(p)(ii).

Details of ELDA are set out in note 43.

(iii) The adjustments for each financial statement line item of the Group and of the Company affected for the years ended 31 December 2005 and 2004 are set out in notes 3(a) and (b).

(f) Amortization of positive goodwill (HKFRS 3, Business combinations and HKAS 36, Impairment of assets)

In prior years, positive goodwill which arose on or after 1 January 2001 was amortized on a straight line basis over its useful life and was subject to impairment testing when there were indications of impairment.

With effect from 1 January 2005, in order to comply with HKFRS 3 and HKAS 36, the Group has changed its accounting policy relating to goodwill. Under the new policy, the Group no longer amortizes positive goodwill but tests it at least annually for impairment. Also with effect from 1 January 2005 and in accordance with HKFRS 3, if the fair value of the net assets acquired in a business combination exceeds the consideration paid (i.e. an amount arises which would have been known as negative goodwill under the previous accounting policy), the excess is recognized immediately in profit or loss as it arises. Further details of these new policies are set out in note 2(f).

The new policy in respect of the amortization of positive goodwill has been applied prospectively in accordance with the transitional arrangements under HKFRS 3. The adjustments for each consolidated financial statement line affected for the year ended 31 December 2005 are set out in note 3(b).

(g) Investment property (HKAS 40, Investment property)

(i) Timing of recognition of movements in fair value in the income statement

In prior years, movements in the fair value of the Group's investment property were recognized directly in the investment property revaluation reserve except when, on a portfolio basis, the reserve was insufficient to cover a deficit on the portfolio, or when a deficit previously recognized in the income statement had reversed, or when an individual investment property was disposed of. In these limited circumstances, movements in the fair value were recognized in the income statement.

In addition, in prior years property (including leasehold land) which the Group held for an undetermined future purpose was accounted for under the cost model in SSAP 17, Property, plant and equipment, whereby the property was carried at cost less accumulated depreciation and impairment.

Upon adoption of HKAS 40 as from 1 January 2005, the Group has adopted a new policy for investment property. Under this new policy:

– all changes in the fair value of investment property are recognized directly in the income statement in accordance with the fair value model in HKAS 40; and

– land held for an undetermined future purpose is recognized as "investment property" if the property is freehold or, if the property is leasehold, the Group has recognized such land as investment property rather than as land held under an operating lease.

Further details of the new policy for investment property are set out in note 2(j).

(ii) Measurement of deferred tax on movements in fair value

In prior years the Group was required to apply the tax rate that would be applicable to the sale of investment property to determine whether any amounts of deferred tax should be recognised on the revaluation of investment property. Consequently, deferred tax was only provided to the extent that tax allowances already given would be clawed back if the property were disposed of at its carrying value, as there would be no additional tax payable on disposal.

As from 1 January 2005, in accordance with HK(SIC) Interpretation 21, the Group recognises deferred tax on movements in the value of an investment property using tax rates that are applicable to the property's use, if the Group has no intention to sell it and the property would have been depreciable had the Group not adopted the fair value model. Further details of the policy for deferred tax are set out in note 2(q).

(iii) Description of transitional provisions and effect of adjustments

While these changes in accounting policy have to be adopted retrospectively, no adjustment to the opening balances as at 1 January 2004 and 1 January 2005 are required because the net surplus on revaluation of investment properties for the year ended 31 December 2003 and 31 December 2004 was taken to the income statement as this related to a deficit on revaluation in respect of the portfolio of investment properties previously charged to the income statement.

The adjustments for each financial statement line items of the Group and the Company affected for the year ended 31 December 2005 are set out in note 3(b).

(h) Definition of related parties (HKAS 24, Related party disclosures)

As a result of the adoption of HKAS 24, Related party disclosures, the definition of related parties as disclosed in note 2(t) has been expanded to clarify that related parties include entities that are under the significant influence of a related party that is an individual (i.e. key management personnel, significant shareholders and/or their close family members) and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group. The clarification of the definition of related parties has not resulted in any material changes to the previously reported disclosures of related party transactions nor has it had any material effect on the disclosures made in the current period, as compared to those that would have been reported had SSAP 20, Related party disclosures, still been in effect.

(i) Changes in presentation (HKAS 1, Presentation of financial statements and HKAS 30, Disclosures in financial statements of banks and similar financial institutions)

(i) Presentation of income statement and balance sheets

In prior years, there were no specific accounting standards governing the presentation of the financial statement of banks. Management, having regard to the overall clarity and the disclosure requirements of the Hong Kong Monetary Authority, exercised its judgement in deciding on the relative prominence given to each item presented on the face of the income statement and balance sheets. As a result, certificates of deposits held were separately presented on the face of the balance sheets. Treasury bills (including Exchange Fund Bills) and money at call and short notice (representing placements with banks and other financial institutions maturing within one month) were included in cash and short-term funds with treasury bills being presented separately as held-to-maturity investments and other investments in securities according to the previous SSAP 24.

With effect from 1 January 2005, in order to comply with HKAS 30 and take into account the measurement basis that has been applied, the Group has changed its presentation of certain items on the face of the income statement and balance sheets. Treasury bills (including Exchange Fund Bills) and certificates of deposit held are included in the four categories of financial instruments under HKAS 39. Placements with banks and other financial institutions maturing within one month are included in placements with banks and other financial institutions. These changes in presentation have been applied retrospectively with comparatives reclassified.

(ii) Minority interests (HKAS 1, Presentation of financial statements and HKAS 27, Consolidated and separate financial statements)

In prior years, minority interests at the balance sheet date were presented in the consolidated balance sheet separately from liabilities and as deduction from net assets. Minority interests in the results of the Group for the year were also separately presented in the consolidated income statement as a deduction before arriving at the profit attributable to shareholders.

With effect from 1 January 2005, in order to comply with HKAS 1 and HKAS 27, the Group has changed its accounting policy relating to the presentation of minority interests. Under the new policy, minority interests are presented as part of equity, separately from interests attributable to the equity shareholders of the Company. These changes in presentation of minority interests in the consolidated balance sheet and income statement have been applied restrospectively with comparatives restated.

4. Interest Income

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Listed securities	410,103	327,940
Unlisted securities	568,930	566,284
Others	2,028,339	1,347,186
	3,007,372	2,241,410

Other interest income includes the amount of interest income accrued on impaired financial assets of HK$28.4 million (2004: Nil) and interest income on unwinding of discount on impairment loan of HK$25.2 million (2004: Nil) for the year ended 31 December 2005.

5. Fee and Commission Income

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Bills commission	40,152	42,281
Cards related income	35,064	23,722
General banking services	50,518	65,801
Insurance	77,964	61,715
Investment and structural investment products	75,888	90,451
Loans, overdrafts and facility fee	159,256	176,955
Others	820	382
	439,662	461,307

6. Net Trading Income

	The Group 2005 HK$'000	2004 (restated) HK$'000
Gains less losses from dealing in foreign currencies	98,707	54,468
Gains less losses from trading securities	137,827	100,893
Gains less losses from other dealing activities	(51,738)	22,583
Interest income on trading assets		
– Listed	26,807	–
– Unlisted	120,050	–
Interest expense on trading liabilities	(8,592)	–
Dividend income from unlisted trading securities	20,405	–
	343,466	177,944

7. Net Income from Financial Instruments Designated at Fair Value Through Profit or Loss

	The Group 2005 HK$'000	2004 HK$'000
Net gains	93,941	–
Interest income		
– Listed	31,348	–
– Unlisted	3,395	–
Interest expense	(106,203)	–
	22,481	–

8. Net Hedging Expense

	The Group 2005 HK$'000	2004 HK$'000
Fair value hedge	(679)	–

9. Other Operating Income

	The Group 2005 HK$'000	2004 (restated) HK$'000
Dividend income from investment securities and other investments in securities		
– Listed investments	–	488
– Unlisted investments	–	10,289
Dividend income from available-for-sale financial assets		
– Unlisted investments	5,312	–
Gross rental income from investment properties of HK$3,231,000 (2004: HK$11,491,000) less direct outgoings of HK$43,000 (2004: HK$1,598,000)	3,188	9,893
Others	70,801	48,528
	79,301	69,198

10. Operating Expenses

		The Group	
		2005	**2004**
			(restated)
		HK$'000	*HK$'000*
(a)	**Staff costs**		
	Salaries and other staff costs	555,101	548,302
	Retirement costs *(note 42)*	37,914	35,866
	Share-based payment expenses *(note 43)*:		
	– Equity-settled share-based payment expenses	5,796	4,308
	– Cash-settled share-based payment expenses	9,029	4,221
		607,840	592,697
(b)	**Depreciation and amortization**		
	Depreciation of premises and equipment *(note 32)*		
	– Assets held for use under operating leases	2,571	932
	– Other assets	110,266	145,467
	Amortization of goodwill *(note 33)*	–	60,336
		112,837	206,735
(c)	**Other operating expenses**		
	Premises and equipment expenses, excluding depreciation		
	– Rental of premises	54,054	33,369
	– Others	77,467	74,839
	Auditors' remuneration	4,325	3,358
	Advertising	63,659	66,651
	Communication, printing and stationery	57,636	52,694
	Legal and professional fee	22,876	22,247
	Others	93,994	64,895
		374,011	318,053
	Total operating expenses	1,094,688	1,117,485

Included in operating expenses are minimum lease payment under operating leases of HK$931,000 (2004: HK$1,372,000) for hire of equipment and HK$50,248,000 (2004: HK$29,619,000) for hire of other assets (including property rentals).

11. Directors' Remuneration

Directors' remuneration disclosed pursuant to section 161 of the Hong Kong Companies Ordinance is as follows:

	2005					
	Directors' fee	**Salaries, allowances and benefits in kind**	**Discretionary bonuses**	**Share-based payments**	**Retirement scheme contributions**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Mrs. Chan Hui Dor Lam Doreen	300	3,600	2,700	480	360	7,440
Mr. Chang Zhenming (resigned on 17 January 2005 and re-appointed on 27 June 2005)	170	–	–	–	–	170
Mr. Chen Xiaoxian (appointed on 17 January 2005)	290	–	–	–	–	290
Mr. Dou Jianzhong	300	2,520	945	–	252	4,017
Mr. Ju Weimin	300	–	–	–	–	300
Mr. Kong Dan	300	–	200	322	–	822
Mr. Kong Siu Chee Kenneth (resigned on 1 January 2006)	300	3,120	1,000	320	312	5,052
Mr. Lam Kwong Siu	300	–	–	–	–	300
Mr. Liu Jifu	300	–	–	–	–	300
Mr. Lo Wing Yat Kelvin	300	2,845	576	288	231	4,240
Mr. Rafael Gil-Tienda	300	–	–	–	–	300
Mr. Roger Clark Spyer (appointed on 2 December 2005)	30	242	1,200	–	–	1,472
Mr. Tsang Yiu Keung Paul	300	–	–	–	–	300
Mr. Wang Dongming	300	–	–	–	–	300
Mr. Yang Chao	300	–	–	–	–	300
Mr. Zhang Enzhao (resigned on 17 March 2005)	60	–	–	–	–	60
Mr. Zhao Shengbiao Peter	300	1,550	377	32	70	2,329
	4,450	13,877	6,998	1,442	1,225	27,992

	2004					
	Directors' fee	Salaries, allowances and benefits in kind	Discretionary bonuses	Share-based payments	Retirement scheme contributions	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Mrs. Chan Hui Dor Lam Doreen	300	3,540	3,600	293	354	8,087
Mr. Chang Zhenming (resigned on 17 January 2005)	300	2,166	903	234	205	3,808
Mr. Dou Jianzhong	300	–	–	–	–	300
Mr. Fan Sheung Tak Stephen (resigned on 19 October 2004)	240	–	–	–	–	240
Mr. Ju Weimin	300	–	–	–	–	300
Mr. Kong Dan	300	1,043	941	234	99	2,617
Mr. Kong Siu Chee Kenneth	300	3,120	1,800	196	312	5,728
Mr. Lee Wing Hung Raymond (resigned on 20 May 2004)	120	–	–	–	–	120
Mr. Lam Kwong Siu	300	–	–	–	–	300
Mr. Liu Jifu	300	–	–	–	–	300
Mr. Lo Wing Yat Kelvin	300	2,845	1,000	180	231	4,556
Mr. Rafael Gil-Tienda (appointed on 1 December 2004)	300	–	–	–	–	300
Mr. Tsang Yiu Keung Paul (appointed on 1 September 2004)	100	–	–	–	–	100
Mr. Wang Dongming	300	–	–	–	–	300
Mr. Yang Chao	300	–	–	–	–	300
Mr. Zhang Enzhao	300	–	–	–	–	300
Mr. Zhao Shengbiao Peter	300	1,605	302	23	62	2,292
	4,660	14,319	8,546	1,160	1,263	29,948

The above emoluments include the value of share options granted to certain directors under The CITIC International Financial Holdings Limited Share Option Scheme (the "New Option Scheme") and the Senior Executive Share Option Scheme (the "Old Option Scheme") of the Company. The details of these benefits in kind are disclosed under the paragraph "Share Option Schemes" in the directors' report and note 43.

12. Individuals with Highest Emoluments

Of the Group's five individuals with the highest emoluments, four of them (2004: three) are directors of the Company and the information in respect of the directors' emoluments are disclosed above.

The emoluments of the remaining one (2004: two) individuals are as follows:

	2005	2004 (restated)
	HK$'000	*HK$'000*
Salaries and other emoluments	2,298	4,728
Discretionary bonuses	1,100	3,050
Pension contributions	220	228
Share-based payments	288	180
	3,906	8,186

The emoluments of the remaining one (2004: two) individuals with the highest emoluments are within the following bands:

	2005 Number of individuals	**2004 Number of individuals**
HK$2,500,001–HK$3,000,000	–	–
HK$3,000,001–HK$4,000,000	1	1
HK$4,000,001–HK$4,500,000	–	1
	1	2

13. Impairment Losses on Loans and Advances to Customers/Charge for Bad and Doubtful Debts

(a) Impairment losses on loans and advances

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Impairment losses (release)/charge on advances to customers and other accounts *(note 25(b))*		
– Additions	266,960	–
– Releases	(226,391)	–
– Recoveries	(98,113)	–
	(57,544)	–

(b) Charge for bad and doubtful debts

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Charge/(release) for bad and doubtful debts *(note 25(c))*		
– Additions	–	430,152
– Releases	–	(307,715)
– Recoveries	–	(44,372)
	–	78,065

14. Income Tax in Consolidated Income Statement

(a) Income tax in the consolidated income statement

	The Group	
	2005	**2004**
		(restated)
	HK$'000	*HK$'000*
Current tax – Hong Kong Profits Tax		
Provision for the year *(note 38(a))*	129,827	156,377
Over-provision in respect of prior years	(19,180)	(1,253)
	110,647	155,124
Current tax – Overseas		
Provision for the year	1,727	2,145
Deferred tax		
Reversal of temporary differences	(168)	(6,092)
Total	112,206	151,177

The provision for Hong Kong Profits Tax is calculated at 17.5% (2004: 17.5%) of the estimated assessable profits for the year. Taxation for branches and subsidiaries outside Hong Kong is charged at the appropriate current rates of taxation ruling in the relevant countries.

(b) Reconciliation between tax expense and accounting profit at applicable tax rates

	The Group	
	2005	**2004**
		(restated)
	HK$'000	*HK$'000*
Profit before tax	1,215,646	1,054,732
Notional tax on profit before tax, calculated at the rates applicable to profits in the countries concerned	202,413	171,055
Tax effect of non-deductible expenses	24,375	56,294
Tax effect of non-taxable revenue	(102,583)	(51,687)
Tax effect of unused tax losses not recognized	2,799	1,593
Tax effect of previous tax losses utilized in current year	(932)	(11,636)
Tax effect of tax cost/(benefit) from tax planning arrangement	2,711	(13,247)
Tax effect of temporary allowance not recognized	1,922	58
Over-provision in prior years	(19,180)	(1,253)
Others	681	–
Actual tax expense	112,206	151,177

15. Profit Attributable to Equity Shareholders

The consolidated profit attributable to equity shareholders of the Company includes a profit of HK$551,442,000 (2004: HK$450,576,000) which has been dealt with in the financial statements of the Company.

16. Dividends

(a) Dividends payable to equity shareholders of the Company attributable to the year

	2005	**2004**
	HK$'000	*HK$'000*
Interim dividend declared and paid of HK$0.113 (2004: HK$0.066) per share	361,358	210,759
Final dividend proposed after the balance sheet date of HK$0.060 (2004: HK$0.075) per share	191,872	239,636
	553,230	450,395

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

(b) Dividends payable to equity shareholders of the Company attributable to the previous financial year, approved and paid during the year

	2005	**2004**
	HK$'000	*HK$'000*
Final dividend in respect of the previous financial year, approved and paid during the year of HK$0.075 (2004: HK$0.063) per share	239,636	200,960
Final dividend in respect of the previous financial year on shares issued under the Old Option Scheme subsequent to the balance sheet date and before the close of the Register of Members of the Company	203	178
	239,839	201,138

(c) Dividends paid during the year

	2005	**2004**
	HK$'000	*HK$'000*
Interim dividend declared and paid of HK$0.113 (2004: HK$0.066) per share	361,358	210,759
Final dividend in respect of the previous financial year, approved and paid during the year of HK$0.075 (2004: HK$0.063) per share	239,636	200,960
Final dividend in respect of the previous financial year on shares issued under the Old Option Scheme subsequent to the balance sheet date and before the close of the Register of Members of the Company	203	178
	601,197	411,897

17. Earnings per Share

(a) Basic earnings per share

The calculation of basic earnings per share is based on profit attributable to equity shareholders of the Company of HK$1,103,395,000 (2004 (restated): HK$903,925,000) and the weighted average of 3,197,198,285 ordinary shares in issue (2004: 3,192,157,892 shares) during the year, calculated as follows:

Weighted average number of ordinary shares

	2005	**2004**
Issued ordinary shares at 1 January *(note 44(a))*	3,194,153,151	3,189,835,394
Effect of share options exercised	3,045,134	2,322,498
Weighted average number of ordinary shares at 31 December	3,197,198,285	3,192,157,892

(b) Diluted earnings per share

The calculation of diluted earnings per share is based on adjusted profit attributable to ordinary equity shareholders of the Company of HK$1,141,126,000 (2004 (restated): HK$907,420,000) and the weighted average number of ordinary shares of 3,524,437,109 (2004: 3,521,197,208), after adjusting for the effects of all dilutive potential ordinary shares, which assuming the exercise of options under the Company's share option scheme:

Weighted average number of ordinary shares (diluted)

	2005	**2004**
Weighted average number of ordinary shares at 31 December	3,197,198,285	3,192,157,892
Effect of deemed issue of ordinary shares under the Company's share option scheme for nil consideration	337,911	2,138,403
Deemed issue of ordinary shares for Convertible Bonds	326,900,913	326,900,913
Weighted average number of ordinary shares (diluted) at 31 December	3,524,437,109	3,521,197,208

18. 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 as the directors consider that this is more relevant to the Group's internal financial reporting.

(i) Business segments

The Group is principally engaged in the provision of banking and related financial services. The Group comprises the following main business segments:

Commercial banking business:	It mainly comprises banking business, which includes retail banking, corporate banking and treasury activities.
Asset management:	It mainly comprises direct investment and distressed assets management.
Investment banking:	It mainly comprises merchant banking, fund management and securities brokerage and dealing.
Unallocated:	It mainly comprises the premises and any items which cannot be reasonably allocated to specific business segments.

	2005					
	Commercial banking	Asset management	Investment banking	Unallocated	Inter-segment elimination	Consolidated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Net interest income	1,100,952	34,821	–	(36,516)	–	1,099,257
Other operating income	798,698	61,221	–	11,475	–	871,394
Total operating income	1,899,650	96,042	–	(25,041)	–	1,970,651
Operating expenses	(1,049,390)	(24,436)	(9)	(20,853)	–	(1,094,688)
	850,260	71,606	(9)	(45,894)	–	875,963
Impairment losses on loans and advances written back/(charged)	83,379	(25,835)	–	–	–	57,544
Impairment losses on held-to-maturity and available-for-sale securities	(2,567)	(2,818)	–	3,874	–	(1,511)
Impairment losses on properties	(354)	–	–	1,871	–	1,517
Impairment losses written back/(charged)	80,458	(28,653)	–	5,745	–	57,550
Operating profit	930,718	42,953	(9)	(40,149)	–	933,513
Net profit on disposal of fixed assets and associates	226,347	–	–	7,523	–	233,870
Revaluation gain on investment properties	2,140	–	–	–	–	2,140
Share of profit less losses of associates	(10,501)	(3,135)	59,759	–	–	46,123
Profit before taxation	1,148,704	39,818	59,750	(32,626)	–	1,215,646
Income tax	(101,661)	(7,160)	–	(3,385)	–	(112,206)
Profit for the year	1,047,043	32,658	59,750	(36,011)	–	1,103,440
Attributable to:						
Equity shareholders of the Company	1,047,043	32,613	59,750	(36,011)	–	1,103,395
Minority interests	–	45	–	–	–	45
Profit for the year	1,047,043	32,658	59,750	(36,011)	–	1,103,440
Depreciation for the year	116,800	298	–	(4,261)	–	112,837
Segment assets	81,777,136	1,295,604	–	1,035,367	(362,609)	83,745,498
Interest in associates	–	108,284	1,182,896	–	–	1,291,180
Total assets	81,777,136	1,403,888	1,182,896	1,035,367	(362,609)	85,036,678
Segment liabilities	74,660,342	12,869	–	1,396,145	(488,531)	75,580,825
Capital expenditure incurred during the year	53,237	585	–	112	–	53,934

	Commercial banking	Asset management	Investment banking	Unallocated	Inter-segment elimination	Consolidated
	2004 (restated)					
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Net interest income	1,456,353	12,417	–	4,687	–	1,473,457
Other operating income	600,994	58,950	–	21,625	–	681,569
Total operating income	2,057,347	71,367	–	26,312	–	2,155,026
Operating expenses	(1,011,556)	(15,306)	–	(90,623)	–	(1,117,485)
	1,045,791	56,061	–	(64,311)	–	1,037,541
Charge for bad and doubtful debts	(100,540)	22,475	–	–	–	(78,065)
Provision written back on held-to-maturity securities	9,682	–	–	–	–	9,682
Impairment loss on goodwill	(9,502)	–	–	–	–	(9,502)
Impairment losses (charged)/ written back	(100,360)	22,475	–	–	–	(77,885)
Operating profit	945,431	78,536	–	(64,311)	–	959,656
Net profit on disposal of fixed assets	19,755	–	–	(7,893)	–	11,862
Revaluation gain on investment properties	7,555	–	–	–	–	7,555
Share of profit less losses of associates	(4,139)	3,995	75,803	–	–	75,659
Profit before taxation	968,602	82,531	75,803	(72,204)	–	1,054,732
Income tax	(151,538)	(54)	–	415	–	(151,177)
Profit for the year	817,064	82,477	75,803	(71,789)	–	903,555
Attributable to:						
Equity shareholders of the Company	817,064	82,477	75,803	(71,419)	–	903,925
Minority interests	–	–	–	(370)	–	(370)
Profit for the year	817,064	82,477	75,803	(71,789)	–	903,555
Depreciation for the year	149,070	87	–	(2,758)	–	146,399
Amortization of goodwill for the year	1,056	–	6,528	52,752	–	60,336
Segment assets	80,101,502	1,320,542	–	1,038,641	(217,770)	82,242,915
Interest in associates	191,450	22,085	1,120,907	–	–	1,334,442
Total assets	80,292,952	1,342,627	1,120,907	1,038,641	(217,770)	83,577,357
Segment liabilities	74,308,120	14,064	–	1,395,300	(462,130)	75,255,354
Capital expenditure incurred during the year	62,784	719	195,866	500	–	259,869

(ii) Geographical segments

The information concerning geographical analysis has been classified by the location of the principal operations of the subsidiaries or branches of its subsidiaries.

	2005					
	Hong Kong	Mainland China	USA	Others	Inter-segment elimination	Consolidated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Operating income from external customers	1,878,501	36,844	54,853	453	–	1,970,651
Total assets	83,788,186	2,060,081	1,776,016	612,632	(3,200,237)	85,036,678
Capital expenditure incurred during the year	45,931	2,718	460	4,825	–	53,934

	2004 (restated)					
	Hong Kong	Mainland China	USA	Others	Inter-segment elimination	Consolidated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Operating income from external customers	2,103,648	16,684	45,380	–	(10,686)	2,155,026
Total assets	83,004,397	690,143	1,742,424	466,479	(2,326,086)	83,577,357
Capital expenditure incurred during the year	245,075	8,008	6,786	–	–	259,869

19. Cash and Balances with Banks and Other Financial Institutions

	The Group	
	2005	2004 (restated)
	HK$'000	*HK$'000*
Cash in hand	140,567	124,313
Balances with the central bank	3,826	233
Balances with banks and authorized institutions	1,016,916	1,364,373
	1,161,309	1,488,919

20. Placements with Banks and Other Financial Institutions

	The Group	
	2005	2004 (restated)
	HK$'000	*HK$'000*
Maturing		
– within one month	4,543,004	6,458,048
– between one month and one year	722,040	364,307
	5,265,044	6,822,355

21. Trade Bills

	The Group	
	2005	2004
	HK$'000	*HK$'000*
Gross trade bills	406,364	248,567
General provision for bad and doubtful debts *(note 25(c))*	–	(2,486)
	406,364	246,081

22. Trading Assets

	The Group		The Company	
	2005	2004	2005	2004
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Debt securities	2,630,327	–	–	–
Equity securities	58,632	–	–	–
Investment funds	3,555,926	–	93,707	–
Trading securities	6,244,885	–	93,707	–
Positive fair values of derivatives *(note 55(b))*	228,144	–	–	–
	6,473,029	–	93,707	–
Issued by:				
Central governments and central banks	557,841	–	–	–
Public sector entities	16,525	–	–	–
Banks and other financial institutions	315,702	–	–	–
Corporate entities	5,354,817	–	93,707	–
	6,244,885	–	93,707	–
Place of listing:				
Listed in Hong Kong	154,488	–	–	–
Listed outside Hong Kong	1,245,415	–	–	–
	1,399,903	–	–	–
Unlisted	4,844,982	–	93,707	–
	6,244,885	–	93,707	–

Following the adoption of HKAS 39 in 2005, certain financial assets were re-designated as trading assets on 1 January 2005. There was no such re-designation in 2004 as retrospective application of HKAS 39 is not permitted.

The carrying amount of trading assets as at 1 January 2005 was HK$3,795,536,000 and these assets were classified as other investment securities at HK$3,795,536,000 as at 31 December 2004.

23. Securities Designated at Fair Value Through Profit or Loss

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Debt securities issued by corporate entities	1,139,908	–
Place of listing:		
Listed in Hong Kong	656,545	–
Listed outside Hong Kong	460,997	–
	1,117,542	–
Unlisted	22,366	–
Total	1,139,908	–

Following the adoption of HKAS 39 in 2005, certain financial assets were re-designated as financial assets through profit or loss on 1 January 2005. There was no such re-designation in 2004 as retrospective application of HKAS 39 is not permitted.

The carrying amount of securities assets designated at fair value through profit or loss as at 1 January 2005 was $1,069,798,000 and these assets were classified as held-to-maturity investments and other investment in securities at HK$998,550,000 and HK$36,332,000 respectively as at 31 December 2004.

24. Other Investment in Securities

	The Group		The Company	
	2005	**2004** (restated)	**2005**	**2004**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Debt securities				
Listed in Hong Kong	–	1,817	–	–
Listed outside Hong Kong	–	570,004	–	
Unlisted	–	960,643	–	–
	–	1,532,464	–	–
Equity securities				
Listed in Hong Kong	–	84,692	–	–
Unlisted	–	318,137	–	–
	–	402,829	–	–
Certificates of deposits held –unlisted	–	89,949	–	–
Investment funds – unlisted	–	2,018,225	–	86,074
	–	4,043,467	–	86,074
Issued by:				
Central governments and central banks	–	1,234	–	–
Banks and other financial institutions	–	346,821	–	–
Corporate entities	–	3,688,912	–	86,074
Public sector entities	–	6,500	–	–
	–	4,043,467	–	86,074
Market value of listed securities				
Debt securities	–	571,821	–	–
Equity securities	–	84,692	–	–
	–	656,513	–	–

Following the adoption of HKAS 39 in 2005, financial assets with carrying amount of HK$4,043,467,000 at 1 January 2005 were re-designated with HK$3,795,536,000, HK$36,332,000, HK$164,750,000 and HK$46,849,000 as trading assets, securities designated at fair value through profit or loss, available-for-sale securities and other items in the balance sheet respectively.

There was no such re-designation in 2004 as restrospective application of HKAS 39 is not permitted.

25. Advances to Customers and Other Accounts

(a) Advances to customers and other accounts less impairment allowances

	The Group		The Company	
	2005	**2004**	**2005**	**2004**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Gross advances to customers	42,961,697	42,672,715	–	–
Less: Impairment allowances				
– Individually assessed *(note 25(b))*	(274,021)	–	–	–
– Collectively assessed *(note 25(b))*	(294,544)	–	–	–
Provisions for bad and doubtful debts				
– Specific *(note 25(c))*	–	(537,056)	–	–
– General *(note 25(c))*	–	(519,351)	–	–
	42,393,132	41,616,308	–	–
Advances to banks and other financial institutions	327,521	20,000	–	–
Accrued interest and other accounts less impairment allowances	1,387,530	1,686,992	18,403	23,963
	44,108,183	43,323,300	18,403	23,963

(b) Movement in impairment allowances on advances to customers

	2005		
	The Group		
	Individually assessed	**Collectively assessed**	**Total**
	HK$'000	*HK$'000*	*HK$'000*
At 1 January 2005 (restated)	549,325	361,177	910,502
Impairment losses released to income statement *(note 13(a))*	(10,701)	(46,843)	(57,544)
Amounts written off	(300,902)	(22,348)	(323,250)
Recoveries of advances written off in previous years	95,471	2,642	98,113
Unwind of discount on loan impairment losses *(note 4)*	(25,224)	–	(25,224)
Exchange and other adjustments	5,899	(84)	5,815
At 31 December 2005	313,868	294,544	608,412
Deducted from:			
Advances to customers *(note 25(a))*	274,021	294,544	568,565
Other accounts	39,847	–	39,847
	313,868	294,544	608,412

(c) Movement in provision for bad and doubtful debts

	2004 The Group			
	Specific	General	Total	Suspended interest
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2004	762,063	546,474	1,308,537	389,638
Amounts written off	(297,765)	–	(297,765)	(140,617)
New provisions charged to the income statement	427,837	2,315	430,152	–
Provisions released to the income statement	(325,087)	(27,000)	(352,087)	–
Amounts recovered	44,372	–	44,372	–
Interest suspended during the year	–	–	–	154,588
Suspended interest recovered	–	–	–	(20,277)
Exchange differences	61	48	109	357
At 31 December 2004	611,481	521,837	1,133,318	383,689
Deducted from:				
Trade bills *(note 21)*	–	2,486	2,486	–
Advances to customers *(note 25(a))*	537,056	519,351	1,056,407	383,689
Other accounts	74,425	–	74,425	–
	611,481	521,837	1,133,318	383,689

(d) Advances to customers analysed by industry sectors

The following economic sector analysis is based on categories and definitions used by the HKMA.

	The Group 2005	The Group 2004
	HK$'000	*HK$'000*
Loans for use in Hong Kong		
Industrial, commercial and financial		
– Property development	410,595	350,668
– Property investment	5,033,111	4,313,945
– Financial concerns	2,355,699	2,702,487
– Stockbrokers	45,606	39,835
– Wholesale and retail trade	2,015,783	2,000,654
– Manufacturing	2,813,124	3,372,328
– Transport and transport equipment	4,280,529	5,404,016
– Others	3,093,252	3,690,455
Individuals		
– Loans for the purchase of flats under the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	18,409	19,394
– Loans for the purchase of other residential properties	11,416,704	10,512,764
– Credit card advances	586,781	538,041
– Others	1,308,935	1,161,561
Trade finance	2,789,104	2,287,943
Loans for use outside Hong Kong	6,794,065	6,278,624
	42,961,697	42,672,715

(e) Impaired/non-performing loans and advances to customers

	The Group 2005 HK$'000	The Group 2004 HK$'000
Gross impaired loans and advances to customers	1,170,839	–
Impairment allowance-individually assessed	(274,021)	–
Gross non-performing loans and advances to customers	–	1,883,882
Specific provisions of bad and doubtful debts	–	(460,587)
	896,818	1,423,295
As a % of total loans and advances to customers		
– Gross impaired loans and advances	2.73%	–
– Gross non-performing loans and advances	–	4.41%

Impaired loans and advances are mainly individually assessed loans with objective evidence of impairment on an individual basis.

Non-performing loans and advances are loans on which interest is being suspended or on which interest accrual has ceased.

Individually assessed impairment allowance were made to write down the carrying value of the advances to the discounted value of future recoverable amounts, including the realisation of collateral.

(f) Net investment in finance leases and hire purchase contracts

Advances to customers include net investment in equipment leased to customers under finance leases and hire purchase contracts having the characteristics of finance leases. The contracts usually run for an initial period of 5 to 20 years, with an option for acquiring the leased asset at nominal value. The total minimum lease payments receivable under finance leases and hire purchase contracts and their present values are as follows:

	The Group					
	2005			2004		
	Present value of the minimum lease payments HK$'000	Interest income relating to future periods HK$'000	Total minimum lease payments HK$'000	Present value of the minimum lease payments HK$'000	Interest income relating to future periods HK$'000	Total minimum lease payments HK$'000
Within 1 year	559,321	198,336	757,657	592,884	101,987	694,871
After 1 year but within 5 years	778,468	614,687	1,393,155	874,284	277,119	1,151,403
After 5 years	2,590,940	1,402,639	3,993,579	2,415,956	551,367	2,967,323
	3,928,729	2,215,662	6,144,391	3,883,124	930,473	4,813,597
Impairment allowances:						
– Individually assessed	(3,718)			–		
– Collectively assessed	(1,095)			–		
– Provisions for bad and doubtful debts	–			(7,795)		
Net investment in finance leases and hire purchase contracts	3,923,916			3,875,329		

26. Amounts Due from Subsidiaries

	The Company	
	2005	**2004**
	HK$'000	*HK$'000*
Placements with banks and other financial institutions	75,583	54,602
Advances to customers and other accounts	949,881	1,015,876
	1,025,464	1,070,478

27. Available-for-sale Securities

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Debt securities	5,790,022	–
Equity securities	140,455	–
Investment funds	77,551	–
	6,008,028	–
Impairment allowances	(62,068)	–
	5,945,960	–
Issued by:		
Banks and other financial institutions	873,122	–
Corporate entities	5,072,838	–
	5,945,960	–
Place of listing:		
Listed outside Hong Kong	4,731,439	–
Unlisted	1,214,521	–
Total	5,945,960	–

Following the adoption of HKAS 39 in 2005, financial assets with carrying amount of HK$6,285,790,000 at 1 January 2005 were re-designated as available-for-sale financial assets. There was no such re-designation in 2004 as retrospective application of HKAS 39 is not permitted.

These assets were classified as follows as at 31 December 2004.

	2004
	HK$'000
Classified as:	
Held-to-maturity securities	5,309,764
Investment in securities	39,841
Other investment in securities	164,750
Carrying amount as at 31 December 2004	5,514,355

28. Held-to-maturity Investments

	The Group 2005	The Group 2004 (restated)
	HK$'000	*HK$'000*
Treasury bills (including Exchange Fund Bills)	247,669	398,823
Certificates of deposit held	499,913	1,276,366
Debt securities	16,456,684	22,270,484
	17,204,266	23,945,673
Impairment allowance – individually assessed	(9,983)	–
Provision for diminution in value	–	(15,492)
	17,194,283	23,930,181
Issued by:		
Central governments and central banks	821,634	688,993
Public sector entities	1,136,047	788,265
Banks and other financial institutions	13,269,677	14,210,694
Corporate entities	1,966,925	8,242,229
	17,194,283	23,930,181
Place of listing:		
Listed in Hong Kong	1,383,224	717,949
Listed outside Hong Kong	3,478,078	7,563,978
	4,861,302	8,281,927
Unlisted	12,332,981	15,648,254
Total	17,194,283	23,930,181
Market value of listed securities:	4,826,519	9,017,797

Following the adoption of HKAS 39 in 2005, a total of HK$6,308,314,000 held-to-maturity securities at 1 January 2005 with a revalued amount of HK$1,033,466,000 and HK$6,081,200,000 were re-designated as financial assets at fair value through profit or loss and available-for-sale securities respectively. There was no such re-designation in 2004 as retrospective application of HKAS 39 is not permitted.

29. Investment Securities

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Debt securities – unlisted	–	15,782
Equity shares – unlisted	–	24,059
	–	39,841
Issued by:		
Corporate entities	–	28,059
Other entities	–	11,782
	–	39,841

Following the adoption of HKAS 39 in 2005, a total of HK$39,841,000 investment securities at 1 January 2005 with a carrying amount of HK$39,841,000 were re-designated as available-for-sale securities. There was no such re-designation in 2004 as retrospective application of HKAS 39 is not permitted.

30. Investments in Subsidiaries

	The Company	
	2005	**2004**
		(restated)
	HK$'000	*HK$'000*
Unlisted shares, at cost	6,245,247	6,239,934

The following list contains the particulars of principal subsidiaries which materially affect the results or assets of the Group.

Name of company	Place of incorporation/ operation	% of shares held	Principal activities	Issued and paid up capital
Beijing Kananten Investment Consulting Limited***	PRC	100%	Investment holding	US$500,000
California Investment LLC**¨	USA	100%	Property holding	US$5,415,000
Carford International Limited*	Hong Kong	100%	Property holding	HK$2
China International Finance Company Limited (Shenzhen)***	PRC	100%	Financial services	RMB500,000,000
CIFH (CB-I) Limited	Cayman Islands/ Hong Kong	100%	Issue of convertible bonds	US$1
CITIC International Assets Management Limited	Hong Kong	100%	Investment holding and assets management	HK$1,261,488,146
CITIC Ka Wah Bank Limited	Hong Kong	100%	Banking	HK$3,083,341,176
CKWB (Cayman Islands) Limited*	Cayman Islands/ Hong Kong	100%	Issue of subordinated notes	US$1
CKWH-UT2 Limited*	Cayman Islands/ Hong Kong	100%	Issue of subordinated notes	US$1
Dramatic Year Limited	British Virgin Islands/ Hong Kong	100%	Investment holding	US$1
HKCB Finance Limited*	Hong Kong	100%	Consumer financing	HK$300,000,000
HKCB Insurance Agency Limited*	Hong Kong	100%	Insurance agency	HK$2
Ka Wah International Merchant Finance Limited*	Hong Kong	100%	Financial services	HK$32,500,000
KS Investment and Consultancy Limited*	British Virgin Islands/ Hong Kong	100%	Investment and consultancy	US$1,200,000
KWB Investment Limited*	Hong Kong	100%	Investment holding	HK$5,000,000
The Hongkong Chinese Bank (Nominees) Limited*	Hong Kong	100%	Nominees services	HK$5,000
The Ka Wah Bank (Trustee) Limited*	Hong Kong	100%	Trustee services	HK$3,000,000
True Worth Investments Limited	British Virgin Islands/ Hong Kong	100%	Investment holding	US$1
Viewcon Hong Kong Limited*	Hong Kong	100%	Mortgage financing	HK$2

All of the above subsidiaries are held directly by the Company except for those indicated below.

* Subsidiaries held indirectly by the Company.

** 99% of the shares of this subsidiary is held directly by the Company and the remaining 1% is held indirectly through another subsidiary of the Company.

*** Subsidiaries held indirectly by the Company incorporated in the PRC and were "Foreign Investment Enterprises" under the PRC Law.

31. Interest in Associates

	The Group	
	2005	**2004**
		(restated)
	HK$'000	*HK$'000*
Share of net assets	1,101,843	1,145,105
Goodwill *(note 31(b))*	189,337	189,337
	1,291,180	1,334,442

Share of associates' taxation for the year amounted to HK$10,129,000 (2004 (restated): HK$4,606,000) relates to share of losses of associates.

Details of the principal associates are as follows:

Name of company	Form of business structure	Place of incorporation/ operation	Group's effective interest	Held by the subsidiaries	Held by the associates	Principal activities	Nominal value of issued shares
CITIC Capital Markets Holdings Limited	Incorporated	Hong Kong	50%	50%	–	Investment holding	HK$28,000,000
CITIC Capital Securities Limited	Incorporated	Hong Kong	50%	–	100%*	Securities brokerage and margin financing	HK$28,000,000
CITIC Capital Markets Limited	Incorporated	Hong Kong	50%	–	100%*	Investment banking	HK$10,000,000
CITIC Capital Futures Limited	Incorporated	Hong Kong	50%	–	100%*	Brokerage of exchange-traded futures and options contracts	HK$20,000,000
CITIC Frontier China Research Limited	Incorporated	Hong Kong	50%	–	100%*	Stock market research and advising on securities	HK$15,000,000

All associated companies are held indirectly by the Company.

* Interest held by a 50% associated company, CITIC Capital Markets Holdings Limited. Their results had been consolidated into the consolidated financial statements of CITIC Capital Markets Holdings Limited, which shown as below.

(a) *Summary financial information on principal associates:*

	Assets	Liabilities	Equity	Revenues	Profit/(loss)
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
CITIC Capital Markets Holdings Limited					
2005					
100%	3,987,136	1,964,148	2,022,988	554,099	114,002
The Group's effective interest	1,993,568	982,074	1,011,494	277,050	59,759
2004					
100%	3,277,865	1,409,173	1,868,692	603,633	186,573
The Group's effective interest	1,638,933	704,587	934,346	301,817	91,295

(b) *Impairment tests for cash-generating units containing goodwill*

In 2004, positive goodwill not already recognized directly in reserves was amortized on a straight-line basis over 20 years. As explained further in note 2(f), with effective from 1 January 2005 the Group no longer amortizes goodwill. In accordance with the transitional provisions set out in HKFRS 3, the accumulated amortization of goodwill as at 1 January 2005 has been eliminated against the cost of goodwill as at that date.

Goodwill is allocated to the investment banking business as cash-generating units (CGU) of the Group.

The recoverable amount of the CGU is determined based on fair value model. These calculations use cash flow projections based on financial budgets covering a five-year period. The present value of the terminal value is calculated based on the price-to-earnings (P/E) exit multiple of 10.3, which does not exceed the average P/E for the business in which the CGU operates.

Management determined the budgeted gross margin based on past performance and its expectation for market development. The discount rate used is 9.7%, which reflects specific risks relating to the relevant segments.

On 16 January 2006, CITIC Capital Holdings Limited (CCHL) has announced to realign its business with other entities within the CITIC Group, the substantial shareholder of the Company through 2 strategic moves.

Firstly, CCHL intends to form a joint venture company with CITIC Securities Co., Ltd (CITIC Securities), a fellow subsidiary of CIFH. The joint venture company, in which CITIC Securities will own a majority stake with CCHL as the minority shareholder, will take over CCHL's existing equities business. Secondly, CCHL intends to acquire 35% interest in CITIC Trust & Investment Co. Ltd (CITIC Trust), a fellow subsidiary of CIFH. Upon the completion of these strategic moves, CCHL will focus on developing its principal businesses in the areas of asset management and investment in private equity, real estate and marketable alternative investment products, and in corporate advisory, structured products and mezzanine financings.

In view of the restructuring has not yet committed up to the date of this report, the Group has not taken into consideration of the restructuring in goodwill impairment assessments.

32. Fixed Assets

(a) The Group

	The Group			
	Investment properties	**Other premises**	**Furniture, fixtures and equipment**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Cost or valuation:				
At 1 January 2004	197,261	1,408,697	675,944	2,281,902
Additions	–	–	64,003	64,003
Disposals	(139,966)	(142,627)	(39,583)	(322,176)
Exchange adjustments	–	60	23	83
Surplus on revaluation	7,555	–	–	7,555
At 31 December 2004	64,850	1,266,130	700,387	2,031,367
The analysis of cost or valuation of the above assets is as follows:				
Cost	–	1,065,686	700,387	1,766,073
Valuation				
–1985	–	50,704	–	50,704
–1988	–	149,740	–	149,740
–2004	64,850	–	–	64,850
	64,850	1,266,130	700,387	2,031,367
At 1 January 2005	64,850	1,266,130	700,387	2,031,367
Additions	–	–	53,934	53,934
Reclassification from other premises	35,904	–	–	35,904
Reclassification to investment properties	–	(43,723)	–	(43,723)
Surplus on revaluation before reclassification	–	8,174	–	8,174
Reclassification	–	(8,174)	–	(8,174)
Disposals	(37,900)	(185,289)	(137,784)	(360,973)
Exchange adjustments	–	(101)	(6)	(107)
Surplus on revaluation	2,140	–	–	2,140
At 31 December 2005	64,994	1,037,017	616,531	1,718,542
The analysis of cost or valuation of the above assets is as follows:				
Cost	–	993,152	616,531	1,609,683
Valuation				
–1985	–	43,865	–	43,865
–2005	64,994	–	–	64,994
	64,994	1,037,017	616,531	1,718,542

	The Group			
	Investment properties	**Other premises**	**Furniture, fixtures and equipment**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Accumulated depreciation:				
At 1 January 2004	–	366,980	361,877	728,857
Charge for the year *(note 10(b))*	–	27,235	119,164	146,399
Written back on disposals	–	(58,725)	(32,644)	(91,369)
Exchange adjustments	–	6	14	20
At 31 December 2004	–	335,496	448,411	783,907
At 1 January 2005	–	335,496	448,411	783,907
Charge for the year *(note 10(b))*	–	22,433	90,404	112,837
Written back on disposals	–	(47,317)	(114,813)	(162,130)
Write back of impairment loss on disposals	–	(1,517)	–	(1,517)
Reclassification to investment properties	–	(15,422)	–	(15,422)
Write back of impairment loss on reclassification	–	(571)	–	(571)
Exchange adjustments	–	(14)	(16)	(30)
At 31 December 2005	–	293,088	423,986	717,074
Net book value:				
At 31 December 2005	64,994	743,929	192,545	1,001,468
At 31 December 2004	64,850	930,634	251,976	1,247,460

(b) *The Company*

	The Company			
	Investment properties	Other premises	Furniture, fixtures and equipment	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Cost or valuation:				
At 1 January 2004	99,916	158,426	11,338	269,680
Additions	–	–	229	229
Disposals	(99,916)	(95,667)	(8,956)	(204,539)
At 31 December 2004	–	62,759	2,611	65,370
The analysis of cost or valuation of the above assets is as follows:				
Cost	–	55,389	2,710	58,099
Valuation –1985	–	7,370	–	7,370
	–	62,759	2,710	65,469
At 1 January 2005	–	62,759	2,611	65,370
Additions	–	–	99	99
At 31 December 2005	–	62,759	2,710	65,469
The analysis of cost or valuation of the above assets is as follows:				
Cost	–	55,389	2,710	58,099
Valuation – 1985	–	7,370	–	7,370
	–	62,759	2,710	65,469
Accumulated depreciation:				
At 1 January 2004	–	50,029	6,916	56,945
Charge for the year	–	2,837	856	3,693
Written back on disposals	–	(46,130)	(6,961)	(53,091)
At 31 December 2004	–	6,736	811	7,547
At 1 January 2005	–	6,736	811	7,547
Charge for the year	–	1,870	487	2,357
At 31 December 2005	–	8,606	1,298	9,904
Net book value:				
At 31 December 2005	–	54,153	1,412	55,565
At 31 December 2004	–	56,023	1,800	57,823

(c) All investment properties of the Group and the Company were revalued at 31 December 2005 by independent firms of surveyors, Vigers Appraisal & Consulting Limited on an open market value basis calculated by reference to net rental income allowing for reversionary income potential. The revaluation surplus amounted to HK$2,140,000 which has been credited to the income statement. Vigers Appraisal & Consulting Limited have among their staff Fellows of the Hong Kong Institute of Surveyors with recent experience in the location and category of property being valued.

The gross rental income arising from investment properties is HK$3,231,000 (2004: HK$11,491,000).

During the year, profit on disposal of investment properties amounted to HK$4,641,000 (2004: HK$8,420,000).

(d) The analysis of net book value of investment properties and other premises are as follows:

	The Group		The Company	
	2005	**2004**	**2005**	**2004**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Freehold				
Held outside Hong Kong	37,371	38,422	2,429	2,670
Leasehold				
Held in Hong Kong				
– Long-term leases				
(over 50 years)	96,711	300,399	–	–
–Medium-term leases				
(10-50 years)	658,180	640,853	51,724	53,353
Held outside Hong Kong				
–Medium-term leases				
(10-50 years)	16,661	15,810	–	–
	808,923	995,484	54,153	56,023

Some of the other premises of the Group and the Company have been revalued in previous year. The net book value of these other premises of the Group and the Company at 31 December 2005 would have been HK$13,674,000 (2004: HK$107,359,000) and HK$2,256,000 (2004: HK$2,481,000) respectively had they been carried at cost less accumulated depreciation.

(e) The Group leases out investment properties under operating leases. The leases typically run for an initial period of two to three years, with an option to renew the leases after that date at which time all terms are renegotiated. None of the leases includes contingent rentals (2004: Nil).

The gross carrying amounts of investment properties of the Group held for use in operating leases were HK$64,994,000 (2004: HK$64,850,000).

The Group's and the Company's total future minimum lease payments under non-cancellable operating leases are receivable as follows:

	The Group		The Company	
	2005	**2004**	**2005**	**2004**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Within 1 year	2,986	2,211	–	–
After 1 year but within 5 years	3,105	3,528	–	–
	6,091	5,739	–	–

33. Goodwill

	The Group
	HK$'000
Cost:	
At 1 January 2004	1,197,158
Written off	(10,558)
At 31 December 2004	1,186,600
At 1 January 2005	1,186,600
Opening balance adjustment to eliminate accumulated amortization	(178,851)
At 31 December 2005	1,007,749
Accumulated amortization and impairment losses:	
At 1 January 2004	119,571
Amortization for the year *(note 10(b))*	60,336
Impairment loss	9,502
Written off	(10,558)
At 31 December 2004	178,851
At 1 January 2005	178,851
Eliminated against cost at 1 January 2005	(178,851)
At 31 December 2005	–
Carrying amount:	
At 31 December 2005	1,007,749
At 31 December 2004	1,007,749

In 2004, positive goodwill not already recognised directly in reserves was amortised on a straight-line basis over 20 years. The amortization of positive goodwill for the year ended 31 December 2004 was included in "other operating expenses (note 10(b))" in the consolidated income statement.

As explained further in note 2(f), with effect from 1 January 2005 the Group no longer amortises goodwill. In accordance with the transitional provisions set out in HKFRS 3, the accumulated amortization of goodwill as at 1 January 2005 has been eliminated against the cost of goodwill as at that date.

Impairment tests for cash-generating units containing goodwill

Goodwill is allocated to the Group's cash-generating units (CGU) identified according to business segment as follows:

	2005
	HK$'000
Commercial banking business	1,007,749

The recoverable amount of the CGU is determined based on value-in-use calculations. These calculations use cash flow projections based on financial budgets approved by management covering a maximum of five-year period. Cash flow in subsequent years are estimated at zero growth rate which does not exceed the long-term average growth rate for the business in which the CGU operates.

Management determined the budgeted gross margin based on past performance and its expectation for market development. The discount rate used is 8.8% which reflects specific risks relating to the relevant segments.

34. Deposits and Balances of Banks and Other Financial Institutions

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Deposits and balances from banks	326,198	85,678
Deposits and balances from other financial institutions	3,831,248	3,470,174
	4,157,446	3,555,852

35. Deposits from Customers

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Demand deposits and current deposits	4,201,868	10,204,982
Savings deposits	8,058,380	11,818,370
Time, call and notice deposits	42,155,031	33,428,375
	54,415,279	55,451,727

36. Trading Liabilities

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Short positions in securities	217,904	–
Negative fair value of derivatives *(Note 55(b))*	443,233	–
	661,137	–

37. Certificates of Deposit Issued

	The Group 2005 HK$'000	2004 HK$'000
Designated at fair value through profit or loss	2,785,924	–
Trading	–	1,379,306
Non-trading	4,682,037	5,580,384
	7,467,961	6,959,690

At 1 January 2005, the Group designated on initial recognition HK$1,561,857,000 of financial liabilities as at fair value through profit or loss upon the adoption of HKAS 39, and these financial liabilities were classified as trading liabilities and non-trading liabilities at HK$1,379,306,000 and HK$177,744,000 respectively as at 31 December 2004.

At 31 December 2005, the difference between the carrying amount and the contractual amount payable at maturity for the Group amounted to HK$150,081,299. Such a decrease in fair value is only attributable to changes in benchmark interest rate.

38. Income Tax in the Balance Sheet

(a) Current taxation in the balance sheet represents

	The Group 2005 HK$'000	2004 HK$'000
Provision for Hong Kong Profits Tax for the year *(note 14(a))*	129,827	156,377
Provisional Profit Tax paid	(127,548)	(151,160)
	2,279	5,217
Balance of Profits Tax provision relating to prior years	46,335	58
	48,614	5,275
Provision for overseas taxation	1,864	1,171
	50,478	6,446

(b) Deferred tax assets and liabilities recognized

The components of deferred tax (assets)/liabilities recognized in the consolidated balance sheet and the movements during the year are as follows:

The Group

	Depreciation allowances in excess of related depreciation	Impairment allowances for loans	Provisions for loans	Fair value adjustments for properties and other assets	Fair value adjustments for available for- sale securities	Cash flow hedge	Others	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Deferred tax arising from:								
At 1 January 2004	51,047	–	(89,558)	(46,689)	–	–	(2,262)	(87,462)
Charged/(credited) to consolidated income statement	(9,749)	–	4,725	(1,068)	–	–	–	(6,092)
At 31 December 2004	41,298	–	(84,833)	(47,757)	–	–	(2,262)	(93,554)
At 1 January 2005								
– as previously reported	41,298	–	(84,833)	(47,757)	–	–	(2,262)	(93,554)
– opening balance adjustment in respect of financial instruments	–	(57,023)	84,833	–	78,191	(1,639)	–	104,362
As restated	41,298	(57,023)	–	(47,757)	78,191	(1,639)	(2,262)	10,808
Charged/(credited) to consolidated income statement	(14,689)	10,401	–	2,526	–	–	1,594	(168)
Charged/(credited) to reserves	–	–	–	1,389	(10,403)	1,639	–	(7,375)
At 31 December 2005	26,609	(46,622)	–	(43,842)	67,788	–	(668)	3,265

	The Group 2005	The Group 2004
	HK$'000	*HK$'000*
Net deferred tax asset recognized on the balance sheet	(42,201)	(93,562)
Net deferred tax liability recognized on the balance sheet	45,466	8
	3,265	(93,554)

(c) *Deferred tax assets not recognized*

The Group and the Company have not recognized deferred tax assets in respect of cumulative tax losses of HK$109,349,000 (2004: HK$106,225,000) and HK$50,581,000 (2004: HK$26,260,000) respectively, as it is not probable that future taxable profits against which the losses can be utilised will be available in the relevant tax jurisdiction and entity. Under the current tax legislation, the expiry dates of the tax losses were as follows:

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Expiring within 5 years	50,026	65,739
No expiry date	59,323	40,486
	109,349	106,225

39. Amounts Due to Subsidiaries

	The Company	
	2005	**2004**
	HK$'000	*HK$'000*
Other liabilities	223	224
Placement from a subsidiary	1,395,922	1,399,384
	1,396,145	1,399,608

40. Debt Securities Issued

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Debt securities issued	2,245,435	2,322,798

The debt securities represent 4.25% per annum notes with face value of US$300 million issued at discount on 17 November 2004. The notes were issued by CKWB and constitute direct, unconditional and unsecured obligations of CKWB. The notes will mature on 17 November 2009.

41. Convertible Bonds Issued

CIFH (CB-I) Limited, a single purpose wholly-owned subsidiary of the Company, issued 0.25% per annum Guaranteed Convertible Bonds ("Bonds") with face value of US$180 million on 8 December 2003. The Company unconditionally and irrevocably guarantees all amounts payable under the Bonds.

Each Bond, at the option of the holder, is convertible on or after 18 January 2004 upto and including 8 November 2008 into fully paid ordinary shares with a par value of HK$1.00 of the Company at an initial conversion price of HK$4.269 per share. The Bonds can be redeemed at their principal amount together with accrued interest on 8 December 2008. The net proceeds from the issue of the Bonds have been used for general corporate purposes of the Group.

The fair values of the liability component and the equity conversion component were determined at the date of waiver of the cash settlement option on 23 December 2004.

The fair values of the liability component, included in long-term borrowings, was calculated using a market interest rate for an equivalent non-convertible bond. The residual amount, representing the value of the equity conversion component, is included in shareholders' equity in Convertible Bond - equity component reserve (note 45).

The convertible bonds recognized in the balance sheet is calculated as follows:

	2005
	HK$'000
Face value of convertible bonds	1,399,384
Equity component	(133,027)
Retained earnings	(7,658)
Liability component on initial recognition at 1 January 2005	1,258,699
Interest expense	37,731
Interest paid	(3,499)
Exchange difference	(3,114)
Liability component at 31 December 2005	1,289,817

	2004
	HK$'000
Convertible bonds	1,399,384

The carrying amount of the liability component of the convertible bonds reflects its current fair value. Interest expense on the bonds is calculated using the effective interest method by applying the effective interest rate of 2.98% to the liability component and for the year end 31 December 2005 amounted to HK$37,731,000. The actual interest paid in 2005 was HK$3,499,000.

The Bonds are embedded with an early redemption option by the Group and an early redemption option by the bondholders. The values of the embedded call and put feature are interdependent and have not been accounted for separately from the host debt.

42. Staff Retirement Scheme

The Group has a defined contribution provident fund scheme (the "Retirement Scheme") under which it contributes 10% of the employees' basic salaries. The Retirement Scheme is an MPF exempted scheme and covers all permanent full-time employees of the Group. No employee contributions are required. Contributions forfeited by leavers prior to vesting fully may not be used by the Group to reduce the existing level of contribution but are transferred to a separate welfare fund which shall be applied for the welfare of the Retirement Scheme's members.

Besides the Retirement Scheme, the Group also participated in an approved MPF scheme effective on 1 December 2000 to provide scheme choice to both existing and new employees. Mandatory benefits are being provided under the MPF Scheme.

During the year, the Group contributed approximately HK$38 million (2004: HK$36 million) (note 10(a)) to these schemes.

43. Share-based Payments

Equity settled share-based transactions

On 16 May 2003, the Company adopted The CITIC International Financial Holdings Limited Share Option Scheme (the "New Option Scheme") and, at the same time, terminated the Senior Executive Share Option Scheme (the "Old Option Scheme") which was adopted by the Company on 30 March 1995. The provisions of the Old Option Scheme remained in full force and effect to the extent necessary to give effect to the exercise of all options granted prior to the termination of the Old Option Scheme on 29 March 2005.

There were no option granted under the Old Option Scheme during the year. As for the options granted under the New Option Scheme, there is a vesting period of two years starting from the date of grant and these options will then remain exercisable until the tenth anniversary day from the date of grant. Each option gives the holder the right to subscribe for one ordinary share in the Company.

(a) The terms and conditions of the options, which will be settled by physical delivery of shares, granted under the New Option Scheme are as follows:

Date of grant/number of employees entitled	Number of options	Vesting conditions	Contractual life of options
Options granted to 273 eligible persons on 17 November 2003	6,758,000	2 years from the date of grant	10 years from the date of grant
Options granted to 293 eligible persons on 6 April 2004	7,412,000	2 years from the date of grant	10 years from the date of grant
Options granted to 275 eligible persons on 13 June 2005	6,800,000	2 years from the date of grant	10 years from the date of grant

(b) The number and weighted average exercise prices of share options are as follows:

	Share options granted in 2005		Share options granted in 2004		Share options granted in 2003	
	Weighted average exercise price *HK$*	Number of options	Weighted average exercise price *HK$*	Number of options	Weighted average exercise price *HK$*	Number of options
Outstanding at the beginning of the year	–	–	3.775	6,544,000	3.540	5,718,000
Forfeited during the year	–	(316,000)	–	(1,220,000)	–	(1,102,000)
Exercised during the year	–	–	–	–	–	–
Granted during the year	2.925	6,800,000	–	–	–	–
Outstanding at the end of the year	2.925	6,484,000	3.775	5,324,000	3.540	4,616,000
Exercisable at the end of the year		216,000		216,000		4,616,000

The options outstanding at 31 December 2005 have the exercise prices fall within the range of HK$2.925 to HK$3.775 and a weighted average contractual life of 10 years.

(c) Fair value of share options and assumptions

The fair value of services received in return for share options granted are measured by reference to the fair value of the share options granted. The estimate of the fair value of the share options granted is measured based on a trinomial model. The 10 years contractual life of the option is used as an input into this model.

	For options granted on 13 June 2005	**For options granted on 6 April 2004**	**For options granted on 17 November 2003**
Fair value at measurement date	HK$0.653	HK$1.248	HK$0.835
Share price	HK$2.925	HK$3.775	HK$3.475
Exercise price	HK$2.925	HK$3.775	HK$3.540
Expected volatility (expressed as volatility used in the trinomial model)	24.30%	34.00%	24.00%
Option life	10 Years	10 Years	10 Years
Expected dividends (continuous Yield)	3.84%	3.71%	3.71%
Risk-free interest rate (based on HKD government bond Yield)	3.22%	4.07%	4.34%

The expected volatility is based on the implied volatilities of our own issued convertible bond on the specified dates.

Share options are granted under a service condition and, for grants to personnel, a non-market performance condition.

Cash settled share-based transactions

CITIC Ka Wah Bank Limited ("CKWB"), a wholly-owned subsidiary of the Company, has offered Equity Linked Deferred Award (the "ELDA") to the eligible employees of CKWB and certain directors of the Company (the "Eligible Persons") whereby the Eligible Persons will receive cash benefit on the specified maturity date, being the earlier of the second calendar anniversary of the offer date and the date of retirement. The amount of cash benefit to be received by the Eligible Persons on the maturity date shall be calculated by multiplying the number of ordinary shares of the Company notionally subject to ELDA by the lower of:

1. the result obtained by subtracting the ELDA price per share from the closing price of the ordinary share of the Company as stated in the daily quotations sheet of the Stock Exchange on the maturity date; and

2. HK$3.00.

The Eligible Persons are not entitled to receive any payment pursuant to the ELDA if the closing price of the ordinary share of the Company as stated in the daily quotations sheet of the Stock Exchange on the maturity date falls below the ELDA price. No ordinary shares of the Company will be allotted or transferred to the Eligible Persons upon the maturity of the ELDA.

The detailed terms of the ELDA offered to the Eligible Persons are as follows:

Offer date	ELDA price per share *(HK$)*	Number of ordinary shares notionally subject to ELDA as at 31 December 2005
16 April 2004	2.55	3,925,398
24 March 2005	2.00	6,051,530
Total:		9,976,928

The fair value of the ELDA is limited to HK$3.00, which is the maximum cash benefit to be received by the Eligible Persons on the maturity date.

Employee expenses

	2005 *HK$'000*	2004 *HK$'000*
(a) Equity settled share-based transactions		
Share options granted in 2003	1,748	2,018
Share options granted in 2004	3,194	2,290
Share options granted in 2005	854	–
Total expense recognized as employee costs *(note 10(a))*	5,796	4,308

	2005 *HK$'000*	2004 *HK$'000*
(b) Cash settled share-based transactions		
ELDA granted in 2004	4,236	4,221
ELDA granted in 2005	4,793	–
Total carrying amount of cash-settled transaction liabilities *(note 10(a))*	9,029	4,221

44. Share Capital

(a) Authorised and issued share capital

	2005 *HK$'000*	2004 *HK$'000*
Authorised:		
6,000,000,000 ordinary shares of HK$1 each	6,000,000	6,000,000
Issued and fully paid:		
At 1 January: 3,194,153,151 (2004: 3,189,835,394) ordinary shares of HK$1 each	3,194,153	3,189,835
Share issued under the Old Option Scheme	3,706	4,318
At 31 December: 3,197,859,375 (2004: 3,194,153,151) ordinary shares of HK$1 each	3,197,859	3,194,153

(b) *Terms of unexpired and unexercised share options at balance sheet date*

Date of grant	Exercise price (HK$)	Number of option granted	Vesting period	Exercisable period	Number of shares acquired on exercise of options for the year ended 31 December 2005	Number of options lapsed for the year ended 31 December 2005	Number of options outstanding as at 31 December 2005	Number of options outstanding as at 31 December 2004
The Old Option Scheme								
17/08/1999	2.217	19,600,000	–	31/10/1999 – 29/03/2005	2,900,000	–	–	2,900,000
28/03/2000	1.758	1,700,000	–	31/03/2000 – 29/03/2005	500,000	–	–	500,000
10/08/2000	2.198	700,000	–	11/08/2001 – 29/03/2005	–	100,000	–	100,000
28/02/2002	1.620	44,813	–	28/02/2002 – 29/03/2005	–	203	–	203
28/02/2002	2.217	481,743	–	28/02/2002 – 29/03/2005	268,880	–	–	268,880
28/02/2002	1.758	74,688	–	28/02/2002 – 29/03/2005	37,344	–	–	37,344
28/02/2002	2.198	26,141	–	28/02/2002 – 29/03/2005	–	4,203	–	4,203
The New Option Scheme								
17/11/2003	3.540	6,758,000	17/11/2003 – 16/11/2005	17/11/2005 – 16/11/2013	–	1,102,000	4,616,000	5,718,000
06/04/2004	3.775	7,412,000	06/04/2004 – 05/04/2006	06/04/2006 – 05/04/2014	–	1,220,000	5,324,000	6,544,000
13/06/2005	2.925	6,800,000	13/06/2005 – 12/06/2007	13/06/2007 – 12/06/2015	–	316,000	6,484,000	–
		43,597,385			3,706,224	2,742,406	16,424,000	16,072,630

Each option entitles the holder to subscribe for one ordinary share in the Company. Further details of these options are set out in note 43 to the financial statements.

45. Reserves

(i) The Group

	Attributable to equity shareholders of the Company										
	Share premium	Capital reserve	General reserve	Exchange differences reserve	Other property revaluation reserve	Fair value reserve	Hedging reserve	Convertible bond-equity component	Share option reserve	Retained profits	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2004											
– as previously reported	1,831,406	2,818	100,000	(597)	11,945	–	–	–	–	2,676,363	4,621,935
– prior period adjustments in respect of											
– HKAS 28	–	–	–	–	–	–	–	–	–	4,754	4,754
As restated	1,831,406	2,818	100,000	(597)	11,945	–	–	–	–	2,681,117	4,626,689
Share premium on shares issued during the year	4,542	–	–	–	–	–	–	–	–	–	4,542
Exchange difference on translation	–	–	–	283	–	–	–	–	–	–	283
Equity settled share-based transactions (restated)	–	–	–	–	–	–	–	–	4,308	–	4,308
Dividends paid in respect of the previous year *(note 16(b))*	–	–	–	–	–	–	–	–	–	(201,138)	(201,138)
Profit for the year (restated)	–	–	–	–	–	–	–	–	–	903,925	903,925
Dividends declared and paid in respect of the current year	–	–	–	–	–	–	–	–	–	(210,759)	(210,759)
At 31 December 2004 (restated)	1,835,948	2,818	100,000	(314)	11,945	–	–	–	4,308	3,173,145	5,127,850

	Attributable to equity shareholders of the Company										
	Share premium	Capital reserve	General reserve	Exchange differences reserve	Other property revaluation reserve	Fair value reserve	Hedging reserve	Convertible bond-equity component	Share option reserve	Retained profits	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2005											
– as previously reported	1,835,948	2,818	100,000	(314)	11,945	–	–	–	–	3,165,805	5,116,202
– prior period adjustments in respect of											
– HKAS 28	–	–	–	–	–	–	–	–	–	4,754	4,754
– HKFRS 2	–	–	–	–	–	–	–	–	4,308	2,586	6,894
As restated, before opening balance adjustments	1,835,948	2,818	100,000	(314)	11,945	–	–	–	4,308	3,173,145	5,127,850
– HKAS 32 & 39	–	–	–	–	–	368,612	(7,725)	133,027	–	144,902	638,816
As restated, after opening balance adjustments	1,835,948	2,818	100,000	(314)	11,945	368,612	(7,725)	133,027	4,308	3,318,047	5,766,666
Share premium on shares issued during the year	4,264	–	–	–	–	–	–	–	–	–	4,264
Revaluation surplus, net of deferred tax	–	–	–	–	6,785	–	–	–	–	–	6,785
Share of share option reserve of associates	–	–	–	–	–	–	–	–	6,500	–	6,500
Share of fair value reserve of associates	–	–	–	–	–	2,894	–	–	–	–	2,894
Transfer to retained profits upon disposal	–	–	–	–	(12,180)	–	–	–	–	12,180	–
Exchange difference on translation	–	–	–	3,371	–	–	–	–	–	–	3,371
Release on disposal of an associate	–	–	–	627	–	–	–	–	–	–	627
Equity settled share-based transactions	–	–	–	–	–	–	–	–	5,796	–	5,796
Available-for-sale securities											
– change in fair value	–	–	–	–	–	(59,442)	–	–	–	–	(59,442)
– deferred tax	–	–	–	–	–	10,403	–	–	–	–	10,403
Cash flow hedge											
– effective portion of changes in fair value	–	–	–	–	–	–	9,364	–	–	–	9,364
– deferred tax	–	–	–	–	–	–	(1,639)	–	–	–	(1,639)
Exchange difference on translation of borrowings	–	–	–	–	–	–	–	(329)	–	–	(329)
Dividends paid in respect of the previous year *(note 16(b))*	–	–	–	–	–	–	–	–	–	(239,839)	(239,839)
Profit for the year	–	–	–	–	–	–	–	–	–	1,103,395	1,103,395
Dividends declared and paid in respect of the current year	–	–	–	–	–	–	–	–	–	(361,358)	(361,358)
At 31 December 2005	1,840,212	2,818	100,000	3,684	6,550	322,467	–	132,698	16,604	3,832,425	6,257,458

(ii) *The Company*

	Attributable to equity shareholders of the Company			
	Share premium	Share option reserve	Retained profits	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2004	1,831,406	–	999,395	2,830,801
Share premium on shares issued during the year	4,542	–	–	4,542
Equity settled share-based transactions (restated)	–	4,308	–	4,308
Dividends paid in respect of the previous year *(note 16(b))*	–	–	(201,138)	(201,138)
Profit for the year (restated)	–	–	449,980	449,980
Dividends declared and paid in respect of the current year	–	–	(210,759)	(210,759)
At 31 December 2004 (restated)	1,835,948	4,308	1,037,478	2,877,734
At 1 January 2005				
– as previously reported	1,835,948	–	1,038,074	2,874,022
– prior period adjustments in respect of – HKFRS 2	–	4,308	(596)	3,712
As restated	1,835,948	4,308	1,037,478	2,877,734
Share premium on shares issued during the year	4,264	–	–	4,264
Equity settled share-based transactions	–	5,796	–	5,796
Dividends paid in respect of the previous year *(note 16(b))*	–	–	(239,839)	(239,839)
Profit for the year	–	–	551,442	551,442
Dividends declared and paid in respect of the current year	–	–	(361,358)	(361,358)
At 31 December 2005	1,840,212	10,104	987,723	2,838,039

(iii) *Nature and purpose of reserves*

(a) Share premium

The application of the share premium account is governed by section 48B of the Hong Kong Companies Ordinance.

(b) Exchange differences reserve

The exchange differences reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations. The reserve is dealt with in accordance with the accounting policies set out in notes 2(r).

(c) Other property revaluation reserve

The other property revaluation reserve is not available for distribution to shareholders because it does not constitute realised profits within the meaning of section 79B(2) of the Hong Kong Companies Ordinance.

(d) Fair value reserve

The fair value reserve comprises the cumulative net change in the fair value of available-for-sale securities held at the balance sheet date and is dealt with in accordance with the accounting policies in note 2(g).

(e) Hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of hedging instruments used in cash flow hedges pending subsequent recognition of the hedged cash flow in accordance with the accounting policies adopted for cash flow hedges in note 2(i).

(f) Convertible bond-equity component

The convertible bond-equity component comprises the fair value of the equity conversion component of the convertible bond issued that were determined at the date of waiver of the cash settlement option on 23 December 2004.

(g) Share option reserve

The share option reserve comprises the fair value of the actual or estimated number of unexercised share options granted to employees of the Group recognised in accordance with the accounting policy adopted for share based payment in note 43.

Included in the share option reserve is an amount of HK$6,500,000 (2004: Nil) being the share option reserve attributable to one of the associate, CITIC Capital Markets Holdings Limited, under its own "Share Option Scheme".

(h) Retained profits

In accordance with the Hong Kong Monetary Authority (the "HKMA") guideline "Impact of the New Hong Kong Accounting Standards on Authorised Institutions' Capital Base and Regulatory Reporting", the Group has earmarked a "Regulatory Reserve" of HK$233,800,000 (2004: Nil) from retained profits as at 31 December 2005.

Included in the retained profits is an amount of HK$445,954,000 (2004 (restated): HK$465,243,000) being the retained profits attributable to associates.

(iv) Distributability of reserve

At 31 December 2005, the aggregate amount of reserves available for distribution to equity shareholders of the Company was HK$987,723,000 (2004 (restated): HK$1,037,478,000). After the balance sheet date the directors proposed a final dividend of HK$0.060 per ordinary share (2004: HK$0.075). This dividend has not been recognised as a liability at the balance sheet date.

46. Minority Interests

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
At 1 January 2005	–	191
Associates acquired during the year	78	–
Others	413	–
Profit for the year	45	(370)
Disposal of subsidiaries during the year	–	179
As 31 December 2005	536	–

47. Loan Capital

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Subordinated notes	4,352,351	4,275,896

The notes represents 7.625% per annum subordinated notes with face value of US$300 million issued on 5 July 2001 and 9.125% per annum perpetual subordinated notes with face value of US$250 million issued on 23 May 2002. The notes were issued by CKWB (Cayman Islands) Ltd and CKWH-UT2 Ltd respectively, two separate single purpose wholly-owned subsidiaries of the Group and qualify as tier 2 capital. The Group unconditionally and irrevocably guarantees all amounts payable under the notes. The 7.625% per annum subordinated notes will mature on 5 July 2011 whereas the 9.125% per annum perpetual subordinated notes will be callable by the CKWH-UT2 Ltd in 2012.

48. Cash and Cash Equivalents

		The Group	
		2005	**2004**
		HK$'000	*HK$'000*
(i)	Components of cash and cash equivalents in the consolidated cash flow statement		
	Cash and balances with banks and other financial institutions	1,161,309	1,488,919
	Placements with banks and other financial institutions with original maturity within three months	4,702,768	6,565,590
	Held-to-maturity investments		
	– Treasury bills with original maturity within three months	148,201	–
		6,012,278	8,054,509
(ii)	Reconciliation with the consolidated balance sheet		
	Cash and balances with banks and other financial institutions	1,161,309	1,488,919
	Placements with banks and other financial institutions	5,265,044	6,822,355
	Held-to-maturity investments		
	– Treasury bills	247,669	398,823
	Amount shown in the consolidated balance sheet	6,674,022	8,710,097
	Less: Amounts with an original maturity of over three months	(661,744)	(655,588)
	Cash and cash equivalents in the consolidated cash flow statement	6,012,278	8,054,509

49. Assets Subject to Sale and Repurchase Transactions

The following assets and liabilities are subject to sale and repurchase transactions:

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Included in held-to-maturity investments	2,205,403	2,909,158
Included in trading assets	462,254	–
	2,667,657	2,909,158
Included in deposits and balances of banks and other financial institutions	2,665,226	3,113,297

50. Assets Pledged as Security

The following assets have been pledged as security for own liabilities:

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Assets pledge:		
Cash and balances with banks and other financial institutions	3,729	441
Held-to-maturity investments	77,528	77,714
	81,257	78,155

As at 31 December 2005, the assets pledged represented statutory deposits pledged to the Office of the Comptroller of Currency in the USA, the People's Bank of China in the PRC and the Monetary Authority of Macao.

As at 31 December 2004, the assets pledged represented statutory deposits pledged to the Office of the Comptroller of Currency in the USA and the People's Bank of China in the PRC.

51. Material Related Party Transactions

In addition to the transactions and balances disclosed elsewhere in these financial statements, the Group entered into the following material related party transactions.

(a) Transactions with group companies

During the year, the Group entered into a number of transactions with related parties, in the ordinary course of its banking business including, inter alia, lending, the acceptance and placement of inter-bank 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.

The amount of related-party transactions during the year and outstanding balances at the end of the year are set out below:

	The Group					
	Ultimate holding company		Fellow subsidiaries		Associates	
	2005	2004	2005	2004	2005	2004
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Interest income	–	3	7,474	6,774	5,936	1,268
Interest expense	(5,719)	(3,411)	(37,625)	(13,207)	(11,820)	(659)
Other operating income	–	–	–	72	16,799	20,214
Operating expenses	(1,000)	(1,248)	(1)	(5)	(10,029)	(2,043)
For the year ended 31 December	(6,719)	(4,656)	(30,152)	(6,366)	886	18,780
Lending activities:						
At 1 January	–	–	299,326	612,858	134,187	19,449
At 31 December	–	–	369,418	299,326	200,000	134,187
Average for the year	–	–	391,829	365,358	171,171	31,843
Other receivables:						
At 1 January	–	–	9,189	21	10,320	1,276
At 31 December	–	–	4,805	9,189	10,810	10,320
Average for the year	–	–	3,130	2,313	45,481	10,820
Acceptance of deposits:						
At 1 January	190,667	529,348	1,114,919	1,107,519	1,383,378	580,988
At 31 December	72,392	190,667	2,219,663	1,114,919	876,868	1,383,378
Average for the year	229,389	420,469	1,536,503	1,312,932	1,089,156	855,957
Other payables:						
At 1 January	9	16	385	1,039	20	1,940
At 31 December	–	9	1,383	385	2,452	20
Average for the year	40	34	914	414	733	66

No impairment allowances was made in respect of the above loans to and placements with related parties.

	The Company Ultimate holding company	
	2005	**2004**
	HK$'000	*HK$'000*
Other operating income	(1,000)	(998)

(b) *Key management personnel remuneration*

Remuneration for key management personnel, including amounts paid to the Company's directors as disclosed in note 11 and certain of the highest paid employee as disclosed in note 12, are as follows:

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Short-term employee benefits	47,160	49,026
Post-employment benefits	2,545	2,721
Termination benefits	–	754
Share-based payments	2,627	2,138
	52,332	54,639

Total remuneration is included in "staff costs" (note 10).

(c) *Credit facilities to key management personnel*

During the year, the Bank provided credit facilities to key management personnel of the Bank and its holding companies and their close family members and companies controlled or significantly influenced by them. The credit facilities were provided in the ordinary course of business and on substantially the same terms as for comparable transactions with persons of a similar standing or, where applicable, with other employees.

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Balance at 1 January	3,604	11,301
As at 31 December	18,100	3,604
Maximum amount during the year	24,865	21,061

(d) *Loans to officers*

Loans to officers of the Group disclosed pursuant to section 161B of the Hong Kong Companies Ordinance are as follows:

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Aggregate amount of relevant loans made by the Group outstanding at 31 December	1,903	2,010
Maximum aggregate amount of relevant loans made by the Group outstanding during the year	2,670	2,630

There was no interest due but unpaid nor any provision made against these loans as at 31 December 2005.

52. Disposal of a Subsidiary

(a) Net liabilities disposed

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Cash and balances with banks and other financial institutions	–	9,198
Advances to customers and other accounts less provisions	–	1,003
Tangible fixed assets	–	794
Current taxation	–	(160)
Other accounts and provisions	–	(11,553)
Minority interests	–	179
Net liabilities	–	(539)
Net profit on disposal of a subsidiary	–	865
Total sales price received, satisfied in cash	–	326

(b) Analysis of net outflow of cash and cash equivalents in respect of the disposal of a subsidiary

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Cash consideration	–	326
Cash and balances with banks and other financial institutions	–	(9,198)
	–	(8,872)

53. Financial Risk Management

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

– Credit risk: loss resulting from client or counterparty default and arises on credit exposure in all forms, including settlement risk.

– Market risk: exposure to market variables such as interest rates, exchange rates and equity markets.

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

– Operational risk: risk arising from matters such as non-adherence to systems and procedures or from frauds resulting in financial or reputation loss.

The Group has established policies and procedures to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and limits continually by means of reliable and up-to-date management and information systems. The Group continually modifies and enhances its risk management policies and systems to reflect changes in markets, products and best practice risk management processes. The internal auditors also perform regular audits to ensure compliance with the policies and procedures.

(a) Credit risk management

Credit risk is managed by a regular analysis of the current and potential risk of loss arising from a customer's or counterparty's inability to meet financial obligations. The Group is exposed to credit risk through its lending, trading and capital markets activities. The Group defines the credit exposure to a customer as the amount of maximum potential loss arising from all these activities. These exposures include both on-and off-balance sheet transactions, including unfunded lending commitments such as loan commitments, letters of credit and financial guarantees.

Credit risk management is effected by monitoring implementation of adopted credit policies that determine the borrower's creditworthiness, credit risks classification, loan application procedure and procedures for lending decisions making. The Group applies the same credit policy in respect of contingent liabilities as in respect of financial instruments recorded on the balance sheet, based on loan approval procedures, use of limits to reduce risk and monitoring. Credit risk is also minimized by obtaining collateral in the form of pledged assets and guarantees from borrowers and third parties.

The Group's credit risk management practices are designed to preserve the independence and integrity of the risk assessment process. The Group assesses credit risk based upon the risk profile of the borrower, the source of repayment and the nature of the underlying collateral after giving consideration to current events and market developments. Credit risk is also managed at portfolio levels in terms of product, industry and geography to manage concentration risk.

Analysis of geographical concentration of the Group's asset is disclosed in note 18 and credit risk concentration of respective financial assets is disclosed in note 22 to 25 and 27 to 29.

(b) Market risk management

The Group's major market risk exposure rested with CITIC Ka Wah Bank Limited ("the Bank"), a wholly-owned subsidiary of the Company. Both short-term trading position and long-term strategic businesses inherit market risk exposures from the movements of foreign exchange rates, interest rates, equity prices and commodity prices.

To identify and control various market risk exposures, the Bank's Credit and Risk Management Committee ("CRMC"), Asset and Liability Management Committee ("ALCO") and its delegated sub-committees set up a hierarchy of limits and a series of risk measurements. Hierarchy limits are composed of policy, business and transaction limits to ensure adequate control from different management level. Each hierarchy level has a combination of profit and loss limits, position limits and sensitivity limits for specific market risk control.

The Bank's Treasury is the centre point to take on and manage market risk exposures within the prescribed hierarchy, product and specific risk limits.

Market Risk Management as the unit under Risk Management Group is responsible for the daily monitoring and reporting functions of market risk exposures to ensure that market risk exposures are within the prescribed limits and are managed properly.

Currency risk

The Group's foreign exchange risk stems from taking foreign exchange position, commercial dealing, investment in foreign currency securities, operations of overseas branches and subsidiaries. All foreign exchange positions are subject to exposure limits approved by ALCO.

Significant foreign currency exposures at the balance sheet date were as follows:

	The Group							
	2005				2004			
Equivalent in HK$'000	US dollars	Renminbi	Other	Total	US dollars	Renminbi	Other	Total
Spot assets	28,078,183	1,327,251	5,453,586	34,859,020	28,674,000	757,264	4,981,384	34,412,648
Spot liabilities	(31,167,025)	(549,815)	(5,084,950)	(36,801,790)	(30,836,628)	(134,181)	(4,656,405)	(35,627,214)
Forward purchases	16,617,043	104,658	3,758,734	20,480,435	7,309,008	–	2,629,869	9,938,877
Forward sales	(13,674,662)	(104,573)	(4,122,558)	(17,901,793)	(5,848,312)	–	(2,943,565)	(8,791,877)
Net options position	(179)	–	179	–	693	–	(693)	–
Net (short)/long position	(146,640)	777,521	4,991	635,872	(701,239)	623,083	10,590	(67,566)

	The Company							
	2005				2004			
Equivalent in HK$'000	US dollars	Renminbi	Other	Total	US dollars	Renminbi	Other	Total
Spot assets	145,175	1,105	–	146,280	144,455	1,080	–	145,535
Spot liabilities	(1,397,518)	(2,081)	(18)	(1,399,617)	(1,400,568)	(1,994)	(21)	(1,402,583)
Net short position	(1,252,343)	(976)	(18)	(1,253,337)	(1,256,113)	(914)	(21)	(1,257,048)

The net options position is calculated using the model user approach.

Interest rate risk

The interest rate risk for the Group comes mainly from the Bank. The Bank's ALCO oversees all interest rate risk arising from the interest rate profile of the Bank's assets and liabilities. This interest rate risk comprises of maturity gaps, basis risk among different interest rate benchmarks, yield curve movements, interest rate re-pricing risk and embedded options if any. ALCO reviews interest rate risk of the banking book through gap mismatch reports, sensitivity analysis and various stress testing. To mitigate interest rate risk, the Bank has used interest rate derivatives, mainly interest rate swaps, to hedge both assets and liabilities such as available-for-sale securities (AFS) and non-trading liabilities (NTL). The Bank has adopted hedge accounting principles to further mitigate interest rate risk by offsetting the fair value changes between the AFS/NTL securities and the corresponding hedging derivative instruments.

The following table indicates the range of effective average interest rates for the year ended 31 December for monetary financial instruments:

	The Group	
	2005	**2004**
	%	%
Assets		
Cash and balances with banks and other financial institutions & placements with banks and other financial institutions	0 – 4.40	0 – 2.17
Trade bills, advances to customers and other accounts	0 – 38.40	0 – 38.40
Securities *(Note)*	0 – 7.71	0 – 6.79
Liabilities		
Deposits and balances of banks and other financial institutions	0 – 4.34	0 – 1.82
Deposits from customers	0 – 7.35	0 – 6.63
Certificates of deposit issued, debt securities issued and loan capital	0.27 – 8.08	0.15 – 6.12

Note: Securities includes:

2005: Available-for-sale securities and held-to-maturity investments.

2004: Other investment in securities, held-to-maturity investments and investment securities.

Trading assets, trading liabilities and financial instruments designated at fair value through profit and loss are not included in the above table because the net income from these financial instruments comprise all gains and losses from changes in fair value (net of accrued coupon) together with interest income and expense and dividend income.

The following tables indicate the expected next repricing dates (or maturity dates whichever are earlier) for the interest bearing assets and liabilities at the balance sheet date.

	The Group 2005					
	Total	**3 months or less (include overdue)**	**3 months to 1 year**	**1 year to 5 years**	**Over 5 years**	**Non-interest bearing**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Assets						
Cash and balances with banks and other financial institutions	1,161,309	–	–	–	–	1,161,309
Placements with banks and other financial institutions	5,265,044	5,207,844	57,200	–	–	–
	6,426,353	5,207,844	57,200	–	–	1,161,309
Trade bills	406,364	281,559	124,805	–	–	–
Trading assets	6,473,029	1,933,197	12,574	602,017	77,318	3,847,923
Securities designated at fair value through profit or loss	1,139,908	–	227,164	808,188	82,190	22,366
Advances to customers and other accounts	44,108,183	37,568,804	3,350,754	445,252	309,234	2,434,139
Available-for-sale securities	5,945,960	–	–	4,013,971	1,767,051	164,938
Held-to-maturity investments	17,194,283	1,572,192	5,711,538	8,433,382	1,471,644	5,527
Non-interest bearing assets	3,342,598	–	–	–	–	3,342,598
Total assets	85,036,678	46,563,596	9,484,035	14,302,810	3,707,437	10,978,800

	The Group 2005					
	Total	3 months or less (include overdue)	3 months to 1 year	1 year to 5 years	Over 5 years	Non-interest bearing
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Liabilities						
Deposits and balances of banks and other financial institutions	4,157,446	3,816,248	15,000	–	–	326,198
Deposits from customers	54,415,279	51,846,176	831,864	160,833	–	1,576,406
Trading liabilities	661,137	217,904	–	–	–	443,233
Certificates of deposit issued	7,467,961	5,017,915	495,660	1,954,386	–	–
Debt securities issued	2,245,435	–	–	2,245,435	–	–
Convertible bond issued	1,289,817	–	–	1,289,817	–	–
Loan capital	4,352,351	–	2,335,961	–	2,016,390	–
Non-interest bearing liabilities	991,399	–	–	–	–	991,399
Total liabilities	75,580,825	60,898,243	3,678,485	5,650,471	2,016,390	3,337,236
Asset – liability gap		(14,334,647)	5,805,550	8,652,339	1,691,047	

	The Group 2004					
	Total	3 months or less (include overdue)	3 months to 1 year	1 year to 5 years	Over 5 years	Non-interest bearing
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Assets						
Cash and balances with banks and other financial institutions	1,488,919	–	–	–	–	1,488,919
Placements with banks and other financial institutions	6,822,355	6,761,821	60,534	–	–	–
	8,311,274	6,761,821	60,534	–	–	1,488,919
Trade bills	246,081	234,660	11,421	–	–	–
Other investment in securities	4,043,467	1,277,661	311,449	5,311	4,064	2,444,982
Advances to customers and other accounts	43,323,300	37,576,823	2,926,661	382,551	329,547	2,107,718
Held-to-maturity investments	23,930,181	2,722,756	5,473,374	11,277,409	4,414,604	42,038
Investment securities	39,841	–	–	–	–	39,841
Non-interest bearing assets	3,683,213	–	–	–	–	3,683,213
Total assets	83,577,357	48,573,721	8,783,439	11,665,271	4,748,215	9,806,711
Liabilities						
Deposits and balances of banks and other financial institutions	3,555,852	3,470,174	–	–	–	85,678
Deposits from customers	55,451,727	52,991,856	1,125,563	62,470	–	1,271,838
Certificates of deposit issued	6,959,690	5,302,640	1,507,050	150,000	–	–
Debt securities issued	2,322,798	–	–	2,322,798	–	–
Convertible bond issued	1,399,384	–	–	1,399,384	–	–
Loan capital	4,275,896	–	–	2,332,307	1,943,589	–
Non-interest bearing liabilities	1,290,007	–	–	–	–	1,290,007
Total liabilities	75,255,354	61,764,670	2,632,613	6,266,959	1,943,589	2,647,523
Asset – liability gap		(13,190,949)	6,150,826	5,398,312	2,804,626	

All assets and liabilities of the Company are non-interest bearing, except an amount due from a subsidiary of HK$75,180,000 and an amount due to a subsidiary of HK$1,395,922,000, which would be repriced within 3 months and between 1 year to 5 years respectively.

(c) Liquidity Risk Management

The Group always maintains high liquidity ratio in order to meet unexpected increase of customer demand on cash. Apart from compliance with statutory ratio requirement, stress tests are being performed regularly. The Group invests its surplus fund in a portfolio of mainly high-grade securities, which can generate liquidity if necessary either through re-purchase arrangement or out-right selling in the secondary market. The Group is also active in wholesale funding by issuing long-term certificate of deposit so as to secure stable source of funding.

Analysis of assets and liabilities by remaining maturity

The following maturity profile is based on the remaining period at the balance sheet date to the contractual maturity date.

	The Group 2005						
	Total	**Repayable on demand**	**3 months or less but not repayable on demand**	**1 year or less but over 3 months**	**5 years or less but over 1 year**	**Over 5 years**	**Undated**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Assets							
Cash and balances with banks and other financial institutions	1,161,309	1,161,309	–	–	–	–	–
Placements with banks and other financial institutions	5,265,044	–	5,186,132	78,912	–	–	–
Trade bills	406,364	–	275,102	131,262	–	–	–
Trading assets	6,473,029	228,144	–	12,574	2,209,584	402,947	3,619,780
Securities designated at fair value through profit or loss	1,139,908	–	–	249,531	808,187	82,190	–
Advances to customers and other accounts	44,108,183	1,459,841	4,101,392	6,135,882	15,259,293	14,700,716	2,451,059
Available-for-sale securities	5,945,960	–	–	–	4,022,971	1,767,051	155,938
Held-to-maturity investments	17,194,283	–	640,998	5,774,696	8,802,617	1,969,999	5,973
Undated assets	3,342,598	–	–	–	–	–	3,342,598
Total assets	85,036,678	2,849,294	10,203,624	12,382,857	31,102,652	18,922,903	9,575,348

	The Group 2005						
	Total	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	Over 5 years	Undated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Liabilities							
Deposits and balances of banks and other financial institutions	4,157,446	326,198	3,816,248	15,000	–	–	–
Deposits from customers	54,415,279	12,260,248	40,494,422	1,429,019	231,590	–	–
Trading liabilities	661,137	443,233	217,904	–	–	–	–
Certificates of deposit issued	7,467,961	–	368,968	1,856,231	5,242,762	–	–
Debt securities issued	2,245,435	–	–	–	2,245,435	–	–
Convertible bond issued	1,289,817	–	–	–	1,289,817	–	–
Loan capital	4,352,351	–	–	–	–	4,352,351	–
Undated liabilities	991,399	–	–	–	–	–	991,399
Total liabilities	75,580,825	13,029,679	44,897,542	3,300,250	9,009,604	4,352,351	991,399
Asset – liability gap		(10,180,385)	(34,693,918)	9,082,607	22,093,048	14,570,552	

	The Group (restated) 2004						
	Total	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	Over 5 years	Undated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Assets							
Cash and balances with banks and other financial institutions	1,488,919	1,488,919	–	–	–	–	–
Placements with banks and other financial institutions	6,822,355	–	6,761,821	60,534	–	–	–
Trade bills	246,081	–	231,963	14,118	–	–	–
Other investments in securities	4,043,467	–	351	50,581	1,252,649	314,904	2,424,982
Advances to customers and other accounts	43,323,300	1,531,097	3,804,515	6,327,196	16,432,807	12,940,980	2,286,705
Held-to-maturity investments	23,930,181	–	1,265,909	5,778,954	11,715,008	5,128,272	42,038
Investment securities	39,841	–	–	–	–	4,000	35,841
Undated assets	3,683,213	–	–	–	–	–	3,683,213
Total assets	83,577,357	3,020,016	12,064,559	12,231,383	29,400,464	18,388,156	8,472,779

The Group (restated) 2004

	Total	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	Over 5 years	Undated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Liabilities							
Deposits and balances of banks and other financial institutions	3,555,852	85,678	3,470,174	–	–	–	–
Deposits from customers	55,451,727	22,023,352	32,125,086	1,085,817	217,472	–	–
Certificates of deposit issued	6,959,690	–	674,999	1,279,926	5,004,765	–	–
Debt securities issued	2,322,798	–	–	–	2,322,798	–	–
Convertible bond issued	1,399,384	–	–	–	1,399,384	–	–
Loan capital	4,275,896	–	–	–	–	4,275,896	–
Undated liabilities	1,290,007	–	–	–	–	–	1,290,007
Total liabilities	75,255,354	22,109,030	36,270,259	2,365,743	8,944,419	4,275,896	1,290,007
Asset – liability gap		(19,089,014)	(24,205,700)	9,865,640	20,456,045	14,112,260	

All assets and liabilities of the Company are undated, except an amount due from a subsidiary of HK$75,180,000 and an amount due to a subsidiary of HK$1,395,922,000 which would be matured within 3 months and between 1 year to 5 years respectively.

(d) Operational risk management

The Group manages its operational risk through the Management Committee at the Group level and the Operations & Control Committee at the Bank level. The Management Committee ensures that all the subsidiaries are operating properly and managed in accordance with pre-set risk policies and procedures of the respective subsidiaries. The Operations & Control Committee comprises the Chief Operating Officer as the chairman and other senior staff from various business lines and support functions. One of its key responsibilities is to periodically review, update, and test as necessary the operational policies, procedures and contingency plans of the Bank.

Operational risk is the risk of losses which the Group may incur as a result of inadequate or failed processes, technology, infrastructure, personnel or from external events. Operational risk is not new to banks. Significant operational risk events in recent years have highlighted the need to manage operational risk more effectively by taking a broader and more comprehensive view. Technology and operational issues remain critically important, but other areas, which could lead to operational losses, must be managed as well.

The Bank currently manages operational risk through a number of ways, such as:

– Operations and technology polices and manuals are developed and reviewed annually to ensure processes are adequately considered and defined.

– Human resources policy and practices are established to define and encourage proper staff behavior, and that staff are qualified and trained for their roles.

– New products and services are evaluated to ensure that staff, processes, and technology can adequately support prior to launching.

– Disaster recovery and business continuity plans are set up and tested annually for major events such as major failure of data centre caused by fire or other events; loss of operating site and sudden and massive customer withdrawal due to market rumors or other reasons.

54. Fair Value Information

(a) Estimation of fair values

Where available, the most suitable measure for fair value is the quoted and observable market prices. In the absence of such quoted and observable market prices for most financial instruments, and in particular for loans, deposits and unlisted derivatives, the fair values are estimated based on a range of methodologies and assumptions regarding risk characteristics of various financial instruments, discount rates, estimates of future cash flows, future expected loss experience and other factors. Changes in the uncertainties and assumptions could materially affect these estimates and the resulting fair value estimates.

(b) Fair value

All financial instruments are stated at fair value or carried at amounts not materially different from their fair values as at 31 December 2005 and 2004 unless otherwise stated.

(i) Financial assets

The Group's financial assets mainly include cash, placements with banks and other financial institutions, loans and advances to customers, investments and financial derivate instruments.

The fair values of placements with banks and other financial institutions are mainly priced at market interest rates and mature within one year. Accordingly, the carrying values approximate the fair values.

The fair values of loans and advances to customers, taking into account the relevant market interest rates and being mostly priced at floating rates close to the market interest rates which are mainly repriced within 3 months, equal their carrying amounts.

Trading assets, securities designated at fair value through profit or loss and available-for-sale securities are stated at fair value in the financial statements. The fair value of held-to-maturity investments approximate their carrying amounts.

(ii) Financial liabilities

The Group's financial liabilities mainly include deposits and balances of banks and other financial institutions, deposits from customers, certificates of deposit issued, debt securities issued, convertible bonds issued and loan capital issued. The carrying values of financial liabilities approximate their fair values as at 31 December 2005, except that the fair values of loan capital issued as at the balance sheet date was HK$4,613 million, which is higher than their carrying value of HK$4,352 million.

55. Derivatives

(a) Notional amounts of derivatives

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

The following is a summary of the notional amounts of each significant type of derivatives entered into by the Group:

	The Group					
	2005			2004		
	Trading	Hedging	Total	Trading	Hedging	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Exchange rate contracts						
Forwards	18,941,850	–	18,941,850	2,637,254	–	2,637,254
Swaps	11,521,138	–	11,521,138	7,447,460	3,504,209	10,951,669
Options purchased	91,471	–	91,471	241,068	–	241,068
Options written	84,553	–	84,553	238,249	–	238,249
Interest rate contracts						
Forwards and futures	3,032,254	–	3,032,254	427,590	–	427,590
Swaps	6,897,921	12,074,747	18,972,668	3,570,070	11,615,697	15,185,767
Options purchased	1,298,984	–	1,298,984	1,671,487	–	1,671,487
Options written	1,298,984	–	1,298,984	1,849,231	–	1,849,231
Equity contracts						
Options purchased	–	–	–	–	1,083	1,083
Options written	–	–	–	–	1,083	1,083
	43,167,155	12,074,747	55,241,902	18,082,409	15,122,072	33,204,481

The above transactions are undertaken by the Group in the foreign exchange, interest rate and equity markets. The notional amounts of these instruments indicate the volume of transactions outstanding and do not represent amounts at risk.

Derivatives use for hedging purpose as at 31 December 2005 represented hedging instruments that were qualified for hedging accounting under HKAS 39.

Derivatives use for hedging purpose as at 31 December 2004 represented all derivatives that had an assets and liability management relationship. The conditions for using hedge accounting under HKAS 39 are not allowed to be applied retrospectively.

(b) Fair values and credit risk weighted amounts of derivatives

	The Group					
	2005			2004		
	Fair value		Credit risk weighted amount	Fair value*		Credit risk weighted amount
	Assets	Liabilities		Assets	Liabilities	
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Interest rate derivatives	157,286	387,765	74,175	268,774	383,276	105,037
Currency derivatives	70,858	55,468	85,145	119,554	127,623	66,096
Other derivatives	–	–	–	90	–	46
	228,144	443,233	159,320	388,418	510,899	171,179

* *Fair values information for 2004 represented 1 January 2005 restated figures.*

Credit risk-weighted amount refers to the amount as computed in accordance with the Third Schedule to the Hong Kong Banking Ordinance on capital adequacy and depends on the status of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% for contingent liabilities and commitments, and from 0% to 50% for exchange rate, interest rate and other derivatives contracts.

The fair values of derivative assets and liabilities and credit risk weighted amount of the off-balance sheet exposures do not take into account the effect of bilateral netting arrangements.

(c) Fair value of derivatives designated as hedging instruments

The following is a summary of the fair values of derivatives held for hedging purposes by product type entered into by the Group:

	The Group 2005	
	Assets	**Liabilities**
	HK$'000	*HK$'000*
Interest rate contracts	104,174	214,693

Fair value hedges

The fair value hedges are principally consisted of interest rate swaps that are used to protect against changes in the fair value of certain fixed rate assets or liabilities due to movements in the market interest rates.

(d) Remaining life of derivatives

The following tables provide an analysis of the notional amounts of derivatives of the Group by relevant maturity grouping based on the remaining periods to settlement at the balance sheet date.

	The Group 2005 Notional amounts with remaining life of			
	Total	**1 year or less**	**Over 1 year to 5 years**	**Over 5 years**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Interest rate derivatives	24,602,890	8,169,222	12,905,087	3,528,581
Currency derivatives	30,639,012	30,561,012	–	78,000
	55,241,902	38,730,234	12,905,087	3,606,581

	The Group 2004 Notional amounts with remaining life of			
	Total	**1 year or less**	**Over 1 year to 5 years**	**Over 5 years**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Interest rate derivatives	19,134,075	1,566,462	12,008,947	5,558,666
Currency derivatives	14,068,240	13,803,903	–	264,337
Equity/index derivatives	2,166	2,166	–	–
	33,204,481	15,372,531	12,008,947	5,823,003

56. Contingent Liabilities and Commitments

(a) Contingent liabilities and commitments to extend credit

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

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Direct credit substitutes	958,516	943,362
Trade-related contingencies	1,058,462	1,165,944
Other commitments:		
– with an original maturity of under 1 year or which are unconditionally cancellable	12,846,765	10,576,584
– with an original maturity of 1 year or over	350,146	588,078
	15,213,889	13,273,968
Credit risk-weighted amounts	991,061	1,072,223

Contingent liabilities and commitments are credit-related instruments which include acceptance, letters of credit, guarantees and commitments to extend credit. The risk involved is essentially the same as the credit risk involved in extending loan facilities to customers. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client default. As the facilities may expire without being drawn upon, the contract amounts do not represent expected future cash flows.

The risk weights used in the computation of credit risk-weighted amounts range from 0% to 100%.

(b) Capital commitments

Capital commitments for purchase of equipment outstanding at 31 December not provided for in the financial statements were as follows:

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Authorised and contracted for:		
Fixed assets	16,610	8,534
Others	63,717	15,160
Authorised but not contracted for:		
Fixed assets	1,352	–
	81,679	23,694

(c) *Lease commitments*

At 31 December, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

	The Group	
	2005	**2004**
	HK$'000	*HK$'000*
Properties, leases expiring		
Within 1 year	67,092	29,700
After 1 year but within 5 years	134,059	43,441
After 5 years	78,409	18,728
	279,560	91,869
Equipment, leases expiring		
Within 1 year	739	847
After 1 year but within 5 years	2,943	5,655
After 5 years	–	1,029
	3,682	7,531

The Group leases a number of properties and items of equipment under operating leases. The leases typically run for an initial period of two to four years, with an option to renew the lease when all terms are renegotiated. None of the leases includes contingent rentals.

(d) *Contingencies*

The Group and its subsidiaries are not involved in any legal actions that would be material to the financial position of the Group.

57. Non-adjusting Post Balance Sheet Events

On 30 November 2005, the Group accepted a tender to sell Unit 9A on G/F, all units on 1/F, 2/F and 3/F and 8 car parking spaces on LG/F of Eastern Central Plaza at 3 Yiu Hing Road for a total consideration of HK$128.2 million. Subsequently, the Group entered into a Memorandum of Agreement for sale and purchase with the purchaser on 2 December 2005. The sale of the Property will be completed on 9 May 2006 (the "Completion Date"). As a result of the sale, a gain of approximately of HK$46 million for the sale will be recognised in the Group's income statement for the financial year ending 31 December 2006.

58. Trust Activities

The Group commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and income arising thereon are excluded from these financial statements, as they are not assets of the Group.

59. Comparative Figures

Certain comparative figures have been adjusted as a result of the changes in accounting policies. Further details are disclosed in note 3.

60. Ultimate Holding Company

At 31 December 2005, the directors consider the ultimate holding company to be CITIC Group, which is incorporated in the People's Republic of China.

61. Accounting Estimates and Judgements

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of these financial statements and the reported amounts of revenues and expenses for the years presented. Changes in assumptions may have a significant impact on the financial statements in the periods where the assumptions are changed. The application of assumptions and estimates means that any selection of different assumptions would cause the Group's reporting to differ. The Group believes that the assumptions that have been made are appropriate and that the financial statements therefore present the financial position and results fairly, in all material respects.

Management discussed with the Audit Committee the development, selection and disclosure of the Group's significant accounting policies and estimates and the application of these policies and estimates.

(a) Key sources of estimation uncertainty

Notes 33 and 43 contain information about the assumptions and their risk factors relating to goodwill impairment, fair value of share options granted. Other key sources of estimation uncertainty are as follows:

(i) Impairment losses

Loans and advances

Loans portfolios are reviewed periodically to access whether impairment losses exist. The Group makes judgements as to whether there is any objective evidence that a loan portfolio is impaired, i.e. whether there is a decrease in estimated future cash flows. Objective evidence for impairment includes observable data that the payments status of borrowers in a group has adversely changed. It may also include observable data in local or economic conditions that correlate with defaults on the assets in the Group. If management has determined, based on their judgement, that objective evidence of impairment exists, expected future cash flows are estimated based on historical loss experience for assets with credit risk characteristics similar to those of the Group. Historical loss experience is adjusted on the basis of the current observable data. Management reviews the methodology and assumptions used in estimating future cash flows regularly to reduce any difference between loss estimates and actual loss experience.

Available-for-sale equity investments

The Group determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. The determination of when a decline in fair value below cost is not recoverable within a reasonable time period is judgemental by nature, so profit and loss could be affected by differences in this judgement.

(ii) Fair value of financial instruments

Fair value estimates are generally subjective in nature, and are made as of a specific point in time based on the characteristics of the financial instruments and relevant market information. Where available, quoted market prices are used. If a quoted price is not available on a recognized stock exchange or from a broker or dealer for non-exchange traded financial instruments or from a readily available latest trading price, the fair value is estimated using present value or other valuation techniques.

All valuation models are validated before they are used as a basis for financial reporting. Wherever possible, the Group compares valuations derived from models with quoted prices of similar financial instruments, and with actual values when realised, in order to further validate and calibrate the models.

These techniques involve uncertainties and are significantly affected by the assumptions used and judgements made regarding risk characteristics of various financial instruments, discount rate, estimates of future cash flows, future expected loss experience and other factors. Changes in assumptions could significantly affect these estimates and the resulting fair values. Derived fair value estimates cannot necessarily be substantiated by comparison to independent markets and, in many cases, could be realized in an immediate sale of the instruments.

(b) *Critical accounting judgements in applying the Group's accounting policies*

Certain critical accounting judgements in applying the Group's accounting policies are described below.

Held-to-maturity investments

The Group classifies non-derivative financial assets with fixed or determinable payments and fixed maturity and where the Group has a positive intention and ability to hold to maturity as held-to-maturity investments. In making this judgment, the Group evaluates its intention and ability to hold such investments till maturity. If the Group fails to hold these investments to maturity other than for certain specific circumstances, the Group will have to reclassify the entire portfolio of held-to-maturity investments as available-for-sale, as such class is deemed to have been tainted.

This would result in held-to-maturity investments being measured at fair value instead of at amortised cost.

62. Possible Impact of Amendments, New Standards and Interpretations Issued but not Yet Effective for the Annual Accounting Year Ended 31 December 2005

Up to the date of issue of these financial statements, the HKICPA has issued the following amendments, new standards and interpretations which are not yet effective for the accounting year ended 31 December 2005 and which have not been adopted in these financial statements:

	Effective for accounting periods beginning on or after
HKFRS 6, Exploration for evaluation of mineral resources	1 January 2006
HK(IFRIC) 4, Determining whether an arrangement contains a lease	1 January 2006
HK(IFRIC) 5, Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds	1 January 2006
HK(IFRIC) 6, Liabilities arising from participating in a specific market – Waste electrical and electronic equipment	1 January 2006
Amendments to HKAS 19, Employee benefits – Actuarial Gains and Losses, Group Plans and Disclosures	1 January 2006
Amendments to HKAS 39, Financial instruments : Recognition and measurement:	
– Cash flow hedge accounting of forecast intragroup transactions	1 January 2006
– The fair value option	1 January 2006
– Financial guarantee contracts	1 January 2006
Amendments, as a consequence of the Hong Kong Companies (Amendment) Ordinance 2005, to:	
– HKAS 1, Presentation of financial statements	1 January 2006
– HKAS 27, Consolidated and separate financial statements	1 January 2006
– HKFRS 3, Business combinations	1 January 2006
HKFRS 7, Financial Instruments: disclosures	1 January 2007
Amendments to HKAS 1, Presentation of financial statements: Capital disclosure	1 January 2007

In addition, the Hong Kong Companies (Amendment) Ordinance 2005 came into effect on 1 December 2005 and would be first applicable to the Group's financial statements for the period beginning 1 January 2006.

The Group is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application. So far it has concluded that:

- HKFRS 7 requires more detailed qualitative and quantitative disclosures, primarily in respect of fair values and risk management. The adoption of this standard is therefore only expected to affect the level of detail of the disclosures, and is not expected to have any financial impact nor result in any changes to the Group's accounting policies.

- The adoption of HKFRS 6 and HK(IFRIC) 5 and the amendments to HKAS 1, HKAS 27 and HKFRS 3 made as a result of the Hong Kong Companies (Amendment) Ordinance 2005 are not applicable to any of the Group's operations and that the adoption of the rest of them is unlikely to have a significant impact on the Group's results of operations and financial position.

63. Approval of Financial Statements

The financial statements were approved and authorised for issue by the Board of Directors on 9 March 2006.

3. MANAGEMENT DISCUSSION AND ANALYSIS

1.0 Background

The Company is the financial flagship of CITIC Group outside Mainland China. As at the Latest Practicable Date, the Company is approximately 52%-owned by CITIC Group. As at 31 December 2005, the Company's wholly-owned subsidiary, CITIC Ka Wah Bank Limited ("CKWB"), a Hong Kong incorporated licensed bank, accounted for approximately 92.0% of its profit before tax and 97.0% of its total assets; its wholly-owned asset management subsidiary, CITIC International Assets Management Limited ("CIAM"), which specialises in distressed asset management, direct investments and advisory services, accounted for approximately 3.2% of its profit before tax and 1.6% of its total assets; and its 50%-owned investment banking associate, CITIC Capital Holdings Limited (formerly known as CITIC Capital Market Holdings Limited hereinafter referred to as "CCHL"), which focuses on China-related merchant banking and investment management services, accounted for approximately 4.8% of its profit before tax and 1.4% of its total assets. The Group had 1,711 staff under its employment at 2005 year-end.

2.0 Strategy

As China becomes increasingly integrated into the global economies, international trade and capital markets, immense opportunities arise from the flourishing two-way cross-border trade business, investment and capital flows between China and the rest of the world. Moreover, as China prepares to fully liberalise its banking sector by the end of 2006, enormous potential will emerge for Chinese financial institutions that have clear strategic visions and distinct competitive edges to optimise domestic and international expansion opportunities. To that end, CITIC Group has been focusing on establishing itself as China's leading international financial services powerhouse with strong global linkages. As CITIC's offshore financial flagship, the Group's vision is to be the effective platform for CITIC's offshore expansion and to establish the CITIC financial services brand internationally.

Accordingly, the Group's priority in 2006 is to successfully execute the following strategies to support this vision, namely:

- to strengthen its expanded core competencies, improve the quality and performance of its core earnings and protect its asset quality;
- to deepen the synergistic collaboration between CKWB and CNCB in order to harness the extensive competitive strengths of the two sister commercial banks, and
- to play an integral role in the realignment of CITIC's cross-border investment banking and other financial service businesses.

3.0 Business Performance

The following business performance for the years ended 31 December 2003 and 2004 was prepared based on the figures before the adoption of the new HKFRS. It may not be directly comparable with the business performance for the year ended 31 December 2005.

3.1 Earnings

Year ended 31 December 2005

For the year ended 31 December 2005, the Group reported operating profit before impairment allowances of HK$876 million, representing a fall of 15.6% over 2004. This was mainly attributed to a 25.4% decline in net interest income, but was mitigated by the Group's continued strong growth in non-interest income at 27.9% over 2004. Prudent cost management also saw operating expenses decreased by 2.0%. Meanwhile, an improvement in asset quality and a reversal in collective assessment allowances led to a HK$58 million release in impairment allowances. The disposal of tangible assets during the year realised a net profit of HK$240 million, which included the HK$227 million gain from the sale of Ka Wah Bank Centre. The Group's share of profits from associates amounted to HK$46 million. After taking into account other items, the Group's profit attributable to shareholders for the year rose 22.1% over 2004 to HK$1,103 million.

Year ended 31 December 2004

The Group's operating profit before provisions for the year ended 31 December 2004 was HK$1,039 million, representing a rise of 3.3% over 2003. The growth in profit was attributed mainly to the substantial growth in non-interest income to HK$683 million, or an increase of 48.7% over 2003. An improvement in asset quality and write-backs of provisions led to a sharp fall in charges for bad and doubtful debts by 84.8%, which resulted in a 95.5% increase in operating profit after provision to HK$961 million. Unlike 2003 when the disposal of held-to-maturity securities realised a profit of HK$125 million, no similar activity took place during 2004. Share of profits and losses of associates was amplified this year with the Group's increased stake in CCHL from 25% to 50%; however, CCHL's core contribution was offset by the underperformance of the H-share and red chip portfolio of CITIC Capital Active Partner Fund Limited, resulting in a fall in net profit arising from associates by 56.5% to HK$76 million in 2004. However, after taking into account net profits arising from the disposal of tangible fixed assets, revaluation surplus on investment properties, provision written back on held-to-maturity securities, taxation and minority interests, the Group reported a record strong performance, with net profit attributable to shareholders rising a significant 37.3% to HK$901 million for the year.

Year ended 31 December 2003

The Group's operating profit before provisions for the year ended 31 December 2003 was HK$1,005 million, representing a fall of 11.4% from 2002. Due to improvements in the property market, the Group recorded HK$24 million in revaluation surpluses on its investment properties while profit from the sale of held-to-maturity securities more than doubled to HK$125 million. During the year, CKWB increased its interest in CITIC Capital Active Partner Fund Limited (formerly 'The Ka Wah Five Arrows China Hong Kong Fund Limited'). Due to the satisfactory performance of the fund and CCHL, net profit from associates rose sharply to HK$175 million. Net profit attributable to shareholders rose 21.9% to HK$657 million.

3.2 Net Interest Income

Year ended 31 December 2005

The Group's net interest income for 2005 fell 25.4% to HK$1,099 million. Under the new accounting standards and after adjusting for funding cost on fund investments, the Group's net interest margin stood at 1.80% at 2005 year-end, compared to 2.00% restated on same basis at 2004 year-end.

The decline in net interest income and net interest margin was attributed mainly to the adverse impact stemming from rising interest rates throughout the year. The adoption of the new accounting standards generated further negative impact.

Year ended 31 December 2004

As a result of pressures on loan yields arising from intense industry competition, the Group's interest income for 2004 suffered and dropped by 11.2%. Nevertheless, helped by the persistent low level of the Hong Kong Interbank Offered Rate, the Group was able to enjoy a substantial reduction in interest expenses of 20.1%. As a result, net interest income registered only a slight decrease, down by 5.6% over 2003 to HK$1,473 million. Add to that the enhancement in the Group's asset and liability management as well as improvements in funding mix, net interest margin contracted slightly by 3 basis points to 2.1%.

Year ended 31 December 2003

The Group's net interest income for 2003 amounted to HK$1,562 million, 7.0% below that of 2002, as a result of subdued loan demand amid a weak local economy and conservative lending policies by CKWB. Outstanding loans fell 5.5% to HK$40.6 billion while net interest margin contracted 20 basis points to 2.1%.

3.3 Non-Interest Income

Year ended 31 December 2005

The Group's non-interest income grew substantially by 27.9% over 2004 to HK$871 million. The growth was derived mainly from CKWB's retail banking business and its fund investments. The proportion of non-interest income to operating income rose significantly to 44.2% in 2005, up from 31.6% in 2004.

Year ended 31 December 2004

The Group's non-interest income grew substantially by 48.7% over 2003 to HK$683 million. This was derived mainly from retail banking fees and commissions (including wealth management services), fee income from corporate loans, income from investments, profits from foreign currency dealings, and commissions from trade bills. The proportion of non-interest income to operating income rose to 31.6%, up from 22.7% in 2003.

Year ended 31 December 2003

The Group's non-interest income fell 8.8% from the 2002 level to HK$459 million. This was due to the reduction of interests in CCHL and CITIC Capital Securities Limited from 51% to 25% in May 2002, resulting in their contribution no longer being consolidated at the subsidiary level. A reduction in new loans during the year also resulted in lower loan fees, which impacted on the overall non-interest income.

3.4 Operating Expenses

Year ended 31 December 2005

The Group's prudent cost control measures, coupled with the exclusion of goodwill amortisation under the new accounting standards, led to a decline of 2.0% in operating expenses to HK$1,095 million for 2005. Nevertheless, given the pressures on operating income, the Group's cost to income ratio rose to 55.6% in 2005 from 51.8% in 2004.

Year ended 31 December 2004

Operating expenses in 2004 reached HK$1,117 million, a 10.0% increase over 2003, due mainly to a 19.4% increase in staff costs and a one-time HK$47 million accelerated depreciation charge due to a change in accounting estimates on computer software and equipment. The sharp rise in staff costs was due to newly acquired subsidiary, changes in staff mix and sales and performance incentive plans. It should be noted, however, that with rigorous cost control measures by the Group, savings were achieved in numerous expense items; premises and equipment expenses before depreciation, in particular, fell 22.0% compared to 2003. Overall, the cost to income ratio (after goodwill) stood at 51.8%.

Year ended 31 December 2003

Operating expenses in 2003 fell 3.2% to HK$1,015 million. This was attributable to a reduction in staff costs, rental expenses, advertising and legal expenses.

3.5 Impairment Allowances

Year ended 31 December 2005

With the improvements in both the Hong Kong economy and property market, strong recoveries in bad debts and the partial benefit of a reversal in collective assessment allowances after the adoption of Hong Kong Accounting Standard 39, the Group recorded a HK$58 million release in impairment allowances in 2005, as compared to a charge of HK$78 million in 2004. Net additional provisions for individually assessed loans during the year amounted to HK$85 million, while net releases in provisions for collectively assessed loans totalled HK$44 million.

Year ended 31 December 2004

The Group lent conservatively and strived to maintain its asset quality. With the rebound in both the Hong Kong economy and property market, net specific provisions for retail and corporate loans registered a sharp decline of 84.6% and 67.5%, respectively, over 2003. Total specific provisions were reduced by over HK$363 million in 2004. Coupled with a HK$25 million net release in general provisions, the charge for bad and doubtful debts saw a sharp decline of 84.8% to HK$78 million in 2004.

Year ended 31 December 2003

The Group lent conservatively and strived to maintain its asset quality amid a weak economic environment. As a result, specific provisions fell 14.9% during the year while the charge for bad and doubtful debts dropped 4.8% to HK$514 million.

4.0 Asset Quality

The following analysis for the years ended 31 December 2003 and 2004 was prepared based on the figures before the adoption of the new HKFRS. It may not be directly comparable with the analysis for the year ended 31 December 2005.

4.1 Asset, Loan, and Deposit Sizes

Year ended 31 December 2005

As at 31 December 2005, the Group's total assets were HK$85.0 billion, representing a 1.7% increase from 2004 year-end. Total loans rose 1.0 % from the end of 2004 to HK$43.4 billion, driven mainly by a rise in residential mortgages, property investment lending, loans for use outside Hong Kong and trade finance. Total deposits were HK$61.9 billion, similar to the level at 2004 year-end.

Year ended 31 December 2004

At the end of December 2004, the Group's total assets reached HK$83.6 billion, representing an increase of 4.6% from 2003 year-end. Total loans rose 5.6% from the end of 2003 to HK$42.9 billion, due mainly to a rise in loans for use outside Hong Kong, transport and transport equipment, and trade finance. Total deposits grew by 1.4% from 2003 year-end to HK$62.4 billion, of which HK$55.5 billion were customer deposits, representing a 2.5% decline from the end of 2003.

Year ended 31 December 2003

As at 31 December 2003, the Group's total assets reached HK$79.9 billion, representing an increase of 4.9% from HK$76.2 billion recorded at the end of 2002. Total loans fell by 5.5% from the 2002 level to HK$40.6 billion, mainly due to a fall in residential mortgages, property investment, as well as transport and transport equipment loans. The proportion of Mainland loans to total customer advances increased from 10.5% in 2002 to 11.1%. Total deposits amounted to HK$61.6 billion, of which HK$56.8 billion were customer deposits, representing a 2.4% increase from 2002.

4.2 Asset Quality Indicators

Set out below is a table setting out the asset quality indicators of the Group for the 3 years ended 31 December 2005 and the restated asset quality indicators as at 1 January 2005.

	31 Dec 2005	**1 Jan 2005[3]**	**31 Dec 2004**	**31 Dec 2003**
Unadjusted capital adequacy[1]	16.0%	16.2%	15.9%	18.4%
Loans to deposits	70.1%	68.8%	68.8%	66.0%
Loans to total assets	51.0%	50.7%	51.4%	50.9%
Classified exposure	2.7%	5.4%	5.4%	8.11%
Impaired loans[2]	2.7%	5.4%	N/A	N/A
Impaired loan loss and collaterals over impaired loans[2]	92.7%	89.6%	N/A	N/A
Loan loss coverage[2]	48.6%	37.0%	N/A	N/A
Collectively assessed impairment allowance over gross loans[2]	0.68%	0.84%	N/A	N/A

(1) The unadjusted capital adequacy ratio is computed on the consolidated basis covering the Company and certain of its subsidiaries as required by the Hong Kong Monetary Authority for its regulatory purposes, and is in accordance with the Third Schedule to the Hong Kong Banking Ordinance.

(2) Calculated on the basis of the new accounting standards.

(3) Asset quantity indicators as at 1 January 2005 have been adjusted after the adoption of new HKFRS.

4.3 Deposits

Set out below is a table setting out more information in respect of the Group's deposits for the 3 years ended 31 December 2005.

Deposits*

		2005	2004	2003
1.	**By type**	**2005**	**2004**	**2003**
	Current	7.7%	18.4%	21.4%
	Savings	14.8%	21.3%	15.8%
	Fixed	77.5%	60.3%	62.8%
	Total	100.0%	100.0%	100.0%
2.	**By maturity**	**2005**	**2004**	**2003**
	On demand	22.6%	39.7%	37.2%
	Less than 3 months	74.4%	57.9%	60.1%
	Over 3 months but less than 1 year	2.6%	2.0%	2.4%
	Over 1 year but less than 5 years	0.4%	0.4%	0.3%
	Total	100.0%	100.0%	100.0%
3.	**By currency**	**2005**	**2004**	**2003**
	HKD	58.0%	59.1%	64.3%
	USD	32.4%	32.4%	26.3%
	Others	9.6%	8.5%	9.4%
	Total	100.0%	100.0%	100.0%
4.	**Number of deposit accounts**	**2005**	**2004**	**2003**
		247,808	234,296	224,582

* *Based on customer deposits only*

4.4 Loan Portfolio

Set out below is a table setting out the information in respect of the loan portfolio of the Group for the 3 years ended 31 December 2005.

Loan Portfolio#

1. By industry sectors	**2005**	**2004**	**2003**
Loans for use in Hong Kong			
Industrial, commercial and financial:			
Property development	1.0%	0.8%	0.8%
Property investment	11.7%	10.1%	10.6%
Financial concerns	5.5%	6.3%	6.7%
Stockbrokers	0.1%	0.1%	0.1%
Wholesale and retail trade	4.7%	4.7%	5.8%
Manufacturing	6.5%	7.9%	8.7%
Transport and transport equipment	9.9%	12.7%	11.3%
Others	7.2%	8.6%	9.3%
Individuals:			
Loans for the purchase of flats under the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	0.1%	0.1%	0.1%
Loans for the purchase of other residential properties	26.6%	24.6%	27.2%
Credit card advances	1.4%	1.3%	1.1%
Others	3.0%	2.7%	3.6%
Trade finance	6.5%	5.4%	5.2%
Loans for use outside Hong Kong	15.8%	14.7%	9.5%
Total	100.0%	100.0%	100.0%

2. By geographical spread	**2005**	**2004**	**2003**
Hong Kong	80.4%	80.7%	82.0%
China	15.2%	13.8%	11.8%
USA	1.8%	1.7%	1.5%
Others	2.6%	3.8%	4.7%
Total	100.0%	100.0%	100.0%

3. By maturity	**2005**	**2004**	**2003**
Repayable on demand	3.4%	3.6%	4.9%
Less than one year	23.1%	23.7%	22.4%
Over 1 year but less than 5 years	35.5%	38.5%	38.2%
Over 5 years	34.2%	30.3%	29.5%
Undated	3.8%	3.9%	5.0%
Total	100.0%	100.0%	100.0%

4. By currency	**2005**	**2004**	**2003**
HKD	84.9%	84.0%	83.5%
USD	14.5%	15.3%	16.1%
Others	0.6%	0.7%	0.4%
Total	100.0%	100.0%	100.0%

5. Number of loan accounts	**2005**	**2004**	**2003**
	194,615	188,389	180,080

Excluding trade bills and advances to banks

5.0 The Group's new products and services introduced

Set out below is a table showing the new products and services introduced for the 3 years ended 31 December 2005.

	New products and services		
	2005	**2004**	**2003**
January	• Five-year HKD callable certificates of deposit • Three-year USD callable step-up certificates of deposit • Credit card "Enjoy Buy-One-Get-One-Free Offer With Your Sales Draft" spending programme • Credit card on-line bill payment double reward programme • Credit card acquisition campaign	• "HOPE Educator" life insurance plan • Credit Card acquisition campaign	• "DocPrep" export document preparation system services • "Dividend Payment Services"
February	• Credit card travel insurance plan • Dollar$mart personal instalment loan express approval	• "RMB+ China Linked Services" • "CEPA Desk" • Enhanced currency-linked deposit • Credit Card – up to five times "Gen-X" bonus points programme	• "NOW Account"
March	• Three-month USD yield enhancement deposit • NOW Account "Monthly Step-Up Bonus Interest Rate Offer" • Credit card "HK$500,000 Jackpot Sharing Programme" • Credit card,"Cash-In" programme • Earn double bonus points by settling second tax payment with credit card • Credit card balance transfer programme	• Principal-protected currency-linked deposit • Credit Card acquisition campaign • Credit Card spending promotion to redeem fabulous gifts at discounted instalment price	• Credit Card "Interest Free Flexi Instalment Plan" – 2% Cash Rebate promotion • "FUTURITY Guaranteed Interest Fund"

New products and services

	2005	**2004**	**2003**
April	• Two-year HKD callable step-up certificates of deposit • Dollar$mart revolving cash card programme	• Acted as placing bank for Hong Kong Link 2004 Limited retail bond • "WARMTH" retirement plan with annuity option • Credit Card "Statement Balance IFFI" programme	• Participated in SME Loan Guarantee Scheme – "Business Installations and Equipment Loans" and "Associated Working Capital Loans" • Participated in "Film Guarantee Fund"
May	• Three-year HKD callable step-up certificates of deposit • Three-year USD callable step-up certificates of deposit • "Guaranteed Retirement Income Plan" • "Business Instalment Loan And Overdraft" services • Credit card spending programme – up to 10 times cash rebate • Credit card personal line of credit	• Dollar$mart personal instalment loan • Fixed-rate mortgage loan • Credit Card "Non-Conventional IFFI" programme • Credit Card May spending promotion • "Customer Member-Get-Member" mortgage loan referral programme	• CITIC Ka Wah SEED Credit Card • Participated in Government's HK$3.5 billion Loan Guarantee Scheme for Severe Acute Respiratory Syndrome Impacted Industries
June	• Gold margin trading • Dual option i-banking two-factor authentication • Renminbi credit card and ATM card • Credit card on-line bill payment reward programme • Credit card acquisition campaign • Dollar$mart interest-free personal instalment loan programme	• Comprehensive range of mortgage plans • Relaunch of "NOW Account" • Acted as placing bank for the Hong Kong Mortgage Corporation Limited retail bond • CIFC launched export account receivable discounting with recourse to export insurance agency	• Enhanced "140% Mortgage Refinancing Service" • "ANNUITY 100 Retirement Plan" • SME Loan Guarantee Scheme – "Accounts Receivable Loans"

New products and services

	2005	2004	2003
July	• On-line time deposit placement promotion • Mortgage overdraft and top-up loan programme • “PowerOne Universal Life” insurance plan • Credit card “Travel And Dine” guaranteed-to-win lucky draw • 2.8% balance transfer new card programme	• HKD callable step-up CDs • Mortgage loan promotion (super gift plan) • Acted as placing bank for the HKSAR Government retail bond • Credit Card July spending promotion	• Factoring Services
August	• Yield enhancement deposit series 1: One-year AUD-linked deposit • Yield enhancement deposit series 2: One-year NZD-linked deposit • “GROWTH Plus” insurance plan • Home contents insurance plan • Credit card on-line bill payment lucky draw programme • Dollar$mart “Free Choice Skip Payment” instalment loan programme	• 95% Mortgage insurance programme • Travel insurance plan	• Credit Card “Reward Cash Rebate”
September	• Interest rate-linked structured deposit series 1: 2.5-year HKD and USD callable deposit • Yield enhancement deposit series 3: Six-month AUD-linked deposit • Ratio par forward FX swaps • Manulife investment solutions • e-Cert “Use More Get More” reward programme • Credit card “One Off Fee Instalment” cash-in plan	• USD callable step-up CDs • Commercial property mortgage promotion • Cross-border interacting trade settlement and financing • “BRIGHT” life insurance plan • Credit Card September spending promotion	• “GROWTH Builder” life insurance plan • “LIFE Savings Plus” life insurance plan • “WARMTH” retirement plan • Credit Card usage spending promotion

	New products and services 2005	2004	2003
October	• Launch of CITIC*first* mass affluent wealth management services to existing customers • Interest rate-linked structured deposit series 2: Two-year-and-nine-month HKD and USD callable deposit • Yield enhancement deposit series 4: Six-month AUD-linked deposit • eIPO services • Credit card "Low Rate Cash-In" plan • Credit card double rewards new card programme • Credit card supplementary card acquisition programme	• Step-up time deposit • "BUSINESS NOW" and Business Credit Card • Dollar$mart Cash Card revolving loan • Credit Card Macau travel programme and "Octopus" automatic add-value service enrolment reward programme	• Non-Delivery Foreign Exchange Forward Contract • New wealth management system
November	• Value-added-tax invoice financing facility • Corporate tax loan • Yield enhancement deposit series 5: Nine-month CAD-linked deposit • Yield enhancement deposit series 6: Six-month CAD-linked deposit • Credit card Christmas guaranteed-to-win lucky draw • Credit card tax instalment plan • Dollar$mart tax loan	• Dollar$mart tax loan • Credit Card tax instalment plan • Credit Card Christmas and New Year offers	• "One Stop Business Support Services" • Pre-approved profit tax loan • Credit Card "Flexi-Instalment for Tax Payment"
December	• Yield enhancement deposit series 7: Nine-month AUD-linked deposit	• Fixed price equity-linked investment offers • The "Link REIT" refund cheque deposit/investment offer • "Grand Pacifica" preferential mortgage plan • Credit Card "Double Bonus Point" tax payment offers	• "CITIC STAR" credit card in collaboration with CITIC Industrial Bank • Credit Card "Interest Free Instalment Cash-in Scheme" and "Easy Cash-in Scheme" • Credit Card Christmas spending gift redemption plan

6.0 Segmental Information

The following table sets out the unaudited segmental information of the Group by geographical area for the three years ended 31 December 2003, 2004 and 2005. The following segmental information are not prepared in accordance to Hong Kong Accounting Standard 14: Segment Reporting ("HKAS 14"). Should the following information be prepared in accordance to HKAS 14, the presentation and figures of the segmental information would have been different.

2005	Profit	Total assets	Total liabilities	Operating income	Contingent liabilities and commitments	Advances to customers	Overdue loans and advances	Impaired loans
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Hong Kong	1,156,927	83,788,186	74,545,299	1,878,501	14,514,746	34,536,529	473,722	507,111
Mainland China	28,509	2,060,081	1,381,984	36,844	71,978	6,534,622	541,945	541,945
USA	31,759	1,776,016	1,684,051	54,853	613,328	793,891	50,495	50,495
Others	(1,549)	612,632	614,181	453	13,837	1,096,655	–	71,288
Less: Inter-segment items	–	(3,200,237)	(2,644,690)	–	–	–	–	–
Total	1,215,646	85,036,678	75,580,825	1,970,651	15,213,889	42,961,697	1,066,162	1,170,839

2004	Profit	Total assets	Total liabilities	Operating income	Contingent liabilities and commitments	Advances to customers	Overdue loans and advances	Non-performing loans
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Hong Kong	1,041,901	83,004,397	74,656,840	2,103,648	12,921,806	34,431,875	1,314,119	1,235,995
Mainland China	9,769	690,143	322,158	16,684	–	5,899,197	596,904	596,904
USA	13,620	1,742,424	1,674,194	45,380	352,162	714,454	50,620	50,620
Others	–	466,479	466,479	–	–	1,627,189	363	363
Less: Inter-segment items	(10,558)	(2,326,086)	(1,864,317)	(10,686)	–	–	–	–
Total	1,054,732	83,577,357	75,255,354	2,155,026	13,273,968	42,672,715	1,962,006	1,883,882

2003	Profit	Total assets	Total liabilities	Operating income	Contingent liabilities and commitments	Advances to customers	Overdue loans and advances	Non-performing loans
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Hong Kong	758,747	78,513,770	66,434,778	1,978,831	13,167,998	32,971,478	1,920,762	1,889,711
Mainland China	152	413,576	27,173	3,882	–	4,738,547	568,987	570,993
USA	13,185	1,911,002	1,855,577	43,689	686,159	611,329	51,754	51,754
Others	–	354,100	354,100	–	–	1,864,819	109,531	103,750
Less: Inter-segment items	–	(1,274,991)	(835,854)	(5,543)	–	–	–	–
Total	772,084	79,917,457	67,835,774	2,020,859	13,854,157	40,186,173	2,651,034	2,616,208

7.0 Remuneration Policy and Staff Development

As at the end of 2005, the Group had 1,711 staff under its employment. As at the end of 2004, the Group had 1,657 staff in its employment and as at the end of 2003, the Group employed 1,488 staff. Management firmly believes that "people" are the critical factor that distinguishes an organisation and makes it successful. In order to attract talent and retain strong performers, it has been making continuous efforts to benchmark its remuneration structure in order to ensure its competitiveness compared to industry peers. All companies under the Group offer discretionary bonus schemes aimed at cultivating common goals among employees, driving individual performance, and generating results for the Group. All bonus schemes are in direct correlation to the Group's profitability, unit performance and individual contributions.

At a shareholder meeting held on 16 May 2003, the Group received approval to implement a new share option scheme and to simultaneously terminate the Senior Executive Share Option Scheme adopted in 1995.

8.0 Core Business Development

8.1 Commercial Banking Business – CITIC Ka Wah Bank Limited ("CKWB")

8.11 Background

CKWB aspires to be the bank of choice, with the best international standards and capabilities, by providing value-creating financial solutions to define and exceed both the wealth management and international business objectives of its Greater China and overseas customers. It operates 31 branches in Hong Kong and also has an established presence in China through its branches in Beijing, Shanghai and Macau, and its wholly-owned finance company, China International Finance Company Limited (Shenzhen). CKWB's overseas branch network covers New York and Los Angeles. CKWB is rated "Baa2" by Moody's Investors Service and "BBB+" by Fitch Ratings.

8.12 Business Performance

8.121 Earnings

For the year ended 31 December 2005, CKWB reported operating profit before impairment allowances of HK$850 million, representing a fall of 18.7% over last year. This was mainly attributed to a 24.4% decline in its net interest income, but was mitigated by its strong non-interest income growth at 32.9% over 2004. Meanwhile, an improvement in asset quality and a reversal in collective assessment allowances led to a HK$80 million release in impairment allowances. The disposal of tangible assets during the year realised a net profit of HK$233 million, which included the HK$227 million gain from the sale of Ka Wah Bank Centre. After taking into account other items, CKWB's profit attributable to shareholders for the year rose 28.2% over 2004 to HK$1,047 million.

8.122 Net Interest Income

CKWB's net interest income for 2005 fell 24.4% to HK$1,101 million. Under the new accounting standards and after adjusting for funding cost on fund investments, CKWB's net interest margin stood at 1.82% at 2005 year-end, compared to 2.00% restated on same basis at 2004 year-end. The major factors attributing to the decline in CKWB's net interest income and the narrowing of its net interest margin are discussed in section 3.2.

8.123 Non-Interest Income

During the year, CKWB recorded a strong 32.9% growth in its non-interest income to HK$799 million as compared to 2004. This lifted the share of its non-interest income in its operating income to 42.0% in 2005 from 29.2% in 2004. The main contributor of this performance came from its Retail Banking Group which registered a 16.6% increase in non-interest income to HK$319 million. The other key contributor was its Fund Investments which more than doubled its income to nearly HK$230 million.

8.124 Operating Expenses

CKWB's operating expenses for 2005 rose by 3.7% year-on-year, primarily due to incremental rental expenses and the rise in staff costs. The former arose as a result of the sale and leaseback agreement of Ka Wah Bank Centre after CKWB disposed of the property as part of its office premise rationalisation plan. Its cost to income ratio rose to 55.2% in 2005 from 49.1% in 2004.

8.125 Impairment Allowances

Consistent with the asset quality trend of the Group, CKWB recorded a HK$80 million release in impairment allowances in 2005, as compared to a charge of HK$100 million in 2004. Net additional provisions for individually assessed loans during the year amounted to HK$58 million, while net releases in provisions for collectively assessed loans totalled HK$44 million.

8.13 Asset Quality

8.131 Asset, Loan, And Deposit Sizes

Total assets of CKWB amounted to approximately HK$81.8 billion as at 31 December 2005, representing a 1.9% increase over 2004 year-end. Total loans rose 1.5% to HK$43 billion on the back of increases in a rise in residential mortgages, property investment lending, loans for use outside Hong Kong and trade finance. Despite a slight 1.5% decline in customer deposits to HK$54.8 billion, total deposits stood at HK$62.3 billion, similar to the level at 2004 year-end.

8.132 Asset Quality Indicators

	31 Dec 2005	1 Jan 2005[3]	31 Dec 2004
Unadjusted capital adequacy[1]	16.4%	16.8%	16.5%
Average liquidity	51.1%	47.9%	47.9%
Loans to deposits	69.0%	67.6%	67.6%
Loans to total assets	52.5%	52.0%	52.7%
Classified exposure	1.9%	4.3%	4.3%
Impaired loans[2]	1.9%	4.3%	N/A
Impaired loans loss and collaterals over impaired loans[2]	87.8%	86.8%	N/A
Loan loss coverage[2]	50.9%	39.3%	N/A
Collectively assessed impairment allowance over gross loans[2]	0.69%	0.85%	N/A
Mainland loans to total loans	15.1%	13.6%	13.6%
Mortgage delinquency ratio	0.14%	0.34%	0.34%
Credit card charge-off ratio	1.4%	3.0%	3.0%

(1) The unadjusted capital adequacy ratio is computed on the consolidated basis covering CKWB and certain of its subsidiaries as required by the Hong Kong Monetary Authority for its regulatory purposes, and is in accordance with the Third Schedule to the Hong Kong Banking Ordinance.

(2) Calculated on the basis of the new accounting standards.

(3) Asset quality indicators as at 1 January 2005 have been adjusted after the adoption of new HKFRS.

8.14 Business Development

8.141 Retail Banking Group

In 2005, CKWB aggressively expanded the scope of its wealth management products and services. Its broad range of structured deposit product initiatives drew in HK$2.1 billion in total funding and attracted over 800 new customers as well as generated nearly HK$30 million in non-interest income. It introduced its new mass affluent wealth management platform, CITIC*first*, in October 2005 targeting customers with minimum net worth of HK$1 million. As at the end of April 2006, about 2,900 new and existing clients of CKWB have signed up for this new service offering.

CKWB also boasts a successful bancassurance business model with Sun Life Financial (Hong Kong) Limited and Manulife (International) Limited as its strategic partners. In 2005, CKWB achieved a year-on-year growth of over 28.7% in its bancassurance-related income.

In the area of credit cards, CKWB's total new sales increased by 21.4% year-on-year in 2005. This compared favourably to the industry's average growth rate at 17.0% as released by VISA International.

Both its mortgage and small- and medium-sized enterprise ("SME") businesses also delivered strong performances last year. Its market share in newly drawn-down mortgage loans was increased by 0.8% over 2004 while its total outstanding mortgage loans rose 9.7%. Outstanding loans to SMEs also grew 43.5% over 2004.

As at the end of March 2006, CKWB's retail banking group has continued to report strong business momentum, with a healthy improvement in net interest income underpinned by the widened Prime-HIBOR spread, and non-interest income growth supported by its continuous programme of new products and services campaigns.

8.142 Wholesale Banking Group

CKWB's Wholesale Banking Group ("WBG") took a strategic decision in 2005 to reposition its business model, with a clear focus to deepen client relationships and to enhance fee income generation capability by delivering value-added services rather than relying on lending as the core product. As part of this exercise, WBG upgraded its corporate and syndication capabilities, established a commercial real estate and structured finance team and launched CITIC Insurance Brokers Limited which is wholly-owned by CKWB. At the same time, it enhanced its capability to deliver treasury solutions to corporate customers.

Meanwhile, CKWB's Macau branch was officially opened in October 2005 to offer one-stop banking services to corporate customers as well as to further reinforce CKWB's geographic reach to service customers in the Pan Pearl River Delta region.

WBG's successful repositioning has already yielded encouraging results. Deal flows have significantly strengthened in the first quarter of 2006 and have already more than doubled that in 2005. The business group is well on track to deliver its goal of double-digit loan and fee income growth in 2006.

8.143 Treasury and Markets Group

CKWB's Treasury and Markets Group ("TMG") successfully established its in-house product manufacturing capability in structured products, and focused on building its distribution during the year by cross-selling to CKWB's retail and corporate customers. TMG is continuing its efforts to improve time-to-market with the introduction of new and innovative products, and have already launched a total of eight structured products via the retail banking channel in the first quarter of this year.

Meanwhile, its fund investments delivered stable year-on-year growth in 2005. Despite the market volatility in the first few months of 2006, the portfolio is still generating healthy positive returns on the back of careful asset allocation and vigilant performance monitoring.

8.144 China Banking

CKWB's China Banking business achieved a number of strategic breakthroughs in 2005. In June 2005, China International Finance Company Limited (Shenzhen) ("CIFC") received approval from the China Banking Regulatory Commission ("CBRC") to offer Renminbi services. Leveraging on the Renminbi licence, CIFC and CKWB are able to offer Renminbi services to its corporate clients as well as to individual clients who are non-Mainland citizens. They will also be able to extend such services to all Mainland citizens when China opens up its banking sector at the end of 2006. In July 2005, CIFC was granted a property insurance agency licence by the China Insurance Regulatory Commission. Subsequently in April 2006, CIFC also received approval from CBRC to prepare for an upgrade to bank status. It is expected that this new development will strengthen CKWB's foothold in the Pearl River Delta region and give it flexibility to develop various banking services in the mainland in due course.

Its Shanghai branch continued to be profitable in 2005, achieving outstanding balances of HK$849 million at the end of 2005. The branch was granted its derivative licence in April 2006. It is expected that this will enable CKWB to strengthen its collaboration with CNCB in the treasury services area as well as to leverage new opportunities with the introduction of the QDII (Qualified Domestic Institutional Investor) programme. The branch is also planning to apply for a Renminbi licence at the end of 2006.

In the area of strategic collaboration between CKWB and CNCB, both banks have established dedicated liaison teams to identify and tap joint business opportunities, and are planning to systematically develop an integrated product and services platform for their corporate clientele, and to build complementary competencies in customer resources, professional know-how, product range, service quality and risk management.

8.2 Asset Management Business – CITIC International Assets Management Limited ("CIAM")

CIAM began to operate independently in 2002, and is primarily responsible for managing distressed loans and assets as well as for allocating resources to earmark debt and equity investments.

In 2005, CIAM reported a consolidated operating profit before impairment allowances of HK$71.6 million and an operating profit of HK$57.3 million. Its net profit after tax amounted to HK$50.2 million.

During the year, CIAM successfully resolved over HK$150 million worth of problem loans, an achievement that was over 5.4 times that in 2004. This represented a 27.1% year-on-year reduction of its NPL balances, and resulted in a decline in the aggregate value of its problem loan assets to HK$370 million.

Although CIAM added few projects to its portfolio of direct investments and structured loans in 2005 due to its focus on consolidating its overall operations, the original debt and equity investment projects have successively started to generate interest income as well as handling fee and other incomes. Coming into the first quarter of 2006, the benign stock market environment in Hong Kong has benefited the performance of CIAM.

Meanwhile, CIAM continued to make progress in establishing strategic co-investment collaborations. Its co-investment entity in China, Shenzhen Guocheng Century Venture Capital Company Limited, was fully funded in early 2005 and has begun to expand its project investments. Separately, in the second half of 2005, CIAM has joined forces with Bahrain's Shamil Bank B.S.C. to develop for the first time a China real estate investment fund. Subscription monies are expected to be deployed starting from the second quarter according to projects' requirement.

On 4 December 2006, the Company entered into an agreement with certain investors of CIAM pursuant to which, such investors will subscribe for and purchase shares in CIAM. Upon completion of such agreement, the Company will be interested in 40% of CIAM and CIAM will no longer be a subsidiary of the Company. Further details of this agreement are set out in the announcement of the Company dated 4 December 2006.

8.3 Investment Banking Business – CITIC Capital Holdings Limited ("CCHL")

8.31 Background and Business Performance

CCHL is 50%-owned by the Group and 50% owned by CITIC Pacific Limited, and is principally engaged in investment banking, asset management and securities brokerage businesses. In 2005, activities in the IPO market for CCHL's target segment of mid- to low-cap enterprises stayed relatively lackluster throughout the year. Additionally, CCHL's investment performance was impeded by a volatile trading environment. As a result, CCHL reported a declined net profit after tax of HK$120 million in 2005. This represented 6.2% return on average equity employed, compared with 11.4% achieved in 2004.

Nevertheless, strong performance in the asset management area helped to bolster CCHL's foundation for further growth. Double-digit growth in both its private equity and hedge fund assets under management was registered in 2005. These two mainstream alternative investment products accounted for around 60% and 40% respectively of its total assets under management of approximately US$800 million at the end of December 2005, which continued with a strong growth momentum during the first quarter of 2006. A total of six China-focused private equity and hedge funds were launched during 2005 to broaden CCHL's product range and to offer more choices to investors, including a fund co-managed by CCHL and Allco, a renowned Australian financial services group, focusing on mezzanine and structured financing opportunities in Greater China, in particular Mainland China.

In the area of securities brokerage, CCHL continued to enhance its capabilities to serve corporate and institutional clients as well as to grow its high net-worth client base, and maintained its market share on the Hong Kong stock market during 2005 at a level similar to the previous year.

8.32 Group Restructuring

More significantly for CCHL were its efforts to optimize opportunities that are emerging from the gradual convergence of capital markets in China and overseas, including Hong Kong. Accordingly, CCHL came up with a series of plans to realign its business mix based on its relative strength and synergies with other entities within the CITIC Group. These strategic plannings culminated in an announcement in January 2006 of its restructuring in two related moves.

CCHL has signed a formal sales and purchase agreement in March 2006 with CITIC Securities Co., Ltd. ("CITIC Securities") to create an integrated, cross-border equities business platform. A new Hong Kong-based joint venture company, in which CITIC Securities will own an 80% stake and CCHL a 20% stake, will take over CCHL's existing equities business, including origination, equity capital markets, institutional and retail sales, equity research and related back office and support functions.

This strategic move has been completed. Now, CCHL focuses on developing its principal businesses in the areas of private equity, asset management, corporate advisory and mezzanine and structured finance.

In addition, CCHL intends to subscribe for a strategic stake in CITIC Trust & Investment Co., Ltd. ("CITIC Trust"), one of the leading trust companies in China. It is envisaged that the combined forces of CITIC Trust and CCHL will enable both companies to better exploit the high growth opportunities offered by an increasing demand for trust and other alternative investment products in China.

9.0 Risk Management

The Group successfully revamped its risk grading system in 2005 and rolled out an expert judgement model that can quantitatively differentiate various levels of credit risk and subsequently calibrates probability of customer default. Sections of credit risk policy, product and investment risk underwriting, exposure control, management information systems and risk infrastructure were realigned into a portfolio risk management unit to take ownership of the new risk grading system.

The Group's market risk exposures come mainly from CKWB. CKWB has set up a hierarchy of limits that comprises policy, business and transaction limits, and has adopted advanced market risk techniques for Value-at-Risk calculation, stress-testing and back-testing of the trading book. It has successfully developed an effective hedge ratio testing method so that hedge accounting principles can be applied to offset the fair value changes in the Available-for-Sale securities or the Non-Trading Liabilities, and corresponding hedging derivative instruments like interest rate swaps can offset each other.

With the preparation done in the past few years for Basel II, the Group is ready to meet the requirements of the Standardised Approach by the end of 2006. A Basel II working committee was formed to coordinate credit risk, market risk and operational risk, implement necessary measures and institute system enhancements.

Meanwhile, the Group successfully implemented unique models for assessing impairment losses of financial assets in accordance with the requirements of sections 32 and 39 in the new Hong Kong Accounting Standards issued by HKICPA.

10.0 Future Prospect

The Group has built the infrastructure and a solid foundation in 2005 to support the transformational growth of its businesses going forward, enabling it to grasp the immense market opportunities that will arise from the implementation of China's 11th Five-Year Plan and from the country's formal accession into the World Trade Organisation.

Last year, while taking care to strengthen and expand its core businesses, the Group focused on establishing new competencies, especially in CKWB, in order to create new impetus to power the growth of its core performance and earnings capabilities going forward. The Group expects these efforts to start making an impact in 2006.

Meanwhile, in view of the increasingly convergent financial and capital markets in the Mainland and Hong Kong, the Group is collaborating with other CITIC Group financial institutions to develop cohesive partnership models. The proposed Acquisition represents an important step towards this goal, and will enable CITIC to harness the competitive strengths of its domestic and offshore commercial banking businesses.

The enhanced depth of collaboration between the Group and CNCB and the strength of CNCB's operations in the PRC will offer a unique platform for the Group to invest into the growth opportunities in the PRC banking sector. It will also improve the Group's service capability and its ability to provide "one-stop" solutions to Greater China and overseas customers who are active in cross-border business and trade with the PRC.

Where the Group is currently constrained by its scale to enter into certain product areas, information technology and personnel investments, the proposed Acquisition will allow the Group to benefit from economies of scale to expand capabilities in business and product developments. The expanded platform and additional development opportunities from the strengthened ties between the two banks will enable the Group to better attract and retain top talents. Additionally, the sharing of expertise and know-how with CNCB will deepen the Group's knowledge in developing business and relationships in China, while the management best practices already established by the Group will help to raise CITIC's combined banking businesses to international standards.

4. INDEBTEDNESS

As at 31 October 2006, the Group had the following indebtedness:

(a) HK$2,253 million of debt securities issued, representing 4.25% per annum notes with face value of US$300 million issued at discount on 17 November 2004. The notes were issued by CKWB and constitute direct, unconditional and unsecured obligations of CKWB. The notes will mature on 17 November 2009.

(b) HK$980 million of convertible bonds issued by CIFH (CB-I) Limited, a single purpose wholly-owned subsidiary of the Company, issued at 0.25% per annum with face value of US$180 million on 8 December 2003. The Company unconditionally and irrevocably guarantees all amounts payable under the convertible bonds.

Each convertible bond, at the option of the holder, is convertible on or after 18 January 2004 up to and including 8 November 2008 into fully paid ordinary shares with a par value of HK$1.00 of the Company at an initial conversion price of HK$4.269 per share. The convertible bonds can be redeemed at their principal amount together with accrued interest on 8 December 2008. The net proceeds from the issue of the convertible bonds have been used for general corporate purposes of the Group.

(c) HK$1,958 million of loan capital representing 9.125% per annum perpetual subordinated notes with face value of US$250 million issued on 23 May 2002. The notes were issued by CKWH-UT2 Ltd., a separate single purpose wholly-owned subsidiary of CKWB and qualify as tier 2 capital. CKWB unconditionally and irrevocably guarantees all amounts payable under the notes. The 9.125% per annum perpetual subordinated notes will be callable by the CKWH-UT2 Ltd. in 2012.

(d) HK$41 million of notes issued representing 1 year USD Tracker Extensible Notes linked to CITIC Capital China Plus Fund with face value of US$5.3 million issued at par on 31 March 2006. The notes were issued by CKWB-SN Limited, a separate single purpose wholly-owned subsidiary of the Group. CKWB unconditionally irrevocably guarantees all amounts payable under the notes. The notes will mature on 17 May 2007 subject to the extended maturity option of the note holders to extend the final maturity date to 14 May 2009.

(e) borrowings from banks and money market takings from banks and other financial institutions, deposits from customers and certificates of deposits that arose from the normal course of our banking business carried on mainly by CKWB, which is a wholly-owned subsidiary of the Company.

(f) direct credit substitutes, transaction-related contingencies, trade-related contingencies and other commitments that arose from the normal course of banking business carried on mainly by CKWB.

Subsequent to 31 October 2006, the Group issued a new debt capital representing subordinated notes with face value of US$250 million issued at par on 11 December 2006, which bear interest at the rate of 1.68% per annum above the London interbank offered rate for three-month US dollar deposits. The notes were issued by CKWB and constitute direct, unconditional and unsecured obligations of CWKB. The notes will mature on 12 December 2011. The notes are redeemable in whole but not in part at the option of CKWB falling on, or nearest to, 12 December 2007 at a redemption price equal to 99% of the notes' principal amount, subject to obtaining the approval of the Hong Kong Monetary Authority.

Except as set out above, we did not have, as at 31 October 2006, any outstanding mortgages, charges, debentures or other loan capital (issued or agreed to be issued), bank overdrafts, loans, liabilities under acceptance or other similar indebtedness, hire purchase and finance lease commitments or any guarantees or other material contingent liabilities.

5. WORKING CAPITAL

Rules 14.69(2) and 14.66(2) of the Listing Rules require a circular in relation to a very substantial acquisition to contain a statement by the Directors that, in their opinion, the working capital available to the Group is sufficient, or if not, how it is proposed to provide the additional working capital thought by the Directors to be necessary. The Company is of the view that the traditional concept of "working capital" does not apply to banking businesses including the business of the Group. CKWB is regulated by the HKMA and is required to meet minimum capital adequacy and liquidity requirements under the Banking Ordinance and requirements on the capital adequacy ratio under the guidelines issued by the HKMA. In addition, the Group is required to and has been regularly reporting its capital adequacy requirements to the HKMA. The Company has applied to the Stock Exchange for a waiver from the strict compliance with the requirements of Rules 14.69(2) and 14.66(2) in relation to the requirement of this circular to contain a statement by the Directors that, in their opinion, the working capital available to the Group is sufficient, or if not, how it is proposed to provide the additional working capital thought by the Directors to be necessary.

6. MATERIAL ADVERSE CHANGES

As at the Latest Practicable Date, save for the transactions set out in this circular and the disposal of interests in CIAM, the details of which are set out in the announcement of the Company dated 4 December 2006, the Directors confirm that there is no material adverse change in the financial or trading position of the Group since 31 December 2005 (being the date to which the latest published audited financial statements of the Company were made up).

As at the Latest Practicable Date, the Directors confirm that there is no material adverse change in relation to the indebtedness and contingent liabilities of the Group since 31 October 2006.

The following are unaudited consolidated results of the Company and its subsidiaries (the "Group") for the six months ended 30 June 2006 and the Group's state of affairs as at that date together with the accompanying notes prepared in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, extracted from the interim report of the Group for the six months ended 30 June 2006:

Consolidated Income Statement

for the six months ended 30 June 2006 – Unaudited (Expressed in Hong Kong dollars)

		Six months ended 30 June		
		2006	**2005**	
			(restated)	*Variance*
	Note	*HK$'000*	*HK$'000*	%
Interest income	*3*	1,974,240	1,289,369	*53.12*
Interest expense		(1,476,382)	(724,570)	*103.76*
Net interest income		497,858	564,799	*(11.85)*
Fee and commission income	*4*	255,582	200,157	*27.69*
Fee and commission expense		(6,916)	(5,920)	*16.82*
Net fee and commission income		248,666	194,237	*28.02*
Net trading income	*5*	195,048	109,896	*77.48*
Net income from financial instruments designated at fair value through profit or loss	*6*	27,729	53,047	*(47.73)*
Net hedging income	*7*	1,465	91	*1,509.89*
Other operating income	*8*	17,707	51,452	*(65.59)*
Operating income		988,473	973,522	*1.54*
Operating expenses	*9*	(530,812)	(499,921)	*6.18*
		457,661	473,601	*(3.37)*
Impairment losses written back on loans and advances		6,335	92,295	*(93.14)*
Impairment losses written back on held-to-maturity investments		146	2,254	*(93.52)*
Impairment losses on available-for-sale securities		(4,849)	(2,817)	*72.13*
Impairment losses written back on properties		–	1,517	*N/A*
Impairment losses written back		1,632	93,249	*(98.25)*
Net profit on disposal of available-for-sale securities		18,870	–	*N/A*
Operating profit		478,163	566,850	*(15.65)*
Loss on disposal of associates		–	(6,155)	*N/A*
Net profit on disposal of property and equipment	*20*	59,042	251,069	*(76.48)*
Revaluation gain on investment properties		6,867	–	*N/A*
Share of profits less losses of associates		46,087	12,304	*274.57*

		Six months ended 30 June		
		2006	2005	
			(restated)	*Variance*
	Note	*HK$'000*	*HK$'000*	*%*
Profit before taxation		590,159	824,068	*(28.38)*
Income tax	*10*	(98,721)	(100,892)	*(2.15)*
Profit after taxation		491,438	723,176	*(32.04)*
Attributable to:				
Equity shareholders of the Company		491,621	723,176	
Minority interests		(183)	–	
Profit after taxation		491,438	723,176	
Dividends payable to equity shareholders of the Company attributable for the period:	*11*			
Interim dividend declared HK$0.077 (2005: HK$0.113) per share		246,516	361,358	
Earnings per share	*12*			
Basic		15.37¢	22.62¢	
Diluted		14.47¢	21.05¢	

Consolidated Balance Sheet

at 30 June 2006 – Unaudited (Expressed in Hong Kong dollars)

	Note	As at 30 June 2006 HK$'000	As at 31 December 2005 HK$'000
Assets			
Cash and balances with banks and other financial institutions	13	890,256	1,161,309
Placements with banks and other financial institutions	14	10,481,273	5,265,044
Trade bills		372,181	406,364
Trading assets	15	6,656,459	6,473,029
Securities designated at fair value through profit or loss	16	825,538	1,139,908
Advances to customers and other accounts	17	47,867,573	44,108,183
Available-for-sale securities	18	5,977,276	5,945,960
Held-to-maturity investments	19	13,237,149	17,194,283
Interest in associates		1,322,877	1,291,180
Property and equipment	20		
– Investment property		168,725	64,994
– Other property and equipment		865,324	936,474
Goodwill		1,007,749	1,007,749
Deferred tax assets	25	28,422	42,201
Total assets		89,700,802	85,036,678
Equity and liabilities			
Deposits and balances of banks and other financial institutions	21	4,258,309	4,157,446
Deposits from customers	22	60,158,563	54,415,279
Trading liabilities	23	516,778	661,137
Certificates of deposit issued	24	6,263,059	7,467,961
Debt securities issued		2,241,122	2,245,435
Convertible bonds issued		1,309,089	1,289,817
Current taxation	25	96,684	50,478
Deferred tax liabilities	25	46,716	45,466
Other liabilities		767,870	895,455
Loan capital		4,275,599	4,352,351
Total liabilities		79,933,789	75,580,825
Equity			
Share capital		3,201,423	3,197,859
Reserves	27	6,565,237	6,257,458
Total equity attributable to equity shareholders of the Company		9,766,660	9,455,317
Minority interests		353	536
Total equity		9,767,013	9,455,853
Total equity and liabilities		89,700,802	85,036,678

Consolidated Statement of Changes in Equity

for the six months ended 30 June 2006 – Unaudited (Expressed in Hong Kong dollars)

		Six months ended 30 June			
		2006		2005	
	Note	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Total equity at 1 January:					
– attributable to equity shareholders of the Company			9,455,317		8,965,090
– minority interests			536		–
			9,455,853		8,965,090
Net income recognized directly in equity:					
Exchange differences on translation of:					
– financial statements of overseas branches, subsidiaries and associates	*27*	2,222		(1,083)	
– related borrowings	*27*	209		–	
– on disposal of an associate	*27*	–		627	
			2,431		(456)
Surplus on revaluation of other premises upon reclassification to investment properties, net of deferred tax	*27*		–		9,724
Cash flow hedge					
– effective portion of changes in fair value		–		11,869	
– transfer to deferred tax		–		(2,077)	
			–		9,792
Changes in fair value					
– of available-for-sale securities	*27*	(6,982)		(29,599)	
– transfer to deferred tax	*27*	1,222		5,186	
			(5,760)		(24,413)
Net profit for the period			491,438		723,176

		Six months ended 30 June			
		2006		**2005**	
	Note	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Total recognized income and expense for the period			488,109		717,823
Attributable to:					
– equity shareholders of the Company		488,292		717,823	
– minority interests		(183)		–	
		488,109		717,823	
Dividends paid during the period	*11*		(192,074)		(239,839)
Movements in equity arising from capital transactions:					
Shares issued under share option scheme		3,564		3,706	
Net share premium received	*27*	12,822		4,264	
Equity settled share-based transactions, net of tax	*27*	(1,261)		2,470	
			15,125		10,440
Total equity at 30 June			9,767,013		9,453,514

Condensed Consolidated Cash Flow Statement

for the six months ended 30 June 2006 – Unaudited (Expressed in Hong Kong dollars)

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Cash generated from operations	4,968,764	41,499
Tax paid	(36,266)	(427)
Net cash generated from operating activities	4,932,498	41,072
Net cash generated from investing activities	40,170	447,495
Net cash used in financing activities	(405,477)	(500,288)
Net increase/(decrease) in cash and cash equivalents	4,567,191	(11,721)
Cash and cash equivalents at 1 January	6,012,278	8,054,509
Cash and cash equivalents at 30 June	10,579,469	8,042,788

Notes to the Interim Financial Report – Unaudited

(Expressed in Hong Kong dollars unless otherwise indicated)

1. BASIS OF PREPARATION

This interim financial report has been prepared in accordance with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with Hong Kong Accounting Standard ("HKAS") 34, Interim financial reporting, issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). It was authorized for issuance on 17 August 2006.

The interim financial report has been prepared in accordance with the same accounting policies adopted in the 2005 annual financial statements.

The preparation of an interim financial report in conformity with HKAS 34 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses on a year to date basis. Actual results may differ from these estimates.

This interim financial report contains condensed consolidated financial statements and selected explanatory notes. The notes 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 2005 annual financial statements. The condensed consolidated interim financial statements and notes thereon do not include all of the information required for full set of financial statements prepared in accordance with the Hong Kong Financial Reporting Standards ("HKFRSs").

The 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 HKICPA. KPMG's independent review report to the Board of Directors is included on page 58.

The financial information relating to the financial year ended 31 December 2005 that is included in the interim financial report as being previously reported information does not constitute the Company's statutory financial statements for that financial year but is derived from those financial statements. Statutory financial statements for the year ended 31 December 2005 are available from the Company's registered office. The auditors have expressed an unqualified opinion on those financial statements in their report dated 9 March 2006.

2. SEGMENT REPORTING

(a) By geographical areas

	Six months ended 30 June			
	2006	**2005**	**2006**	**2005**
	Profit/(loss) from ordinary activities before taxation	**Profit from ordinary activities before taxation** *(restated)*	**Operating income**	**Operating income**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Hong Kong	563,171	809,259	922,588	937,388
Mainland China	12,747	1,137	27,633	9,360
USA	15,598	13,672	33,302	26,774
Others	(1,438)	–	4,869	–
Less: Inter-segment items	81	–	81	–
	590,159	824,068	988,473	973,522

Profit/(loss) from Hong Kong included share of profits of associates amounting to HK$46,087,000 (2005: HK$12,304,000).

Share of an associate's taxation for the period ended 30 June 2005 was reclassified to share of profits less losses of associates in compliance with HKAS 1.

The above geographical analysis is classified by the location of the principal operations of the subsidiaries or branches of its subsidiaries.

(b) By business segments

The Group is principally engaged in the provision of banking and related financial services. The Group comprises the following main business segments:

Commercial banking business	:	It mainly comprises banking business, which includes retail banking, wholesale banking and treasury activities.
Asset management	:	It mainly comprises direct investment and distressed assets management.
Investment banking	:	It mainly comprises merchant banking and fund management.
Unallocated	:	It mainly comprises the premises and any items which cannot be reasonably allocated to specific business segments.

	Six months ended 30 June			
	2006	**2005**	**2006**	**2005**
	Profit from ordinary activities before taxation	**Profit/(loss) from ordinary activities before taxation** *(restated)*	**Operating income/ (loss)**	**Operating income/ (loss)**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Commercial banking business	445,433	773,441	988,336	925,533
Asset management	21,863	44,601	17,249	62,290
Investment banking	45,698	22,028	–	–
Unallocated	77,165	(16,002)	(17,112)	(14,301)
	590,159	824,068	988,473	973,522

Profit/(loss) from commercial banking business, asset management and investment banking included share of losses of associates amounting to HK$NIL and profits of HK$389,000 and HK$45,698,000 respectively (2005 (restated): share of losses of associates amounting to HK$10,501,000 and profits of HK$777,000 and HK$22,028,000 respectively).

Share of an associate's taxation for the period ended 30 June 2005 was reclassified to share of profits less losses of associates in compliance with HKAS 1.

3. INTEREST INCOME

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Listed securities	256,964	184,656
Unlisted securities	238,105	289,222
Others	1,479,171	815,491
	1,974,240	1,289,369

Other interest income includes the amount of interest income accrued on impaired financial assets of HK$6,450,000 (2005: NIL) and interest income on unwinding of discount on impairment loan of HK$24,236,000 (2005: HK$9,346,000) for the period ended 30 June 2006.

4. FEE AND COMMISSION INCOME

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Bills commission	22,542	19,250
Cards related income	16,122	16,051
General banking services	23,244	18,191
Insurance	35,582	33,455
Investment and structured investment products	54,958	37,819
Loans, overdrafts and facility fee	102,829	75,197
Others	305	194
	255,582	200,157

5. NET TRADING INCOME

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Gains less losses from dealing in foreign currencies	70,083	31,221
Gains less losses from trading securities	40,781	46,938
Gains less losses from other dealing activities	(26,735)	(31,243)
Interest income on trading assets		
– Listed	29,918	13,362
– Unlisted	66,971	47,257
Interest expense on trading liabilities	(2,089)	(3,085)
Dividend income from unlisted trading securities	16,119	5,446
	195,048	109,896

6. NET INCOME FROM FINANCIAL INSTRUMENTS DESIGNATED AT FAIR VALUE THROUGH PROFIT OR LOSS

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Net gains	54,269	84,356
Interest income		
– Listed	18,110	16,177
Interest expense	(44,650)	(47,486)
	27,729	53,047

7. NET HEDGING INCOME

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Fair value hedge	1,465	91

8. OTHER OPERATING INCOME

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Dividend income from available-for-sale financial assets		
– Unlisted investments	3,097	4,107
Gross rental income from investment properties of HK$2,046,000 (2005: HK$943,000) less direct outgoings of HK$12,000 (2005: HK$27,000)	2,034	916
Others*	12,576	46,429
	17,707	51,452

* *For the period ended 30 June 2005, others included an income of HK$37,600,000 arising from the forfeiture of deposit paid by counterparty.*

9. OPERATING EXPENSES

	Six months ended 30 June 2006 HK$'000	2005 HK$'000
(a) Staff costs		
Salaries and other staff costs	281,039	261,746
Retirement costs	19,591	18,428
Share-based payment expenses		
– Equity-settled share-based payment expenses	2,223	2,469
– Cash-settled share-based payment expenses	4,455	2,959
	307,308	285,602
(b) Depreciation		
Depreciation of property and equipment		
– Assets held for use under operating leases	3,357	920
– Other assets	50,651	57,366
	54,008	58,286
(c) Other operating expenses		
Property and equipment expenses, excluding depreciation		
– Rental of property	35,583	25,660
– Others	30,804	35,032
Auditors' remuneration	1,789	1,505
Advertising	17,689	27,416
Communication, printing and stationery	28,286	24,946
Legal and professional fee	4,666	7,747
Others	50,679	33,727
	169,496	156,033
Total operating expenses	530,812	499,921

Included in operating expenses are minimum lease payment under operating leases of HK$466,000 (2005: HK$466,000) for hire of equipment and HK$35,368,000 (2005: HK$25,333,000) for hire of other assets (including property rentals).

10. INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT

Taxation in the consolidated income statement represents:

	Six months ended 30 June	
	2006	**2005**
		(restated)
	HK$'000	*HK$'000*
Current tax – Hong Kong Profits Tax		
Provision for the period	81,307	95,450
(Over)/under provision in respect of prior years	(747)	1,033
	80,560	96,483
Current tax – Overseas		
Provision for the period	1,910	707
Under provision in respect of prior years	–	9
	1,910	716
Deferred tax		
Origination and reversal of temporary differences	16,251	3,693
Total income tax expense	98,721	100,892

The provision of Hong Kong Profits Tax is calculated at 17.5% (six months ended 30 June 2005: 17.5%) of the estimated assessable profits for the period. Taxation for subsidiaries and branches of a subsidiary outside Hong Kong is charged at the appropriate current rates of taxation ruling in the relevant countries.

Share of an associate's taxation for the period ended 30 June 2005 was reclassified to share of profits less losses of associates in compliance with HKAS 1.

11. DIVIDENDS

(a) Dividends attributable to the interim period

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Interim dividend declared of HK$0.077 per share (2005: HK$0.113 per share)	246,516	361,358

The interim dividend has not been recognized as a liability at the balance sheet date.

(b) Dividends attributable to the previous financial year, approved and paid during the interim period

	Six months ended 30 June 2006	2005
	HK$'000	*HK$'000*
Final dividend in respect of the financial year ended 31 December 2005, approved and paid during the following interim period of HK$0.060 per share (year ended 31 December 2004: HK$0.075 per share)	191,872	239,636
Final dividend in respect of the previous financial year on shares issued under the Old Option Scheme subsequent to the balance sheet date and before the close of the Register of Members of the Company	–	203
Final dividend in respect of the previous financial year on shares issued under the New Option Scheme subsequent to the balance sheet date and before the close of the Register of Members of the Company	202	–
	192,074	239,839

12. EARNINGS PER SHARE

(a) Basic earnings per share

The calculation of basic earnings per share for the six months ended 30 June 2006 is based on profit attributable to equity holders of the Company of HK$491,621,000 (six months ended 30 June 2005: HK$723,176,000) and the weighted average number of ordinary shares of 3,199,247,550 (2005: 3,196,526,236).

(b) Diluted earnings per share

The calculation of diluted earnings per share for the six months ended 30 June 2006 is based on adjusted profit attributable to equity holders of the Company of HK$510,659,000 (six months ended 30 June 2005: HK$741,867,000) and the weighted average number of ordinary shares of 3,528,158,751 (2005: 3,523,868,310), after adjusting for the effects of all dilutive potential ordinary shares.

13. CASH AND BALANCES WITH BANKS AND OTHER FINANCIAL INSTITUTIONS

	As at 30 June 2006	As at 31 December 2005
	HK$'000	*HK$'000*
Cash in hand	127,668	140,567
Balances with the central bank	18,158	3,826
Balances with banks and authorized institutions	744,430	1,016,916
	890,256	1,161,309

14. PLACEMENTS WITH BANKS AND OTHER FINANCIAL INSTITUTIONS

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Maturing		
– within one month	7,103,593	4,543,004
– between one month and one year	3,377,680	722,040
	10,481,273	5,265,044

15. TRADING ASSETS

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Debt securities	2,924,956	2,630,327
Equity securities	33,067	58,632
Investment funds	3,364,953	3,555,926
Treasury bills	99,339	–
Trading securities	6,422,315	6,244,885
Positive fair value of derivatives *(note 30(b))*	234,144	228,144
	6,656,459	6,473,029
Issued by:		
Central governments and central banks	100,525	557,841
Public sector entities	16,488	16,525
Banks and other financial institutions	546,238	315,702
Corporate entities	5,759,064	5,354,817
	6,422,315	6,244,885
Place of listing:		
Listed in Hong Kong	33,128	154,488
Listed outside Hong Kong	1,279,982	1,245,415
	1,313,110	1,399,903
Unlisted	5,109,205	4,844,982
Total	6,422,315	6,244,885

16. SECURITIES DESIGNATED AT FAIR VALUE THROUGH PROFIT OR LOSS

	As at 30 June 2006 HK$'000	As at 31 December 2005 HK$'000
Debt securities	787,413	1,139,908
Investment funds	38,125	–
	825,538	1,139,908
Issued by:		
Corporate entities	825,538	1,139,908
	825,538	1,139,908
Place of listing:		
Listed in Hong Kong	545,943	656,545
Listed outside Hong Kong	222,512	460,997
	768,455	1,117,542
Unlisted	57,083	22,366
Total	825,538	1,139,908

Financial assets are designated at fair value including financial assets with embedded derivatives or financial assets with the corresponding derivative financial instrument. Also, investment funds are designated at fair value through profit or loss as they are held for backing certain fund linked debt securities issued, thus eliminating or significantly reducing the accounting mismatch.

17. ADVANCES TO CUSTOMERS AND OTHER ACCOUNTS

(a) Advances to customers and other accounts less impairment allowances

	As at 30 June 2006 HK$'000	As at 31 December 2005 HK$'000
Gross advances to customers	46,469,915	42,961,697
Less: Impairment allowances		
– Individual assessed	(244,309)	(274,021)
– Collective assessed	(248,852)	(294,544)
	45,976,754	42,393,132
Advances to banks and other financial institutions	389,228	327,521
Accrued interest and other accounts less impairment allowances	1,501,591	1,387,530
	47,867,573	44,108,183

(b) Advances to customers analyzed by industry sectors

The following economic sector analysis is based on categories and definitions used by the Hong Kong Monetary Authority (the "HKMA").

	As at 30 June 2006 *HK$'000*	**As at 31 December 2005** *HK$'000*
Loans for use in Hong Kong		
Industrial, commercial and financial		
– Property development	294,287	410,595
– Property investment	5,147,480	5,033,111
– Financial concerns	3,073,600	2,355,699
– Stockbrokers	130,782	45,606
– Wholesale and retail trade	2,127,591	2,015,783
– Manufacturing	2,752,262	2,813,124
– Transport and transport equipment	4,360,892	4,280,529
– Others	2,508,820	3,093,252
Individuals		
– Loans for the purchase of flats under the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	17,513	18,409
– Loans for the purchase of other residential properties	11,565,542	11,416,704
– Credit card advances	491,657	586,781
– Others	1,428,558	1,308,935
Trade finance	3,383,416	2,789,104
Loans for use outside Hong Kong	9,187,515	6,794,065
	46,469,915	42,961,697

(c) Impaired loans and advances to customers

	As at 30 June 2006 *HK$'000*	**As at 31 December 2005** *HK$'000*
Gross impaired loans and advances to customers	1,255,015	1,170,839
Impairment allowance – individually assessed	(244,309)	(274,021)
	1,010,706	896,818
As a % of total loans and advances to customers		
– Gross impaired loans and advances	2.70%	2.73%

Impaired loans and advances are mainly individually assessed loans with objective evidence of impairment on an individual basis.

Individually assessed impairment allowances were made to write down the carrying value of the advances to the discounted value of future recoverable amounts, including the realization of collateral.

There were no impaired loans and advances to banks and other financial institutions as at 30 June 2006 and 31 December 2005.

18. AVAILABLE-FOR-SALE SECURITIES

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Debt securities	5,607,186	5,790,022
Equity securities	157,746	140,455
Investment funds	77,674	77,551
Treasury bills	198,218	–
	6,040,824	6,008,028
Impairment allowance		
– individually assessed	(63,548)	(62,068)
	5,977,276	5,945,960
Issued by:		
Central governments and central banks	198,219	–
Banks and other financial institutions	833,915	873,122
Corporate entities	4,945,142	5,072,838
	5,977,276	5,945,960
Place of listing:		
Listed outside Hong Kong	4,637,552	4,731,439
Unlisted	1,339,724	1,214,521
Total	5,977,276	5,945,960

19. HELD-TO-MATURITY INVESTMENTS

	As at 30 June 2006 HK$'000	As at 31 December 2005 HK$'000
Treasury bills	107,653	247,669
Certificates of deposit held	352,955	499,913
Debt securities	12,786,378	16,456,684
	13,246,986	17,204,266
Impairment allowance		
– individually assessed	(9,837)	(9,983)
	13,237,149	17,194,283
Issued by:		
Central governments and central banks	603,666	821,634
Public sector entities	796,890	1,136,047
Banks and other financial institutions	9,903,653	13,269,677
Corporate entities	1,932,940	1,966,925
	13,237,149	17,194,283
Place of listing:		
Listed in Hong Kong	1,173,461	1,383,224
Listed outside Hong Kong	4,241,579	3,478,078
	5,415,040	4,861,302
Unlisted	7,822,109	12,332,981
Total	13,237,149	17,194,283
Market value of listed securities	5,247,457	4,826,519

20. PROPERTY AND EQUIPMENT

In January 2005, the disposal of Ka Wah Bank Centre, 232 Des Voeux Road, Central, with sales proceeds of HK$351,000,000 was completed. The Group recognized a gain of HK$226,700,000 in its income statement for the six months ended 30 June 2005.

In May 2006, the disposal of Unit 9A on G/F, all units on 1/F, 2/F and 3/F and 8 car parking spaces on LG/F of Eastern Central Plaza at 3 Yiu Hing Road, Shaukeiwan, with sales proceeds of HK$128,200,000 was completed. The Group recognized a gain of HK$46,500,000 in its income statement for the six months ended 30 June 2006.

In May 2006, the Group purchased 8/F, Tower 1, Lippo Centre, Admiralty, with a purchase price of HK$122,100,000.

21. DEPOSITS AND BALANCES OF BANKS AND OTHER FINANCIAL INSTITUTIONS

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Deposits and balances from banks	128,693	326,198
Deposits and balances from other financial institutions	4,129,616	3,831,248
	4,258,309	4,157,446

22. DEPOSITS FROM CUSTOMERS

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Demand deposits and current deposits	5,001,902	4,201,868
Savings deposits	7,131,789	8,058,380
Time, call and notice deposits	48,024,872	42,155,031
	60,158,563	54,415,279

23. TRADING LIABILITIES

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Short positions in securities	–	217,904
Negative fair value of derivatives *(note 30(b))*	516,778	443,233
	516,778	661,137

24. CERTIFICATES OF DEPOSIT ISSUED

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Designated at fair value through profit or loss	2,478,952	2,785,924
Non-trading	3,784,107	4,682,037
	6,263,059	7,467,961

25. INCOME TAX IN THE BALANCE SHEET

(a) Current taxation in the balance sheet represents:

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Provision for Hong Kong Profits Tax for the period	81,307	129,827
Provisional Profits Tax paid	(34,203)	(127,548)
	47,104	2,279
Balance of Profits Tax provision relating to prior years	47,092	46,335
	94,196	48,614
Provision for overseas taxation	2,488	1,864
	96,684	50,478

(b) Deferred tax assets and liabilities recognized

The components of deferred tax (assets)/liabilities recognized in the consolidated balance sheet and the movements during the period are as follows:

	Depreciation allowances in excess of related depreciation *HK$'000*	Impairment allowances for loans *HK$'000*	Fair value adjustments for properties and other assets *HK$'000*	Fair value adjustments for available-for-sale securities *HK$'000*	Cash flow hedge *HK$'000*	Others *HK$'000*	Total *HK$'000*
Deferred tax arising from:							
At 1 January 2005	41,298	(57,023)	(47,757)	78,191	(1,639)	(2,262)	10,808
Charged/(credited) to consolidated income statement	(14,689)	10,401	2,526	–	–	1,594	(168)
Charged/(credited) to reserves	–	–	1,389	(10,403)	1,639	–	(7,375)
At 31 December 2005	26,609	(46,622)	(43,842)	67,788	–	(668)	3,265
At 1 January 2006	26,609	(46,622)	(43,842)	67,788	–	(668)	3,265
Charged/(credited) to consolidated income statement	(6,685)	6,623	16,567	–	–	(254)	16,251
Credited to reserves	–	–	–	(1,222)	–	–	(1,222)
At 30 June 2006	19,924	(39,999)	(27,275)	66,566	–	(922)	18,294

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Net deferred tax (assets) recognized on the balance sheet	(28,422)	(42,201)
Net deferred tax liabilities recognized on the balance sheet	46,716	45,466
	18,294	3,265

(c) Deferred tax assets not recognized

The Group has not recognized deferred tax assets in respect of cumulative tax losses of HK$98,097,000 (2005: HK$109,349,000), as it is not probable that future taxable profits against which the losses can be utilised will be available in the relevant tax jurisdiction and entity. Under the current tax legislation, the expiry dates of the tax losses are as follows:

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*
Expiring within 5 years	38,774	50,026
No expiry date	59,323	59,323
	98,097	109,349

26. MATURITY PROFILE

The following maturity profile is based on the remaining period at the balance sheet date to the contractual maturity date:

	As at 30 June 2006						
	Total	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	After 5 years	Undated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Asset							
Cash and balances with banks and other financial institutions	890,256	890,256	–	–	–	–	–
Placements with banks and other financial institutions	10,481,273	–	10,033,700	447,573	–	–	–
Trade bills	372,181	–	240,941	131,240	–	–	–
Trading assets	6,656,459	234,144	109,127	1,475	2,125,401	783,138	3,403,174
Securities designated at fair value through profit or loss	825,538	–	–	23,973	681,120	82,320	38,125
Advances to customers and other accounts	47,867,573	1,426,921	5,077,608	5,510,918	18,663,828	14,631,202	2,557,096
Available-for-sale securities	5,977,276	–	198,219	255,566	5,019,240	332,380	171,871
Held-to-maturity investments	13,237,149	–	735,549	4,007,828	6,701,775	1,785,951	6,046
Undated assets	3,393,097	–	–	–	–	–	3,393,097
Total assets	89,700,802	2,551,321	16,395,144	10,378,573	33,191,364	17,614,991	9,569,409
Liabilities							
Deposits and balances of banks and other financial institutions	4,258,309	128,693	4,114,616	15,000	–	–	–
Deposits from customers	60,158,563	12,133,691	46,531,465	911,337	582,070	–	–
Trading liabilities	516,778	516,778	–	–	–	–	–
Certificates of deposit issued	6,263,059	–	604,984	1,987,160	3,670,915	–	–
Debt securities issued	2,241,122	–	–	38,125	2,202,997	–	–
Convertible bond issued	1,309,089	–	–	–	1,309,089	–	–
Loan capital	4,275,599	–	2,330,389	–	–	1,945,210	–
Undated liabilities	911,270	–	–	–	–	–	911,270
Total liabilities	79,933,789	12,779,162	53,581,454	2,951,622	7,765,071	1,945,210	911,270
Asset – liability gap		(10,227,841)	(37,186,310)	7,426,951	25,426,293	15,669,781	

	As at 31 December 2005						
	Total	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	After 5 years	Undated
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Assets							
Cash and balances with banks and other financial institutions	1,161,309	1,161,309	–	–	–	–	–
Placements with banks and other financial institutions	5,265,044	–	5,186,132	78,912	–	–	–
Trade bills	406,364	–	275,102	131,262	–	–	–
Trading assets	6,473,029	228,144	–	12,574	2,209,584	402,947	3,619,780
Securities designated at fair value through profit or loss	1,139,908	–	–	249,531	808,187	82,190	–
Advances to customers and other accounts	44,108,183	1,459,841	4,101,392	6,135,882	15,259,293	14,700,716	2,451,059
Available-for-sale securities	5,945,960	–	–	–	4,022,971	1,767,051	155,938
Held-to-maturity investments	17,194,283	–	640,998	5,774,696	8,802,617	1,969,999	5,973
Undated assets	3,342,598	–	–	–	–	–	3,342,598
Total assets	85,036,678	2,849,294	10,203,624	12,382,857	31,102,652	18,922,903	9,575,348
Liabilities							
Deposits and balances of banks and other financial institutions	4,157,446	326,198	3,816,248	15,000	–	–	–
Deposits from customers	54,415,279	12,260,248	40,494,422	1,429,019	231,590	–	–
Trading liabilities	661,137	443,233	217,904	–	–	–	–
Certificates of deposit issued	7,467,961	–	368,968	1,856,231	5,242,762	–	–
Debt securities issued	2,245,435	–	–	–	2,245,435	–	–
Convertible bond issued	1,289,817	–	–	–	1,289,817	–	–
Loan capital	4,352,351	–	–	–	–	4,352,351	–
Undated liabilities	991,399	–	–	–	–	–	991,399
Total liabilities	75,580,825	13,029,679	44,897,542	3,300,250	9,009,604	4,352,351	991,399
Asset – liability gap		(10,180,385)	(34,693,918)	9,082,607	22,093,048	14,570,552	

27. RESERVES

	Attributable to equity shareholders of the Company										
	Share premium	Capital reserve	General reserve	Exchange differences reserve	Other property revaluation reserve	Fair value reserve	Hedging reserve	Convertible bond – equity component	Share option reserve	Retained profits*	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2005	1,835,948	2,818	100,000	(314)	11,945	368,612	(7,725)	133,027	4,308	3,318,047	5,766,666
Share premium on shares issued during the year	4,264	–	–	–	–	–	–	–	–	–	4,264
Revaluation surplus, net of deferred tax	–	–	–	–	6,785	–	–	–	–	–	6,785
Share of share option reserve of associates	–	–	–	–	–	–	–	–	6,500	–	6,500
Share of fair value reserve of associates	–	–	–	–	–	2,894	–	–	–	–	2,894
Transfer to retained profits upon disposal of property	–	–	–	–	(12,180)	–	–	–	–	12,180	–
Exchange difference on translation	–	–	–	3,371	–	–	–	–	–	–	3,371
Release on disposal of an associate	–	–	–	627	–	–	–	–	–	–	627
Equity settled share-based transactions	–	–	–	–	–	–	–	–	5,796	–	5,796
Available-for-sale securities											
– change in fair value	–	–	–	–	–	(59,442)	–	–	–	–	(59,442)
– deferred tax	–	–	–	–	–	10,403	–	–	–	–	10,403
Cash flow hedge											
– effective portion of changes in fair value	–	–	–	–	–	–	9,364	–	–	–	9,364
– deferred tax	–	–	–	–	–	–	(1,639)	–	–	–	(1,639)
Exchange difference on translation of borrowings	–	–	–	–	–	–	–	(329)	–	–	(329)
Dividends paid in respect of the previous year *(note 11(b))*	–	–	–	–	–	–	–	–	–	(239,839)	(239,839)
Profit for the year	–	–	–	–	–	–	–	–	–	1,103,395	1,103,395
Dividends declared and paid in respect of the current year	–	–	–	–	–	–	–	–	–	(361,358)	(361,358)
At 31 December 2005	1,840,212	2,818	100,000	3,684	6,550	322,467	–	132,698	16,604	3,832,425	6,257,458

	Attributable to equity shareholders of the Company										
	Share premium	Capital reserve	General reserve	Exchange differences reserve	Other property revaluation reserve	Fair value reserve	Hedging reserve	Convertible bond – equity component	Share option reserve	Retained profits*	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
At 1 January 2006	1,840,212	2,818	100,000	3,684	6,550	322,467	–	132,698	16,604	3,832,425	6,257,458
Share premium on shares issued during the year	12,822	–	–	–	–	–	–	–	–	–	12,822
Exchange difference on translation	–	–	–	2,222	–	–	–	–	–	–	2,222
Equity settled share-based transactions	–	–	–	–	–	–	–	–	(1,261)	–	(1,261)
Available-for-sale securities											
– change in fair value	–	–	–	–	–	(6,982)	–	–	–	–	(6,982)
– deferred tax	–	–	–	–	–	1,222	–	–	–	–	1,222
Exchange difference on translation of borrowings	–	–	–	–	–	–	–	209	–	–	209
Dividends paid in respect of the previous year *(note 11(b))*	–	–	–	–	–	–	–	–	–	(192,074)	(192,074)
Profit for the period	–	–	–	–	–	–	–	–	–	491,621	491,621
At 30 June 2006	1,853,034	2,818	100,000	5,906	6,550	316,707	–	132,907	15,343	4,131,972	6,565,237

* *The Group complies with the HKMA's requirement to maintain minimum impairment allowances in excess of those required under Hong Kong Accounting Standards. As at 30 June 2006, an amount of HK$322,300,000 (30 June 2005: HK$233,800,000) was included in the retained profits in this respect which was distributable to equity shareholders of the Company subject to consultation with the HKMA.*

28. ASSETS SUBJECT TO SALE AND REPURCHASE TRANSACTIONS

The following assets and liabilities are subject to sale and repurchase transactions:

	As at 30 June 2006	As at 31 December 2005
	HK$'000	*HK$'000*
Included in held-to-maturity investments	2,643,141	2,205,403
Included in available-for-sale securities	878,785	–
Included in trading assets	–	462,254
	3,521,926	2,667,657
Included in deposits and balances from banks and other financial institutions	3,305,018	2,665,226

29. MATERIAL RELATED PARTY TRANSACTIONS

In addition to the transactions and balances disclosed elsewhere in these financial statements, the Group entered into the following material related party transactions:

(a) Transactions with group companies

During the period, the Group entered into a number of transactions with related parties, in the ordinary course of its banking business including, inter alia, lending, acceptance and placement of inter-bank 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.

The amount of related party transactions during the period and outstanding balances at the end of the period are set out below:

	Ultimate holding company		Fellow subsidiaries		Associates	
	Six months ended 30 June					
	2006	**2005**	**2006**	**2005**	**2006**	**2005**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Interest income	–	–	3,197	3,023	4,911	1,504
Interest expense	(6,917)	(1,451)	(32,841)	(14,729)	(10,537)	(1,691)
Other operating income	–	–	–	–	10,858	8,663
Operating expenses	(503)	(1,000)	(1)	–	(1,709)	(7,120)
	(7,420)	(2,451)	(29,645)	(11,706)	3,523	1,356

	Ultimate holding company		Fellow subsidiaries		Associates	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Lending activities:						
At 1 January	–	–	369,418	299,326	200,000	134,187
At 30 June 2006/31 December 2005	–	–	319,792	369,418	200,000	200,000
Average for the period/for the year	–	–	344,860	391,829	200,000	171,171
Other receivables:						
At 1 January	–	–	4,805	9,189	10,810	10,320
At 30 June 2006/31 December 2005	–	–	771	4,805	9,500	10,810
Average for the period/for the year	–	–	3,032	3,130	9,914	45,481
Acceptance of deposits:						
At 1 January	72,392	190,667	2,219,663	1,114,919	876,868	1,383,378
At 30 June 2006/31 December 2005	443,200	72,392	1,507,851	2,219,663	842,665	876,868
Average for the period/for the year	354,500	229,389	1,593,917	1,536,503	905,124	1,089,156
Other payables:						
At 1 January	–	9	1,383	385	2,452	20
At 30 June 2006/31 December 2005	600	–	3,390	1,383	916	2,452
Average for the period/for the year	400	40	2,624	914	2,703	733

No impairment allowance was made in respect of the above loans to and placements with related parties.

(b) Key management personnel remuneration

Remuneration for key management personnel, including amounts paid to directors and certain employees with the highest emoluments, are as follows:

	Six months ended 30 June	
	2006	**2005**
	HK$'000	*HK$'000*
Short-term employee benefits	17,105	17,846
Share-based payments	1,521	1,875
	18,626	19,721

Total remuneration is included in staff costs (note 9(a)).

(c) Credit facilities to key management personnel

During the year, the Bank provided credit facilities to key management personnel, including amounts paid to directors and certain employees with the highest emoluments, of the Bank and its holding companies and their close family members and companies controlled or significantly influenced by them. The credit facilities were provided in the ordinary course of business and on substantially the same terms as for comparable transactions with persons of a similar standing or, where applicable, with other employees.

	As at 2006	**As at 2005**
	HK$'000	*HK$'000*
Balance at 1 January	18,100	3,604
As at 30 June 2006/31 December 2005	20,051	18,100
Maximum amount during the period/year	24,184	24,865

30. DERIVATIVES

(a) Notional amounts of derivatives

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

The following is a summary of the notional amounts of each significant type of derivatives entered into by the Group:

	As at 30 June 2006			**As at 31 December 2005**		
	Trading	**Hedging**	**Total**	**Trading**	**Hedging**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Exchange rate contracts						
Forwards	31,028,925	–	31,028,925	18,941,850	–	18,941,850
Swaps	10,977,114	–	10,977,114	11,521,138	–	11,521,138
Options purchased	157,035	–	157,035	91,471	–	91,471
Options written	146,829	–	146,829	84,553	–	84,553
Interest rate contracts						
Forwards and futures	1,635,028	–	1,635,028	3,032,254	–	3,032,254
Swaps	12,377,446	6,819,880	19,197,326	6,897,921	12,074,747	18,972,668
Options purchased	1,116,556	–	1,116,556	1,298,984	–	1,298,984
Options written	1,116,556	–	1,116,556	1,298,984	–	1,298,984
	58,555,489	6,819,880	65,375,369	43,167,155	12,074,747	55,241,902

The above transactions are undertaken by the Group in the foreign exchange, interest rate and equity markets. The notional amounts of these instruments indicate the volume of transactions outstanding and do not represent amounts at risk.

Derivatives used for hedging purpose as at 30 June 2006 and 31 December 2005 represented hedging instruments that were qualified for hedging accounting under HKAS 39.

(b) Fair values and credit risk-weighted amounts of derivatives

	As at 30 June 2006			As at 31 December 2005		
	Fair value		Credit risk-weighted	Fair value		Credit risk-weighted
	Assets	Liabilities	amount	Assets	Liabilities	amount
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Interest rate derivatives	120,882	384,936	62,385	157,286	387,765	74,175
Currency derivatives	113,262	131,842	130,526	70,858	55,468	85,145
	234,144	516,778	192,911	228,144	443,233	159,320

Credit risk-weighted amount refers to the amount as computed in accordance with the Third Schedule to the Hong Kong Banking Ordinance on capital adequacy and depends on the status of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% for contingent liabilities and commitments, and from 0% to 50% for exchange rate, interest rate and other derivatives contracts.

The above derivative assets and liabilities, being the positive or negative marked-to-market value of the respective derivative contracts, represent gross replacement costs, as none of these contracts are subject to any bilateral netting arrangements.

(c) Fair value of derivatives designated as hedging instruments

The following is a summary of the fair values of derivatives held for hedging purposes by product type entered into by the Group:

	As at 30 June 2006		As at 31 December 2005	
	Assets	Liabilities	Assets	Liabilities
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Interest rate contracts	33,060	144,509	104,174	214,693

The fair value hedges principally consist of interest rate swaps that are used to protect against changes in the fair value of certain fixed rate assets or liabilities due to movements in the market interest rates.

(d) Remaining life of derivatives

The following tables provide an analysis of the notional amounts of derivatives of the Group by relevant maturity grouping based on the remaining periods to settlement at the balance sheet date:

	As at 30 June 2006			
	Notional amounts with remaining life of			
	Total	**1 year or less**	**Over 1 year to 5 years**	**Over 5 years**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Interest rate derivatives	23,065,466	9,168,257	11,644,677	2,252,532
Currency derivatives	42,309,903	42,231,903	–	78,000
	65,375,369	51,400,160	11,644,677	2,330,532

	As at 31 December 2005			
	Notional amounts with remaining life of			
	Total	**1 year or less**	**Over 1 year to 5 years**	**Over 5 years**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Interest rate derivatives	24,602,890	8,169,222	12,905,087	3,528,581
Currency derivatives	30,639,012	30,561,012	–	78,000
	55,241,902	38,730,234	12,905,087	3,606,581

31. CONTINGENT LIABILITIES AND COMMITMENTS

(a) Contingent liabilities and commitments to extend credit

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

	As at 30 June 2006	**As at 31 December 2005**
	HK$'000	*HK$'000*
Direct credit substitutes	1,384,373	958,516
Trade-related contingencies	1,269,539	1,058,462
Forward forward deposits placed	530,000	–
Other commitments:		
– with an original maturity of under 1 year or which are unconditionally cancellable	13,125,114	12,846,765
– with an original maturity of 1 year or over	1,648,353	350,146
	17,957,379	15,213,889
Credit risk-weighted amounts	1,756,997	991,061

Contingent liabilities and commitments are credit-related instruments which include acceptance, letters of credit, guarantees and commitments to extend credit. The risk involved is essentially the same as the credit risk involved in extending loan facilities to customers. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client default. As the facilities may expire without being drawn upon, the contractual amounts do not represent expected future cash flows.

The risk weights used in the computation of credit risk-weighted amounts range from 0% to 100%.

(b) Capital commitments

Capital commitments for purchase of equipment outstanding at

30 June not provided for in the financial statements are as follows:

	As at 30 June 2006	**As at 31 December 2005**
	HK$'000	*HK$'000*
Authorized and contracted for:		
Property and equipment	2,250	16,610
Others	67,044	63,717
Authorized but not contracted for:		
Property and equipment	–	1,352
	69,294	81,679

32. COMPARATIVE FIGURES

Share of an associate's taxation for the period ended 30 June 2005 was reclassified to share of profits less losses of associates in compliance with HKAS 1. The comparative figures have been restated accordingly to conform with the current period's presentation.

33. POST BALANCE SHEET EVENT

(i) The Company had on 13 April 2006 entered into a formal sale and purchase agreement (the "Formal Sale and Purchase Agreement") with CITIC Group, the controlling shareholder of the Company, for the acquisition of 19.9% of the existing interest in China CITIC Bank ("CNCB") (the "Acquisition"). The consideration of the Acquisition (the "Consideration") represents 1.153 times of 19.9% of the audited consolidated net asset value of CNCB for the year ended 31 December 2005 prepared in accordance with International Financial Reporting Standards ("Transaction Value"). However, if the Transaction Value is lower than 19.9% of the appraised value of the net asset of CNCB as at 31 December 2005 as approved by the Ministry of Finance ("Approved Valuation"), the Consideration shall be calculated based on the Approved Valuation subject to the Approved Valuation being no more than 120% of the Transaction Value. The Consideration is to be satisfied by the issue and allotment of new ordinary shares of HK$1.00 each of the Company to CITIC Group (the "Consideration Shares") at HK$3.41 per share.

Subsequent to the entering of the Formal Sale and Purchase Agreement, the Company has been informed that on 30 June 2006, CITIC Group has injected further capital into CNCB in the sum of RMB5 billion by cash. The capital injection has been made consistent with CITIC Group's undertaking to assume responsibility for any additional capital requirements by CNCB prior to the investment by a strategic investor and/or the listing of CNCB, while assuring that the Company's equity interest in CNCB will not be less than 15% following the capital injection. The interest of the Company in CNCB upon completion of the Acquisition and taking into account the capital injection will be approximately 16.4%.

Completion of the Acquisition will be subject to the satisfaction of various conditions precedent including, inter alia, the approval by the independent shareholders, which have been obtained by the Company at the extraordinary general meeting held on 19 July 2006. Completion shall take place within 10 business days after the fulfillment or waiver of all other conditions precedent to the Agreement, the latest date of which is 31 December 2006 or such later date as the Company and CITIC Group may agree in writing.

(ii) Subordinated note with a coupon of 7.625% per annum and with face value of US$300,000,000 (HK$ equivalent 2,330,206,000) issued on 5 July 2001 by CKWB (Cayman Islands) Ltd., a wholly owned subsidiary of CITIC Ka Wah Bank Limited, was early redeemed on 6 July 2006.

Unaudited Supplementary Financial Information

(Expressed in Hong Kong dollars unless otherwise indicated)

Summary of Financial Position

	As at 30 June 2006 *HK$'000*	As at 31 December 2005 *HK$'000*	Variance *%*
Advances to customers and trade bills	46,842,096	43,368,061	8.01
Impairment allowances	493,161	568,565	(13.26)
Total assets	89,700,802	85,036,678	5.48
Total deposits	66,421,622	61,883,240	7.33
Total equity attributable to equity shareholders of the Company	9,766,660	9,455,317	3.29
Financial ratios			
Unadjusted capital adequacy ratio*	14.99%	16.01%	
Loans to deposits	70.52%	70.08%	
Loans to total assets	52.22%	51.00%	
Cost to income	53.70%	55.55%	
Return on assets	1.07%	1.31%	
Return on average total equity attributable to equity shareholders of the Company	9.69%	12.41%	

* *The unadjusted capital adequacy ratio is computed on the consolidated basis covering the Company and certain of its subsidiaries as required by the Hong Kong Monetary Authority (the "HKMA") for its regulatory purposes, and is in accordance with the Third Schedule to the Hong Kong Banking Ordinance.*

Management Discussion and Analysis

1.0 Review of Operations

Healthy domestic consumption saw Hong Kong's economy grow further in the first half of 2006. Apart from steadily declining unemployment and the buoyant turnover in the local stock market, the economy was also helped by continued strong external trade performance. All these factors, coupled with the widening of the spread between the Prime Lending Rate ("Prime") and the Hong Kong Interbank Offer Rate ("HIBOR"), created a favourable operating environment for the local banking industry. Nonetheless, the growth in commercial and mortgage lending suffered obvious blows as the local interest rate up-cycle persisted well beyond its second year. Loan yields were also depressed by intense industry competition. Meanwhile, the Hong Kong financial sector faced additional challenges brought on by the resilient flattening of the yield curve, the uncertain interest rate outlook, increasing inflationary pressures, as well as the successive macro-economic tightening policies introduced by the Mainland Chinese government in its attempt to further rein in the nation's robust economic growth.

In the first half of 2006, CITIC International Financial Holdings Limited (the "Group") stayed focused on its priorities to defend its core performance, build new competencies, and maximise opportunities for the CITIC financial services brand internationally. On 31 March 2006, the Group kicked off its major strategic development plan with the announcement of its acquisition of a 19.9% stake in China CITIC Bank ("CNCB") (The strategic stake was subsequently lowered to 16.4% following a RMB5 billion capital injection into CNCB by CITIC Group on 30 June 2006). The transaction has been approved by the Group's independent shareholders at an Extraordinary General Meeting held on 19 July 2006, and is now pending final approvals by the relevant regulatory authorities in the PRC. Upon the completion of the transaction, the Group will become the major foreign investor in CNCB. The Group's management hopes to deliver enhanced shareholder value by maximising the synergistic benefits to be derived from leveraging the complementary competencies of the Group and CNCB.

2.0 Business Performance

2.1 Earnings

The Group reported a strong 53.1% increase in interest income in the first half of 2006; however, interest expenses doubled as funding cost soared as a result of the sharp rise in market interest rates. This led to a fall in net interest income by 11.9% year-on-year. However, much of this impact was offset by the Group's continued strong growth in non-interest income at 20.0% in the first half of 2006. Net of operating expenses, operating profit before impairment allowances decreased by 3.4% to HK$458 million. Meanwhile, despite a normalising credit cycle in the first half of 2006, the Group recorded a net release of HK$2 million in impairment allowances during the period. This compared to a net release of HK$93 million in the corresponding period last year that was then helped primarily by asset quality improvements as well as a reversal in collective assessment. As a result, operating profit dropped 16.0% over the same period last year to HK$478 million. Unlike in 2005, when the sale of Ka Wah Bank Centre realised a one-off gain of HK$227 million from the disposal of tangible assets, a similar scale of gain was not repeated in the first half of 2006. After taking into account other items, the Group's profit attributable to shareholders for the first half of 2006 dropped 32.0% year-on-year to HK$492 million.

2.2 Net Interest Income

The Group reported substantial growth in its interest income by 53.1% during the period, driven primarily by strong loan growth resulting from the strengthened core business infrastructure and competencies of CITIC Ka Wah Bank Limited ("CKWB"), as well as by the widening of the Prime-HIBOR spread.

At the same time, the average three-month HIBOR in the first half of 2006 climbed by 2.2 percentage points to 4.4% compared to the same period last year. That, coupled with the prolonged flat yield curve, significantly intensified funding cost pressures on the Group's deposits, held-to-maturity fixed income investment portfolio and fund investments, and led to a 103.8% rise in overall interest expense. As a result, net interest income declined by 11.9% to HK$498 million.

As gross income for the fund investments was recognised as non-interest income, in order to provide an accurate reflection of the Group's interest earning capability, the Group calculated its net interest margin by adding back the portfolio's funding cost to net interest income to arrive at 1.76% for the first half of 2006, as compared to 1.78% restated on the same basis for the first half of 2005.

Looking ahead, note should be taken of several factors that will impact the Group's net interest income. Firstly, CKWB recalled its US$300 million subordinated debt issue in July 2006, which will help to reduce the Group's interest expense. As CKWB does not have any pressing need for capital, any decision to replace the subordinated debt issue will depend on market conditions. Secondly, the Group plans to relieve funding cost pressures from its held-to-maturity fixed income investment portfolio by redeploying capital from maturing securities for better balance sheet management. However, prudent expansion of the Group's fund investments will correspondingly exert further pressures on both funding costs and net interest income.

2.3 Non-Interest Income

The Group delivered an outstanding 20.0% non-interest income growth to HK$491 million in the first half of 2006 as compared to the same period last year. The growth was mainly derived from CKWB's strengthened core business performance in loans, investment and treasury-related products. The share of non-interest income in the Group's operating profit rose to 49.6% for the first half of 2006 from 42.0% for the corresponding period last year. The Group will strive to maintain this ratio above 40%.

2.4 Operating Expenses

The Group's operating expenses for the first half of 2006 rose by 6.2% year-on-year, primarily due to the rise in staff-related costs as well as one-time relocation expenses related to CKWB's office rationalisation plan (Please see 4.124 for details). Cost to income ratio rose to 53.7% from 51.4% for the first half of 2005, but was slightly improved from 55.6% as at 2005 year-end. The Group has already put in place prudent cost control measures, and will strive to further reduce this ratio by the end of 2006.

2.5 Impairment Allowances

The Group lent conservatively and strived to continually improve its risk management and asset quality. With the credit cycle normalising in the first half of 2006, the Group reported a HK$29 million charge for individually assessed loans, and a HK$35 million release for collectively assessed loans, resulting in a net release in loan impairment allowances for the period of HK$6 million. Including impairment on other assets, the Group registered a HK$2 million net release in impairment allowances, compared to a net release of HK$93 million in the corresponding period last year that was then helped by asset quality improvements as well as a reversal in collective assessment.

2.6 Interim Dividend

The Board of Directors proposed an interim dividend of HK$0.077 per share, representing a pay-out ratio of 50.2%. The interim dividend for the first half of 2005 was HK$0.113 per share.

3.0 Asset Quality

3.1 Asset, Loan, and Deposit Sizes

The Group's asset size expanded significantly during the period, and stood at HK$89.7 billion as at 30 June 2006, representing a 5.5% increase from 2005 year-end. Total loans rose 8.0% from the end of 2005 to HK$46.8 billion, driven mainly by a rise in loans for use outside Hong Kong as well as financial sector related loans and trade finance. Total deposits grew by 7.3% from 2005 year-end to HK$66.4 billion.

3.2 Asset Quality Indicators

During the period, the Group reported slight improvements in its asset quality indicators, including an expansion of its coverage ratio to 98.2% from 92.7% at 2005 year-end.

3.3 Financial Position

As at 30 June 2006, the Group's unadjusted capital adequacy ratio was 15.0%. Its loans to deposits ratio was 70.5%, and its loans to total assets ratio was 52.2%.

CITIC International Financial Holdings' Key Financial Indicators

	30 June 2006	**31 December 2005**
Unadjusted capital adequacy	15.0%	16.0%
Loans to deposits	70.5%	70.1%
Loans to total assets	52.2%	51.0%
Impaired loans	2.7%	2.7%
Coverage*	98.2%	92.7%
Loan loss coverage	39.3%	48.6%
Collective assessment coverage	0.53%	0.68%

* *Calculated by dividing the sum of individually assessed impairment allowances and collateral of impaired loans by the gross impaired loans*

4.0 Core Business Development

4.1 CITIC Ka Wah Bank Limited ("CKWB")

4.11 Operating Environment

CKWB focused on strengthening its fundamentals and building competencies last year in order to enhance its competitive advantages and to drive future business expansion. The results of such efforts were evident in the strong performances delivered by all its major business departments in the first half of 2006.

4.12 Business Performance

4.121 Earnings

CKWB accounted for 74.1% of the Group's net profit, as such its overall results performance was similar to that of the Group. For the first half of 2006, CKWB's interest income grew by a significant 53.1% year-on-year, but soaring funding costs saw its net interest income reduced by 13.7%. Nevertheless, a strong 39.8% non-interest income growth helped to offset the decline in net interest income and the rise in operating expenses. As a result, it reported a 7.1% rise over the same period last year in operating profit before impairment allowances to HK$480 million. A net provision of HK$13 million in impairment losses was recorded in the first half of 2006 as compared to a net release of HK$99 million in the corresponding period last year. As a result, operating profit dropped 11.2% over the same period last year to HK$486 million. CKWB's profit attributable to shareholders for the first half of 2006 dropped 46.7% to HK$364 million on a financial accounting basis as compared to the same period last year; apart from reasons cited above and the fact that the previous year's results included a one-off gain of HK$227 million from the sale of Ka Wah Bank Centre, the current year's results also carried a net book loss of HK$47 million from the sale of bank premises. It should be noted, however, that the property transaction itself did not create a real loss, and it was instead carried as a net disposal gain of HK$45 million in the Group's consolidated accounts due to the release of a property valuation reserve created in 2002. If the gains from the sale of bank premises had been fully taken into account, CKWB's contribution to the Group's profit attributable to shareholders would have been HK$471 million.

4.122 Net Interest Income

CKWB's efforts to strengthen its core business fundamentals have resulted in strong performances in both its wholesale and retail loan portfolios. This, coupled with the widening of the Prime-HIBOR spread, helped push interest income up by 53.1% during the period. However, the sharp rise in market interest rates doubled its funding costs, resulting in a 13.7% year-on-year contraction in its net interest income to HK$492 million in the first half of 2006. After adjusting for the funding cost on its fund investments, CKWB's net interest margin stood at 1.76% for the first half of 2006 as compared to 1.81% restated on the same basis for the first half of 2005.

4.123 Non-Interest Income

For the first half of 2006, strong performances by CKWB's core businesses contributed to a significant 39.8% growth in its non-interest income to HK$496 million compared to the same period last year. The growth was mainly derived from a 48.4% increase in gross income from fund investments, a 42.7% increase in corporate loans related fees, a 31.3% increase in retail banking fee and commission income as well as a 110.5% increase in foreign exchange trading gains. The share of non-interest income in its operating profit rose significantly to 50.2% for the first half of 2006 from 38.4% for the corresponding period last year. CKWB will strive to maintain this ratio above 40% for the foreseeable future.

4.124 Operating Expenses

CKWB's operating expenses for the first half of 2006 rose by 6.5% year-on-year, primarily due to the rise in staff-related costs as well as one-time relocation expenses related to the consolidation of its retail and back-office operations in Somerset House in Quarry Bay under its office premise rationalisation plan. Its cost to income ratio fell slightly to 51.5% from 51.6% for the first half of 2005, but was better compared to 55.2% recorded at 2005 year-end. With prudent cost control measures in place, CKWB will strive to further reduce this ratio by the end of 2006.

4.125 Impairment Allowances

CKWB lent conservatively and strived to continually improve its risk management and asset quality. With the credit cycle normalising in the first half of 2006, CKWB recorded a HK$49 million charge for individually assessed loans and a HK$36 million release for collectively assessed loans, resulting in a HK$13 million net charge in loan impairment allowances in the first half of 2006. Including impairment on other assets, CKWB still registered a HK$13 million net charge in impairment allowances, compared to a net release of HK$99 million in the corresponding period last year.

4.13 Asset Quality

4.131 Asset, Loan, and Deposit Sizes

In tandem with the continuous growth in CKWB's core businesses, its asset size has also expanded significantly. As at 30 June 2006, CKWB's total assets were HK$86.3 billion, representing a 5.5% increase from 2005 year-end. Total loans rose 8.1% from 2005 year-end to HK$46.4 billion, driven mainly by a rise in loans for use outside Hong Kong as well as financial sector related loans and trade finance. Total deposits grew by 7.3% from 2005 year-end to HK$66.8 billion.

4.132 Asset Quality Indicators

CKWB reported improvements in its asset quality indicators during the period. Its coverage expanded from 87.8% as at 2005 year-end to 97.4% as at 30 June 2006. Its mortgage delinquency ratio in June 2006 fell further from 0.14% as at 2005 year-end to 0.13%. Its credit card charge-off ratio also fell further from 1.36% as at 2005 year-end to 1.33%.

4.133 Financial Position

As at 30 June 2006, CKWB's unadjusted capital adequacy ratio was 15.2%. Its average liquidity ratio was 45.7%. Its loans to deposits ratio was 69.5% and its loans to total assets ratio was 53.8%.

CITIC Ka Wah Bank's Key Financial Indicators

	30 June 2006	**31 December 2005**
Unadjusted capital adequacy	15.2%	16.4%
Average liquidity	45.7%	51.1%
Loans to deposits	69.5%	69.0%
Loans to total assets	53.8%	52.5%
Impaired loans	1.88%	1.89%
Coverage*	97.4%	87.8%
Loan loss coverage	41.9%	50.9%
Collective assessment coverage	0.54%	0.69%
Mainland loans to total customer advances	14.5%	15.1%

* *Calculated by dividing the sum of individually assessed impairment allowances and collateral of impaired loans by the gross impaired loans*

4.14 Business Development

4.141 Retail Banking Group

CKWB's Retail Banking Group ("RBG") reported strong business momentum in the first half of 2006, with a healthy improvement in net interest income underpinned by the widened Prime-HIBOR spread, and non-interest income growth supported by its continuous programme of new products and services campaigns.

Its key strategic focus during the period was to develop its new mass affluent wealth management service, CITIC*first*. Following its soft launch to existing clients in October 2005, the full marketing launch of CITIC*first* was rolled out in March 2006, and by the end of June, CITIC*first* had attracted over 4,900 customers with average assets under management exceeding HK$3.5 million. The launch of CITIC*first* also boosted CKWB's wealth management income in the first half of 2006, with a 18.4% year-on-year growth in its unit trust income, a 61.8% year-on-year increase in its securities income and a 79.6% year-on-year rise in its equity-linked and foreign currency-linked investment products income. CKWB targets to increase its penetration of the affluent market from 2% to 5% within three years.

In mortgage lending, although CKWB did not match the rate-cutting competition by its peers, its market share of newly drawn residential mortgages grew from 2.6% to 3.6%. This was achieved through the offer of several new mortgage solutions, and was further helped by increased mortgage lending activities in older districts through CKWB's subsidiary, HKCB Finance Limited.

CKWB also experienced good growth momentum in the business segment targeting small-and medium-sized enterprises, registering total loans growth of 35.8% year-on-year, of which trade finance loans increased by 69.9% year-on-year.

4.142 Wholesale Banking Group

CKWB's Wholesale Banking Group ("WBG") took a strategic decision in 2005 to reposition itself from a pure lender to a solutions bank. Its aim is to deepen client relationships by offering value-added solutions, and thereby to broaden its fee income generation capability. This strategy has already yielded encouraging results in the first half of 2006.

Its expanded Syndication Department completed 13 syndicated loans in the first half of 2006, of which it acted as lead arranger for eight of the transactions. Total underwritten amount from these syndicated deals totalled HK$4.3 billion. In March 2006, its Commercial Banking Department launched CITIC Partner, a membership programme for selected corporate clients that contributed to a significant 35.7% growth in trade finance for the first half of 2006. The establishment of CITIC Insurance Brokers Limited in April 2005 enabled CKWB to change its insurance intermediary role from that of an insurance agency to an insurance broker, and it recorded a 15.9% year-on-year increase in total premiums while insurance commission grew by 60.6% year-on-year in just one year's time.

4.143 Treasury and Markets Group

CKWB's Treasury and Markets Group ("TMG") continued to increase its structured product distribution through the bank's own wholesale and retail banking channels, with a total of 16 products launched in the first half of 2006 which attracted total funds of HK$928 million.

Meanwhile, TMG continued to focus on developing its fund investments portfolio. The scale of the portfolio increased from HK$5.4 billion at 2005 year-end to HK$5.9 billion at the end of June 2006; gross revenue generated increased year-on-year by 48.4% to HK$141 million from HK$95 million in the first half of 2005. As a result of rigorous asset allocation and vigilant performance monitoring, the portfolio was able to weather market volatilities in the first half of 2006 and delivered stable and positive returns for the period. As at the end of June 2006, its year-to-date annualised return was 5.0% compared to 5.2% for the same period last year, and its annualised return since inception in April 2004 was at 5.6%.

With a two-year solid performance track record, TMG is preparing to establish fund investments as a CKWB core business, and to extend this expertise to corporate and financial institutional clients in the Greater China region. Capitalising on the launch of China's Qualified Domestic Institutional Investors ("QDII") programme, CKWB is also looking closely into collaborative opportunities with CNCB in this area.

Another strategic focus for TMG going forward is to actively manage down its existing held-to-maturity fixed income investment portfolio by redeploying free funds from maturing securities for various uses, including to support CKWB's loan growth and to manage the bank's liquidity through active money market gapping activities.

4.144 China Banking

CKWB's China Banking business continued to deliver improving performances. The share of profit contribution by China International Finance Company Limited (Shenzhen) ("CIFC") to CKWB in the first half of 2006 significantly increased by more than three times as compared to the corresponding period in 2005. Last year, CIFC received approval from the China Banking Regulatory Commission to offer Renminbi services to corporate customers and non-Mainland citizens. Leveraging on this Renminbi licence, CKWB and CIFC will also be able to extend Renminbi services to all Mainland citizens when China opens up its banking sector at the end of 2006.

The Shanghai branch was granted its derivatives licence in April 2006 and successfully launched its first derivative product in early August 2006. A series of additional derivative products will be introduced in the remainder of 2006. Apart from allowing CKWB to deliver more effective solutions to its existing clients, the new derivatives licence will also allow CKWB to strengthen its collaboration with CNCB in the treasury services area and to leverage new opportunities to develop relevant QDII products and services. Meanwhile, the branch also plans to apply for a Renminbi licence at the end of 2006.

Separately in Beijing, CKWB has received regulatory approval to prepare for the upgrade of its representative office to branch status. The Beijing branch is expected to start business in the latter half of 2006.

CKWB will continue to pursue organic growth of its PRC business through its existing network in the Mainland, and will simultaneously tap brand new opportunities arising from its collaboration with CNCB (Please see 4.145).

4.145 Synergistic Collaboration with CNCB

As the Group progresses to complete its acquisition of a strategic stake in CNCB, CKWB and CNCB will collaborate to more effectively optimise their complementary competencies. Broadly speaking, CKWB's priority will be to leverage its international business experience and expertise as well as its network in the Mainland to provide solutions to its Hong Kong and cross-border clientele on the one hand, and on the other hand to cater to PRC customers with two-way business needs between China, Hong Kong and elsewhere. Meanwhile, apart from focusing on building its leadership position in China, CNCB will work with CKWB to deliver domestic banking, trade and other China-based products and services in joint cross-border one-stop solutions for customers.

CKWB and CNCB have already preliminarily identified areas of business collaboration, some of which have started to bring synergistic benefits.

Both banks have established dedicated liaison teams to identify and tap joint business opportunities, and are planning to systematically develop an integrated product and services platform for their corporate clientele, as well as to build complementary competencies in customer resources, professional know-how, product range, service quality and risk management.

In the area of wholesale banking, the two banks plan to develop a common customer set, for which it will develop compatible risk management and underwriting standards. Specific areas for collaboration may include syndications, joint cross-border financing solutions, international trade settlement and remittances.

In the area of treasury services, the two banks will look at sharing skill sets and expertise as well as building scale in inter national money market management and funds investments.

Training and development will be another area of collaborative opportunities for the two banks, and priority focus will be given to such areas as credit and risk management, private wealth management and bancassurance.

4.2 CITIC International Assets Management Limited ("CIAM")

4.21 Business Performance

CIAM continued its diligence in managing its asset and business portfolio, but the focus in the first half of 2006 has been to consolidate its overall resources and operations as it sought appropriate opportunities to develop its future business. Meanwhile, market volatility also exerted pressures on the performance of its investments activities. For the period ended 30 June 2006, it reported a consolidated operating income of over HK$17 million, which represented a 72.3% decline compared to last year's first-half figure of HK$62 million. A release in net impairment allowances in problem loans and assets amounting to HK$13 million helped to lift its consolidated operating profit before tax to over HK$21 million, which represented a 51.1% decline over the same period last year. Consolidated net profit reported for the period amounted to over HK$17 million, a decline of 51.5% compared to the same period last year of HK$35 million.

4.22 Problem Loans and Assets

Since its establishment in 2002, CIAM has resolved close to 50% of its problem loans and assets portfolio. In the first half of 2006, CIAM continued to make steadfast progress in its efforts to continue to scale down its portfolio and problem loans resolved during the period amounted to HK$7 million. It also sold or signed agreements to sell collateral valued at over HK$25 million. This contributed to aggregate net releases in impairment allowances of over HK$13 million in related problem loans and assets. As at 30 June 2006, the gross book value of its aggregate problem loans amounted to HK$390 million.

4.23 Direct Investment and Structured Loans

During the first half of 2006, CIAM continued to place more focus on strengthening and monitoring its existing investments, thus it did not embark on any new investments or lending activities of this kind. Despite market volatility and impairment charges on certain individually assessed projects, the successful listing of individual investment contributed to an appreciation of over HK$19 million in the original direct investment and structured loan portfolio during the period. In addition, the structured loans also generated over HK$4 million in interest income during the period. In the long run, CIAM is confident that this portfolio will generate more profits and value-added contributions.

4.24 Cooperation with Other Investment Institutions

To pave the way for future business development, CIAM's co-investment entity, Shenzhen Guocheng Century Venture Capital Company Limited, successively increased its investment in quality projects as planned. Meanwhile, the China real estate investment fund jointly developed by CIAM and Bahrain's Shamil Bank B.S.C. has successively received its planned capital injection and has been actively pursuing investments in the latter half of 2006.

4.3 CITIC Capital Holdings Limited ("CCHL")

4.31 Business Performance

The first half of 2006 was a remarkable period for CCHL. The firm underwent a corporate restructuring by transferring its equity capital markets business (comprising Corporate Finance and Brokerage) to CITIC Securities (HK) Company Limited ("CSHK") in May 2006 and repositioned itself as an investment management and advisory firm. Following the restructuring, CCHL is now focused on its core businesses of asset management, private equity, real estate financing, structured finance and financial advisory, and it also keeps a 20% equity stake in CSHK. Its total assets under management reached approximately US$1 billion at the end of June 2006 as a result of the launch of a new property fund (see below) and the growth of its other funds. To reflect its refined business focus, the firm was renamed CITIC Capital Holdings Limited ("CCHL") from CITIC Capital Markets Holdings Limited on 15 June 2006. In the first half of 2006, CCHL achieved a consolidated profit after tax of HK$91 million, a 107.3% increase over the same period in 2005. This sharp rise in profit was largely attributed to the one-time disposal gain arising from the transfer of its equity capital markets business as mentioned above.

4.32 Asset Management

CCHL continued to expand and diversify its investor base in the Asset Management Business both geographically and by investor type. In April, it collaborated with CKWB's RBG and TMG to launch its first structured note linked to its flagship China long/short equity fund.

4.33 Private Equity

CCHL's two existing international private equity funds performed well and continued to pursue private equity investments with a China angle in Japan and the US. With a good deal pipeline in China, CCHL has also started marketing its flagship China private equity fund and has received strong investor interest. It is expected that its first third-party closing will take place before the year-end.

4.34 Real Estate, Structured Finance and Advisory

CITIC Capital China Property Investment Fund, an investment property fund managed by CCHL, raised additional capital and made another investment in the first half of 2006. In March 2006, CCHL teamed up with Vanke, a leading Chinese property developer, to launch a new property development fund, CITIC Capital Vanke China Property Development Fund. The fund has secured a blue chip institutional investor in the US as anchor investor and has already invested in two projects by June 2006.

CCHL also partnered with Allco Finance, a well-known Australian structured finance group, to manage CITIC Allco Investment Limited, a fund that targets mezzanine finance opportunities in China. In addition, CCHL continued to leverage its financial expertise and China knowledge to provide debt related and financial advisory services to its clients.

4.35 CITIC Securities (HK) Company Limited

Activities in the Hong Kong capital markets were buoyant during the first half of 2006, with significant growth in daily market turnover registered by the stock market and in total funds raised through initial public offerings. The equity capital markets businesses of CSHK have benefited from this favourable environment, although challenges of varying degrees were also experienced in terms of increasing competition and narrowing profit margins. Backed by CITIC Securities' leadership position in China's capital market, CSHK is set to solidify the competitive niches of its equity capital markets businesses in Hong Kong and to become a recognised H-share and red chip expert and market leader. CSHK will also collaborate closely with CITIC Securities to leverage on the vast combined resources to focus on business development and tap into other mutually beneficial business areas.

5.0 Progress in Basel II Accord Implementation

Over the past few years, the Group has dedicated efforts to leverage on the implementation of the Basel II Accord to enhance and position its risk management practices as one of its core competencies to strengthen the Group's business capability. With the help of an external consultant, the Group has already put in use an advanced rating system for effective risk ranking and effective risk-based pricing. The Group is well prepared and confident that it complies with the requirements of the Standardised Approach as per the schedule stipulated by the Hong Kong Monetary Authority.

The implementation of the Basel II Accord will have neutral impact on the Group's capital level from the credit risk and market risk perspectives. The Group is also comfortable that its existing capital levels will be sufficient to meet the additional capital requirements arising from operational risk and undrawn commitments.

6.0 Future Development

Having successfully built the foundations in 2005 to capture growth opportunities, the Group's focus this year will be on building its cross-border capabilities. With this in mind, the Group has undertaken a number of important strategic initiatives. The acquisition of a strategic stake in CNCB will improve the Group's ability to provide one-stop financial solutions to Greater China and overseas customers who are active in cross-border business and trade with the PRC. The transaction also underlines the Group's role as the offshore financial flagship of the CITIC Group, and confirms its role as the platform to build the "CITIC" financial services brand internationally.

Going forward, to prepare for the immense opportunities arising from China's formal accession into the World Trade Organisation, the Group plans to closely collaborate with a suitable strategic international partner, and to embark on a journey for overseas expansion that will position CITIC as a leading financial services brand in the global markets.

1. ACCOUNTANTS' REPORT ON CHINA CITIC BANK
(established in the People's Republic of China)

KPMG

8th Floor
Prince's Building
10 Chater Road
Central
Hong Kong

29 December 2006

The Board of Directors
CITIC International Financial Holdings Limited
Suites 1801-1802
Bank of America Tower
12 Harcourt Road
Central
Hong Kong

Dear Sirs,

INTRODUCTION

We set out below our report on the financial information relating to China CITIC Bank (the "Bank") and its subsidiaries (collectively the "Group"), in Sections I to V, including the consolidated balance sheets of the Group as at 31 December 2003, 2004 and 2005, and 30 June 2006, balance sheets of the Bank as at 31 December 2003, 2004 and 2005, and 30 June 2006, and the related consolidated income statements, consolidated statements of changes in equity and consolidated statements of cash flows of the Group for each of the years ended 31 December 2003, 2004 and 2005, and for the six months ended 30 June 2006 (the "Relevant Periods") and the notes thereto (collectively the "Financial Information"), together with the unaudited financial information of the Group including the consolidated income statement, consolidated statement of changes in equity and consolidated statement of cash flows for the six months ended 30 June 2005 and the notes thereto (the "30 June 2005 Corresponding Information"), for inclusion in the circular of CITIC International Financial Holdings Limited ("CIFH") dated 29 December 2006 (the "Circular") in connection with the proposed acquisition of further interest in the Bank.

The Bank is a state-owned financial institution established in the People's Republic of China (the "PRC" or "Mainland China"), excluding for the purpose of this report, the Hong Kong Special Administrative Region of the PRC, or Hong Kong, the Macau Special Administrative Region of the PRC, or Macau and Taiwan. The registered office of the Bank is located at Block C, Fuhua Mansion, 8 Chaoyangmen Beidajie, Dongcheng District, Beijing, the PRC.

The Group has adopted December 31 as their financial year end date.

As a state-owned financial institution, the Bank prepared its financial statements for the years ended 31 December 2003 and 2004 in accordance with the Accounting Standards for Business Enterprises, the Accounting Regulations for Financial Enterprises (jointly issued by the Ministry of Finance of the PRC (the "MOF") and the People's Bank of China (the "PBOC") in 1993) and other relevant regulations issued by the MOF (collectively "Previous PRC GAAP") and prepared its financial statements for the year ended 31 December 2005 in accordance with the Accounting Standards for Business Enterprises, the Accounting Regulations for Financial Enterprises (issued by the MOF in 2001) and other regulations issued by the MOF (collectively named as "PRC GAAP"). These statutory financial statements were audited by Shine Wing Certified Public Accountants, a firm of professional accountants registered in the PRC. The Group also prepared a set of its consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") and its interpretations promulgated by the International Accounting Standards Board ("IASB").

China Investment and Finance Limited ("CIFL") is a principal subsidiary of the Bank during the relevant periods. Throughout the Relevant Periods, Deloitte Touche Tohmatsu have acted as auditors of CIFL.

No financial statements of the Group have been audited subsequent to 30 June 2006.

BASIS OF PREPARATION

The Financial Information, together with the 30 June 2005 Corresponding Information, has been prepared by the Directors of the Bank in accordance with IFRS and its interpretations promulgated by the IASB based on the audited financial statements, or where appropriate, unaudited financial statements of the Group. Adjustments have been made, for the purpose of this report, to restate the statutory financial statements of the Group in accordance with the basis set out in Section V to conform with IFRS and the disclosure requirements of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited.

RESPONSIBILITY

The Directors of the Bank are responsible for preparing the Financial Information which gives a true and fair view. In preparing the Financial Information which gives a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently, that judgments and estimates are made which are prudent and reasonable and that reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on the Financial Information.

BASIS OF OPINION

As a basis for forming an opinion on the Financial Information of the Group, for the purpose of this report, we have carried out appropriate audit procedures in respect of the Financial Information for the relevant periods in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") and have carried out such additional procedures as we considered necessary in accordance with the Auditing Guideline "Prospectuses and the Reporting Accountant" issued by the HKICPA. We have not audited any financial statements of the Group in respect of any period subsequent to 30 June 2006.

An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Financial Information. It also includes an assessment of the significant estimates and judgments made by the Directors in the preparation of the Financial Information, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the Financial Information is free from material misstatement. In forming our opinion, we also evaluated the overall adequacy of the presentation of the Financial Information. We believe that our audit provides a reasonable basis for our opinion.

REVIEW WORK PERFORMED

For the purpose of this report, we have also reviewed the 30 June 2005 Corresponding Information, for which the Directors of the Bank are responsible, in accordance with Statement of Auditing Standard 700 "Engagements to review interim financial reports" issued by the HKICPA.

A review consists principally of making enquiries of Directors and management, and applying analytical procedures to the 30 June 2005 Corresponding Information and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the 30 June 2005 Corresponding Information.

OPINION

In our opinion, for the purpose of this report, all adjustments considered necessary have been made and the Financial Information on the basis set out in Section V, gives a true and fair view of the state of affairs of the Group as at 31 December 2003, 2004 and 2005, and 30 June 2006, of its consolidated results and consolidated cash flows for each of the three years ended 31 December 2003, 2004 and 2005, and for the six months ended 30 June 2006 and the state of the affairs of the Bank as at 31 December 2003, 2004 and 2005, and 30 June 2006, and have been properly prepared in accordance with IFRS.

REVIEW CONCLUSION

On the basis of our review of the 30 June 2005 Corresponding Information which does not constitute an audit, for the purpose of this report, we are not aware of any material modifications that should be made to the unaudited financial information presented for the six months ended 30 June 2005.

I CONSOLIDATED INCOME STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

		Years ended 31 December			Six months ended 30 June	
	Note	**2003**	**2004**	**2005**	**2005** (unaudited)	**2006**
Interest income		12,967	17,795	22,511	10,676	13,327
Interest expense		(5,294)	(7,412)	(9,851)	(4,659)	(5,983)
Net interest income	*3*	7,673	10,383	12,660	6,017	7,344
Fee and commission income	*4*	353	449	608	266	402
Fee and commission expense		(88)	(131)	(190)	(96)	(76)
Net fee and commission income		265	318	418	170	326
Dividend income		–	1	1	–	–
Net profit on disposal of fixed assets		1	11	12	9	9
Net gain from trading securities	*5*	124	34	109	39	16
Net (loss)/gain from investment securities	*6*	(92)	11	(24)	(15)	5
Net gain arising from foreign currency dealing		151	227	266	145	219
Other operating income		246	161	213	58	97
Operating income		8,368	11,146	13,655	6,423	8,016
General and administrative expenses	*7*	(3,940)	(5,451)	(7,104)	(3,282)	(3,943)
Impairment losses charge	*8*	(2,145)	(1,634)	(1,098)	(635)	(944)
Profit before taxation		2,283	4,061	5,453	2,506	3,129
Income tax	*12*	(862)	(1,633)	(2,369)	(1,176)	(1,362)
Net profit		1,421	2,428	3,084	1,330	1,767
Attributable to:						
Equity owner of the Bank		1,419	2,427	3,083	1,330	1,767
Minority interests		2	1	1	–	–
Net profit		1,421	2,428	3,084	1,330	1,767

II CONSOLIDATED BALANCE SHEETS

(Expressed in millions of Renminbi)

	Note	31 December 2003	31 December 2004	31 December 2005	30 June 2006
Assets					
Cash and balances with central bank	14	49,299	54,253	84,453	75,125
Amounts due from banks and other financial institutions	15	31,848	20,899	31,352	23,551
Loans and advances to customers	16	240,539	291,921	358,030	430,006
Investments	17	58,403	110,903	104,416	102,395
Property and equipment	18	6,826	8,090	8,614	8,444
Deferred tax assets	19	5,999	5,424	4,082	3,356
Other assets	20	3,903	3,955	3,655	4,320
Total assets		396,817	495,445	594,602	647,197
Liabilities					
Amounts due to central bank		3,921	300	240	160
Amounts due to banks and other financial institutions	21	37,600	38,190	28,021	27,291
Deposits from customers	22	345,356	435,020	530,573	570,995
Current tax liabilities		914	1,052	1,132	675
Deferred tax liabilities	19	74	–	71	46
Other liabilities and provisions	23	3,550	4,120	5,340	6,575
Subordinated debts/bonds issued	25	–	6,000	6,000	12,000
Total liabilities		391,415	484,682	571,377	617,742
Equity					
Owner's capital	26	14,032	17,790	26,661	31,661
Reserves	26	(8,633)	(7,031)	(3,441)	(2,211)
Minority interests		3	4	5	5
Total equity		5,402	10,763	23,225	29,455
Total equity and liabilities		396,817	495,445	594,602	647,197

II BALANCE SHEETS OF THE BANK

(Expressed in millions of Renminbi)

		31 December			30 June
	Note	**2003**	**2004**	**2005**	**2006**
Assets					
Cash and balances with central bank		49,298	54,248	84,452	75,125
Amounts due from banks and other financial institutions		32,406	21,439	31,813	24,183
Loans and advances to customers		240,375	291,810	357,985	429,849
Investment		57,970	110,421	103,933	101,844
Investments in subsidiaries	*1(c)*	33	33	33	33
Property and equipment		6,801	8,066	8,589	8,420
Deferred tax assets		5,999	5,424	4,082	3,356
Other assets		3,893	3,946	3,647	4,316
Total assets		396,775	495,387	594,534	647,126
Liabilities					
Amounts due to central bank		3,921	300	240	160
Amounts due to banks and other financial institutions		37,600	38,190	28,021	27,291
Deposits from customers		345,356	435,020	530,573	570,995
Current tax liabilities		914	1,052	1,132	674
Deferred tax liabilities		73	–	71	46
Other liabilities and provisions		3,546	4,113	5,332	6,575
Subordinated debts/bonds issued		–	6,000	6,000	12,000
Total liabilities		391,410	484,675	571,369	617,741
Equity					
Owner's capital		14,032	17,790	26,661	31,661
Reserves		(8,667)	(7,078)	(3,496)	(2,276)
Total equity		5,365	10,712	23,165	29,385
Total equity and liabilities		396,775	495,387	594,534	647,126

III CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(Expressed in millions of Renminbi)

	Note	Owner's capital	Capital Reserve	Investment revaluation reserve	Properties revaluation reserve	Retained earnings	Minority interests	Total equity
As at 1 January 2003		6,809	–	295	1,179	(10,591)	1	(2,307)
Capital injection and capitalisation of earnings	26	7,223	–	–	–	(1,223)	–	6,000
Net profit		–	–	–	–	1,419	2	1,421
Net change in fair value of available-for-sale investments		–	–	(9)	–	–	–	(9)
Realised on disposal of available-for-sale investments		–	–	(119)	–	–	–	(119)
Revaluation gain of bank premises		–	–	–	416	–	–	416
Transfer of revaluation gain realised through disposal		–	–	–	(1)	1	–	–
As at 31 December 2003		14,032	–	167	1,594	(10,394)	3	5,402
Capital injection and capitalisation of earnings	26	3,758	–	–	–	(1,258)	–	2,500
Net profit		–	–	–	–	2,427	1	2,428
Net change in fair value of available-for-sale investments		–	–	(174)	–	–	–	(174)
Realised on disposal of available-for-sale investments		–	–	(2)	–	–	–	(2)
Revaluation gain of bank premises		–	–	–	609	–	–	609
Transfer of revaluation gain realised through disposal		–	–	–	(10)	10	–	–
As at 31 December 2004		17,790	–	(9)	2,193	(9,215)	4	10,763
Capital injection and capitalisation of earnings	26	8,871	–	–	–	(271)	–	8,600
Net profit		–	–	–	–	3,083	1	3,084
Net change in fair value of available-for-sale investments		–	–	138	–	–	–	138
Realised on disposal of available-for-sale investments		–	–	52	–	–	–	52
Revaluation gain of bank premises		–	–	–	588	–	–	588
Transfer of revaluation gain realised through disposal		–	–	–	(9)	9	–	–
As at 31 December 2005		26,661	–	181	2,772	(6,394)	5	23,225

	Note	Owner's capital	Capital Reserve	Investment revaluation reserve	Properties revaluation reserve	Retained earnings	Minority interests	Total equity
As at 1 January 2005		17,790	–	(9)	2,193	(9,215)	4	10,763
Net profit		–	–	–	–	1,330	–	1,330
Net change in fair value of available-for-sale investments		–	–	81	–	–	–	81
Realised on disposal of available-for-sale investments		–	–	63	–	–	–	63
Transfer of revaluation gain realised through disposal		–	–	–	(9)	9	–	–
As at 30 June 2005		17,790	–	135	2,184	(7,876)	4	12,237
As at 1 January 2006		26,661	–	181	2,772	(6,394)	5	23,225
Capital injection	26	5,000	–	–	–	–	–	5,000
Net profit		–	–	–	–	1,767	–	1,767
Net change in fair value of available-for-sale investments		–	–	(42)	–	–	–	(42)
Realised on disposal of available-for-sale investments		–	–	3	–	–	–	3
Transfer of revaluation gain realised through disposal		–	–	–	(11)	11	–	–
Appropriation of accrued welfare to capital reserve		–	102	–	–	–	–	102
Profit distribution		–	–	–	–	(600)	–	(600)
As at 30 June 2006		31,661	102	142	2,761	(5,216)	5	29,455

IV CONSOLIDATED CASH FLOW STATEMENT

(Expressed in millions of Renminbi)

		Years ended 31 December			Six months ended 30 June	
Operating activities	*Note*	**2003**	**2004**	**2005**	**2005**	**2006**
					(unaudited)	
Profit before taxation		2,283	4,061	5,453	2,506	3,129
Adjustments for:						
– Revaluation gain on investments and derivatives		(19)	(5)	(83)	(24)	(49)
– Net gain on disposal of fixed assets		(1)	(11)	(12)	(9)	(9)
– Unrealised foreign exchange gain		(24)	(1)	(119)	–	(45)
– Impairment losses		2,145	1,634	1,098	635	944
– Depreciation and amortisation		600	579	681	339	348
– Interest expense on subordinated debts/bonds issued		–	136	298	147	151
		4,984	6,393	7,316	3,594	4,469
Changes in operating assets and liabilities:						
(Decrease)/increase in balances with central bank		(1,792)	(5,774)	(32,797)	(8,641)	10,813
(Increase)/decrease in amounts due from banks and other financial institutions		(2,365)	5,883	(5,979)	(599)	4,111
Increase in loans and advances to customers		(62,504)	(52,971)	(67,164)	(42,218)	(72,839)
Decrease/(increase) in other operating assets		1,288	(9,235)	5,065	4,065	360
Increase/(decrease) in amounts due to central bank		1,596	(3,621)	(60)	–	(80)
Increase/(decrease) in amounts due to banks and other financial institutions		1,173	590	(10,169)	4,826	(730)
Increase in deposits from customers		73,258	89,664	95,553	39,503	40,422
Income tax paid		(915)	(902)	(964)	(945)	(1,093)
Increase in other operating liabilities		360	229	1,549	1,321	1,326
Net cash flows from operating activities		15,083	30,256	(7,650)	906	(13,241)

Investing activities	Note	Years ended 31 December 2003	2004	2005	Six months ended 30 June 2005 (unaudited)	2006
Proceeds from disposal and redemption of investments		69,859	97,221	212,481	146,885	93,016
Proceeds from disposal of property and equipment, land use rights, and other assets		90	385	476	98	272
Payments on acquisition of investments		(83,807)	(123,666)	(207,956)	(138,877)	(97,874)
Payments on acquisition of property and equipment, and land use rights		(562)	(390)	(670)	(104)	(280)
Net cash used in investing activities		(14,420)	(26,450)	4,331	8,002	(4,866)
Financing activities						
Proceeds from capital injection		6,000	2,500	8,600	–	5,000
Interest paid on subordinated debts/bonds issued		–	(14)	(285)	(240)	(253)
Proceeds from debts issue		–	6,000	–	–	6,000
Dividends paid to CITIC Group		–	–	–	–	(600)
Net cash from financing activities		6,000	8,486	8,315	(240)	10,147
Net increase in cash and cash equivalents		6,663	12,292	4,996	8,668	(7,960)
Cash and cash equivalents as at 1 January		46,894	53,621	66,335	66,335	70,130
Effect of exchange rate changes on cash held		64	422	(1,201)	(967)	(11)
Cash and cash equivalents as at 31 December/30 June	*28*	53,621	66,335	70,130	74,036	62,159
Cash flows from operating activities include:						
Interest received		11,111	15,646	19,565	9,247	11,650
Interest paid, excluding interest expense on subordinated debts/bonds issued		(5,158)	(6,863)	(9,141)	(3,910)	(5,158)

V NOTES TO THE FINANCIAL INFORMATION

(Expressed in millions of Renminbi unless otherwise stated)

1. BACKGROUND AND PRINCIPAL ACTIVITIES

(a) Background

The Bank (previously known as "CITIC Industrial Bank") was established on 7 April 1987, as a state-owned financial institution with a registered capital of RMB800 million in accordance with the notice, Guo Ban Han [1987] No. 14 "Approval on the incorporation of CITIC Industrial Bank" issued by the General Office of the State Council and the notice, Yin Fa [1987] No.75 "Notice to the incorporation of CITIC Industrial Bank" issued by the PBOC. The Bank holds the business licence of No.1000001000600 issued by the State Administration for Industry and Commerce and the financial business licence of No. B10611000H0001 issued by the China Banking Regulatory Commission (the "CBRC").

The Bank is wholly owned by the CITIC Group Company (or the "CITIC Group"), which was previously known as China International Trust and Investment Corporation. The name of CITIC Industrial Bank was changed to China CITIC Bank on 2 August 2005.

(b) Principal activities

The principal activities of the Bank and its subsidiaries are the provision of corporate and personal banking services, conducting treasury business and corresponding banking business, and the provision of asset management, entrusted lending and custodian services.

As at 30 June 2006, the Bank had established branches and sub-branches in 18 provinces and municipalities directly under the central government in the PRC.

(c) Details of its subsidiaries

The results and affairs of its subsidiaries have been consolidated into the Financial Information of the Group. The particulars of the Bank's principal subsidiary as at 30 June 2006 are set out below

Name of the company	Place of incorporation and operation	Particulars of the issued and paid up capital	% of ownership directly held by the Bank	Principal Activities
CIFL	Hong Kong	250,000 shares of HK$100 each	95%	Money lending

2. SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of compliance

The Financial Information has been prepared in accordance with IFRS and its interpretations promulgated by the IASB, and the disclosure requirements of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted and consistently applied by the Group in the preparation of the Financial Information is set out below.

All IFRS in issue which are relevant to the Group have been applied, except for IFRS 7 Financial Instruments: Disclosures ("IFRS 7") and the amendment to IAS 1 Presentation of Financial Statements: Capital Disclosures ("IAS 1 Amendment") both of which were issued in August 2005 and are effective for the period beginning 1 January 2007.

IFRS 7 requires more detailed qualitative and quantitative disclosures primarily on fair value information and risk management. The Group has assessed the impact of IFRS 7 and concluded that IFRS 7 would only affect the level of details in the disclosure of the financial statements, and would not have financial impact nor result in a change in the Group's accounting policies.

The Group has concluded that the disclosures required by IAS 1 Amendment on how the Group manages its capital and complies with external capital requirements would not have any financial impact nor result in a change in the Group's accounting policies.

(b) Basis of preparation of the Financial Information

The Financial Information is presented in Renminbi ("RMB"), which is the Group's functional and presentation currency, rounded to the nearest million.

The Financial Information is prepared using the historical cost basis, except for the following assets and liabilities which are stated at their fair value: financial assets and financial liabilities at fair value through profit or loss and available-for-sale assets, except those for which a reliable measure of fair value is not available; and property.

The preparation of the Financial Information in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of policies and the reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and other factors that are believed to be reasonable under the circumstances. The results of such estimates and assumptions form the basis of judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the year in which the estimate is revised if the revision affects only that year, or in the year of the revision and future years if the revision affects both current and future years.

Judgments made by management in the application of IFRS that have significant effect on the Financial Information and estimates with a significant risk of material adjustment in the subsequent period are discussed in Note 36.

(c) Basis of consolidation

The consolidated Financial Information includes the Financial Information of the Bank and its subsidiaries. Subsidiaries are those enterprises controlled by the Bank. Control exists when the Bank has the power, directly or indirectly, to govern the financial and operational policies of an enterprise so as to obtain benefits from its activities. The results and affairs of subsidiaries are included in the consolidated Financial Information from the date that control commences until the date that control ceases.

Investments in controlled subsidiaries are consolidated into the consolidated Financial Information from the date that control commences until the date that control ceases.

Intra-group balances and transactions and any unrealised profits arising from intra-group transactions are eliminated in full in preparing the consolidated Financial Information. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains but only to the extent that there is no evidence of impairment.

Minority interests at the balance sheet date, being the portion of the net assets of subsidiary attributable to equity interests that are not owned by the Bank, whether directly or indirectly through subsidiary, are presented in the consolidated balance sheet and consolidated statement of changes in equity within equity, separately from equity attributable to the equity owner of the Bank. Minority interests in the results of the Group are presented on the face of the consolidated income statement as an allocation of the net profit or loss for the year between minority interests and the equity owner of the Bank.

Where losses applicable to the minority exceed the minority's interest in the equity of a subsidiary, the excess, and any further losses applicable to the minority, are charged against the Group's interest except to the extent that the minority has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Group's interest is allocated all such profits until the minority's share of losses previously absorbed to the Group has been recovered.

In the Bank's balance sheet, investments in subsidiaries are stated at cost less allowances for impairment losses.

(d) Foreign currency translations

Transactions in foreign currencies are translated into Renminbi at the foreign exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the foreign exchange rates ruling at that date. Non-monetary assets and liabilities that are measured at historical cost in a foreign currency are translated using the foreign exchange rates at the date of the transaction. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated using the foreign exchange rates at the date the fair value is determined. When the gain or loss on a non-monetary item is recognised directly in equity, any exchange component of that gain or loss is recognised directly in equity, all other foreign exchange differences arising on settlement and translation of monetary and non-monetary assets and liabilities are recognised in the income statement.

The assets and liabilities of the subsidiaries are translated into Renminbi at the foreign exchange rates ruling at the balance sheet date. The revenue, expenses and cash flows of the subsidiaries are translated into Renminbi at rates approximating the foreign exchange rates ruling at the date of the transaction. Foreign exchange differences arising on translation are recognised directly in equity.

(e) Financial instruments

(i) Recognition and measurement

All financial assets and financial liabilities are recognised in the balance sheet, when and only when, the Group or the Bank, as appropriate, becomes a party to the contractual provisions of the instrument. Financial assets are derecognised on the date when the contractual rights to the cash flows expire or substantially all the risks and rewards of ownership are transferred. Financial liabilities are derecognised on the date when the obligations specified in the contracts are discharged, cancelled or expired.

At initial recognition, all financial assets and financial liabilities are measured at fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include observable market data. Transaction costs for financial assets and financial liabilities at fair value through profit or loss are expensed immediately.

Financial assets and financial liabilities are categorised as follows:

– loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market, other than those that the Group intends to sell immediately or in the near term, and those that are designated as available for sale upon initial recognition, or those where the Group may not recover substantially all of its initial investment, other than because of credit determination, which will be classified as available-for-sale;

– held-to-maturity assets are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intent and ability to hold to maturity, other than those that meet the definition of loans and receivables, or that the Group designated as at fair value through profit or loss or as available-for-sale;

– financial assets and financial liabilities at fair value through profit or loss include trading assets and liabilities of those financial assets and financial liabilities held principally for the purpose of short term profit taking and financial assets and financial liabilities that are designated by the Group upon recognition as at fair value through profit or loss.

  All derivatives not qualified for hedging purposes are included in this category and are carried as assets when their fair value is positive and as liabilities when their fair value is negative; and

– available-for-sale assets are non-derivative financial assets that are designated as available for sale or are not classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity assets.

Subsequent to initial recognition, financial assets and financial liabilities are measured at fair value, without any deduction for transaction costs that may occur on sale or other disposal except for loans and receivables, held-to-maturity financial assets and financial liabilities not designated at fair value through profit or loss, which are measured at amortised cost using the effective interest rate method. Financial assets and financial liabilities that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are stated at cost.

Gains and losses from changes in the fair value of financial instruments at fair value through profit or loss are included in the income statement when they arise. Gains and losses arising from a change in the fair value of available-for-sale assets are recognised directly in equity, except for impairment losses and foreign exchange gains and losses, until the financial asset is derecognised at which time the cumulative gains or losses previously recognised in equity will be recognised in the income statement. For financial assets and liabilities carried at amortised cost, a gain or loss is recognised in the income statement when the financial asset or liability is derecognised or impaired, and through the amortisation process.

(ii) Impairment

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

The carrying amount of assets is reduced through the use of an allowance for impairment losses and a corresponding provision for impairment losses is recognised in the income statement.

Losses expected as a result of future events, no matter how likely, are not recognised because the necessary loss event has not yet occurred.

– Loans and receivables

The impairment allowance of loans and receivables are measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Receivables with a short duration are not discounted if the effect of discounting is immaterial.

The total allowance for credit losses consists of two components: individual impairment allowances and collective impairment allowances.

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

(ii-1) Individual impairment allowances

All loans and advances in the corporate lending portfolios are considered individually significant and assessed individually for impairment. Individually impaired loans and advances are graded at a minimum at substandard (see note 34(a) for the definitions of the loan classification).

Loans and advances which are assessed individually for impairment are evaluated in the light of objective evidence of loss events, for example:

– Significant financial difficulty of the borrower

– A breach of contract, such as default or delinquency in interest payments or principal repayments

– For economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the Group would not otherwise consider

– It becoming probable that the borrower will enter bankruptcy or other financial reorganisation

It may not be possible to identify a single, discrete event that caused the impairment but it may be possible to identify impairment through the combined effect of several events.

The individual impairment allowance is based upon management's best estimate of the present value of the cash flows which are expected to be received discounted at the original effective interest rate. In estimating these cash flows, management makes judgments about the borrower's financial situation and the net realisable value of any underlying collateral or guarantees in favour of the Group. Each impaired asset is assessed on its merits.

(ii-2) Collective impairment allowances

Loans and receivables, which include the following, are assessed for impairment losses on a collective basis:

– All homogeneous groups of loans (representing all the retail loan portfolios) which are all considered not individually significant

– Individually assessed loans with no objective evidence of impairment on an individual basis

The collective impairment loss is assessed after taking into account:

– Historical loss experience in portfolios of similar risk characteristics;

– The emergence period between a loss occurring and that loss being identified; and

– The current economic and credit environments and whether in management's experience these indicate that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience.

The emergence period between a loss occurring and its identification is determined by management based on the historical experience of the markets where the Group operates.

Impairment losses recognised on a collective basis represent an interim step pending the identification of impairment losses on individual assets (which are subject to individual assessment) in the pool of financial assets that are collectively assessed for impairment.

As soon as information is available that specifically identifies objective evidence of impairment on individual assets in a pool, those assets are removed from the pool of financial assets. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment for impairment.

Any subsequent changes to the amounts and timing of the expected future cash flows compared to the prior estimates that can be linked objectively to an event occurring after the write-down, will result in a change in the impairment allowances on loans and receivables and be charged or credited to the income statement.

When the borrower or the guarantor fails to repay the loan principal and interest, and repossessed assets are received by the Group for recovery of the impaired loans, the carrying value of the impaired loans is adjusted, if necessary, to the estimated fair value of the repossessed assets through impairment allowances. The adjusted carrying value of the impaired loans is transferred to repossessed assets, net of impairment allowances.

When there is no reasonable prospect of recovery for the loan and the related interest receivables, the loan and the interest receivables as well as impairment allowances are written off.

– Held-to-maturity assets

For held-to-maturity financial assets, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. (i.e. the effective interest rate computed at initial recognition of these assets). Impairment losses are recognised in the income statement. Held-to-maturity assets with a short duration are not discounted if the effect of discounting is immaterial.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss is reversed through the income statement. A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years.

– Available-for-sale assets

When a decline in the fair value of an available-for-sale asset has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised directly in equity is removed from equity and recognised in the income statement even though the financial asset has not been derecognised.

The amount of the cumulative loss that is removed from equity and recognised in the income statement is the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that financial asset previously recognised in the income statement. For an available-for-sale asset that is not carried at fair value because its fair value cannot be reliably measured, such as an unquoted equity instrument, the amount of any impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed, with the amount of the reversal being recognised in the income statement. Impairment losses recognised in the income statement for an investment in an equity instrument classified as available-for-sale are not reversed through the income statement. Any increase in the fair value of such assets is recognised directly in equity.

(iii) Fair value measurement

The fair value of financial assets is based on their quoted market price in an active market at the valuation date without any deduction for transaction costs. A quoted market price is from an active market where price information is readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and that price information represents actual and regularly occurring market transactions on an arm's length basis. If a quoted market price is not available, the fair value of the financial assets is established using valuation techniques.

Valuation techniques applied include recent arm's length market transactions between knowledgeable and willing parties referenced to the fair value of another instrument that is substantially the same, discounted cash flow analysis and option pricing models. Periodically the Group calibrates the valuation techniques and tests them for validity.

In estimating the fair value of a financial asset and financial liability, the Group considers all factors, including but not limited to, interest rate, credit risk, foreign currency exchange price and market volatility, that are likely to affect the fair value of the financial asset and financial liability.

The Group obtains market data in the same market where the financial instrument was originated or purchased.

(iv) Derivative financial instruments

The Group's derivative financial instruments are principally undertaken in response to customers' needs or for the group's own asset and liability management purposes. The Group also uses derivative financial instruments to hedge its exposure to market risks arising from its investment activities. Derivatives that do not qualify for hedge accounting are accounted for as financial assets and financial liabilities at fair value through profit or loss.

Derivative financial instruments are recognised at fair value. The gain or loss on re-measurement to fair value is recognised immediately in the income statement. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged.

(f) Repurchase and resale agreements

Assets purchased subject to commitments to resell them at future dates are not recognised. The amounts paid are accounted for as balances with central bank, amounts due from banks and other financial institutions or loans and advances to customers depending on the identity of the counterparty.

Assets sold under repurchase agreements continue to be recognised in the balance sheet and are measured in accordance with the accounting policy for these assets. The proceeds from the sale of the assets are reported as amounts due to central bank, banks or other financial institutions depending on the identity of the counterparty.

The difference between the purchase and resale consideration or the sale and repurchase consideration is amortised over the period of the transaction and is included in interest income or expense, as appropriate.

(g) Property and equipment

(i) Cost or revaluation

Property and equipment are stated at cost upon initial recognition.

Subsequent to initial recognition, the Group adopts a revaluation policy to carry all classes of property at revaluation, being their fair value at the date of the revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Equipment is stated at cost less accumulated depreciation and impairment losses.

Increases in the carrying amount arising on revaluation of each property are credited to revaluation reserves in owner's equity. Decreases that offset previous increases of the same asset are charged against revaluation reserves; all other decreases are charged to the income statement.

Construction in progress represents property under construction and is stated at cost less impairment losses. Capitalisation of these costs ceases and the construction in progress is transferred to an appropriate class of property and equipment when the asset is substantially ready for its intended use.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

(ii) Subsequent costs

The Group recognises in the carrying amount of an item of property and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised in the income statement as an expense when incurred.

(iii) Depreciation

Depreciation is calculated to write off the cost or revalued value, less residual value if applicable, of property and equipment and is charged to the income statement on a straight-line basis over the estimated useful lives of each part of an item of property and equipment. The estimated useful lives are as follows:

	Estimated useful lives
Bank premises	30 – 35 years
Computer equipment	3 – 5 years
Others	5 – 10 years

No depreciation is provided in respect of construction in progress.

The residual value, if not insignificant, is reassessed annually.

(iv) Impairment

The carrying amount of property and equipment is reviewed periodically in order to assess whether the recoverable amount has declined below the carrying amount. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The amount of the reduction is recognised in the income statement except for property where it is carried at valuation and the impairment loss does not exceed the revaluation surplus for the same asset, in which case it is treated as a revaluation decrease. The recoverable amount is the greater of the net selling price and value in use.

If in a subsequent period the amount of impairment loss decreases and the decrease can be linked objectively to an event occurring after the write-down, the write-down or allowances are reversed through the income statement. A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in the income statement in prior years.

(v) Disposal and retirement

Gains or losses arising from the disposal or retirement of property and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement on the date of disposal or retirement. In respect of the disposal or retirement of property, any revaluation reserve balance remaining attributable to the relevant asset is transferred to retained earnings and is shown as a movement in reserves.

(h) Land use rights

Land use rights are stated at cost less amortisation. Land use rights are amortised on a straight-line basis over the respective periods of grant.

(i) Repossessed assets

Repossessed assets are initially recognised at the carrying value of the loan principal and interest receivable, net of respective allowances for impairment losses, upon the seizure of these assets in lieu of the rights on the loans and advances and interest receivable. An impairment loss is recognised in the income statement whenever the carrying amount of such an asset exceeds its recoverable amount.

(j) Fiduciary activities

The Group acts in a fiduciary capacity as a custodian, trustee or an agent for customers. Assets held by the Group and the related undertakings to return such assets to customers are excluded from the balance sheet as the risks and rewards of the assets reside with the customers.

Entrusted lending is one of the principal fiduciary activities of the Group. The Group enters into entrusted loan agreements with a number of customers, whereby the customers provide funding (the "entrusted funds") to the Group, and the Group grants loans to third parties (the "entrusted loans") at the instruction of the customers. As the Group does not assume the risks and rewards of the entrusted loans and the corresponding entrusted funds, entrusted loans and funds are recorded as off-balance sheet items at their principal amounts and no impairment assessments are made for these entrusted loans.

(k) *Provisions and contingent liabilities*

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events, are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(l) *Employee benefits*

(i) Employment benefits

Salaries and bonuses, housing benefits and costs for social security benefits are accrued in the year in which the services are rendered by employees of the Group. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) Post employment benefits

Post employment benefits of the Group mainly include retirement benefits and supplementary retirement benefits.

Obligations for contributions to defined contribution retirement schemes are recognised as an expense in the income statement as incurred for current employees.

The Group's obligations in respect of supplementary retirement benefits are calculated by estimating the amount of future benefits that the Group is committed to pay to the employee after their retirement using actuarial techniques. Such benefits are discounted to determine their present values. The discount rate is the yield on PRC government bonds at the balance sheet date, the maturity dates of which approximate to the terms of the Group's obligations. In calculating the Group's obligations, any actuarial gains and losses are recognised in the income statement immediately in the same financial year.

(m) *Income recognition*

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in the income statement as follows:

(i) Interest income

Interest income for all interest-bearing assets is recognised in the income statement using the effective interest method or an applicable floating rate. Interest income includes the amortisation of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

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

The accrual of interest income of a loan where principal or interest of which is overdue over 90 days based on the original terms of the claim is discontinued. Instead, interest will continue to be recognised on the impaired financial assets using the rate of interest used to discount future cash flows ("unwinding of discount") for the purpose of measuring the related impairment loss.

(ii) Fee and commission income

Fee and commission income is recognised in the income statement when the corresponding service is provided.

Origination or commitment fees received by the Group which result in the creation or acquisition of a financial asset are deferred and recognised as an adjustment to the effective interest rate. If the commitment expires without the Group making a loan, the fee is recognised as revenue on expiry.

(iii) Dividend

Dividend is recognised in the income statement on the date when the Group's right to receive payment is established.

(n) Offsetting

Financial assets and financial liabilities are offset and the net amount is reported in the balance sheet when the Group has a legally enforceable right to set off the recognised amounts and the transactions are intended to be settled on a net basis, or realise the asset and settle the liability simultaneously.

(o) Cash and cash equivalents

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise cash, non-restricted balances with central bank, banks and other financial institutions, and short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

(p) Operating lease payments

Payments made under operating leases are recognised in the income statement on a straight-line basis over the terms of the leases.

(q) Income tax

Income tax in the income statement comprises current tax and movements in deferred tax balances. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date. Deferred tax assets also arise from unused tax losses and unused tax credits.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(r) *Profit appropriations*

Profit appropriations are recognised as a liability in the year in which they are approved and declared.

(s) *Related parties*

Parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party, exercise significant influence or joint control over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control, common joint control or common significant influence. Related parties may be individuals and other entities.

(t) *Segment reporting*

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

3. NET INTEREST INCOME

	Years ended 31 December			Six months ended 30 June	
	2003	**2004**	**2005**	**2005**	**2006**
				(unaudited)	
Interest income arises from:					
Balances with central bank	627	853	713	327	410
Amounts due from banks and other financial institutions	506	754	607	286	285
Loans and advances to customers *(note (i))*					
– corporate loans	8,161	11,449	14,482	6,896	8,849
– personal loans	760	1,288	1,972	945	1,103
– discounted bills	1,249	1,488	1,728	660	1,095
Investments in debt securities *(note (ii))*	1,664	1,963	3,009	1,562	1,585
	12,967	17,795	22,511	10,676	13,327
Interest expense arises from:					
Balance due to central bank	(39)	(30)	(12)	(7)	(5)
Amounts due to banks and other financial institutions					
– rediscounted bills	(297)	(379)	(383)	(224)	(307)
– others	(640)	(686)	(646)	(332)	(280)
Deposits from customers	(4,318)	(6,181)	(8,512)	(3,949)	(5,240)
Subordinated debts/bonds issued	–	(136)	(298)	(147)	(151)
	(5,294)	(7,412)	(9,851)	(4,659)	(5,983)
Net interest income	7,673	10,383	12,660	6,017	7,344

Notes:

(i) Interest income arising from loans and advances to customers includes interest income accrued on individually assessed impaired loans and advances to customers of RMB179 million for the six months ended 30 June 2006 (2005: RMB306 million, 2004: RMB350 million; 2003: RMB396 million, six months ended 30 June 2005 (unaudited): RMB170 million), which includes interest income on the unwinding of discount of allowances for loan impairment losses of RMB141 million for the six months ended 30 June 2006 (2005: RMB275 million, 2004: RMB307 million; 2003: RMB346 million, six months ended 30 June 2005 (unaudited): RMB152 million) (Note 16(b)).

(ii) Interest income from investments in debt securities is mainly derived from unlisted investments.

4. FEE AND COMMISSION INCOME

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005	2006
				(unaudited)	
Settlement fees	106	133	166	74	101
Guarantee fees	84	129	162	81	94
Agency fee for underwriting bonds and commission fee from bonds	34	37	113	24	61
Bank card fees	39	58	86	42	77
Commission for underwriting investment funds, agency fee for insurance services and other agency fees	4	24	24	7	20
Others	86	68	57	38	49
Total	353	449	608	266	402

5. NET GAIN FROM TRADING SECURITIES

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005	2006
				(unaudited)	
Net gain/(loss) on debt securities trading	19	(17)	66	37	6
Revaluation gain of investments and derivatives	19	5	83	24	49
Others	86	46	(40)	(22)	(39)
Total	124	34	109	39	16

6. NET (LOSS)/GAIN FROM INVESTMENT SECURITIES

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005	2006
				(unaudited)	
Net (loss)/gain on disposal	(269)	8	53	79	10
Net revaluation gain/(loss) transferred from equity on disposal	177	3	(77)	(94)	(5)
Total	(92)	11	(24)	(15)	5

Net (loss)/gain on disposal primarily relates to available-for-sale securities.

7. GENERAL AND ADMINISTRATIVE EXPENSES

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005	2006
				(unaudited)	
Staff costs					
– salaries, bonuses and staff welfare expenses	894	1,215	1,661	780	895
– contributions to defined contribution retirement schemes	83	107	125	58	80
– housing fund	31	63	67	34	34
– supplementary retirement benefits	–	9	–	–	–
– others	152	187	233	85	147
	1,160	1,581	2,086	957	1,156
Property and equipment expense					
– depreciation	553	548	617	306	312
– rent and property management expenses	314	345	376	169	216
– electronic equipment operating expenses	64	95	141	69	55
– maintenance	64	83	92	36	29
– others	86	96	112	44	56
	1,081	1,167	1,338	624	668
Other general and administrative expenses *(note (i))*	1,131	1,580	2,125	891	1,078
Management fee payable to CITIC Group	–	300	500	300	375
Business tax and surcharges *(note (ii))*	521	792	991	477	630
Amortisation expense	47	31	64	33	36
	3,940	5,451	7,104	3,282	3,943

Notes:

(i) The amount includes auditors' remuneration of RMB2 million for the six months ended 30 June 2006 (2005: RMB2 million, 2004: RMB1 million; 2003: RMB1 million; six months ended 30 June 2005 (unaudited): 1 million).

(ii) Business tax of 5% is levied primarily on interest income from loans and advances to customers, and fee and commission income.

The surcharges, which include education surcharges and city construction tax, are charged at 3% and 7% of business tax paid respectively.

8. IMPAIRMENT LOSSES CHARGE

	Years ended 31 December			Six months ended 30 June	
	2003	**2004**	**2005**	**2005**	**2006**
				(unaudited)	
Impairment losses charge/ (release) on					
– loans and advances to customers	2,136	1,589	1,055	617	863
– bad and doubtful debts	23	16	46	18	28
– investments	–	61	1	–	11
– amount due from banks and other financial institutions	–	(17)	(6)	(3)	–
– others	(14)	(15)	2	3	42
	2,145	1,634	1,098	635	944

9. DIRECTORS' AND SUPERVISORS' EMOLUMENTS

The Board of Directors and the Board of Supervisors of the Bank were set up on 28 December 2005 and no director or supervisor was appointed by the Bank prior to this date. During the period from 28 December 2005 to 31 December 2005, no emoluments were paid or payable to any director or supervisor. The aggregate emolument of Directors' and Supervisors' during the six months ended 30 June 2006 are as follows:

	Six months ended 30 June 2006
Salaries, other emoluments and discretionary bonus	1
Contributions to defined contribution retirement schemes	–
	1

The number of the directors and supervisors whose emoluments fell within the following bands is set out below:

	Six months ended 30 June 2006
RMB0 – RMB1,000,000	3

10. INDIVIDUALS WITH HIGHEST EMOLUMENTS

The aggregate emolument of the five individuals with the highest emoluments for the year ended 31 December 2003, 2004, 2005 and six months ended 30 June 2006 and 2005 (unaudited) are as follows:

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005 (unaudited)	2006
Salaries and other emoluments	1	1	1	1	1
Discretionary bonus	4	5	9	1	1
Contributions to defined contribution retirement schemes	1	1	1	–	–
	6	7	11	2	2

The number of the five highest paid individuals whose emoluments fell within the following bands is set out below:

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005 (unaudited)	2006
RMB0 – RMB1,000,000	1	–	–	5	4
RMB1,000,001 – RMB1,500,000	4	4	–	–	–
RMB1,500,001 – RMB2,000,000	–	1	4	–	–
RMB2,500,001 – RMB3,000,000	–	–	1	–	–

Of the five individuals with the highest emoluments for the six months ended June 30, 2006, the aggregate of the emoluments in respect of one individual whose emoluments is disclosed in Note 9 above.

11. LOANS TO DIRECTORS, SUPERVISORS AND OFFICERS

Loans to the Directors, Supervisor and Officers (and their affiliates) of the Bank as defined under section 161B of the Hong Kong Companies Ordinance during the three years ended 31 December 2003, 2004, 2005 and six months ended 30 June 2006 and 2005 (unaudited) are as follows:

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005 (unaudited)	2006
Aggregate amount of relevant loans outstanding at year end	1	1	1	2	6

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005 (unaudited)	2006
Maximum aggregate amount of relevant loans outstanding during the year	1	1	1	2	6

12. INCOME TAX

(a) Recognised in the income statement

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005 (unaudited)	2006
Current tax					
– Mainland China	1,023	1,041	1,044	368	636
– Hong Kong	1	–	–	–	–
Deferred tax *(Note 19(b))*	(162)	592	1,325	808	726
Income tax	862	1,633	2,369	1,176	1,362

(b) Reconciliation of profit before tax to income tax

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005 (unaudited)	2006
Profit before tax	2,283	4,061	5,453	2,506	3,129
Expected PRC income tax charged at statutory tax rate of 33% *(note (i))*	753	1,340	1,799	827	1,033
Tax impact on non-deductible expenses					
– Staff costs	239	343	485	227	257
– Others *(note (ii))*	78	193	293	235	173
	317	536	778	462	430
Tax impact on non-taxable income					
– Interest income from PRC government bonds	(208)	(230)	(189)	(112)	(92)
– Others	–	(13)	(19)	(1)	(9)
	(208)	(243)	(208)	(113)	(101)
Income tax	862	1,633	2,369	1,176	1,362

Notes:

(i) The provision for PRC income tax of the Group is calculated based on the statutory tax rate of 33% in accordance with the relevant PRC income tax rules and regulations.

(ii) The amounts primarily represent management fee payable to CITIC Group, entertainment expenses, depreciation and amortisation charges exceeding the deductible amount, which are not tax deductible.

13. EARNINGS PER SHARE

Earnings per share is not disclosed as the Bank is not a shareholding company.

14. CASH AND BALANCES WITH CENTRAL BANK

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Cash	1,375	1,459	1,678	2,232
Balances with central bank				
– Statutory deposit reserve funds *(note (i))*	18,369	23,717	29,282	32,735
– Surplus deposit reserve funds *(note (ii))*	29,499	28,595	25,779	26,710
– Fiscal deposits reserve funds	56	482	274	448
– Balances under resale agreement with the PBOC	–	–	27,440	13,000
	47,924	52,794	82,775	72,893
Total	49,299	54,253	84,453	75,125

Notes:

(i) Statutory deposit reserve funds placed with the PBOC were calculated at 7% of eligible RMB customers deposits of the Bank prior to 25 April 2004 and 7.5% thereafter. The Bank was also required to deposit an amount equivalent to 2% of its foreign currency deposits from customers as statutory deposit reserve funds prior to 15 January 2005. This was increased to 3% on 15 January 2005.

The statutory deposit reserve funds are not available for the Group's daily business.

(ii) The surplus deposit reserve funds were maintained with the PBOC for the purposes of clearing.

15. AMOUNTS DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

(a) Analysed by nature

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Deposits	18,035	10,378	17,771	12,906
Money market placements	4,241	4,073	1,104	1,685
Balances under resale agreements	10,085	6,917	12,819	9,302
Gross balances	32,361	21,368	31,694	23,893
Less: Allowances for impairment losses *(Note 15(e))*	(513)	(469)	(342)	(342)
Net balances	31,848	20,899	31,352	23,551

(b) Analysed by original maturity

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Balances maturing				
– less than one month	23,088	16,066	27,191	17,251
– between one month and one year	8,818	4,032	3,483	6,294
– more than one year	455	1,270	1,020	348
Gross balances	32,361	21,368	31,694	23,893

(c) Analysed by geographical location

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Balances with				
– banks in Mainland China	20,792	12,880	20,291	13,723
– other financial institutions in Mainland China *(note)*	3,086	3,043	5,047	3,550
	23,878	15,923	25,338	17,273
Balances with banks outside Mainland China	8,483	5,445	6,356	6,620
Gross balances	32,361	21,368	31,694	23,893

Note: Other financial institutions in Mainland China represent finance companies, investment trust companies and leasing companies which are registered with and under the supervision of the CBRC other than banks in Mainland China, and securities companies and investment fund companies registered with and under the supervision of the China Securities Regulatory Commission.

(d) Analysed by legal form of counterparty

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
Balances with				
– PRC policy banks	2,800	–	2	538
– PRC state-owned banks and other financial institutions	7,803	9,147	16,734	3,747
– PRC joint-stock banks and other financial institutions	13,198	7,190	8,602	12,988
– Foreign-invested banks and other financial institutions	8,560	5,031	6,356	6,620
Gross balances	32,361	21,368	31,694	23,893
Less: Allowances for impairment losses on balances with				
– PRC state-owned banks and other financial institutions	(158)	(144)	(144)	(144)
– PRC joint-stock banks and other financial institutions	(355)	(325)	(198)	(198)
Total allowances for impairment losses	(513)	(469)	(342)	(342)
Net balances	31,848	20,899	31,352	23,551

(e) Movements of allowances for impairment losses

	Years ended 31 December 2003	Years ended 31 December 2004	Years ended 31 December 2005	Six months ended 30 June 2006
As at 1 January	(513)	(513)	(469)	(342)
Reversal for the year	–	17	6	–
Write-offs	–	27	121	–
As at 31 December/30 June	(513)	(469)	(342)	(342)

(f) Amounts due from banks and other financial institutions and allowances

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Gross impaired amounts due from banks and other financial institutions	1,002	604	419	409
Impairment allowances against gross impaired amounts due from banks and other financial institutions *(note (i))*	(513)	(469)	(342)	(342)
Net total	489	135	77	67
Gross impaired amounts due from banks and other financial institutions as a percentage of total amounts due from banks and other financial institutions	3.10%	2.83%	1.32%	1.71%

Note:

(i) The allowances for impairment losses for amounts due from banks and financial institutions are individually assessed.

16. LOANS AND ADVANCES TO CUSTOMERS

(a) Analysed by nature

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Corporate loans	194,517	256,422	282,275	345,074
Personal loans	17,237	31,730	37,834	42,187
Discounted bills	45,559	18,727	50,151	53,701
Gross loans and advances to customers	257,313	306,879	370,260	440,962
Less:				
– Individual impairment allowances	(14,764)	(12,485)	(9,622)	(7,918)
– Collective impairment allowances	(2,010)	(2,473)	(2,608)	(3,038)
Less: Impairment allowances *(Note 16(b))*	(16,774)	(14,958)	(12,230)	(10,956)
Net loans and advances to customers	240,539	291,921	358,030	430,006

(b) Movements of allowances for impairment losses

	Years ended 31 December			Six months ended 30 June
	2003	**2004**	**2005**	**2006**
As at 1 January	(15,360)	(16,774)	(14,958)	(12,230)
Charge for the year	(2,136)	(1,589)	(1,055)	(863)
Unwinding of discount	346	307	275	141
Transfers out	307	73	6	60
Write-offs	69	3,035	3,519	2,017
Recoveries of loans and advances previously written off	–	(10)	(17)	(81)
As at 31 December/30 June	(16,774)	(14,958)	(12,230)	(10,956)

(c) Loans and advances to customers and allowances

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Gross impaired loans and advances to customers *(note (i))*	23,205	19,280	15,311	12,894
Impairment allowances against gross impaired loans				
– individually assessed	(14,764)	(12,485)	(9,622)	(7,918)
– collectively assessed	(165)	(213)	(225)	(298)
Subtotal	(14,929)	(12,698)	(9,847)	(8,216)
Net total	8,276	6,582	5,464	4,678
Gross impaired loans and advances to customers as a percentage of total loans and advances to customers	9.02%	6.28%	4.14%	2.92%

Notes:

(i) Impaired loans and advances include loans for which objective evidence of impairment exists and which have been assessed as bearing significant impairment losses. These loans include loans and advances for which objective evidence of impairment has been identified:

– individually (representing corporate loans and advances which are graded substandard, doubtful or loss); or

– collectively; that is the portfolios of homogeneous loans (representing retail loans and advances which are graded substandard, doubtful or loss).

(ii) The definitions of the loan classification as stated above are described in Note 34(a).

(d) Analysed by legal form of borrowers

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
Corporate loans to				
– Joint-stock enterprises	83,086	119,369	130,157	162,525
– State-owned enterprises	64,826	84,252	100,738	123,188
– Foreign invested enterprises	22,156	27,171	27,040	31,257
– Private enterprises	8,398	11,662	13,636	16,511
– Collectively-controlled enterprises	7,730	6,386	4,480	5,233
– Others	8,321	7,582	6,224	6,360
Subtotal	194,517	256,422	282,275	345,074
Personal loans				
– Home mortgage loans	8,149	17,838	26,246	30,705
– Credit card advances	11	208	447	655
– Others	9,077	13,684	11,141	10,827
Subtotal	17,237	31,730	37,834	42,187
Discounted bills	45,559	18,727	50,151	53,701
Gross loans and advances to customers	257,313	306,879	370,260	440,962
Less: Impairment allowances	(16,774)	(14,958)	(12,230)	(10,956)
Net loans and advances to customers	240,539	291,921	358,030	430,006

17. INVESTMENTS

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
Held-to-maturity debt securities *(Note 17(a))*	30,710	61,370	67,727	78,076
Available-for-sale				
– debt securities *(Note 17(b))*	26,351	40,411	31,564	20,311
– equity investments *(Note 17(c))*	259	338	312	318
	26,610	40,749	31,876	20,629
Debt securities at fair value through profit or loss *(Note 17(d))*	1,083	8,784	4,813	3,690
Total	58,403	110,903	104,416	102,395

(a) Held-to-maturity debt securities

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Issued by:				
Government				
– of Mainland China	15,295	18,022	17,545	14,292
– outside Mainland China	467	467	2,905	2,879
PBOC	1,245	23,883	17,569	29,306
Policy banks				
– in Mainland China	9,543	11,199	13,816	14,855
– outside Mainland China	206	262	274	542
Banks and other financial institutions				
– in Mainland China	1,219	1,268	917	852
– outside Mainland China	1,692	2,925	5,137	5,991
Public sector entities outside Mainland China	223	852	6,759	7,316
Corporate entities				
– in Mainland China	112	1,028	961	900
– outside Mainland China	708	1,464	1,844	1,143
Total	30,710	61,370	67,727	78,076
Listed in Hong Kong	109	83	80	214
Listed outside Hong Kong	1,491	3,639	5,386	5,754
Unlisted	29,110	57,648	62,261	72,108
Total	30,710	61,370	67,727	78,076
Market value of listed securities	1,657	3,763	5,425	5,818

(b) Available-for-sale debt securities

	31 December			30 June
	2003	**2004**	**2005**	**2006**
At fair value and issued by:				
Government				
– of Mainland China	6,492	3,284	2,844	2,490
– outside Mainland China	3,027	8,645	1,936	533
PBOC	498	7,892	8,259	1,784
Policy banks				
– in Mainland China	4,167	2,887	3,057	1,991
– outside Mainland China	829	224	113	411
Banks and other financial institutions				
– in Mainland China	239	199	–	–
– outside Mainland China	8,171	6,285	8,765	8,288
Public sector entities outside Mainland China	747	9,453	2,413	1,362
Corporate entities				
– in Mainland China	129	–	2,690	2,745
– outside Mainland China	2,052	1,542	1,487	707
Total	26,351	40,411	31,564	20,311
Listed in Hong Kong	332	363	352	440
Listed outside Hong Kong	4,592	18,257	7,040	8,188
Unlisted	21,427	21,791	24,172	11,683
Total	26,351	40,411	31,564	20,311

(c) Available-for-sale equity investments

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
At fair value and issued by:				
Banks and other financial institutions				
– in Mainland China	56	56	56	70
– outside Mainland China	125	220	220	248
Corporate entities				
– in Mainland China	49	38	36	–
– outside Mainland China	29	24	–	–
Total	259	338	312	318

All of the above equity investments are unlisted.

(d) Debt securities at fair value through profit or loss

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
At fair value and issued by:				
Government				
– of Mainland China	–	2,128	932	253
– outside Mainland China	–	83	–	–
PBOC	–	2,280	1,589	198
Policy banks in Mainland China	10	3,415	1,400	2,258
Banks and other financial institutions				
– in Mainland China	–	35	37	–
– outside Mainland China	745	511	572	874
Corporate entities				
– in Mainland China	–	41	–	107
– outside Mainland China	328	291	283	–
Total	1,083	8,784	4,813	3,690
Listed outside Hong Kong	183	77	118	121
Unlisted	900	8,707	4,695	3,569
Total	1,083	8,784	4,813	3,690

All of the above securities are held for trading purposes.

18. PROPERTY AND EQUIPMENT

	Bank premises *(Note 18(a))*	Construction in progress	Computer equipment	Others	Total
Cost or valuation:					
As at 1 January 2003	4,944	177	1,136	1,049	7,306
Additions	156	185	196	170	707
Disposals	(40)	–	(18)	(82)	(140)
Transfers	127	(134)	7	–	–
Surplus on revaluation	416	–	–	–	416
Elimination of accumulated depreciation on revaluation	(174)	–	–	–	(174)
As at 31 December 2003	5,429	228	1,321	1,137	8,115
As at 1 January 2004	5,429	228	1,321	1,137	8,115
Additions	1,021	57	68	120	1,266
Disposals	(56)	(2)	(46)	(89)	(193)
Transfers	63	(70)	3	4	–
Surplus on revaluation	609	–	–	–	609
Elimination of accumulated depreciation on revaluation	(171)	–	–	–	(171)
As at 31 December 2004	6,895	213	1,346	1,172	9,626
As at 1 January 2005	6,895	213	1,346	1,172	9,626
Additions	30	121	361	97	609
Disposals	(37)	(1)	(18)	(136)	(192)
Transfers	102	(264)	150	12	–
Surplus on revaluation	588	–	–	–	588
Elimination of accumulated depreciation on revaluation	(223)	–	–	–	(223)
As at 31 December 2005	7,355	69	1,839	1,145	10,408
As at 1 January 2006	7,355	69	1,839	1,145	10,408
Additions	30	11	78	64	183
Disposals	(30)	(2)	(20)	(125)	(177)
Transfers	–	(2)	2	–	–
As at 30 June 2006	7,355	76	1,899	1,084	10,414

	Bank premises *(Note 18(a))*	Construction in progress	Computer equipment	Others	Total
Accumulated depreciation and impairment losses:					
As at 1 January 2003	–	–	(456)	(534)	(990)
Depreciation charges	(175)	–	(208)	(170)	(553)
Disposals	1	–	6	73	80
Elimination on revaluation	174	–	–	–	174
As at 31 December 2003	–	–	(658)	(631)	(1,289)
As at 1 January 2004	–	–	(658)	(631)	(1,289)
Depreciation charges	(172)	–	(214)	(162)	(548)
Disposals	1	–	42	87	130
Elimination on revaluation	171	–	–	–	171
As at 31 December 2004	–	–	(830)	(706)	(1,536)
As at 1 January 2005	–	–	(830)	(706)	(1,536)
Depreciation charges	(224)	–	(283)	(110)	(617)
Disposals	1	–	–	135	136
Elimination on revaluation	223	–	–	–	223
As at 31 December 2005	–	–	(1,113)	(681)	(1,794)
As at 1 January 2006	–	–	(1,113)	(681)	(1,794)
Depreciation charges	(124)	–	(124)	(64)	(312)
Disposals	1	–	16	119	136
As at 30 June 2006	(123)	–	(1,221)	(626)	(1,970)
Net carrying value:					
As at 31 December 2003	5,429	228	663	506	6,826
As at 31 December 2004	6,895	213	516	466	8,090
As at 31 December 2005	7,355	69	726	464	8,614
As at 30 June 2006	7,232	76	678	458	8,444

Note: As at 30 June 2006, the net book value of the Group's bank premises for which the registration procedures for ownership had not been completed was approximately RMB808 million. The Group anticipates that there would be no significant issues and costs in completing such procedures.

(a) Analysed by remaining term of leases

The net carrying value of bank premises at the balance sheet date is analysed by the remaining terms of the leases as follows:

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Long term leases (over 50 years), held in Hong Kong	25	24	24	25
Medium term leases (10-50 years), held in the PRC	5,404	6,871	7,331	7,207
Total	5,429	6,895	7,355	7,232

(b) Valuation

The bank premises of the Group were revalued at 31 December of each year at their open market value by reference to recent market transactions in comparable properties. The valuations were carried out by an independent firm of valuer, China Enterprise Appraisals Co., Ltd.

The revaluation surpluses have been transferred to the properties revaluation reserve of the Group.

Had these bank premises been carried at cost less accumulated depreciation, the carrying amounts would have been RMB4,827 million in 30 June 2006 (2005: RMB4,926 million, 2004: RMB4,980 million; 2003: RMB4,027 million).

19. DEFERRED TAX ASSETS

(a) Analysed by nature

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Deferred tax assets	5,999	5,424	4,082	3,356
Deferred tax liabilities	(74)	–	(71)	(46)
Net balance	5,925	5,424	4,011	3,310

(b) The components of deferred tax assets/(liabilities) recognised in the balance sheet and the movements during the year are as follows:

	Impairment loss on loans and advances to customers	Impairment on repossessed assets	Fair value *Note (i)*	Others	Total deferred tax assets/ (liabilities)
As at 1 January 2003	4,421	409	(126)	976	5,680
Recognised in income statement	277	82	(18)	(179)	162
Recognised in equity	–	–	83	–	83
As at 31 December 2003	4,698	491	(61)	797	5,925
As at 1 January 2004	4,698	491	(61)	797	5,925
Recognised in income statement	(466)	19	12	(157)	(592)
Recognised in equity	–	–	91	–	91
As at 31 December 2004	4,232	510	42	640	5,424
As at 1 January 2005	4,232	510	42	640	5,424
Recognised in income statement	(854)	(23)	(14)	(434)	(1,325)
Recognised in equity	–	–	(88)	–	(88)
As at 31 December 2005	3,378	487	(60)	206	4,011
As at 1 January 2006	3,378	487	(60)	206	4,011
Recognised in income statement	(638)	17	(59)	(46)	(726)
Recognised in equity	–	–	25	–	25
As at 30 June 2006	2,740	504	(94)	160	3,310

Notes:

(i) Unrealised gains or losses arising from fair value adjustments for securities and derivatives are subject to tax when realised.

(ii) The Group did not have significant unrecognised deferred taxation arising at the balance sheet date.

20. OTHER ASSETS

	31 December 2003	2004	2005	30 June 2006
Interest receivable				
– debt securities	666	900	888	857
– loans and advances to customers	518	675	736	843
– others	13	12	26	11
	1,197	1,587	1,650	1,711
Repossessed assets	1,180	1,020	826	793
Positive fair value of derivatives *(Note 33)*	477	301	211	407
Land use rights	217	212	195	192
Intangible assets	22	21	40	44
Management fee prepaid to CITIC Group	–	–	–	375
Others	810	814	733	798
Total	3,903	3,955	3,655	4,320

21. AMOUNTS DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

(a) Analysed by nature

	31 December 2003	2004	2005	30 June 2006
Deposits	31,870	29,661	25,993	23,352
Balances under repurchase agreements	450	6,351	1,280	2,269
Money market takings	5,280	2,178	748	1,670
Total	37,600	38,190	28,021	27,291

(b) Analysed by geographical location

	31 December 2003	2004	2005	30 June 2006
Balances payable on demand				
– Banks in Mainland China	12,349	11,251	8,784	8,470
– Other financial institutions in Mainland China	12,162	8,724	7,906	9,631
	24,511	19,975	16,690	18,101
– Banks outside Mainland China	–	–	2	–
Term deposits				
– Banks in Mainland China	4,070	9,571	5,465	2,329
– Other financial institutions in Mainland China	8,688	8,644	5,864	5,114
	12,758	18,215	11,329	7,443
– Banks outside Mainland China	331	–	–	1,747
Total	37,600	38,190	28,021	27,291

(c) Analysed by legal form of counterparty

	31 December			30 June
	2003	2004	2005	2006
Balances with				
– PRC policy banks	389	799	304	409
– PRC state-owned banks and other financial institutions	1,947	2,078	1,053	1,909
– PRC joint-stock banks and other financial institutions	34,933	35,313	26,662	23,226
– Foreign-invested banks and other financial institutions	331	–	2	1,747
Total	37,600	38,190	28,021	27,291

22. DEPOSITS FROM CUSTOMERS

(a) Analysed by nature

	31 December			30 June
	2003	2004	2005	2006
Demand deposits				
– Corporate customers	159,876	179,106	232,933	225,399
– Personal customers	5,778	6,811	10,110	14,703
	165,654	185,917	243,043	240,102
Time deposits *(i)*				
– Corporate customers	153,176	208,140	226,388	256,994
– Personal customers	26,526	40,963	61,142	73,899
	179,702	249,103	287,530	330,893
Total *(ii)*	345,356	435,020	530,573	570,995

Notes:

(i) The time deposits include notice deposits.

(ii) Deposits from customers include structured deposits, which are designated at fair value through profit or loss. The change in the fair value of these structured deposits is mainly attributable to changes in benchmark interest rates. The carrying amount of structured deposits as at 30 June 2006 was RMB15,153 million (2005: RMB12,656 million, 2004: RMB7,032 million; 2003: RMB772 million).

(b) Analysed by geographical segments

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
Bohai Rim	131,092	167,713	207,676	203,276
Yangtze River Delta	95,109	127,269	146,579	167,804
Pearl River Delta and West Strait	50,914	59,003	72,855	82,486
Central	24,747	32,420	47,214	54,176
Western	31,619	34,250	39,204	40,999
Northeastern	11,121	13,793	16,579	21,317
Head Office	754	572	466	937
Total	345,356	435,020	530,573	570,995

See Note 32(b) for the definitions of geographical segments.

23. OTHER LIABILITIES AND PROVISIONS

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
Interest payable				
– deposits from customers	1,471	1,861	2,303	2,978
– others	23	182	165	61
	1,494	2,043	2,468	3,039
Salaries and welfare payables *(Note 23(a))*	288	576	1,064	840
Supplementary retirement benefit obligations *(Note 24(b))*	36	44	42	41
Settlement accounts	122	177	346	256
Business and other tax payables	158	270	318	369
Negative fair value of derivatives *(Note 33)*	228	314	314	755
Government Bond redemption payable	69	87	143	339
Dormant accounts	17	16	70	35
Payment and collection clearance account	23	39	57	70
Short positions in securities	658	111	–	161
Others	457	443	518	670
Total	3,550	4,120	5,340	6,575

(a) Salaries and welfare payables

Included under salaries and welfare payables, the Group has the following payables to defined contribution retirement schemes at the balance sheet date:

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
As at 31 December/30 June	19	17	18	13

24. RETIREMENT BENEFITS

(a) Defined contribution retirement schemes

In accordance with the labour regulations of the PRC, the Group participates in defined contribution retirement schemes organised by the municipal and provincial governments for its employees in Mainland China. The Group is required to make contributions to the government administered retirement schemes at certain rates of the salaries, bonuses and certain allowances of its employees.

In addition to the above retirement schemes, the Group has established a supplementary defined contribution plan for its qualified employees. The plan is administered by CITIC Group. The Group contributes an equivalent of 3% of qualified employees' salary and bonus to the plan each year, which amounting to RMB17 million for the six months ended 30 June 2006 (2005: RMB25 million, 2004: RMB21 million; 2003: RMB19 million).

The Group is also required to make contributions to Mandatory Provident Fund Scheme for employees working in Hong Kong at the rate set up by the local laws and regulations.

The Group's total contributions during the relevant periods are disclosed in note 7.

The Group has no other material obligations for the payment of its employees' retirement and other post retirement benefits other than the contributions described above and in note 24(b) below.

(b) Supplementary retirement benefit obligations

The Group pays supplementary retirement benefits for all of its qualified retired employees in Mainland China. These benefits cover both employees currently employed and those retired. The amounts recognised in the balance sheets represent the present value of the unfunded obligations.

The Group's obligations in respect of the supplementary retirement benefits at the balance sheet date were reviewed by an independent actuary company, Mercer Human Resources Consulting, using the projected unit credit actuarial cost method. Mercer Human Resources Consulting employs professional actuaries, who are members of Society of Actuaries of the United States of America.

Net liabilities recognised in the balance sheet represent:

		31 December		30 June
	2003	2004	2005	2006
Present value of the obligations	36	44	42	41

Movements in the net liabilities recognised in the balance sheet are as follows:

		Years ended 31 December		Six months ended 30 June
	2003	2004	2005	2006
As at 1 January	39	36	44	42
Payments made	(1)	(1)	(1)	–
Net (income)/expense recognised in the income statement	(2)	9	(1)	(1)
As at 31 December/30 June	36	44	42	41

Net expense/(income) recognised as staff cost/(other income) in the income statement comprises:

	Years ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005 (unaudited)	2006
Current service cost	2	1	1	–	–
Interest cost on obligation	1	1	1	1	1
Actuarial (gain)/loss	(5)	7	(3)	(5)	(2)
Net (income)/expense	(2)	9	(1)	(4)	(1)

Principal actuarial assumptions at the balance sheet date are as follows:

		31 December			30 June
		2003	2004	2005	2006
Discount rate		4.00%	3.00%	3.50%	3.75%

	1995 – 2005	2006 – 2007	2008 – 2010	2011 – 2015	Since 2016
Earnings inflation rate	16.00%	14.00%	12.00%	9.00%	6.50%

25. SUBORDINATED DEBTS/BONDS ISSUED

During the relevant periods, the Group issued the following subordinated debts/bonds upon the approval of the PBOC and the CBRC. The carrying value of the Group's subordinated debts/bonds at the balance sheet date represents:

		31 December			30 June
	Note	2003	2004	2005	2006
Subordinated floating rate debts maturing					
– in June 2010	*(i)*	–	4,778	4,778	4,778
– in July 2010	*(i)*	–	602	602	602
– in September 2010	*(i)*	–	300	300	300
– in June 2010	*(ii)*	–	320	320	320
Subordinated fixed rate bonds maturing					
– in June 2016	*(iii)*	–	–	–	4,000
– in June 2021	*(iv)*	–	–	–	2,000
Total nominal value		–	6,000	6,000	12,000

Notes:

(i) The interest rate per annum on the subordinated floating rate debts is the PBOC one-year fixed deposit rate which is reset on anniversary, plus an interest margin of 2.72%.

(ii) The interest rate per annum on the subordinated floating rate debts is the PBOC one-year fixed deposit rate which is reset on anniversary, plus an interest margin of 2.60%.

(iii) The interest rate per annum on the subordinated fixed rate bonds is 3.75%. The Group has an option to redeem the debts on 22 June 2011. If they are not redeemed early, the interest rate of the debts will increase in June 2011 to 6.75% per annum for the next five years.

(iv) The interest rate per annum on the subordinated fixed rate bonds is 4.12%. The Group has an option to redeem the debts on 22 June 2016. If they are not redeemed early, the interest rate of the debts will increase in June 2016 to 7.12% per annum for the next five years.

26. EQUITY

(a) Owner's capital

	31 December			30 June
	2003	**2004**	**2005**	**2006**
At 1 January	6,809	14,032	17,790	26,661
Capitalisation of retained earnings	1,223	1,258	271	–
Capital injection by cash	6,000	2,500	8,600	5,000
At 31 December/30 June	14,032	17,790	26,661	31,661

The movements in the owner's capital of the Bank during the relevant periods are as follows:

(i) In July 2003, the Bank appropriated RMB1,223 million from retained earnings to capital based on a resolution notice made by CITIC Group. Beijing Zhong Sheng CPA Company Limited verified the capital contribution and issued a capital verification report ([2003] No. 07006) on 3 August 2003.

In December 2003, CITIC Group made a capital injection of RMB6,000 million in cash to the Bank. Shine Wing Certified Public Accountants verified the capital contribution and issued a capital verification report (XYZH/A304047) on 10 February 2004.

The owner's capital of the Bank was RMB14,032 million as at 31 December 2003.

(ii) In December 2004, the Bank appropriated RMB1,258 million from retained earnings to capital based on a resolution notice made by CITIC Group. In addition, CITIC Group made a capital injection of RMB2,200 million and USD 36 million (equivalent to RMB300 million) in cash to the Bank. Shine Wing Certified Public Accountants verified the capital contributions and issued a capital verification report (XYZH/A305032) on 6 January 2005.

The owner's capital of the Bank was RMB17,790 million as at 31 December 2004.

(iii) In December 2005, the Bank appropriated RMB271 million from retained earnings to increase the capital of the Bank based on a resolution notice made by CITIC Group. In addition, CITIC Group made a capital injection of RMB8,600 million in cash to the Bank. Shine Wing Certified Public Accountants verified the capital contributions and issued a capital verification report (XYZH/2005A3012-10) on 11 January 2006.

The owner's capital of the Bank was RMB26,661 million as at 31 December 2005.

(iv) In June 2006, CITIC Group made a capital injection of RMB5,000 million in cash to the Bank. Shine Wing Certified Public Accountant verified the capital contributions and issued a capital verification report (XYZH/2005A3069-1) on 30 June 2006. Related amendments to the commercial registration are in progress.

The owner's capital of the Bank was RMB31,661 million as at 30 June 2006.

(b) Surplus reserves

Surplus reserves consist of statutory surplus reserve, discretionary surplus reserve and statutory public welfare fund.

(i) Statutory surplus reserve and discretionary surplus reserve

The Bank is required to appropriate 10% of its net profit, as determined under PRC GAAP, to a statutory surplus reserve until the reserve balance reaches 50% of the registered capital. After making the appropriation to a statutory surplus reserve, the Bank may also appropriate its net profit to the discretionary surplus reserve upon approval by board of directors.

Subject to the approval of board of directors, statutory and discretionary surplus reserves may be used to make good prior year losses, if any, and may be converted into capital, provided that the balance of statutory surplus reserve after such capitalisation is not less than 25% of the registered capital.

(ii) Statutory public welfare fund

Prior to 1 January 2006, the Bank is required to appropriate 5% of its net profit, as determined under PRC GAAP, to the statutory public welfare fund. In accordance with The Company Law of the PRC (revised in 2005), which was issued on 27 October 2005 and effective from 1 January 2006, the Bank is no longer required to make further appropriation to the statutory public welfare fund with effect from 1 January 2006.

This fund can only be used to purchase capital items for the collective benefit of the Bank's employees such as the construction of dormitories, canteens and other staff welfare facilities.

The fund is non-distributable other than in liquidation.

The Group has adopted the Accounting Regulations for Financial Enterprises (issued by the MOF in 2001) since 1 January 2005. Accordingly, the Group has made retrospective adjustments resulting in a negative balance of the retained earnings as at 31 December 2005. As a result, the surplus reserves previously made have been used to partially set off the negative balance of the retained earnings and have been adjusted to nil.

(c) Investment revaluation reserve

Investment revaluation reserve has been accounted for in accordance with the accounting policies adopted for the measurement of the available-for-sale investments at fair value.

(d) Properties revaluation reserve

Properties revaluation reserve has been made in accordance with the accounting policies adopted for the Group's bank premises.

(e) Capital reserve

In accordance with the notice "Accounting Treatment on Salary Payables for Enterprise Restructuring" (Cai Ban Qi [2006] No.23) issued by MOF on 17 March 2006, RMB102 million of the accrued welfare has been appropriated to the capital reserve.

27. PROFIT APPROPRIATIONS

The Bank appropriated profits of RMB1,223 million, RMB1,258 million and RMB271 million from retained earnings as capital for the years ended 31 December 2003, 2004 and 2005 respectively.

The Bank appropriated profit of RMB600 million to CITIC Group for the six months ended 30 June 2006.

28. NOTES TO CONSOLIDATED CASH FLOW STATEMENT

Cash and cash equivalents

	Years ended 31 December			Six months ended 30 June	
	2003	**2004**	**2005**	**2005** (unaudited)	**2006**
Cash	1,375	1,459	1,678	1,649	2,232
Surplus deposit reserve funds	29,499	28,595	25,779	18,209	26,710
Amounts due from banks and other financial institutions	31,848	20,899	31,352	30,161	23,551
Less:					
– amounts due over three months when acquired	(3,989)	(1,318)	(1,522)	(2,629)	(928)
– balances under resale agreements	(10,085)	(6,917)	(12,819)	(6,209)	(9,302)
	17,774	12,664	17,011	21,323	13,321
Investment securities	4,973	23,617	25,662	32,855	19,896
Total	53,621	66,335	70,130	74,036	62,159

29. COMMITMENTS AND CONTINGENT LIABILITIES

(a) Credit commitments

At any given time the Group has outstanding commitments to extend credit. These commitments take the form of approved loans and credit card limits.

The Group provides financial guarantees and letters of credit to guarantee the performance of customers to third parties.

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers. The Group expects most acceptances to be settled simultaneously with the reimbursement from the customers.

The contractual amounts of commitments and contingent liabilities are set out in the following table by category. The amounts reflected in the table for commitments assume that amounts are fully advanced. The amount reflected in the table for guarantees and letters of credit represents the maximum potential loss that would be recognised at the balance sheet date if counterparties failed completely to perform as contracted.

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Contractual amount				
Loan commitments				
– with an original maturity of under one year	166	25	86	60
– with an original maturity of one year or over	2,126	1,458	2,440	3,920
	2,292	1,483	2,526	3,980
Guarantees and letters of credit	22,298	32,194	36,947	44,149
Acceptances	64,000	94,836	105,783	119,301
Credit card commitments	189	2,232	4,836	5,811
	88,779	130,745	150,092	173,241

These commitments and contingent liabilities have off-balance sheet credit risk. Before the commitments are fulfilled or expire, management assess and make allowances, which are recorded in other liabilities, for any probable losses accordingly. As the facilities may expire without being drawn upon, the total of the contractual amounts is not representative of expected future cash outflows.

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Credit risk weighted amount of contingent liabilities and commitments	35,523	47,787	50,037	54,477

The credit risk weighted amount refers to the amount as computed in accordance with the rules set out by the CBRC and depends on the status of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% of contingent liabilities and commitments. The credit risk weighted amounts stated above have taken into account the effects of bilateral netting arrangements.

There are no relevant standards prescribed by IFRS in calculating the above credit risk weighted amounts.

(b) Capital commitments

The Group had the following authorised capital commitments at the balance sheet date:

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Purchase of property and equipment				
– Contracted for	75	38	10	10

(c) Operating lease commitments

The Group leases certain properties under operating leases, which typically run for an initial period of one to five years and may include an option to renew the lease when all terms are renegotiated. At the balance sheet date, the Group's future minimum lease payments under non-cancellable operating leases for premises were as follows:

		31 December		30 June
	2003	**2004**	**2005**	**2006**
Within one year	200	248	298	272
After one year but within five years	604	675	781	685
After five years	260	407	459	394
Total	1,064	1,330	1,538	1,351

(d) Outstanding litigation and disputes

As at 30 June 2006, the Group was the defendant in certain pending litigations with gross claims of RMB262 million (2005: RMB229 million, 2004: RMB296 million 2003; RMB177 million). The Group considered that no provision was required for these litigations based upon the opinions of the Group's internal and external legal counsel.

(e) Underwriting obligations

At the balance sheet date, the unexpired underwriting commitments of PRC bonds were as follows:

		31 December		30 June
	2003	**2004**	**2005**	**2006**
Underwriting obligations	–	310	550	3,250

(f) Redemption obligations

As an underwriting agent of PRC government bonds, the Group has the responsibility to buy back those bonds sold by it should the holders decide to early redeem the bonds held. The redemption price for the bonds at any time before their maturity date is based on the coupon value plus any interest unpaid and accrued up to the redemption date. Accrued interest payables to the bond holders are calculated in accordance with relevant rules of the MOF and the PBOC. The redemption price may be different from the fair value of similar instruments traded at the redemption date.

The redemption obligations below represent the nominal value of government bonds underwritten and sold by the Group, but not yet matured at the balance sheet date:

		31 December		30 June
	2003	**2004**	**2005**	**2006**
Redemption obligations	9,922	13,302	14,662	18,790

The Group expects the amount of redemption before the maturity date of these government bonds through the Group will not be material.

(g) **Provision against commitments and contingent liabilities**

The Group has assessed and has made provision for any probable outflow of economic benefits in relation to the above commitments and contingent liabilities in accordance with the accounting policies. Except for the provisions made against outstanding litigation and disputes, the Group has not made other provisions in respect of the above commitments and contingent liabilities at the balance sheet date.

30. ASSETS PLEDGED AS SECURITY

The following assets have been pledged as security for bills rediscounting transactions and securities sold under repurchase agreements. The related secured liabilities are recorded as amounts due to central bank, or banks and other financial institutions of approximately similar carrying value at the balance sheet date.

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Available-for-sale debt securities	300	3,930	865	1,599
Discounted bills	6,197	2,223	75	–
Total	6,497	6,153	940	1,599

31. ENTRUSTED LENDING BUSINESS

The Group provides entrusted lending business services to corporations and individuals. All entrusted loans are made under the instruction or at the direction of these entities or individuals and are funded by entrusted funds from them.

For entrusted assets and liabilities and entrusted provident housing fund mortgage business, the Group generally does not take on credit risk in relation to these transactions. The Group acts as an agent to hold and manage these assets and liabilities at the direction of the entrustor and receives fee income for the services provided.

Trust assets are not assets of the Group and are not recognised in the balance sheet. Surplus funding is accounted for as deposits from customers. Income received and receivable for providing these services is included in the income statement as fee income.

At the balance sheet date, the entrusted assets and liabilities were as follows:

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Entrusted loans	6,118	10,145	14,849	18,856
Entrusted funds	6,118	10,145	14,849	18,856

32. SEGMENT REPORTING

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

(a) Business segments

The Group comprises the following main business segments:

Corporate banking

This segment represents the provision of a range of financial products and services to corporations, government agencies and financial institutions. The products and services include corporate loans, trade financing, deposit taking activities, agency services, remittance and settlement services and guarantee services.

Personal banking

This segment represents the provision of a range of financial products and services to individual customers. The products and services comprise personal loans, deposit services and securities agency services.

Treasury business

This segment covers the Group's treasury operations. The treasury enters into inter-bank money market transactions and repurchase transactions, and invests in debt instruments. It also trades in debt instruments, derivatives and foreign currency for its own account. The treasury carries out customer driven transactions on derivatives and foreign currency trading. Its function also includes the management of the Group's overall liquidity position, including the issuance of subordinated debts/bonds.

Others and unallocated

These represent equity investments and head office assets, liabilities, income and expenses that are not directly attributable to a segment or cannot be allocated on a reasonable basis.

	Year ended 31 December 2003				
	Corporate Banking	Personal Banking	Treasury Business	Others and unallocated	Total
External net interest income/(expense)	5,641	396	1,655	(19)	7,673
Internal net interest income/(expense)	721	316	(893)	(144)	–
Net interest income/(expense)	6,362	712	762	(163)	7,673
Net fee and commission income	162	40	17	46	265
Dividend income	–	–	–	–	–
Net gain arising from disposal of fixed assets	–	–	–	1	1
Net (loss)/gain arising from trading securities	(4)	–	128	–	124
Net loss arising from investment securities	–	–	(92)	–	(92)
Net gain/(loss) arising from foreign currencies dealing	82	–	89	(20)	151
Other income	65	1	1	179	246
Operating income	6,667	753	905	43	8,368
General and administrative expenses					
– depreciation and amortisation	(354)	(132)	(31)	(83)	(600)
– others	(2,244)	(594)	(213)	(289)	(3,340)
Impairment losses charge	(2,108)	(33)	–	(4)	(2,145)
Profit/(loss) before tax	1,961	(6)	661	(333)	2,283
Capital expenditure	407	151	39	128	725
	31 December 2003				
Segment assets	246,074	20,243	120,994	9,506	396,817
Segment liabilities	314,515	32,690	42,295	1,915	391,415
Off-balance sheet credit commitments	88,590	189	–	–	88,779

	Year ended 31 December 2004				
	Corporate Banking	Personal Banking	Treasury Business	Others and unallocated	Total
External net interest income/(expense)	7,580	829	1,996	(22)	10,383
Internal net interest income/(expense)	1,043	260	(1,163)	(140)	–
Net interest income/(expense)	8,623	1,089	833	(162)	10,383
Net fee and commission income	222	70	19	7	318
Dividend income	–	–	1	–	1
Net gain arising from disposal of fixed assets	–	–	–	11	11
Net gain arising from trading securities	–	–	34	–	34
Net gain arising from investment securities	–	–	11	–	11
Net gain/(loss) arising from foreign currencies dealing	111	–	120	(4)	227
Other income	83	8	–	70	161
Operating income/(expense)	9,039	1,167	1,018	(78)	11,146
General and administrative expenses					
– depreciation and amortisation	(322)	(140)	(30)	(87)	(579)
– others	(2,941)	(869)	(259)	(803)	(4,872)
Impairment losses charge	(1,553)	(37)	(28)	(16)	(1,634)
Profit/(loss) before tax	4,223	121	701	(984)	4,061
Capital expenditure	167	75	15	57	314
	31 December 2004				
Segment assets	288,292	36,214	161,652	9,287	495,445
Segment liabilities	391,723	48,189	42,646	2,124	484,682
Off-balance sheet credit commitments	128,513	2,232	–	–	130,745

	Year ended 31 December 2005				
	Corporate Banking	Personal Banking	Treasury Business	Others and unallocated	Total
External net interest income/(expense)	9,113	840	2,717	(10)	12,660
Internal net interest income/(expense)	1,310	743	(1,783)	(270)	–
Net interest income/(expense)	10,423	1,583	934	(280)	12,660
Net fee and commission income/(expense)	309	102	57	(50)	418
Dividend income	–	–	1	–	1
Net gain arising from disposal of fixed assets	–	–	–	12	12
Net gain arising from trading securities	–	–	109	–	109
Net loss arising from investment securities	–	–	(24)	–	(24)
Net gain/(loss) arising from foreign currencies dealing	172	–	183	(89)	266
Other income	105	14	–	94	213
Operating income/(expense)	11,009	1,699	1,260	(313)	13,655
General and administrative expenses					
– depreciation and amortisation	(355)	(240)	(33)	(53)	(681)
– others	(3,720)	(1,422)	(367)	(914)	(6,423)
Impairment losses (charge)/release	(1,022)	(33)	2	(45)	(1,098)
Profit/(loss) before tax	5,912	4	862	(1,325)	5,453
Capital expenditure	316	238	30	61	645
	31 December 2005				
Segment assets	352,336	44,611	190,234	7,421	594,602
Segment liabilities	462,199	71,949	34,337	2,892	571,377
Off-balance sheet credit commitments	145,256	4,836	–	–	150,092

	Six months ended 30 June 2005 (unaudited)				
	Corporate Banking	Personal Banking	Treasury Business	Others and unallocated	Total
External net interest income/(expense)	4,120	445	1,459	(7)	6,017
Internal net interest income/(expense)	597	284	(777)	(104)	–
Net interest income/(expense)	4,717	729	682	(111)	6,017
Net fee and commission income	136	47	14	(27)	170
Dividend income	–	–	–	–	–
Net gain arising from disposal of fixed assets	–	–	–	9	9
Net (loss)/gain arising from trading securities	–	–	39	–	39
Net loss arising from investment securities	–	–	(15)	–	(15)
Net gain/(loss) arising from foreign currencies dealing	65	–	68	12	145
Other income	32	–	–	26	58
Operating income	4,950	776	788	(91)	6,423
General and administrative expenses					
– depreciation and amortisation	(178)	(108)	(16)	(37)	(339)
– others	(1,665)	(581)	(165)	(532)	(2,943)
Impairment losses charge	(544)	(73)	3	(21)	(635)
Profit/(loss) before tax	2,563	14	610	(681)	2,506
Capital expenditure	134	76	12	26	248

	Six months ended 30 June 2006				
	Corporate Banking	Personal Banking	Treasury Business	Others and unallocated	Total
External net interest income/(expense)	5,358	408	1,597	(19)	7,344
Internal net interest income/(expense)	650	585	(1,024)	(211)	–
Net interest income/(expense)	6,008	993	573	(230)	7,344
Net fee and commission income	229	73	31	(7)	326
Dividend income	–	–	–	–	–
Net gain arising from disposal of fixed assets	–	–	–	9	9
Net (loss)/gain arising from trading securities	–	–	16	–	16
Net loss arising from investment securities	–	–	5	–	5
Net gain/(loss) arising from foreign currencies dealing	120	–	105	(6)	219
Other income	45	–	–	52	97
Operating income	6,402	1,066	730	(182)	8,016
General and administrative expenses					
– depreciation and amortisation	(177)	(126)	(17)	(27)	(347)
– others	(1,977)	(786)	(211)	(622)	(3,596)
Impairment losses charge	(881)	(24)	(11)	(28)	(944)
Profit/(loss) before tax	3,367	130	491	(859)	3,129
Capital expenditure	108	72	10	16	206

	Six months ended 30 June 2006				
Segment assets	422,474	50,163	167,061	7,499	647,197
Segment liabilities	486,105	89,339	39,697	2,601	617,742
Off-balance sheet credit commitments	167,428	5,811	–	–	173,239

(b) Geographical segments

The Group operates principally in Mainland China with branches and sub-branches located in 18 provinces, autonomous regions and municipalities directly under the central government. The Group's principal subsidiary, CIFL, is registered and operating in Hong Kong.

In presenting information by geographical segment, operating income is allocated based on the location of the branches that generated the revenue. Segment assets and capital expenditure are allocated based on the geographical location of the underlying assets.

Geographical segments, as defined for management reporting purposes, are as follows:

– "Yangtze River Delta" refers to the following areas where tier-1 branches of the Group are located: Shanghai, Nanjing, Suzhou, Hangzhou and Ningbo;

– "Pearl River Delta and West Strait" refers to the following areas where tier-1 branches of the Group are located: Guangzhou, Shenzhen, Dongguan and Fuzhou;

– "Bohai Rim" refers to the following areas where tier-1 branches of the Group are located: Beijing, Tianjin, Dalian, Qingdao, Shijiazhuang and Jinan;

– "Central" region refers to the following areas where tier-1 branches of the Group are located: Hefei, Zhengzhou, Wuhan and Changsha;

– "Western" region refers to the following areas where tier-1 branches of the Group are located: Chengdu, Chongqing, Xi'an and Kunming;

– "Northeastern" region refers to the following areas where tier-1 branch of the Group is located: Shenyang;

– "Head Office" refers to the head office quarter of the Group which is located at Beijing; and

– "Hong Kong" region refers to the Hong Kong Special Administrative Region where the subsidiaries of the Bank are located.

	Year ended 31 December 2003									
	Yangtze River Delta	Pearl River Delta and West Strait	Bohai Rim	Central	Western	North-eastern	Head Office	Hong Kong	Elimination	Total
External net interest income	1,913	901	1,871	360	534	175	1,899	20	–	7,673
Internal net interest income/(expense)	337	332	775	126	54	40	(1,654)	(10)	–	–
Net interest income	2,250	1,233	2,646	486	588	215	245	10	–	7,673
Net fee and commission income	72	24	107	12	15	7	28	–	–	265
Dividend income	–	–	–	–	–	–	–	–	–	–
Net gain/(loss) arising from disposal of fixed assets	1	1	–	–	–	–	(1)	–	–	1
Net gain arising from trading securities	–	–	–	–	–	–	124	–	–	124
Net (loss)/gain arising from investment securities	–	–	–	–	–	–	(95)	3	–	(92)
Net gain/(loss) arising from foreign currencies dealing	51	23	79	5	3	2	(12)	–	–	151
Other income	55	14	48	7	2	1	115	4	–	246
Operating income	2,429	1,295	2,880	510	608	225	404	17	–	8,368
General and administrative expenses										
– depreciation and amortisation	(173)	(52)	(159)	(34)	(45)	(16)	(121)	–	–	(600)
– others	(980)	(557)	(955)	(201)	(242)	(94)	(302)	(9)	–	(3,340)
Impairment losses (charge)/release	(142)	(812)	(912)	(106)	(113)	(63)	3	–	–	(2,145)
Profit/(loss) before tax	1,134	(126)	854	169	208	52	(16)	8	–	2,283
Capital expenditure	93	50	127	174	37	17	227	–	–	725
	31 December 2003									
Segment assets	104,856	62,110	154,270	27,647	30,227	12,077	176,310	774	(171,454)	396,817
Segment liabilities	106,792	70,023	159,954	27,795	30,157	12,186	155,256	706	(171,454)	391,415
Off-balance sheet credit commitments	28,090	5,902	32,767	10,314	6,396	5,121	189	–	–	88,779

	Year ended 31 December 2004									
	Yangtze River Delta	Pearl River Delta and West Strait	Bohai Rim	Central	Western	North-eastern	Head Office	Hong Kong	Elimination	Total
External net interest income	2,998	1,028	2,509	578	777	244	2,218	31	–	10,383
Internal net interest income/(expense)	380	356	909	127	80	41	(1,873)	(20)	–	–
Net interest income	3,378	1,384	3,418	705	857	285	345	11	–	10,383
Net fee and commission income/(expense)	100	24	138	22	20	15	(1)	–	–	318
Dividend income	–	–	–	–	–	–	1	–	–	1
Net gain/(loss) arising from disposal of fixed assets	4	(3)	(3)	–	–	4	9	–	–	11
Net (loss)/gain arising from trading securities	–	–	(1)	–	–	–	35	–	–	34
Net gain arising from investment securities	–	–	–	–	–	–	11	–	–	11
Net gain/(loss) arising from foreign currencies dealing	68	32	125	9	4	2	(13)	–	–	227
Other income	62	14	51	7	5	2	17	3	–	161
Operating income	3,612	1,451	3,728	743	886	308	404	14	–	11,146
General and administrative expenses										
– depreciation and amortisation	(171)	(53)	(154)	(30)	(44)	(14)	(113)	–	–	(579)
– others	(1,443)	(658)	(1,198)	(283)	(319)	(112)	(850)	(9)	–	(4,872)
Impairment losses (charge)/release	(230)	(428)	(570)	(135)	(192)	(82)	3	–	–	(1,634)
Profit/(loss) before tax	1,768	312	1,806	295	331	100	(556)	5	–	4,061
Capital expenditure	15	7	24	8	7	2	251	–	–	314
	31 December 2004									
Segment assets	134,756	72,707	184,773	35,288	38,713	14,125	242,617	767	(228,301)	495,445
Segment liabilities	135,908	80,770	189,462	35,354	38,595	14,224	217,985	685	(228,301)	484,682
Off-balance sheet credit commitments	46,108	7,683	44,129	13,897	9,906	6,790	2,232	–	–	130,745

	Year ended 31 December 2005									
	Yangtze River Delta	Pearl River Delta and West Strait	Bohai Rim	Central	Western	North-eastern	Head Office	Hong Kong	Elimination	Total
External net interest income	3,681	2,011	2,225	972	841	290	2,618	22	–	12,660
Internal net interest income/(expense)	436	(272)	1,530	129	206	77	(2,086)	(20)	–	–
Net interest income	4,117	1,739	3,755	1,101	1,047	367	532	2	–	12,660
Net fee and commission income	142	18	170	37	21	14	16	–	–	418
Dividend income	1	–	–	–	–	–	–	–	–	1
Net gain arising from disposal of fixed assets	9	–	–	1	–	1	1	–	–	12
Net gain/(loss) arising from trading securities	1	1	1	–	–	–	106	–	–	109
Net gain/(loss) arising from investment securities	5	1	1	1	1	–	(33)	–	–	(24)
Net gain/(loss) arising from foreign currencies dealing	90	34	219	19	8	3	(107)	–	–	266
Other income	65	14	65	16	2	2	46	3	–	213
Operating income	4,430	1,807	4,211	1,175	1,079	387	561	5	–	13,655
General and administrative expenses										
– depreciation and amortisation	(134)	(47)	(143)	(39)	(36)	(9)	(273)	–	–	(681)
– others	(1,844)	(854)	(1,493)	(497)	(450)	(139)	(1,139)	(7)	–	(6,423)
Impairment losses release/(charge)	25	(155)	(576)	(281)	(81)	(28)	(2)	–	–	(1,098)
Profit/(loss) before tax	2,477	751	1,999	358	512	211	(853)	(2)	–	5,453
Capital expenditure	203	121	157	30	30	11	93	–	–	645
	31 December 2005									
Segment assets	165,024	83,440	232,848	52,229	46,004	17,797	314,697	693	(318,130)	594,602
Segment liabilities	164,419	88,901	235,735	52,240	45,770	17,803	284,036	603	(318,130)	571,377
Off-balance sheet credit commitments	56,987	13,546	43,773	15,277	9,774	5,899	4,836	–	–	150,092

	Six months ended 30 June 2005 (unaudited)									
	Yangtze River Delta	Pearl River Delta and West Strait	Bohai Rim	Central	Western	North-eastern	Head Office	Hong Kong	Elimination	Total
External net interest income	1,731	681	1,257	455	450	150	1,282	11	–	6,017
Internal net interest income/(expense)	236	113	570	61	38	23	(1,033)	(8)	–	–
Net interest income	1,967	794	1,827	516	488	173	249	3	–	6,017
Net fee and commission income	62	(15)	74	18	11	7	13	–	–	170
Dividend income	–	–	–	–	–	–	–	–	–	–
Net gain/(loss) arising from disposal of fixed assets	13	–	(22)	(2)	(1)	21	–	–	–	9
Net gain arising from trading securities	2	–	–	–	–	–	37	–	–	39
Net (loss)/gain arising from investment securities	–	–	(14)	–	–	–	(1)	–	–	(15)
Net gain/(loss) arising from foreign currencies dealing	28	14	94	7	3	1	(2)	–	–	145
Other income	14	5	20	2	2	1	4	10	–	58
Operating income	2,086	798	1,979	541	503	203	300	13	–	6,423
General and administrative expenses										
– depreciation and amortisation	(87)	(24)	(83)	(21)	(21)	(5)	(98)	–	–	(339)
– others	(789)	(368)	(659)	(207)	(190)	(61)	(666)	(3)	–	(2,943)
Impairment losses release/(charge)	121	(264)	(272)	(188)	(21)	21	(32)	–	–	(635)
Profit/(loss) before tax	1,331	142	965	125	271	158	(496)	10	–	2,506
Capital expenditure	78	47	59	12	12	4	36	–	–	248

	Six months ended 30 June 2006									
	Yangtze River Delta	Pearl River Delta and West Strait	Bohai Rim	Central	Western	North-eastern	Head Office	Hong Kong	Elimination	Total
External net interest income	2,299	821	1,259	631	663	233	1,425	13	–	7,344
Internal net interest income/(expense)	35	185	927	72	8	3	(1,217)	(13)	–	–
Net interest income	2,334	1,006	2,186	703	671	236	208	–	–	7,344
Net fee and commission income	90	28	115	29	14	7	43	–	–	326
Dividend income	–	–	–	–	–	–	–	–	–	–
Net gain/(loss) arising from disposal of fixed assets	1	8	24	(1)	–	(23)	–	–	–	9
Net gain arising from trading securities	9	–	4	–	–	–	3	–	–	16
Net (loss)/gain arising from investment securities	1	–	5	–	–	–	(1)	–	–	5
Net gain/(loss) arising from foreign currencies dealing	55	21	81	15	10	3	34	–	–	219
Other income	59	8	(20)	3	8	1	22	16	–	97
Operating income	2,549	1,071	2,395	749	703	224	309	16	–	8,016
General and administrative expenses										
– depreciation and amortisation	(94)	(29)	(72)	(20)	(21)	(9)	(102)	–	–	(347)
– others	(892)	(457)	(771)	(260)	(243)	(91)	(879)	(3)	–	(3,596)
Impairment losses (charge)/release	(66)	49	(473)	(129)	(198)	(89)	(38)	–	–	(944)
Profit/(loss) before tax	1,497	634	1,079	340	241	35	(710)	13	–	3,129
Capital expenditure	43	34	14	14	20	50	31	–	–	206
	Six months ended 30 June 2006									
Segment assets	217,103	98,513	251,948	66,711	56,034	26,743	297,193	793	(367,841)	647,197
Segment liabilities	216,209	105,326	256,632	66,843	56,047	26,867	256,968	691	(367,841)	617,742
Off-balance sheet credit commitments	67,231	15,531	51,282	16,732	10,349	6,305	5,811	–	–	173,241

33. DERIVATIVES

Derivatives include forward, swap and option transactions undertaken by the Group in the foreign exchange and interest rate markets. The Group, through the operations of its branch network, acts as an intermediary between a wide range of customers for structuring deals to produce risk management products to suit individual customer needs. These positions are actively managed through entering back to back deals with external parties to ensure the Group's net exposures are within acceptable risk levels. The Group also uses derivatives (principally foreign exchange options and swaps, and interest rate swaps) in the management of its own asset and liability portfolios and structural positions.

The following tables provide an analysis of the notional amounts of derivatives of the Group by relevant maturity groupings based on the remaining periods to settlement and the corresponding fair values at the balance sheet date. The notional amounts of the derivatives indicate the volume of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

	Year ended 31 December 2003						
	Notional amounts with remaining life of					Fair values	
	Less than three months	Between three months and one year	Between one year and five years	More than five years	Total	Assets	Liabilities
Interest rate derivatives							
Interest rate swaps	9,814	2,779	4,176	2,586	19,355	44	(92)
Cross-currency swaps	–	243	895	–	1,138	19	(18)
Forward rate agreement	2,295	44,078	–	–	46,373	30	(28)
Interest rate caps	–	–	331	414	745	6	–
Interest rate options	166	–	–	–	166	–	–
	12,275	47,100	5,402	3,000	67,777	99	(138)
Currency derivatives							
Spot	205	–	–	–	205	–	–
Forwards	1,022	640	–	–	1,662	50	(49)
Foreign exchange swaps	7,772	577	–	–	8,349	293	(11)
Currency options	899	67	–	–	966	30	(30)
	9,898	1,284	–	–	11,182	373	(90)
Credit derivatives							
Credit default swap	–	–	414	–	414	5	–
Total						477	(228)
						(Note 20)	*(Note 23)*

	Year ended 31 December 2004						
	Notional amounts with remaining life of					Fair values	
	Less than three months	Between three months and one year	Between one year and five years	More than five years	Total	Assets	Liabilities
Interest rate derivatives							
Interest rate swaps	9,802	3,235	3,208	745	16,990	30	(122)
Cross-currency swaps	215	1,168	724	–	2,107	21	(14)
Forward rate agreement	16,426	26,150	–	–	42,576	31	(33)
Interest rate caps	–	331	–	331	662	6	–
Interest rate options	414	–	–	–	414	6	(3)
	26,857	30,884	3,932	1,076	62,749	94	(172)
Currency derivatives							
Spot	352	–	–	–	352	–	–
Forwards	7,748	925	383	204	9,260	111	(112)
Foreign exchange swaps	6,278	39	–	–	6,317	71	(11)
Currency options	603	102	–	–	705	17	(17)
	14,981	1,066	383	204	16,634	199	(140)
Credit derivatives							
Credit default swap	–	–	414	–	414	3	(2)
Asset swap	–	–	41	–	41	5	–
	–	–	455	–	455	8	(2)
Total						301	(314)
						(Note 20)	*(Note 23)*

	Year ended 31 December 2005						
	Notional amounts with remaining life of					Fair values	
	Less than three months	Between three months and one year	Between one year and five years	More than five years	Total	Assets	Liabilities
Interest rate derivatives							
Interest rate swaps	10,456	8,107	6,280	3,418	28,261	75	(209)
Cross-currency swaps	6	104	84	–	194	3	(3)
Forward rate agreement	1,073	23,628	–	–	24,701	4	(2)
Interest rate options	242	81	–	–	323	–	(5)
	11,777	31,920	6,364	3,418	53,479	82	(219)
Currency derivatives							
Spot	507	–	–	–	507	–	–
Forwards	1,218	10,142	595	126	12,081	84	(66)
Foreign exchange swaps	19,237	707	–	–	19,944	37	(24)
Currency options	272	1,103	–	–	1,375	5	(5)
	21,234	11,952	595	126	33,907	126	(95)
Credit derivatives							
Credit default swap	–	162	242	323	727	2	–
Asset swap	–	40	–	–	40	1	–
	–	202	242	323	767	3	–
Total						211	(314)
						(Note 20)	*(Note 23)*

	Six months ended 30 June 2006						
	Notional amounts with remaining life of					Fair values	
	Less than three months	Between three months and one year	Between one year and five years	More than five years	Total	Assets	Liabilities
Interest rate derivatives							
Interest rate swaps	15,105	15,579	9,913	3,288	43,885	140	(527)
Cross-currency swaps	103	–	62	656	821	19	(19)
Forward rate agreement	4,214	63,754	2,300	–	70,268	28	(20)
Interest rate options	200	96	–	–	296	–	(10)
	19,622	79,429	12,275	3,944	115,270	187	(576)
Currency derivatives							
Spot	3,014	–	–	–	3,014	–	–
Forwards	11,063	13,060	592	94	24,809	151	(148)
Foreign exchange swaps	9,046	1,301	–	–	10,347	66	(31)
Currency options	421	1,173	–	–	1,594	–	–
	23,544	15,534	592	94	39,764	217	(179)
Credit derivatives							
Credit default swap	–	–	280	320	600	3	–
	–	–	280	320	600	3	–
Total						407	(755)
						(Note 20)	*(Note 23)*

The replacement costs and credit risk weighted amounts in respect of these derivatives are as follows. These amounts have taken into account the effects of bilateral netting arrangements.

Replacement costs

	31 December			30 June
	2003	2004	2005	2006
Interest rate derivatives	99	94	82	187
Currency derivatives	373	199	126	217
Credit derivatives	5	8	3	3
	477	301	211	407

Replacement cost represents the cost of replacing all contracts which have a positive value when marked to market. Replacement cost is a close approximation of the credit risk for these derivative contracts as at the balance sheet date.

Credit risk weighted amounts

	31 December			30 June
	2003	2004	2005	2006
Interest rate derivatives	226	127	161	158
Currency derivatives	104	100	116	154
	330	227	277	312

The credit risk weighted amount has been computed in accordance with the rules set by the CBRC, and depends on the status of the counterparty and the maturity characteristics of the instrument.

34. FINANCIAL RISK MANAGEMENT

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

– **Credit risk:** the loss resulting from customer or counterparty default and arising on credit exposure in all forms, including settlement risk.

– **Market risk:** the exposure to market variables such as interest rates, exchange rates and equity markets.

– **Liquidity risk:** where Group is unable to meet its payment obligations when due, or that it is unable, on an ongoing basis, to borrow funds in the market on an unsecured, or even secured basis at an acceptable price to fund actual or proposed commitments.

– **Operational risk:** the risk arising from matters such as non-adherence to systems and procedures or from fraud resulting in financial or reputation loss.

The Group has established policies and procedures to identify and analyse these risks, to set appropriate risk limits and controls, and to constantly monitor the risks and limits by means of reliable and up-to-date management information systems. The Group regularly modifies and enhances its risk management policies and systems to reflect changes in markets, products and best practice risk management processes. Internal auditors also perform regular audits to ensure compliance with policies and procedures.

(a) Credit risk

This category includes credit and counterparty risks from loans and advances, issuer risks from the securities business, counterparty risks from trading activities, and country risks. The Group identifies and manages this risk through its target market definitions, credit approval process, post-disbursement monitoring and remedial management procedures.

In addition to underwriting standards, the principal means of managing credit risk is the credit approval process. The Group has policies and procedures to evaluate the potential credit risk of a particular counterparty or transaction and to approve the transaction.

The Group undertakes ongoing credit analysis and monitoring at several levels. The policies are designed to promote early detection of counterparty, industry or product exposures that require special monitoring. The Risk Management Committee monitors overall portfolio risk as well as individual problem loans, both actual and potential, on a regular basis.

In respect of the loan portfolio, the Group adopts a risk-based loan classification methodology and classifies loans into five categories: normal, special-mention, substandard, doubtful and loss, in accordance with the guidelines issued by the PBOC and the CBRC.

The core definitions of the five categories of loans and advances are set out below:

Normal	Borrowers can honour the terms of their loans. There is no reason to doubt their ability to repay principal and interest in full on a timely basis.
Special mention	Borrowers are able to service their loans currently, although repayment may be adversely affected by specific factors.
Substandard	Borrowers' abilities to service their loans are in question as they cannot rely entirely on normal business revenues to repay principal and interest. Losses may ensue even when collateral or guarantees are invoked.
Doubtful	Borrowers cannot repay principal and interest in full and significant losses will need to be recognised even when collateral or guarantees are invoked.
Loss	Only a small portion or no principal and interest can be recovered after taking all possible measures and exhausting all legal remedies.

The Group applies a series of criteria in determining the classification of loans. The loan classification criteria focuses on a number of factors, including (i) the borrower's ability to repay the loan; (ii) the borrower's repayment history; (iii) the borrower's willingness to repay; (iv) the net realisable value of any collateral; and (v) the prospect for the support from any financially responsible guarantor. The Bank also takes into account the length of time for which payments of principal and interest on a loan are overdue. In general, unsecured loans with principal or interest overdue for more than 90 days and secured loans with principal or interest overdue for more than 180 days are classified at substandard or below.

The Group's retail credit policy and approval process are designed for the fact that there are high volumes of relatively homogeneous, small value transactions in each retail loan category. Because of the nature of retail banking, the credit policies are based primarily on statistical analyses of risks with respect to different products and types of customers. The Group monitors its own and industry experience to determine and periodically revise product terms and desired customer profiles.

The risks involved in credit-related commitments and contingencies are essentially the same as the credit risk involved in extending loan facilities to customers. These transactions are, therefore, subject to the same credit application, portfolio maintenance and collateral requirements as for customers applying for loans.

Concentration of credit risk exists when changes in geographic, economic or industry factors similarly affect the Group's counterparties whose aggregate credit exposure is material in relation to the Group's total exposures. The Group's portfolio of financial instruments is diversified along industry, geographic and product sectors.

(i) Loans and advances to customers analysed by economic sector concentrations at the balance sheet date:

	31 December						30 June	
	2003		2004		2005		2006	
		%		%		%		%
Corporate loans								
– Manufacturing	51,860	20.2	71,247	23.2	81,537	22.0	101,890	23.1
– Production and supply of electric power, gas and water	9,857	3.8	23,825	7.8	26,559	7.2	36,187	8.2
– Wholesale and retail	23,099	9.0	26,023	8.5	29,902	8.1	35,009	7.9
– Transportation, storage and post service	20,882	8.1	22,459	7.3	23,633	6.4	30,633	6.9
– Real Estate	25,313	9.8	27,640	9.0	22,957	6.2	23,823	5.4
– Water, environment and public utility management	10,926	4.3	18,109	5.9	20,811	5.6	26,603	6.0
– Rent and business service	7,370	2.9	14,538	4.7	18,566	5.0	26,357	6.0
– Construction	8,752	3.4	13,980	4.6	15,963	4.3	20,976	4.8
– Public management and social organizations	3,148	1.2	5,748	1.9	7,858	2.1	8,893	2.0
– Financing	6,148	2.4	7,376	2.4	9,188	2.5	5,631	1.3
– Other customers	27,162	10.5	25,477	8.3	25,301	6.8	29,072	6.6
Subtotal	194,517	75.6	256,422	83.6	282,275	76.2	345,074	78,2
Personal loans	17,237	6.7	31,730	10.3	37,834	10.2	42,187	9.6
Discounted bills	45,559	17.7	18,727	6.1	50,151	13.6	53,701	12.2
Gross loans and advances to customers	257,313	100.0	306,879	100.0	370,260	100.0	440,962	100.0
Less: Impairment allowance	(16,774)		(14,958)		(12,230)		(10,956)	
Net loans and advances to customers	240,539		291,921		358,030		430,006	

(ii) Loans and advances to customers analysed by geographical sector risk concentrations at the balance sheet date:

	31 December						30 June	
	2003		2004		2005		2006	
		%		%		%		%
Yangtze River Delta	70,051	27.2	91,672	29.9	120,026	32.4	144,761	32.8
Pearl River Delta and West Strait	46,780	18.2	49,491	16.1	52,885	14.3	62,181	14.1
Bohai Rim (including Head Office)	89,770	34.9	100,195	32.6	115,706	31.2	129,081	29.3
Central	21,396	8.3	27,477	9.0	36,255	9.8	44,356	10.1
Western	21,075	8.2	27,943	9.1	32,029	8.7	42,127	9.6
Northeastern	7,961	3.1	9,880	3.2	13,207	3.6	18,299	4.1
Hong Kong	280	0.1	221	0.1	152	–	157	–
Gross loans and advances to customers	257,313	100.0	306,879	100.0	370,260	100.0	440,962	100.0
Less: Impairment allowances	(16,774)		(14,958)		(12,230)		(10,956)	
Net loans and advances to customers	240,539		291,921		358,030		430,006	

See Note 32(b) for the definitions of geographical segments.

(b) *Market risk*

Market risk arises on all market risk sensitive financial instruments, including securities, foreign exchange contracts, equity and derivative instruments, as well as from balance sheet or structural positions. Market risk arises from adverse movement in market rates including interest rates, foreign exchange rates and stock prices etc. as well as their volatility. Market risk would arise from both the Group's trading and non-trading business. The objective of market risk management is to avoid excessive exposure of earnings and equity to loss and to reduce the Group's exposure to the volatility inherent in financial instruments.

The Financial Planning Department is responsible for formulating the Group's market risk management policies, and managing its overall market risk exposures. The Financial Planning Department sets the trigger and limit on the interest rates and foreign exchange rates of the Group, articulates periodical reviews and decide on future business strategy with respect to interest rates and foreign exchange rates. The Financial Planning Department has delegated the responsibility for ongoing trading book market risk to the Treasury Department. The Treasury Department manages the Group's RMB and foreign currency investment portfolios, conducts proprietary and customer-driven trades, implements market risk management policies and rules and performs daily identification, measurement, assessment and control of risks.

The use of derivatives for proprietary trading and their sale to customers as risk management products is an integral part of the Group's business activities. These instruments are also used to manage the Group's own exposures to market risk as part of its asset and liability management process. The principal derivative instruments used by the Group are interest and foreign exchange rate related contracts, which are primarily over-the-counter derivatives.

Sensitivity analysis and foreign currency exposure analysis are the key methods used by the Group to measure and monitor the market risk of its trading business with Value-at-Risk ("VaR") as a supplementary method. Gap analysis is the key method used by the Group to monitor the market risk of its non-trading business.

The Group applies a wide range of sensitivity analyses to assess the potential impact on the Group's earnings as a result of a set of forward-looking movements in market prices and the result is regularly reviewed.

Foreign currency exposure analysis is a method to measure the effect on the Group's net earnings by foreign exchange rate changes. The Group calculates individual foreign currency exposure for both net spot and net forward positions. All the individual foreign currency exposures are then aggregated to form an overall exposure. Foreign currency exposure limits are set for individual currencies as well as the overall level. The Group also distinguishes between trading and non-trading foreign currency exposures.

VaR is a technique that estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence. The Group's Treasury Department calculates interest rate VaR using historical movement in market rates and prices, at 99% confidence level, with a 10-day holding period on its foreign currency denominated investments.

Gap analysis is a technique to project future cash flows in order to quantify the differences, for a range of future dates, between assets and liabilities.

Currently, the Group is upgrading its present market risk management information system to monitor its overall market risk through new Assets and Liability Management (ALM) and Fund Transfer Pricing (FTP) systems.

The Group does not actively trade in financial instruments and, in the opinion of the directors, the market risk related to trading activities to which the Group is exposed is not material. Accordingly, no quantitative market risk disclosures have been prepared.

(c) Interest rate risk

The Group's interest rate positions arise from treasury and commercial banking activities. Interest rate risk primarily results from the timing differences in the repricing of interest-bearing assets, liabilities and commitments. The Group sets sensitivity related limits to manage interest rate risk arising from trading business.

The following tables indicate the effective interest rates for the year and the expected next repricing dates (or maturity dates whichever are earlier) for the assets and liabilities at the balance sheet date.

			31 December 2003				
	Effective interest rate *(note (i))*	Total	Non-interest bearing	Less than three months	Between three months and one year	Between one and five years	More than five years
Assets							
Cash and balances with central bank	1.91%	49,299	1,375	47,924	–	–	–
Amounts due from banks and other financial institutions	1.97%	31,848	–	24,265	7,128	455	–
Loans and advances to customers *(note (ii))*	4.66%	240,539	–	102,908	136,216	1,415	–
Investments	3.38%	58,403	–	15,122	13,128	17,216	12,937
Others	–	16,728	16,728	–	–	–	–
Total assets		396,817	18,103	190,219	156,472	19,086	12,937
Liabilities							
Amounts due to central bank	3.16%	3,921	–	3,921	–	–	–
Amounts due to banks and other financial institutions	1.78%	37,600	–	35,973	373	788	466
Deposits from customers	1.55%	345,356	3,056	263,203	62,933	10,450	5,714
Others	–	4,538	4,538	–	–	–	–
Total liabilities		391,415	7,594	303,097	63,306	11,238	6,180
Asset-liability gap		5,402	10,509	(112,878)	93,166	7,848	6,757

	Effective interest rate *(note (i))*	Total	Non-interest bearing	31 December 2004 Less than three months	Between three months and one year	Between one and five years	More than five years
Assets							
Cash and balances with central bank	1.80%	54,253	1,459	52,794	–	–	–
Amounts due from banks and other financial institutions	2.20%	20,899	–	18,296	1,333	1,270	–
Loans and advances to customers *(note (ii))*	4.85%	291,921	–	134,079	155,869	1,973	–
Investments	3.19%	110,903	–	44,721	31,224	21,913	13,045
Others	–	17,469	17,469	–	–	–	–
Total assets		495,445	18,928	249,890	188,426	25,156	13,045
Liabilities							
Amounts due to central bank	3.20%	300	–	300	–	–	–
Amounts due to banks and other financial institutions	1.72%	38,190	–	30,998	5,091	1,312	789
Deposits from customers	1.66%	435,020	5,182	336,007	75,541	12,815	5,475
Subordinated debts/ bonds issued	4.96%	6,000	–	6,000	–	–	–
Others	–	5,172	5,172	–	–	–	–
Total liabilities		484,682	10,354	373,305	80,632	14,127	6,264
Asset-liability gap		10,763	8,574	(123,415)	107,794	11,029	6,781

				31 December 2005			
	Effective interest rate *(note (i))*	Total	Non-interest bearing	Less than three months	Between three months and one year	Between one and five years	More than five years
Assets							
Cash and balances with central bank	1.53%	84,453	1,677	82,776	–	–	–
Amounts due from banks and other financial institutions	2.19%	31,352	–	27,084	3,248	1,020	–
Loans and advances to customers *(note (ii))*	5.18%	358,030	–	158,629	197,656	1,745	–
Investments	3.05%	104,416	–	50,201	17,864	23,060	13,291
Others	–	16,351	16,351	–	–	–	–
Total assets		594,602	18,028	318,690	218,768	25,825	13,291
Liabilities							
Amounts due to central bank	4.33%	240	–	240	–	–	–
Amounts due to banks and other financial institutions	1.87%	28,021	–	22,515	692	2,810	2,004
Deposits from customers	1.86%	530,573	18,929	416,860	78,392	11,916	4,476
Subordinated debts/ bonds issued	4.96%	6,000	–	6,000	–	–	–
Others	–	6,543	6,543	–	–	–	–
Total liabilities		571,377	25,472	445,615	79,084	14,726	6,480
Asset-liability gap		23,225	(7,444)	(126,925)	139,684	11,099	6,811

				30 June 2006			
	Effective interest rate *(note (i))*	Total	Non-interest bearing	Less than three months	Between three months and one year	Between one and five years	More than five years
Assets							
Cash and balances with central bank	1.43%	75,125	2,232	72,893	–	–	–
Amounts due from banks and other financial institutions	2.84%	23,551	–	21,119	2,084	348	–
Loans and advances to customers *(note (ii))*	5.15%	430,006	–	184,300	243,296	2,347	63
Investments	3.07%	102,395	–	38,242	28,058	22,268	13,827
Others		16,120	16,120	–	–	–	–
Total assets		647,197	18,352	316,554	273,438	24,963	13,890
Liabilities							
Amounts due to central bank	5.52%	160	–	160	–	–	–
Amounts due to banks and other financial institutions	2.18%	27,291	–	24,706	1,455	387	743
Deposits from customers	1.94%	570,995	3,000	436,021	115,625	12,795	3,554
Subordinated debts/bonds issued	4.85%	12,000	–	6,000	–	–	6,000
Others		7,296	7,296	–	–	–	–
Total liabilities		617,742	10,296	466,887	117,080	13,182	10,297
Asset-liability gap		29,455	8,056	(150,333)	156,358	11,781	3,593

Notes:

(i) Effective interest rate represents the ratio of interest income/expense to average interest bearing assets/liabilities.

(ii) For loans and advances to customers, the above "Less than three months" category includes overdue amounts (net of allowances for impairment losses) of RMB7,378 million as at 30 June 2006 (2005: RMB7,718 million, 2004: RMB7,724 million; 2003: RMB8,219 million). Overdue amounts represent loans, of which the whole or part of the principals was overdue, or interest was overdue for more than 90 days but for which principal was not yet due.

(d) *Currency risk*

The Group's foreign currency positions arise from foreign exchange dealing, commercial bank operations and foreign currency capital related structural exposures. The foreign currency exposures arising in branch daily operations are aggregated to Treasury Department through back to back transactions.

The Treasury Department manages the currency risk within the limits approved by the Financial Planning Department by closing the exposure positions through external market transactions.

The Group manages other currency risk by spot and forward foreign exchange transactions and matching its foreign currency denominated assets with corresponding liabilities in the same currencies.

The exposures at the balance sheet date were as follows:

	31 December 2003			
	RMB	*USD*	*Others*	*Total*
Assets				
Cash and balances with central bank	47,410	1,668	221	49,299
Amounts due from banks and other financial institutions	22,461	8,480	907	31,848
Loans and advances to customers	228,794	10,342	1,403	240,539
Investments	37,468	18,849	2,086	58,403
Others	13,705	2,545	478	16,728
Total assets	349,838	41,884	5,095	396,817
Liabilities				
Amounts due to central bank	3,921	–	–	3,921
Amounts due to banks and other financial institutions	29,776	3,798	4,026	37,600
Deposits from customers	309,239	30,196	5,921	345,356
Others	4,338	161	39	4,538
Total liabilities	347,274	34,155	9,986	391,415
Net on-balance sheet position	2,564	7,729	(4,891)	5,402
Credit commitments	76,069	9,806	2,904	88,779
Derivatives *(note)*	(83)	(3,737)	4,096	276

The exposures at the balance sheet date were as follows:

	31 December 2004			
	RMB	*USD*	*Others*	*Total*
Assets				
Cash and balances with central bank	52,052	1,954	247	54,253
Amounts due from banks and other financial institutions	14,564	3,261	3,074	20,899
Loans and advances to customers	279,503	10,533	1,885	291,921
Investments	75,752	24,052	11,099	110,903
Others	15,912	1,310	247	17,469
Total assets	437,783	41,110	16,552	495,445
Liabilities				
Amounts due to central bank	300	–	–	300
Amounts due to banks and other financial institutions	30,272	2,845	5,073	38,190
Deposits from customers	391,516	26,759	16,745	435,020
Subordinated debts/bonds issued	6,000	–	–	6,000
Others	2,445	2,692	35	5,172
Total liabilities	430,533	32,296	21,853	484,682
Net on-balance sheet position	7,250	8,814	(5,301)	10,763
Credit commitments	114,192	12,994	3,559	130,745
Derivatives *(note)*	–	(3,328)	3,371	43

The exposures at the balance sheet date were as follows:

	31 December 2005			
	RMB	*USD*	*Others*	*Total*
Assets				
Cash and balances with central bank	81,554	2,485	414	84,453
Amounts due from banks and other financial institutions	14,394	6,129	10,829	31,352
Loans and advances to customers	339,589	17,045	1,396	358,030
Investments	69,327	28,266	6,823	104,416
Others	14,405	1,848	98	16,351
Total assets	519,269	55,773	19,560	594,602
Liabilities				
Amounts due to central bank	240	–	–	240
Amounts due to banks and other financial institutions	23,756	2,237	2,028	28,021
Deposits from customers	463,068	43,958	23,547	530,573
Subordinated debts/bonds issued	6,000	–	–	6,000
Others	6,523	–	20	6,543
Total liabilities	499,587	46,195	25,595	571,377
Net on-balance sheet position	19,682	9,578	(6,035)	23,225
Credit commitments	129,258	16,456	4,378	150,092
Derivatives *(note)*	699	(6,304)	5,707	102

The exposures at the balance sheet date were as follows:

	30 June 2006			
	RMB	*USD*	*Others*	*Total*
Assets				
Cash and balances with central bank	72,784	2,032	309	75,125
Amounts due from banks and other financial institutions	14,401	7,686	1,464	23,551
Loans and advances to customers	408,821	19,571	1,614	430,006
Investments	69,481	26,970	5,944	102,395
Others	15,243	642	235	16,120
Total assets	580,730	56,901	9,566	647,197
Liabilities				
Amounts due to central bank	160	–	–	160
Amounts due to banks and other financial institutions	19,943	5,820	1,528	27,291
Deposits from customers	519,540	43,728	7,727	570,995
Subordinated debts/bonds issued	12,000	–	–	12,000
Others	6,522	691	83	7,296
Total liabilities	558,165	50,239	9,338	617,742
Net on-balance sheet position	22,565	6,662	228	29,455
Credit commitments	146,695	21,636	4,910	173,241
Derivatives *(note)*	2,724	(2,379)	409	754

Note:

The derivatives represent the net notional amount of currency derivatives, including undelivered foreign exchange spot, foreign exchange forward, foreign exchange swap and currency option.

(e) *Liquidity risk*

The purpose of liquidity management is to ensure sufficient cash flows for the Group to meet all financial commitment and to capitalise on opportunities for business expansion. This includes the Group's ability to meet deposit withdrawals either on demand or at contractual maturity, to repay borrowings in full amounts as they mature, or to meet other obligations for payments, to comply with the statutory liquidity ratio, and to make new loans and investments as opportunities arise.

Liquidity is managed on a daily basis according to the Group's liquidity objectives by the Treasury under the direction of the Asset and Liability Committee. It is responsible for ensuring that the Group has adequate liquidity for RMB and foreign currency operations.

The Group manages liquidity risk by holding sufficient liquid assets (e.g. deposits at PBOC, other short term funds and securities) of appropriate quality to ensure that short term funding requirements are covered within prudent limits. Adequate standby facilities are maintained to provide strategic liquidity to meet unexpected and material demand for payments in the ordinary course of business.

The Group regularly stress tests its liquidity position.

In terms of measuring liquidity risk, the Group principally uses liquidity gap analysis. Different scenarios are applied to assess the impact on liquidity for proprietary trading and client businesses.

The following tables provide an analysis of assets and liabilities of the Group into relevant maturity groupings based on the remaining periods to repayment at the balance sheet date.

	31 December 2003						
	Overdue/ repayable on demand	**Less than three months**	**Between three months and one year**	**Between one and five years**	**More than five years**	**Undated**	**Total**
Assets							
Cash and balances with central bank *(note (i))*	30,874	–	–	–	–	18,425	49,299
Amounts due from banks and other financial institutions	16,419	7,846	7,128	455	–	–	31,848
Loans and advances to customers *(note (ii))*	8,229	68,802	102,333	43,053	18,122	–	240,539
Investments *(note (iii))*							
– Held-to-maturity debt securities	–	1,659	2,221	14,424	12,406	–	30,710
– Available-for-sale investments	–	6,706	4,066	6,867	8,971	–	26,610
– Debt securities at fair value through profit or loss	–	117	119	847	–	–	1,083
Others	294	620	1,114	132	50	14,518	16,728
Total assets	55,816	85,750	116,981	65,778	39,549	32,943	396,817
Liabilities							
Amounts due to central bank	–	3,621	300	–	–	–	3,921
Amounts due to banks and other financial institutions	30,065	5,908	373	788	466	–	37,600
Deposits from customers	170,492	66,640	63,447	34,442	6,645	3,690	345,356
Others	147	2,899	427	17	35	1,013	4,538
Total liabilities	200,704	79,068	64,547	35,247	7,146	4,703	391,415
Long/(short) position	(144,888)	6,682	52,434	30,531	32,403	28,240	5,402

	31 December 2004						
	Overdue/ repayable on demand	Less than three months	Between three months and one year	Between one and five years	More than five years	Undated	Total
Assets							
Cash and balances with central bank *(note (i))*	30,054	–	–	–	–	24,199	54,253
Amounts due from banks and other financial institutions	10,245	8,050	1,334	1,270	–	–	20,899
Loans and advances to customers *(note (ii))*	7,921	57,247	130,006	56,573	40,174	–	291,921
Investments *(note (iii))*							
– Held-to-maturity debt securities	–	8,282	23,391	16,550	13,147	–	61,370
– Available-for-sale investments	–	23,381	4,871	7,728	4,769	–	40,749
– Debt securities at fair value through profit or loss	–	–	2,380	3,179	3,225	–	8,784
Others	259	819	1,136	136	47	15,072	17,469
Total assets	48,479	97,779	163,118	85,436	61,362	39,271	495,445
Liabilities							
Amounts due to central bank	–	–	300	–	–	–	300
Amounts due to banks and other financial institutions	25,333	5,665	5,091	1,312	789	–	38,190
Deposits from customers	197,246	97,005	75,911	50,085	5,955	8,818	435,020
Subordinated debts/bonds issued	–	–	–	–	6,000	–	6,000
Others	125	3,422	486	16	44	1,079	5,172
Total liabilities	222,704	106,092	81,788	51,413	12,788	9,897	484,682
Long/(short) position	(174,225)	(8,313)	81,330	34,023	48,574	29,374	10,763

	31 December 2005						
	Overdue/ repayable on demand	Less than three months	Between three months and one year	Between one and five years	More than five years	Undated	Total
Assets							
Cash and balances with central bank *(note (i))*	27,456	27,440	–	–	–	29,557	84,453
Amounts due from banks and other financial institutions	17,152	9,932	3,248	1,020	–	–	31,352
Loans and advances to customers *(note (ii))*	8,147	68,142	172,168	61,230	48,343	–	358,030
Investments *(note (iii))*							
– Held-to-maturity debt securities	–	16,655	9,323	26,362	15,387	–	67,727
– Available-for-sale investments	–	12,906	4,155	7,487	7,328	–	31,876
– Debt securities at fair value through profit or loss	–	2,470	863	1,090	390	–	4,813
Others	264	790	1,063	120	37	14,077	16,351
Total assets	53,019	138,335	190,820	97,309	71,485	43,634	594,602
Liabilities							
Amounts due to central bank	–	–	240	–	–	–	240
Amounts due to banks and other financial institutions	20,230	2,285	692	2,810	2,004	–	28,021
Deposits from customers	268,150	107,268	80,352	47,086	3,396	24,321	530,573
Subordinated debts/bonds issued	–	–	–	6,000	–	–	6,000
Others	277	4,548	376	70	42	1,230	6,543
Total liabilities	288,657	114,101	81,660	55,966	5,442	25,551	571,377
Long/(short) position	(235,638)	24,234	109,160	41,343	66,043	18,083	23,225

	30 June 2006						
	Overdue/ repayable on demand	Less than three months	Between three months and one year	Between one and five years	More than five years	Undated	Total
Assets							
Cash and balances with central bank *(note (i))*	28,942	13,000	–	–	–	33,183	75,125
Amounts due from banks and other financial institutions	12,513	8,606	2,084	348	–	–	23,551
Loans and advances to customers *(note (ii))*	8,013	98,191	185,225	83,072	55,505	–	430,006
Investments *(note (iii))*							
– Held-to-maturity debt securities	–	20,194	16,075	26,619	15,188	–	78,076
– Available-for-sale investments	–	4,097	1,993	5,839	8,700	–	20,629
– Debt securities at fair value through profit or loss	–	200	1,215	1,820	455	–	3,690
Others	766	824	1,255	103	37	13,135	16,120
Total assets	50,234	145,112	207,847	117,801	79,885	46,318	647,197
Liabilities							
Amounts due to central bank	–	–	160	–	–	–	160
Amounts due to banks and other financial institutions	18,182	6,524	1,455	387	743	–	27,291
Deposits from customers	243,349	151,917	125,834	39,665	3,625	6,605	570,995
Subordinated debts/bonds issued	–	–	–	6,000	6,000	–	12,000
Others	244	5,249	956	35	41	771	7,296
Total liabilities	261,775	163,690	128,405	46,087	10,409	7,376	617,742
Long/(short) position	(211,541)	(18,578)	79,442	71,714	69,476	38,942	29,455

Notes:

(i) For cash and balances with central bank, undated amount represents statutory deposit reserve funds and fiscal balances maintained with the PBOC.

(ii) For loans and advances to customers, overdue amount included in the above "overdue/repayable on demand" category represents loans of which the whole or part of the principals was overdue, or interest was overdue for more than 90 days but for which principal was not yet due. The overdue amount is stated net of appropriate allowances for impairment losses.

(iii) For debt securities held for trading purposes, the remaining term to maturities does not represent the Group's intention to hold them to final maturity.

(f) Operational risk

Operational risk includes the risk of direct or indirect loss due to an event or action causing failure of technology, processes, infrastructure and personnel, and other risks having an operational impact.

The Group manages this risk through a control-based environment by establishing a framework of policies and procedures in order to identify, assess, control, manage and report risks. The framework covers all business functions ranging from finance, credit, accounting, settlement, savings, treasury, intermediary business, computer applications and management, special assets resolution and legal affairs. This has allowed the Group to identify and address comprehensively the operational risk inherent in all key products, activities, processes and systems. Key controls include:

– authorisation limits for various business activities to branches are delegated after consideration of their respective business scope, risk management capabilities and credit approval procedures. Such authorities are revised on a timely basis to reflect changes in market conditions and business development and risk management needs;

– the use of the single legal responsibility framework and strict disciplinary measures in order to ensure accountability;

– systems and procedures to identify, control and report on the major risks: credit, market, liquidity and operational;

– promotion of a risk management culture throughout the organisation by building a team of risk management professionals, providing formal training and having an appraisal system in place, to raise the overall risk awareness among the Group's employees;

– from December 2002 onwards, the Accounting Department was appointed to be responsible for overseeing that cash management and account management are in compliance with the relevant regulations, and for improving training on anti-money laundering to ensure our staff are well-equipped with the necessary knowledge and basic skills;

– the review and approval by senior management of comprehensive financial and operating plans which are prepared by branches;

– the assessment of individual branches' financial performance against the comprehensive financial and operating plan; and

– the maintenance of contingent facilities (including backup systems and disaster recovery schemes) to support all major operations, especially back office operations, in the event of an unforeseen interruption. Insurance cover is arranged to mitigate potential losses associated with certain operational events.

In addition to the above, the Bank's Internal Audit Department, which directly reports to the Internal Audit Committee, examines and independently evaluates its risk management policies and procedures and internal controls. The Internal Audit Committee is under the direct supervision of the Executive Management Committee led by the President of the Bank.

The Internal Audit Committee determines the frequency and priority of audits of the Bank's different operating units and branches based on their assessment of the level of risk of those units and branches.

35. FAIR VALUE

(a) Financial assets

The Group's financial assets mainly include cash, amounts due from central bank, banks and other financial institutions, loans and advances to customers, and investments.

Amounts due from central bank, banks and other financial institutions

Amounts due from central bank, banks and other financial institutions are mainly priced at market interest rates and mature within one year. Accordingly, the carrying values approximate the fair values.

Loans and advances to customers

Loans and advances to customers are mostly priced at floating rates close to the PBOC rates. Accordingly, their carrying values approximate the fair values.

Investments

Available-for-sale investments and trading debt securities are stated at fair value in the balance sheet. The following table summarises the carrying values and the fair values of held-to-maturity debt securities which are not presented on the balance sheet at their fair values.

	Carrying values				**Fair values**			
	31 December			**30 June**	**31 December**			**30 June**
	2003	**2004**	**2005**	**2006**	**2003**	**2004**	**2005**	**2006**
Held-to-maturity debt securities	30,710	61,370	67,727	78,076	31,170	61,272	68,068	78,052

(b) Financial liabilities

The Group's financial liabilities mainly include amounts due to banks and other financial institutions, deposits from customers and subordinated debts/bonds issued. The carrying values of financial liabilities approximated their fair values at the balance sheet date.

36. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGMENTS

In determining the carrying amounts of some assets and liabilities, the Group makes assumptions of the effects of uncertain future events on those assets and liabilities at the balance sheet date. These estimates involve assumptions about such items as risk adjustment to cash flows or discount rates used, future changes in salaries and future changes in prices affecting other costs. The Group's estimates and assumptions are based on historical experience and expectations of future events and are reviewed periodically. In addition to assumptions and estimations of future events, judgments are also made during the process of applying the Group's accounting policies.

(a) Impairment losses on loans and advances

Loan portfolios are assessed periodically to assess whether impairment losses exist and if they exist, the amounts of impairment losses. Objective evidence for impairment includes observable data indicating that there is a measurable decrease in the estimated future cash flows identified with an individual loan. It also includes observable data indicating adverse changes in the repayment status of borrowers in the loan portfolio or national or local or economic conditions that correlate with defaults on the loans in the portfolio. The impairment loss for a loan that is individually evaluated for impairment is the decrease in the estimated future cash flow of that loan.

When loans and advances are collectively evaluated for impairment, the estimate is based on historical loss experience for assets with credit risk characteristics similar to the loans and advances. Historical loss experience is adjusted on the basis of the relevant observable data that reflect current economic conditions. Management review the methodology and assumptions used in estimating future cash flows regularly to reduce any difference between loss estimates and actual loss experience.

(b) *Impairment of available-for-sale equity investments*

For available-for-sale equity investments, a significant or prolonged decline in fair value below cost is considered to be objective evidence of impairment. Judgment is required when determining whether a decline in fair value has been significant or prolonged. In making this judgment, the historical data on market volatility as well as in the share price of the specific equity investment are taken into account. The Group also takes into account other factors, such as industry and sector performance and financial information regarding the investee.

(c) *Fair value of financial instruments*

The fair values for those financial instruments, where no quoted prices from an active market exist, are established by using valuation techniques. These techniques include using recent arm's length market transactions, reference to the current fair value of similar instruments and discounted cash flow analysis and option pricing models. The Group has established a process to ensure that valuation techniques are constructed by qualified personnel and are validated and reviewed by personnel independent of the area that constructed the valuation techniques. Valuation techniques are certified before being implemented for valuation and are calibrated to ensure that outputs reflect actual market conditions. Valuation models established by the Group make the maximum use of market inputs and rely as little as possible on Group-specific data. However, it should be noted that some inputs, such as credit and counterparty risk, and risk correlations, require management estimates. Management estimates and assumptions are reviewed periodically and are adjusted if necessary.

(d) *Held-to-maturity investments*

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity investments if the Group has the intention and ability to hold them until maturity. In evaluating whether the requirements to classify a financial asset as held-to-maturity are met, management make significant judgments. Failure in correctly assessing the Group's intention and ability to hold specific investments until maturity may result in reclassification of the whole portfolio as available-for-sale.

(e) *Income taxes*

Determining income tax provisions involves judgment on the future tax treatment of certain transactions. The Group carefully evaluates tax implications of transactions and tax provisions are set up accordingly. The tax treatment of such transactions is reconsidered periodically to take into account all changes in tax legislations.

Deferred tax assets are recognised for tax losses not yet used and temporary deductible differences. As those deferred tax assets can only be recognised to the extent that it is probable that future taxable profit will be available against which the unused tax credits can be utilised. Management's judgment is required to assess the probability of future taxable profits. Management's assessment is constantly reviewed and additional deferred tax assets are recognised if it becomes probable that future taxable profits will allow the deferred tax asset to be recovered.

37. RELATED PARTIES

CITIC Group, the equity owner of the Bank, is a state-owned company established in 1979. CITIC Group's core business ranges from financial industry, industrial investment to service industries in both the Mainland China and overseas. The Group's related party transactions are the transactions between the Group and CITIC Group and its subsidiaries.

(a) Related transactions

During the relevant periods, the Group entered into transactions with related parties in the ordinary course of its banking business including lending, investment, deposit and off-balance sheet transactions. The banking transactions were priced at the relevant market rates prevailing at the time of each transaction. Interest rates on loans and deposits are required to be set in accordance with the benchmark rates set by the PBOC.

Transactions during relevant periods and the corresponding balances outstanding at the balance sheet date are as follows:

	For the year ended 31 December 2003		
	Ultimate holding Company	**Fellow Subsidiaries**	**Subsidiaries** *(note(i))*
Interest income	183	151	10
Interest expense	86	41	–
Management fee to CITIC Group	–	–	–
Other service fees	–	29	–
Loan impairment losses charge	–	71	–

	For the year ended 31 December 2004		
	Ultimate holding Company	**Fellow Subsidiaries**	**Subsidiaries** *(note(i))*
Interest income	171	139	19
Interest expense	92	49	–
Management fee to CITIC Group	300	–	–
Other service fees	–	25	–
Loan impairment losses release	–	(15)	–

	For the year ended 31 December 2005		
	Ultimate holding Company	**Fellow Subsidiaries**	**Subsidiaries** *(note(i))*
Interest income	176	114	20
Interest expense	50	49	–
Management fee to CITIC Group	500	–	–
Other service fees	–	15	–
Loan impairment losses release	–	(89)	–

	For the six months ended 30 June 2005 (unaudited)		
	Ultimate holding Company	**Fellow Subsidiaries**	**Subsidiaries** *(note(i))*
Interest income	124	68	9
Interest expense	35	29	–
Management fee to CITIC Group	300	–	–
Other service fees	–	9	–

	For the six months ended 30 June 2006		
	Ultimate holding Company	**Fellow Subsidiaries**	**Subsidiaries** *(note(i))*
Interest income	38	41	13
Interest expense	23	43	–
Management fee to CITIC Group	375	–	–
Other service fees	–	5	–

	31 December 2003		
	Ultimate holding Company	**Fellow Subsidiaries**	**Subsidiaries** *(note(i))*
Gross loans and advances to customers	2,680	3,806	117
Less: Impairment allowances	–	(829)	–
Net loans and advances to customers	2,680	2,977	117
Amounts due from banks and other financial institutions	–	192	557
Investments	1,093	33	66
Deposits from customers	2,255	1,686	1
Amounts due to banks and other financial institutions	–	1,623	–
Other liabilities	42	157	7
Off-balance sheet transactions	424	436	–
Guarantee for loans to third parties	–	138	–

	31 December 2004		
	Ultimate holding Company	Fellow Subsidiaries	Subsidiaries *(note(i))*
Gross loans and advances to customers	2,680	3,699	110
Less: Impairment allowances	–	(814)	–
Net loans and advances to customers	2,680	2,885	110
Amounts due from banks and other financial institutions	–	122	542
Investments	1,110	66	33
Deposits from customers	2,513	1,493	16
Amounts due to banks and other financial institutions	–	2,287	–
Other liabilities	38	180	3
Off-balance sheet transactions	527	250	–
Guarantee for loans to third parties	–	176	–

	31 December 2005		
	Ultimate holding Company	Fellow Subsidiaries	Subsidiaries *(note(i))*
Gross loans and advances to customers	2,620	2,848	106
Less: Impairment allowances	–	(725)	–
Net loans and advances to customers	2,620	2,123	106
Amounts due from banks and other financial institutions	–	368	462
Investments	908	65	32
Deposits from customers	2,428	3,693	25
Amounts due to banks and other financial institutions	–	1,039	–
Other liabilities	37	61	–
Off-balance sheet transactions	604	171	–
Guarantee for loans to third parties	–	210	–

	30 June 2006		
	Ultimate holding Company	**Fellow Subsidiaries**	**Subsidiaries** *(note(i))*
Gross loans and advances to customers	540	1,768	–
Less: Impairment allowances	–	–	–
Net loans and advances to customers *(note (ii))*	540	1,768	–
Amounts due from banks and other financial institutions	–	114	633
Investments	899	101	32
Other assets	375	–	–
Deposits from customers	1,535	3,745	–
Amounts due to banks and other financial institutions	–	4,219	–
Other liabilities	28	28	8
Off-balance sheet transactions	474	205	–
Guarantee for loans to third parties	–	189	–

Notes:

(i) The related party transactions between the Bank and the subsidiaries are eliminated in consolidation.

(ii) The Group disposed loans due from related parties with principle of RMB1,142 million and net book value of RMB417 million in June 2006. These loans were sold at a price of net book value to CITIC Group.

(b) Key management personnel and their close family members and related companies

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

The Group enters into banking transactions with key management personnel and their close family members and those companies controlled or significantly influenced by them in the normal course of business. In the opinion of the directors, other than the total amounts of loans to directors, supervisors and officers as disclosed in note 11, there are no material transactions and balances between the Group and these individuals or those companies controlled or significantly influenced by them.

The aggregate of the compensations in respect of Directors and Supervisors is disclosed in Note 9. The Executive Officers' compensations during the year are as follows:

	Year ended 31 December			Six months ended 30 June	
	2003	2004	2005	2005 (unaudited)	2006
Salaries and other emoluments	2	2	2	1	1
Discretionary bonuses	6	7	11	1	1
Contributions to defined contribution retirement schemes	1	1	1	1	1
	9	10	14	3	3

(c) Contributions to defined contribution retirement schemes

The Group participates in defined contribution retirement schemes organised by municipal and provincial governments for its employees in Mainland China.

The Group has also established a supplementary defined contribution plan for its qualified employees. The plan is administered by CITIC Group.

The Group is also required to make contributions to the Mandatory Provident Fund Scheme for its employees in Hong Kong at the rate set up by the local laws and regulations.

The details of the Group's defined contribution retirement schemes are described in Notes 23(a) and 24(a).

(d) Transactions with other state-owned entities in the PRC

The Group operates in an economic regime currently predominated by entities directly or indirectly owned by the PRC government through its government authorities, agencies, affiliations and other organizations ("state-owned entities").

Transactions with other state-owned entities include but are not limited to the following:

– lending and deposit taking;

– taking and placing of inter-bank balances;

– entrusted lending and other custody services;

– insurance and securities agency, and other intermediary services;

– sale, purchase, underwriting and redemption of bonds issued by other state-owned entities;

– purchase, sale and leases of property and other assets; and

– rendering and receiving of utilities and other services.

These transactions are conducted in the ordinary course of the Group's banking business on terms similar to those that would have been entered into with non-state-owned entities. The Group has also established its pricing strategy and approval processes for major products and services, such as loans, deposits and commission income. The pricing strategy and approval processes do not depend on whether the customers are state-owned entities or not. Having due regard to the substance of the relationships, the Directors are of opinion that none of these transactions are material related party transactions that require separate disclosure.

38. POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE ACCOUNTING PERIOD ENDED 30 JUNE 2006

Up to the date of issue of this Accountants' Report, the IASB has issued the following amendments, new standards and interpretations which are not yet effective for the accounting period ending 30 June 2006 and which have not been adopted in the Financial Information:

		Effective for accounting periods beginning on or after
IFRS 7	Financial Instruments: Disclosures	1 January 2007
Amendment to IAS 1	Presentation of Financial Statements: Capital Disclosures	1 January 2007

The Group has assessed the impact of these amendments, new standards and new interpretations and concluded that they would only affect the level of details in the disclosure of the Financial Information, and would not have financial impact nor result in a change in the Group's accounting policies.

39. POST BALANCE SHEET DATE EVENT

Subsequent to 30 June 2006, the State Council, the CBRC and the MOF have approved the Bank to be restructured into a limited liability joint stock company and to be named China CITIC Bank Corporation Limited (the "Joint Stock Company"). The business operations, assets and liabilities of the Bank as at 31 December 2005 will be succeeded by the Joint Stock Company. The value of the succeeded assets and liabilities as at 31 December 2005 will be based on the revaluation report dated 6 September 2006 issued by an independent professional valuer in the PRC, China Enterprise Appraisals Co., Ltd. CITIC Group and CIFH will be the joint promoters of the Joint Stock Company. The share capital of the Joint Stock Company is intended to be RMB31,113 million. The Joint Stock Company will be established upon the issuance of the business licence by the State Administration for Industry and Commerce.

40. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the current period's presentation.

Yours faithfully,
KPMG
Certified Public Accountants
Hong Kong, China

2. Unaudited supplementary financial information

(Expressed in millions of Renminbi unless otherwise stated)

The information set out below does not form part of the audited financial information, and is included herein for information purposes only.

(a) Liquidity ratios

	31 December			30 June
	2003	2004	2005	2006
RMB current assets to RMB current liabilities	57.82%	61.28%	60.69%	46.25%
Foreign currency current assets to foreign currency current liabilities	57.87%	74.52%	68.00%	103.89%

The above liquidity ratios are calculated in accordance with the formula promulgated by the People's Bank of China (the "PBOC") and China Banking Regulatory Commission ("CBRC") and based on the financial statements of China CITIC Bank (the "Bank") prepared in accordance with the Accounting Standards for Business Enterprises, the Accounting Regulations for Financial Enterprises (jointly issued by the Ministry of Finance of the PRC (the "MOF") and the PBOC in 1993) and other relevant regulations issued by the MOF (collectively "Previous PRC GAAP") (for 31 December 2003 and 2004) and in accordance with the Accounting Standards for Business Enterprises, the Accounting Regulations for Financial Enterprises (issued by the MOF in 2001) and other regulations issued by the MOF (collectively named as "PRC GAAP") (for 31 December 2005 and 30 June 2006).

(b) Capital adequacy ratio

The capital adequacy ratio is prepared on a solo basis in accordance with the guideline "Regulation Governing Capital Adequacy of Commercial Banks" (Order [2004] No.2) effective on 1 March 2004, which may have significant differences with the relevant requirements in Hong Kong Special Administrative Region of the PRC or other countries.

The capital adequacy ratios as at 31 December 2003 and 31 December 2004 reported to the CBRC respectively are not presented. The Group is of the opinion that they are not value added to the equity owner, given that the capital adequacy ratios are calculated based on the quantitative financial information of the Bank in accordance with the Previous PRC GAAP and the guideline issued by PBOC which was applicable for calculating capital adequacy ratios in 2003 has been replaced by the CBRC guideline since March 2004.

Capital Adequacy Guidelines

PRC commercial banks are subject to a minimum capital adequacy ratio of 8% and a minimum core capital adequacy ratio of 4%. The capital adequacy ratio and core capital adequacy ratio are calculated based on the quantitative financial information of the Bank in accordance with the PRC GAAP as follows:

$$\text{Capital Adequacy Ratio} = \frac{\text{Capital - Deductions from capital}}{\text{Risk-weighted assets + (12.5 x capital charge for market risk)}} \text{ x } 100\%$$

$$\text{Core Capital Adequacy Ratio} = \frac{\text{Core capital – Deductions from core capital}}{\text{Risk-weighted assets + (12.5 x capital charge for market risk)}} \text{ X } 100\%$$

Components of Capital

Total capital consists of core capital and supplementary capital. Supplementary capital may not exceed core capital.

Core capital includes the following items:

– paid-in capital;

– capital reserves;

– surplus reserves, including statutory and discretionary surplus reserves and the statutory public welfare fund;

– retained earnings; and

– minority interests.

Supplementary capital includes the following:

– up to 70% of the revaluation reserve;

– the general allowances for impairment losses under the CBRC's requirements;

– preference shares;

– qualifying bonds convertible into common shares; and

– qualifying subordinated debt with a maturity exceeding 5 years, not exceeding 50% of core capital.

Deductions from total capital consist of the following:

– goodwill;

– 100% of equity investments in non-consolidated financial institutions; and

– 100% of capital investments in real estate not used for the bank's own operations or equity investments in non-financial institutions.

Deductions from core capital consist of the following:

– goodwill;

– 50% of equity investments in non-consolidated financial institutions; and

– 50% of capital investments in real estate not used for the bank's own operations or equity investments in non-financial institutions.

Risk-weighted Assets

The guidelines provide for the calculation of risk-weighted assets net of any allowance for impairment losses by multiplying on-balance sheet items by their corresponding risk weighting. Off-balance sheet items, including foreign exchange contracts, interest rate contracts and other derivative contracts, are first converted to balance sheet credit-equivalent amounts by multiplying the nominal principal amount by a credit conversion factor. In addition, loans secured by certain types of pledges or guarantees are allocated the risk weighting of the pledges or guarantors. Partially pledged or guaranteed loans receive such lower risk-weighting only on the portion of the loan that is pledged or guaranteed. The following table sets forth risk weightings for different assets.

Risk Weighting	Assets
0%	– Cash
	– Gold
	– Claims on PRC incorporated commercial banks with an original maturity of four months or less
	– Claims on the PRC central government or deposits at the PBOC
	– Claims on the PBOC
	– Claims on PRC policy banks
	– Bonds issued by PRC financial asset management companies for the purpose of acquiring non-performing loans from state-owned banks
	– Claims on non-PRC central governments or central banks in countries or regions where the sovereign or region is rated AA – or above (These ratings refer to credit ratings of Standard & Poor's or equivalent rating agencies).
	– Claims on multilateral development banks
20%	– Claims on PRC incorporated commercial banks with an original maturity of more than four months
	– Claims on non-PRC commercial banks and securities companies incorporated in other countries or regions where the sovereign or region is rated AA – or above (These ratings refer to credit ratings of Standard & Poor's or equivalent rating agencies).
50%	– Residential mortgages
	– Claims on PRC public-sector entities owned by the central government
	– Claims on non-PRC public-sector entities owned by governments of countries or regions where the sovereign or region is rated AA – or above (These ratings refer to credit ratings of Standard & Poor's or equivalent rating agencies).
100%	– All other assets

Capital Charge for Market Risk

Since the first quarter of 2005, domestic banks with trading books greater than the lower of 10% of on- and off-balance sheet assets in aggregate and RMB8.5 billion are required to take into consideration market risk arising from trading activities when determining capital adequacy. Market risk is the aggregated risk charge applied to the balance of each trading security where the risk charge is determined based on the type of the security and the counterparty and the remaining maturity of the security. The value of securities in the trading book must be marked to market. If the market risk capital charge is applicable, capital must be applied against the sum of risk-weighted assets and market risk to determine capital adequacy.

The capital adequacy ratios and the related components of the Bank as at 31 December 2005 and 30 June 2006 calculated based on the financial statements prepared in accordance with PRC GAAP, were as follows:

	31 December 2005	**30 June 2006**
Core capital adequacy ratio	5.72%	6.31%
Capital adequacy ratio	8.11%	9.52%
Components of capital base		
Core capital:		
– Paid up capital	26,661	31,661
– Reserves	(5,321)	(4,734)
	21,340	26,927
Supplementary capital:		
– General provision for loans and advances	2,961	2,740
– Subordinated debts/bonds	6,000	10,980
Total supplementary capital	8,961	13,720
Total capital base before deductions	30,301	40,647
Deductions:		
– Unconsolidated equity investments	142	102
Total capital base after deductions	30,159	40,545
Risk weighted assets	372,000	425,957

(c) Currency concentrations

	31 December 2003			
	US Dollars	HK Dollars	Others	Total
Spot assets	41,884	1,445	3,650	46,979
Spot liabilities	(34,155)	(2,980)	(7,006)	(44,141)
Forward purchases	3,513	2,105	5,820	11,438
Forward sales	(7,675)	(1,045)	(2,477)	(11,197)
Net option position	46	–	36	82
Net long position	3,613	(475)	23	3,161

	31 December 2004			
	US Dollars	HK Dollars	Others	Total
Spot assets	41,110	1,616	14,936	57,662
Spot liabilities	(32,296)	(5,399)	(16,454)	(54,149)
Forward purchases	7,955	2,522	7,633	18,110
Forward sales	(10,004)	(1,634)	(6,510)	(18,148)
Net option position	26	–	(26)	–
Net long position	6,791	(2,895)	(421)	3,475

	31 December 2005			
	US Dollars	HK Dollars	Others	Total
Spot assets	55,773	10,343	9,217	75,333
Spot liabilities	(46,195)	(14,139)	(11,456)	(71,790)
Forward purchases	13,026	7,949	6,557	27,532
Forward sales	(19,599)	(4,487)	(4,171)	(28,257)
Net option position	61	–	(61)	–
Net long position	3,066	(334)	86	2,818

	30 June 2006			
	US Dollars	HK Dollars	Others	Total
Spot assets	56,901	1,415	8,151	66,467
Spot liabilities	(50,239)	(3,125)	(6,213)	(59,577)
Forward purchases	17,487	1,784	7,866	27,137
Forward sales	(20,106)	(576)	(9,478)	(30,160)
Net option position	(221)	–	897	676
Net long position	3,822	(502)	1,223	4,543

(d) Cross-border claims

The Group is principally engaged in business operations within Mainland China, and regards all claims on third parties outside Mainland China as cross-border claims.

For the purpose of these unaudited supplementary financial information, Mainland China excludes Hong Kong, the Macau Special Administrative Region of the PRC and Taiwan.

Cross-border claims include loans and advances, balances and placements with banks and other financial institutions, holding of trade bills and certificates of deposit and investment securities.

Cross-border claims have been disclosed by different country or geographical areas. A country or geographical areas is reported where it constitutes 10% or more of the aggregate amount of cross-border claims, after taking into account any risk transfers. Risk transfers are only made 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.

	31 December 2003			
	Banks and other financial institutions	Public sector entities	Others	Total
Asia Pacific excluding Mainland China	2,706	293	770	3,769
– of which attributed to Hong Kong	1,250	293	419	1,962
Europe	4,983	10	2,237	7,230
North and South America	10,680	971	4,787	16,438
	18,369	1,274	7,794	27,437

	31 December 2004			
	Banks and other financial institutions	Public sector entities	Others	Total
Asia Pacific excluding Mainland China	3,772	250	961	4,983
– of which attributed to Hong Kong	1,547	250	311	2,108
Europe	3,610	117	9,686	13,413
North and South America	6,977	10,197	2,363	19,537
	14,359	10,564	13,010	37,933

	31 December 2005			
	Banks and other financial institutions	Public sector entities	Others	Total
Asia Pacific excluding Mainland China	3,701	531	1,140	5,372
– of which attributed to Hong Kong	1,317	482	164	1,963
Europe	6,492	49	1,006	7,547
North and South America	10,548	9,083	6,687	26,318
	20,741	9,663	8,833	39,237

	30 June 2006			
	Banks and other financial institutions	Public sector entities	Others	Total
Asia Pacific excluding Mainland China	4,720	80	1,511	6,311
– of which attributed to Hong Kong	2,372	80	115	2,567
Europe	5,823	50	307	6,180
North and South America	12,266	8,628	4,438	25,332
	22,809	8,758	6,256	37,823

(e) Overdue loans and advances to customers by geographic sector

	31 December 2003		
	Gross loans and advances	Loans and advances overdue over 3 months	Impaired Loans
Yangtze River Delta	70,051	2,515	3,120
Bohai Rim	89,770	9,782	10,890
Pearl River Delta and West Strait	46,780	7,526	8,241
Central	21,396	467	487
Western	21,075	201	178
Northeastern	7,961	238	289
Hong Kong	280	–	–
Total	257,313	20,729	23,205

	31 December 2004		
	Gross loans and advances	Loans and advances overdue over 3 months	Impaired Loans
Yangtze River Delta	91,672	1,376	1,491
Bohai Rim	100,195	7,217	8,237
Pearl River Delta and West Strait	49,491	8,072	8,196
Central	27,477	408	419
Western	27,943	597	593
Northeastern	9,880	249	344
Hong Kong	221	–	–
Total	306,879	17,919	19,280

		31 December 2005	
	Gross loans and advances	Loans and advances overdue over 3 months	Impaired Loans
Yangtze River Delta	120,026	683	925
Bohai Rim	115,706	6,059	6,029
Pearl River Delta and West Strait	52,885	6,086	6,467
Central	36,255	651	754
Western	32,029	602	660
Northeastern	13,207	203	476
Hong Kong	152	–	–
Total	370,260	14,284	15,311

		30 June 2006	
	Gross loans and advances	Loans and advances overdue over 3 months	Impaired Loans
Yangtze River Delta	144,761	687	682
Bohai Rim	129,081	5,739	5,673
Pearl River Delta and West Strait	62,181	4,369	4,616
Central	44,356	904	924
Western	42,127	627	613
Northeastern	18,299	233	386
Hong Kong	157	–	–
Total	440,962	12,559	12,894

Impaired loans and advances include loans for which objective evidence of impairment exists and which have been assessed as bearing significant impairment losses. These loans include loans for which objective evidence of impairment has been identified:

– individually (including corporate loans and advances which are graded substandard, doubtful or loss); or

– collectively: that is portfolios of homogeneous loans (including retail loans and advances which are graded substandard, doubtful or loss).

(f) Gross amount of overdue amounts due from banks and other financial institutions and overdue loans and advances to customers

(i) Gross overdue amounts due from banks and other financial institutions

	31 December			30 June
	2003	**2004**	**2005**	**2006**
Gross amounts due from banks and other financial institutions which have been overdue	1,002	604	419	409
As a percentage of total gross amounts due from banks and other financial institutions	3.10%	2.83%	1.32%	1.71%

Note: All overdue amounts have been overdue over 12 months.

(ii) Gross amounts of overdue loans and advances to customers

	31 December			30 June
	2003	2004	2005	2006
Gross loans and advances to customers which have been overdue with respect to either principal or interest for periods of:				
– between 3 and 6 months	802	1,414	1,283	1,715
– between 6 and 12 months	784	1,565	1,149	1,555
– over 12 months	19,143	14,940	11,852	9,289
Total	20,729	17,919	14,284	12,559
As a percentage of total gross loans and advances to customers:				
– between 3 and 6 months	0.31%	0.46%	0.35%	0.39%
– between 6 and 12 months	0.30%	0.51%	0.31%	0.35%
– over 12 months	7.44%	4.87%	3.20%	2.11%
Total	8.05%	5.84%	3.86%	2.85%

The overdue loans represent loans of which the whole or part of the principal was overdue, or interest was overdue. The definitions of overdue loans with various repayment terms are set out below:

- Loans with a specific repayment date are classified as overdue when the principal or interest is overdue and remains unpaid at year end.

- Where one or more instalments of a loan repayable by regular instalments are overdue and remain unpaid at year end, the entire loan balance is considered overdue.

– Loans repayable on demand are classified as overdue when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the demand notice. If loans and advances repayable on demand are continuously outside the approved limit that was advised to the borrower, they are also considered as overdue.

(g) Rescheduled amounts due from banks and other financial institutions and rescheduled loans and advances to customers

(i) Rescheduled amounts due from banks and other financial institutions

The Group does not have any rescheduled amounts due from banks and other financial institutions for the year ended 31 December 2003, 2004 and 2005 and for the six months ended 30 June 2006.

(ii) Rescheduled loans and advances to customers

	31 December						30 June	
	2003		2004		2005		2006	
		% of total loans and advances		% of total loans and advances		% of total loans and advances		% of total loans and advances
Rescheduled loans and advances	8,919	3.47%	9,148	2.98%	6,619	1.79%	4,954	1.12%
Less:								
– rescheduled loans and advances but overdue more than 90 days	4,268	1.66%	4,040	1.32%	3,249	0.88%	2,192	0.50%
Rescheduled loans and advances overdue less than 90 days	4,651	1.81%	5,108	1.66%	3,370	0.91%	2,762	0.62%

Rescheduled loans and advances are those loans and advances which have been restructured or renegotiated because of a deterioration in the financial position of the borrower, or of the inability of the borrower to meet the original repayment schedule and for which the revised repayment terms are a concession that the Group would not otherwise consider. Rescheduled loans and advances are required to be graded at a minimum of substandard (see Note 34(a) for the core definitions of the loan classification) and subject to an observation period of six months, until when no upgrade to a higher loan classification is considered.

(h) Impairment allowances against loans and advances to customers recorded in the Accountants' Report prepared under IFRS and those recorded in the Bank's statutory financial statements prepared under Previous PRC GAAP and PRC GAAP

Impairment allowances	2003	2004	2005
As disclosed in the Accountants' Report prepared under IFRS	16,774	14,958	12,230
As disclosed in the statutory financial statements prepared under Previous PRC GAAP and PRC GAAP	3,127	3,922	11,938

Under IFRS, the Group is required to assess whether its loans and advances to customers are impaired and recognize impairment losses based on their estimated recoverable amounts.

The impairment allowances as recorded under Previous PRC GAAP and PRC GAAP for loans and advances to customers are made in accordance with relevant PRC rules and regulations on loan loss provisioning. Previous PRC GAAP does not require recognition of impairment losses against the assets based on their estimated recoverable amounts. Only an allowance of 1% of the total gross amount of certain assets, including loans and investments, is required to be made. In the Bank's 2005 statutory financial statements prepared under PRC GAAP, impairment allowances for loans and advances to customers are accrued based on a range of reference rates for each of the five loan categories as stated in "Guidelines on Loan Loss Provisions" issued by PBOC on 24 April 2002.

3. MANAGEMENT DISCUSSION AND ANALYSIS

The following discussion and analysis should be read in conjunction with the accountants' report on CNCB set out in section 1 of Appendix III in this circular.

Background

CNCB (previously known as "CITIC Industrial Bank") was established on 7 April 1987, as a state-owned financial institution. CNCB is wholly-owned by the CITIC Group. The principal activities of CNCB and its subsidiaries are the provision of corporate and personal banking services, conducting treasury business and corresponding banking business, and the provision of asset management, entrusted lending and custodian trustee services. As at 31 December 2005, CNCB had established branches and sub-branches in 18 provinces, autonomous regions and municipalities directly under the central government in the PRC.

Business Performance

Earnings

For the six months ended 30 June 2006, the CNCB Group reported operating income of RMB8,016 million. For the year ended 31 December 2005, the CNCB Group reported operating income of RMB13,655 million, representing an increase of 22.51% over 2004. For the year ended 31 December 2004, the CNCB Group reported operating income of RMB11,146 million, representing an increase of 33.20% over 2003. The increase in operating income for the two years ended 31 December 2005 and 2004 was mainly attributable to (a) an increase in net interest income and (b) an increase in net fee and commission income.

For the year ended 31 December 2003, the CNCB Group reported operating income of RMB8,368 million.

Net Interest Income

The net interest income of the CNCB Group accounts for the largest portion of the total operating income of the CNCB Group, representing 92.71%, 93.15% and 91.69% of the total operating income of CNCB Group for the years ended 31 December 2005, 2004 and 2003 respectively and 91.62% of the total operating income of CNCB Group for the six months ended 30 June 2006. Set out below is a table showing the interest income, interest expense and net interest income of the CNCB Group for the years ended 31 December 2005, 2004 and 2003.

	31 December 2003 *(expressed in millions of RMB)*	**31 December 2004** *(expressed in millions of RMB)*	**31 December 2005** *(expressed in millions of RMB)*	**Six months ended 30 June 2006** *(expressed in millions of RMB)*
Interest income	12,967	17,795	22,511	13,327
Interest expense	(5,294)	(7,412)	(9,851)	(5,983)
Net interest income	7,673	10,383	12,660	7,344

The net interest income for the six months ended 30 June 2006 was RMB7,344 million. For the year ended 31 December 2005, the net interest income of the CNCB Group increased by 21.93% to RMB12,660 million compared to RMB10,383 million for the year ended 31 December 2004. This increase reflects both an increase in interest income, which grew by 26.50% compared to the year ended 31 December 2004, and an increase in interest expense, which grew by 32.91% compared to the same period. For the year ended 31 December 2004, the net interest income of CNCB Group increased by 35.32% to RMB10,383 million compared to RMB7,673 million for the year ended 31 December 2003. This increase reflects both an increase in interest income, which grew by 37.23% compared to the year ended 31 December 2003, and an increase in interest expense, which grew by 40.01% compared to the same period. The increase in net interest income over the period from 2003 to 2005 was mainly attributable to the continued growth in loans and advances to customers of CNCB Group.

The table below sets out the principal components of the interest income and interest expense of CNCB:

	2003 (expressed in millions of RMB)	2004 (expressed in millions of RMB)	2005 (expressed in millions of RMB)	Six months ended 30 June 2006 (expressed in millions of RMB)
Interest income arises from:				
Balances with central bank	627	853	713	410
Amounts due from banks and other financial institutions	506	754	607	285
Loans and advances to customers *(note (i))*	10,170	14,225	18,182	11,047
Investments in debt securities *(note (ii))*	1,664	1,963	3,009	1,585
	12,967	17,795	22,511	13,327
Interest expense arises from:				
Balances due to central bank	(39)	(30)	(12)	(5)
Amounts due to banks and other financial institutions	(937)	(1,065)	(1,029)	(587)
Deposits from customers	(4,318)	(6,181)	(8,512)	(5,240)
Subordinated debts issued	–	(136)	(298)	(151)
	(5,294)	(7,412)	(9,851)	(5,983)
Net interest income	7,673	10,383	12,660	7,344

Notes:

(i) Interest income arising from loans and advances to customers includes interest income accrued on individually assessed impaired loans and advances to customers of RMB179 million for the six months ended 30 June 2006 (2005: RMB306 million; 2004: RMB350 million; 2003: RMB396 million; six months ended 30 June 2005 (unaudited): RMB170 million), which includes interest income on the unwinding of discount of allowances for loan impairment losses of RMB141 million for the six months ended 30 June 2006 (2005: RMB275 million; 2004: RMB307 million; 2003: RMB346 million; six months ended 30 June 2005 (unaudited): RMB152 million).

(ii) Interest income from investments in debt securities is mainly derived from unlisted investments.

Non-Interest Income

CNCB's non-interest income for the six months ended 30 June 2006 was RMB672 million. CNCB's non-interest income for the year ended 31 December 2005 grew significantly by 30.41% to RMB995 million compared to RMB763 million for the year ended 31 December 2004. For the year ended 31 December 2004, CNCB's non-interest income grew by 9.78% to RMB763 million compared to RMB695 million for the year ended 31 December 2003. The increase in CNCB's non-interest income over the period from 2003 to 2005 was primarily due to an increase in the net fee and commission income and net gains arising from foreign currency dealing.

The proportion of non-interest income to total operating income for the years ended 31 December 2005, 2004 and 2003 was 7.29%, 6.85% and 8.31% respectively and for the six months ended 30 June 2006 was 8.38%.

Set out below is a table showing a breakdown of the non-interest income for the years ended 31 December 2005, 2004 and 2003 and for the six months ended 30 June 2006.

	For the year ended 31 December 2003 *(expressed in millions of RMB)*	**For the year ended 31 December 2004** *(expressed in millions of RMB)*	**For the year ended 31 December 2005** *(expressed in millions of RMB)*	**For the six months ended 30 June 2006** *(expressed in millions of RMB)*
Net fee and commission income	265	318	418	326
Dividend income	–	1	1	–
Net profit on disposal of fixed assets	1	11	12	9
Net gain from trading securities	124	34	109	16
Net (loss)/gain from investment securities	(92)	11	(24)	5
Net gains arising from foreign currency dealing	151	227	266	219
Other operating income	246	161	213	97
	695	763	995	672

General and Administrative Expenses

The general and administrative expenses of CNCB for the six months ended 30 June 2006 was RMB3,943 million. The general and administrative expenses of CNCB increased by 30.32% to RMB7,104 million for the year ended 31 December 2005 compared to RMB5,451 million for the year ended 31 December 2004. This was primarily due to (a) the continued increase in staff costs resulting from an increase in the number of staff employed by CNCB Group and (b) an increase in other general and administrative expenses including management fees payable to CITIC Group.

For the year ended 31 December 2004, the general and administrative expenses of CNCB increased by 38.35% to RMB5,451 million for the year ended 31 December 2004 compared to RMB3,940 million for the year ended 31 December 2003. This is primarily due to (a) a significant increase in staff costs as the CNCB Group expands its operations and (b) an increase in other general and administrative expenses.

Set out below is a table showing the principal components of general and administrative expenses for the three years ended 31 December 2005, 2004 and 2003 and the six months ended 30 June 2006:

	2003	**2004**	**2005**	**Six months ended 30 June 2006**
	(expressed in millions of RMB)	*(expressed in millions of RMB)*	*(expressed in millions of RMB)*	*(expressed in millions of RMB)*
Staff costs				
– salaries, bonuses and staff welfare expenses	894	1,215	1,661	895
– contributions to defined contribution retirement schemes	83	107	125	80
– housing fund	31	63	67	34
– supplementary retirement benefits	–	9	–	–
– others	152	187	233	147
	1,160	1,581	2,086	1,156
Property and equipment expense				
– depreciation	553	548	617	312
– rent and property management expenses	314	345	376	216
– electronic equipment operating expenses	64	95	141	55
– maintenance	64	83	92	29
– others	86	96	112	56
	1,081	1,167	1,338	668
Other general and administrative expenses	1,131	1,580	2,125	1,078
Management fee payable to CITIC Group	–	300	500	375
Business tax and surcharges *(note (i))*	521	792	991	630
Amortisation expense	47	31	64	36
	3,940	5,451	7,104	3,943

Note:

(i) Business tax of 5% is levied primarily on interest income from loans and advances to customers, and fee and commission income.

The surcharges, which include education surcharges and city construction tax, are charged at 3% and 7% of business tax paid respectively.

Impairment Losses Charge

The impairment losses charge comprises mainly of provision for loans and advances to customers which represents approximately 96.08%, 97.25% and 99.58% of the total impairment losses charges for the three years ended 31 December 2005, 2004 and 2003 respectively and 91.42% for the six months ended 30 June 2006.

For the six months ended 30 June 2006, the total impairment charges on loans and advances to customers was RMB863 million. For the year ended 31 December 2005, total impairment charges on loans and advances to customers decreased by 33.61% from RMB1,589 million in 2004 to RMB1,055 million in 2005. For the year ended 31 December 2004, total impairment charges on loans and advances to customers decreased by 25.61% from RMB2,136 million in 2003 to RMB1,589 million in 2004. Such decrease over the three years was primarily due to the improvement in the loan portfolio of CNCB due to the adoption of various risk management procedures and continued improvement in the control over the lending process of CNCB.

Total Assets

As at 30 June 2006, CNCB Group's total assets were RMB647,197 million. As at 31 December 2005, CNCB Group's total assets were RMB594,602 million representing a 20.01% increase from RMB495,445 million for the year ended 31 December 2004. As at 31 December 2004, CNCB Group's total assets were RMB495,445 million representing a 24.85% increase from RMB396,817 million for the year ended 31 December 2003.

Loans and advances to customers is a major component of the total assets of CNCB Group and represents approximately 60.21%, 58.92% and 60.62% of the total assets of CNCB Group as at 31 December 2005, 2004 and 2003 respectively and approximately 66.44% of the total assets of CNCB Group as at 30 June 2006. Investments constitute the second largest component of the total assets of CNCB Group and represents approximately 17.56%, 22.38% and 14.72% of the total assets of CNCB Group as at 31 December 2005, 2004 and 2003 respectively and approximately 15.82% of the total assets of CNCB Group as at 30 June 2006.

The table below sets out the components of the assets of CNCB Group for the years ended 31 December 2005, 2004 and 2003 and the six months ended 30 June 2006.

	2003 *(expressed in millions of RMB)*	2004 *(expressed in millions of RMB)*	2005 *(expressed in millions of RMB)*	Six months ended 30 June 2006 *(expressed in millions of RMB)*
Assets				
Cash and balances with central bank	49,299	54,253	84,453	75,125
Amounts due from banks and other financial institutions	31,848	20,899	31,352	23,551
Loans and advances to customers	240,539	291,921	358,030	430,006
Investments *(note)*	58,403	110,903	104,416	102,395
Property and equipment	6,826	8,090	8,614	8,444
Deferred tax assets	5,999	5,424	4,082	3,356
Other assets	3,903	3,955	3,655	4,320
Total assets	396,817	495,445	594,602	647,197

Note: Please refer to note 17 of the accountants' report of CNCB Group.

Customer Loans and Deposits

As at 30 June 2006, customer loans were RMB430,006 million. As at 31 December 2005, customer loans were RMB358,030 million representing an increase of 22.65% from the 2004 year end. Total deposits as at 31 December 2005 were RMB530,573 million representing an increase of 21.97% from the 2004 year end. As at 31 December 2004, customer loans were RMB291,921 million representing an increase of 21.36% from the 2003 year end. Total deposits as at 31 December 2004 were RMB435,020 million representing an increase of 25.96% from the 2003 year end. As at 31 December 2003, customer loans were RMB240,539 million and total deposits were RMB345,356 million.

The increase in customer loans over the period from 2003 to 30 June 2006 was due to an increased demand for loans resulting from the growth in the business of CNCB Group.

Loan Portfolio

Set out below is a table setting out further information in respect of the loan portfolio of CNCB for the years ended 31 December 2005, 2004, 2003 and the six months ended 30 June 2006.

(a) Analysed by nature

	2003	**2004**	**2005**	**30 June 2006**
	(expressed in millions of RMB)	*(expressed in millions of RMB)*	*(expressed in millions of RMB)*	*(expressed in millions of RMB)*
Corporate loans	194,517	256,422	282,275	345,074
Personal loans	17,237	31,730	37,834	42,187
Discounted bills	45,559	18,727	50,151	53,701
Gross loans and advances to customers	257,313	306,879	370,260	440,962
Less:				
– Individual impairment allowances	(14,764)	(12,485)	(9,622)	(7,918)
– Collective impairment allowances	(2,010)	(2,473)	(2,608)	(3,038)
Less: Impairment allowances	(16,774)	(14,958)	(12,230)	(10,956)
Net loans and advances to customers	240,539	291,921	358,030	430,006

(b) Analysed by legal form of borrowers

	2003	**2004**	**2005**	**30 June 2006**
	(expressed in millions of RMB)	*(expressed in millions of RMB)*	*(expressed in millions of RMB)*	*(expressed in millions of RMB)*
Corporate loans to				
– Joint-stock enterprises	83,086	119,369	130,157	162,525
– State-owned enterprises	64,826	84,252	100,738	123,188
– Foreign invested enterprises	22,156	27,171	27,040	31,257
– Private enterprises	8,398	11,662	13,636	16,511
– Collectively-controlled enterprises	7,730	6,386	4,480	5,233
– Others	8,321	7,582	6,224	6,360
Subtotal	194,517	256,422	282,275	345,074
Personal loans				
– Home mortgage loans	8,149	17,838	26,246	30,705
– Credit card advances	11	208	447	655
– Others	9,077	13,684	11,141	10,827
Subtotal	17,237	31,730	37,834	42,187
Discounted bills	45,559	18,727	50,151	53,701
Gross loans and advances to customers	257,313	306,879	370,260	440,962
Less: Impairment allowances	(16,774)	(14,958)	(12,230)	(10,956)
Net loans and advances to customers	240,539	291,921	358,030	430,006

(c) Loans and advances to customers analysed by expected next repricing date and effective interest rate

	Effective interest rate	Total	Non-interest bearing	Less than three months	Between three months and one year	Between one and five years	More than five years
For the year 2003	4.66%	240,539	–	102,908	136,216	1,415	–
For the year 2004	4.85%	291,921	–	134,079	155,869	1,973	–
For the year 2005	5.18%	358,030	–	158,629	197,656	1,745	–
For the 6 months ended 30 June 2006	5.15%	430,006	–	184,300	243,296	2,347	63

Deposits

Set out below is a table setting out further information on the deposits of CNCB for the years ended 31 December 2005, 2004, 2003 and the six months ended 30 June 2006:

(a) Analysed by nature

	2003	2004	2005	30 June 2006
	(expressed in millions of RMB)	*(expressed in millions of RMB)*	*(expressed in millions of RMB)*	*(expressed in millions of RMB)*
Demand deposits				
– Corporate customers	159,876	179,106	232,933	225,399
– Personal customers	5,778	6,811	10,110	14,703
	165,654	185,917	243,043	240,102
Time deposits				
– Corporate customers	153,176	208,140	226,388	256,994
– Personal customers	26,526	40,963	61,142	73,899
	179,702	249,103	287,530	330,893
Total	345,356	435,020	530,573	570,995

(b) Analysed by geographical segments

	2003 *(expressed in millions of RMB)*	2004 *(expressed in millions of RMB)*	2005 *(expressed in millions of RMB)*	30 June 2006 *(expressed in millions of RMB)*
Bohai Rim	131,092	167,713	207,676	203,276
Yangtze River Delta	95,109	127,269	146,579	167,804
Pearl River Delta and West Strait	50,914	59,003	72,855	82,486
Central	24,747	32,420	47,214	54,176
Western	31,619	34,250	39,204	40,999
Northeastern	11,121	13,793	16,579	21,317
Head Office	754	572	466	937
Total	345,356	435,020	530,573	570,995

(c) Deposits from customers analysed by expected next repricing date and effective interest rate

	Effective interest rate	Total	Non-interest bearing	Less than three months	Between three months and one year	Between one and five years	More than five years
For the year 2003	1.55%	345,356	3,056	263,203	62,933	10,450	5,714
For the year 2004	1.66%	435,020	5,182	336,007	75,541	12,815	5,475
For the year 2005	1.86%	530,573	18,929	416,860	78,392	11,916	4,476
For the period June 2006	1.94%	570,995	3,000	436,021	115,625	12,795	3,554

Key Financial Ratios

Set out below is a table setting out the asset quality indicators of CNCB for the years ended 31 December 2005, 2004 and 2003 and six months ended 30 June 2006.

	31 December 2003	31 December 2004	31 December 2005	30 June 2006
Capital adequacy ratio[(1)]	–	–	8.11%	9.52%
RMB current assets to RMB current liabilities[(2)]	57.82%	61.28%	60.69%	46.25%
Foreign currency current assets to foreign currency current liabilities[(2)]	57.87%	74.52%	68.00%	103.89%
Loans to deposits[(3)]	74.51%	70.54%	69.78%	77.23%
Loans to total assets[(4)]	64.84%	61.94%	62.27%	68.13%
Gross impaired loans and advances to customers as a percentage of total loans and advances to customers	9.02%	6.28%	4.14%	2.92%
Loan loss coverage[(5)]	72.29%	77.58%	79.88%	84.97%

Notes

(1) The capital adequacy ratio is calculated in accordance with the guideline "Regulation Governing Capital Adequacy of Commercial Banks" Order (2004) No. 21 effective on 1 March 2004 and based on CNCB's financial statements prepared in accordance with the Accounting Standards for Business Enterprises, the Accounting Regulations for Financial Enterprises (issued by the MOF in 2001) and other regulations issued by the MOF (collectively named as "PRC GAAP"). It is calculated by dividing the total capital base after deduction by risk weighted assets.

The capital adequacy ratios as at 31 December 2003 and 31 December 2004 reported to the CBRC respectively are not presented as the Group is of the opinion that they provide no real value to the equity owner given that they are based on the financial information of CNCB calculated in accordance with the Accounting Standards for Business Enterprises, the Accounting Regulations for Financial Enterprises (jointly issued by the MOF and PBOC in 1993) and other relevant regulations issued by the MOF (collectively "Previous PRC GAAP") and the guideline issued by the PBOC, which has been replaced by the CBRC guideline since March 2004.

(2) Calculated in accordance with the formula promulgated by the PBOC and CBRC and based on CNCB's financial statements prepared in accordance with Previous PRC GAAP (for the 31 December 2003 and 2004) and in accordance with PRC GAAP (for 31 December 2005).

(3) Calculated by dividing the total gross advances to customers by the total of deposits from customers.

(4) Calculated by dividing the total gross advances to customers by the total assets.

(5) Calculated by dividing the allowance for impairment losses for total gross loans and advances to customers by the gross impaired loans and advances to customers.

Segmental Information

An analysis of the segment information in respect of the business of CNCB Group is set out in note 32 to the accountants' report on CNCB set out in Appendix III to this circular.

Staff and Remuneration Policy

As at the end of 2005, CNCB Group had 13,485 staff under its employment and the total staff costs were RMB2,086 million, representing an increase of 31.94% from 2004. As at the end 2004, CNCB Group had 11,598 staff in its employment and the total staff costs were RMB1,581 million, representing an increase of 36.29% from RMB1,160 million in 2003.

Charges on Assets and Contingent Liabilities

The following assets have been pledged as security for bills rediscounting transactions and securities sold under repurchase agreements. The related secured liabilities are recorded as amounts due to central bank, or banks and other financial institutions of approximately similar carrying value at the balance sheet date.

				30 June
	2003	2004	2005	2006
Available-for-sale debt securities	300	3,930	865	1,599
Discounted bills	6,197	2,223	75	–
Total	6,497	6,153	940	1,599

An analysis of the contingent liabilities of CNCB Group is set out in note 29 to the accountants' report on CNCB set out in Appendix III to this circular.

Hedging and Currency Exposure

CNCB Group has undertaken forward, swap and option transactions in the foreign exchange and interest rate markets and, through the operations of its branch network, acts as an intermediary between a wide range of customers structuring deals to produce risk management products for its customers. These positions are managed through back to back deals entered into by CNCB Group with external parties to ensure that the CNCB Group's net exposures are within acceptable risk levels. A table setting out an analysis of the notional amounts of derivatives of CNCB Group is set out in note 33 to the accountants' report on CNCB in Appendix III to this circular.

CNCB Group's foreign currency positions arise from foreign exchange dealing, commercial bank operations and foreign currency capital related structural exposures. CNCB Group has a treasury department which manages the currency risk within its internal approved limits and manages other currency risk by spot and forward foreign exchange transactions and matching its foreign currency denominated assets with corresponding liabilities in the same currencies.

Future Plans

CNCB has plans to list its shares on the Stock Exchange and to expand its business.

INTRODUCTION

The unaudited pro forma financial information of the Combined Group is based on a number of assumptions, estimates, uncertainties and currently available information, and is provided for illustrative purposes. Accordingly, as a result of the uncertain nature of the accompanying unaudited pro forma financial information of the Combined Group, it may not give a true picture of the actual financial position or results of the Combined Group's operations that would have been attained had the Acquisition in CNCB Group, the Top Up Acquisition in CNCB Group and Subscription of the Company's shares by BBVA (Collectively known as "the Transactions") actually occurred on the dates indicated herein. Further, the accompanying unaudited pro forma financial information of the Combined Group does not purport to predict the Combined Group's future financial position or results of operations.

The Unaudited Pro Forma Financial Information of the Combined Group should be read in conjunction with the unaudited interim financial information of the Group as set out in Appendix II to this circular, the financial information of CNCB Group as set out in Appendix III to this circular and other financial information included elsewhere in this circular.

1. UNAUDITED PRO FORMA COMBINED CONSOLIDATED BALANCE SHEET OF THE GROUP AFTER COMPLETION

For illustrative purpose only, the following is the unaudited pro forma combined consolidated balance sheet of the Group, assuming that the Transactions had been completed on 30 June 2006. The unaudited pro forma combined consolidated balance sheet is prepared based on the unaudited consolidated balance sheet of the Group as at 30 June 2006, as extracted from the interim report of the Group for the period ended 30 June 2006 and adjusted to reflect the effect of the Transactions. As the unaudited pro forma combined consolidated balance sheet is prepared for illustrative purpose only and because of its nature, it may not give a true picture of the financial position of the Group as at the date to which it is made up to or at any future date.

Unaudited Pro Forma Combined Consolidated Balance Sheet
as at 30 June 2006
(Expressed in Hong Kong dollars)

	CIFH	CIFH's investment in CNCB Group (a)	CIFH's Top Up investment in CNCB Group (b)	BBVA's share subscription in CIFH (c)	Combined Balance
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Assets					
Cash and balances with banks and other financial institutions	890,256	–	–	–	890,256
Placements with banks and other financial institutions	10,481,273	–	(7,196,000)	3,897,789	7,183,062
Trade bills	372,181	–	–	–	372,181
Trading assets	6,656,459	–	–	–	6,656,459
Securities designated at fair value through profit or loss	825,538	–	–	–	825,538
Advances to customers and other accounts	47,867,573	–	–	–	47,867,573
Available-for-sale securities	5,977,276	–	–	–	5,977,276
Held-to-maturity investments	13,237,149	–	–	–	13,237,149
Interest in associates	1,322,877	5,327,612	7,196,000	–	13,846,489
Property and equipment					
– Investment property	168,725	–	–	–	168,725
– Other property and equipment	865,324	–	–	–	865,324
Goodwill	1,007,749	–	–	–	1,007,749
Deferred tax assets	28,422	–	–	–	28,422
Total assets	89,700,802	5,327,612	–	3,897,789	98,926,203

	CIFH	CIFH's investment in CNCB Group (a)	CIFH's Top Up investment in CNCB Group (b)	BBVA's share subscription in CIFH (c)	Combined Balance
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Equity and liabilities					
Deposits and balances of banks and other financial institutions	4,258,309	–	–	–	4,258,309
Deposits from customers	60,158,563	–	–	–	60,158,563
Trading liabilities	516,778	–	–	–	516,778
Certificates of deposit issued	6,263,059	–	–	–	6,263,059
Debt securities issued	2,241,122	–	–	–	2,241,122
Convertible bonds issued	1,309,089	–	–	–	1,309,089
Current taxation	96,684	–	–	–	96,684
Deferred tax liabilities	46,716	–	–	–	46,716
Other liabilities	767,870	–	–	–	767,870
Loan capital	4,275,599	–	–	–	4,275,599
Total liabilities	79,933,789	–	–	–	79,933,789
Equity					
Share capital	3,201,423	1,562,350	–	668,574	5,432,347
Reserves	6,565,237	3,765,262	–	3,229,215	13,559,714
Total equity attributable to equity shareholders of the Company	9,766,660	5,327,612	–	3,897,789	18,992,061
Minority interests	353	–	–	–	353
Total equity	9,767,013	5,327,612	–	3,897,789	18,992,414
Total equity and liabilities	89,700,802	5,327,612	–	3,897,789	98,926,203

2. UNAUDITED PRO FORMA COMBINED CONSOLIDATED INCOME STATEMENT OF THE GROUP

For illustrative purpose only, the following is the unaudited pro forma combined income statement of the Group, assuming that the Transactions had been completed on 1 January 2006. The unaudited pro forma combined consolidated income statement is prepared based on the unaudited consolidated income statement of the Group for the six months ended 30 June 2006, as extracted from the interim report of the Group for the six months ended 30 June 2006 and adjusted to reflect the effect of the Transactions.

Unaudited Pro Forma Combined Consolidated Income Statement
For the six months ended 30 June 2006
(Expressed in Hong Kong dollars)

	CIFH	CNCB Group (d)	Adjustment on interest income and tax (e)	Combined Balance
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Interest income	1,974,240	–	(67,778)	1,906,462
Interest expense	(1,476,382)	–	–	(1,476,382)
Net interest income	497,858	–	(67,778)	430,080
Fee and commission income	255,582	–	–	255,582
Fee and commission expense	(6,916)	–	–	(6,916)
Net fee and commission income	248,666	–	–	248,666
Net trading income	195,048	–	–	195,048
Net income from financial instruments designated at fair value through profit or loss	27,729	–	–	27,729
Net hedging income	1,465	–	–	1,465
Other operating income	17,707	–	–	17,707
Operating income	988,473	–	(67,778)	920,695
Operating expenses	(530,812)	–	–	(530,812)
	457,661	–	(67,778)	389,883
Impairment losses written back on loans and advances	6,335	–	–	6,335
Impairment losses written back on held-to-maturity investments	146	–	–	146
Impairment losses on available-for-sale securities	(4,849)	–	–	(4,849)

	CIFH	CNCB Group (d)	Adjustment on interest income and tax (e)	Combined Balance
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*
Impairment losses written back	1,632	–	–	1,632
Net profit on disposal of available-for-sale securities	18,870	–	–	18,870
Operating profit	478,163	–	(67,778)	410,385
Net profit on disposal of property and equipment	59,042	–	–	59,042
Revaluation gain on investment properties	6,867	–	–	6,867
Share of profits less losses of associates	46,087	264,986	–	311,073
Profit before taxation	590,159	264,986	(67,778)	787,367
Income tax	(98,721)	–	11,861	(86,860)
Profit after taxation	491,438	264,986	(55,917)	700,507
Attributable to:				
Equity shareholders of the Company	491,621	264,986	(55,917)	700,690
Minority interests	(183)	–	–	(183)
Profit after taxation	491,438	264,986	(55,917)	700,507
Earnings per share				
Basic	15.37¢			12.90¢
Diluted	14.47¢			12.50¢

3. UNAUDITED PRO FORMA COMBINED CONDENSED CONSOLIDATED CASH FLOW STATEMENT

For illustrative purpose only, the following is the unaudited pro forma combined condensed consolidated cash flow statement of the Group, assuming that the Transactions had been completed on 1 January 2006. The unaudited pro forma combined condensed consolidated cash flow statement is prepared based on the unaudited condensed consolidated cash flow statement of the Group for the six months ended 30 June 2006, as extracted from the interim report of the Group for the six months ended 30 June 2006 and adjusted to reflect the effect of the Transactions.

Unaudited Pro Forma Combined Condensed Consolidated Cash Flow Statement
For the six months ended 30 June 2006
(Expressed in Hong Kong dollars)

	CIFH	CIFH's Top-up investment in CNCB Group (b)	BBVA's share subscription in CIFH (c)	Adjustment on interest income and tax (e)	Combined Balance
	HK$'000			*HK$'000*	*HK$'000*
Cash generated from operations	4,968,764	–	–	(67,778)	4,900,986
Tax paid	(36,266)	–	–	–	(36,266)
Net cash generated from operating activities	4,932,498	–	–	(67,778)	4,864,720
Net cash (used)/generated from investing activities	40,170	(7,196,000)	–	–	(7,155,830)
Net cash generated/(used) in financing activities	(405,477)	–	3,897,789	–	3,492,312
Net increase/(decrease) in cash and cash equivalents	4,567,191	(7,196,000)	3,897,789	(67,778)	1,201,202
Cash and cash equivalents at 1 January	6,012,278	–	–	–	6,012,278
Cash and cash equivalents at 30 June	10,579,469	(7,196,000)	3,897,789	(67,778)	7,213,480

Notes to the Unaudited Pro Forma Combined Condensed Consolidated Cash Flow Statement

(1) The share of profits for CNCB does not have any effect on the unaudited pro forma combined condensed consolidated cash flow statement.

(2) The investment in CNCB in accordance to the Original Agreement with CITIC Group is settled by issuance of new Shares and thus does not have any effect in the unaudited pro forma combined condensed consolidated cash flow statement.

Major assumptions for Unaudited Pro Forma Information of the Group After completion

(1) The translation of Renminbi into Hong Kong dollars has been made at the assumed Completion Exchange Rate of RMB1.00 to HK$0.999757.

(2) The maximum Top Up Consideration of HK$7,196 million was used in the preparation of the Unaudited Pro Forma Financial Information. As discussed on Page 20 of this circular, the Top Up Consideration (on the basis that this is not aggregated with the Original Investment) shall not result in any of the Company's "percentage ratios" under Rule 14.07 of the Listing Rules exceeding 25%. Assuming the "consideration test" under Rule 14.07(4) is the most relevant to determining the Top Up Consideration, this translates to a maximum of approximately HK$7,196 million (based on the market capitalisation of the Company as at 22 November 2006 as enlarged by the issue of 1,562,349,676 Shares under the Original Agreement).

(3) After the Top Up investments in CNCB Group, the Company owns 15% equity interests in CNCB Group and the Company is able to exercise significant influence over CNCB through board representation. As discussed on Page 20 of this circular, on the CNCB Top Up Completion Date, the percentage of equity interests that will be held by the Company in the Joint Stock Company as of the Top Up Completion Date shall be no less than 15% of the total equity interests in CNCB (or its successor, the Joint Stock Company), as enlarged by the issue of the Top Up Shares, on a fully diluted basis.

(4) There is no indication of goodwill impairment on the interest in associate relating to the acquisition of CNCB. Therefore no goodwill impairment adjustment is required.

(5) The accounting policy on property valuation between CNCB group and CIFH is not the same. Subsequent to initial recognition, CNCB adopts a revaluation policy to carry all classes of property at revaluation less accumulated depreciation and impairment losses. Meanwhile, CIFH adopts a cost method to carry property held under operating leases at cost less accumulated depreciation and impairment losses. The share of profits for CNCB in the unaudited pro forma combined consolidated income statement of the Combined Group has not taken into account the adjustment needed to be made for standardising the accounting policy as the effect is not material to the Group's results.

(6) Any profit/(loss) effect of the deemed disposal as a result of any further capital injection by CITIC Group or BBVA into CNCB Group and any other form of capital expansion of CNCB Group occurring subsequent to the Acquisition in CNCB Group in accordance with the Original Agreement with CITIC Group and before the completion of the Top Up Acquisition has not been taken into account in the Unaudited Pro Forma Financial Information.

(7) Intangible assets were acquired as part of the acquisition of CNCB Shares and were included in the interest in associates. The Unaudited Pro Forma Financial Information has not taken into account the adjustment needed to be made for the amortisation of the acquired intangibles as the effect is not expected to be material to the Group's results.

(8) The direct cost incurred in connection with the Transactions has not been taken into account in the Unaudited Pro Forma Financial Information as the effect is not expected to be material to the acquisition cost.

(9) Banco Bilbao Vizcaya Argentaria, S.A. did not exercise the "Convertible Bond Top Up Right" and the "Anti-Dilution Top Up Right" to subscribe for additional new shares of the Company.

The Pro Forma adjustments reflect the following

(a) Being the acquisition of 19.9% equity stake in CNCB Group contemplated under the Original Agreement entered into with CITIC Group on 13 April 2006. The consideration is equivalent to 1.153 times 19.9% of the audited consolidated net asset value of CNCB as at 31 December 2005 prepared in accordance with IFRS and is satisfied by the issue and allotment by the Company of the consideration shares to CITIC Group at HK$3.41 per Share.

(b) Being the acquisition of further interest in CNCB Group contemplated under the Top Up Agreement entered into with CITIC Group on 22 November 2006, which is a continuation of the CIFH's investment in CNCB. The cash consideration is calculated based on the assumption (2) set out above.

(c) Being the share subscription in CIFH by Banco Bilbao Vizcaya Argentaria, S.A. with a cash consideration of HK$3,897,788,600 for 668,574,374 Shares at a price of HK$5.83 each.

(d) Being share of 15% of profit of CNCB Group for the six months ended 30 June 2006 after the completion of the CIFH's investment in CNCB and the CIFH's Top Up investment in CNCB Group on 1 January 2006. The effective ownership of 15% in CNCB Group by CIFH is based on assumption (3) set out above.

(e) Being the effect of decrease in interest income due to the settlement of cash consideration in CIFH's Top Up investment in CNCB Group net of the cash proceeds from BBVA upon its share subscription in the Company. The period average 6-month Hong Kong Dollar Interbank Offered Rates for January 2006 of 4.11% as obtained from the Monthly Statistical Bulletin of the Hong Kong Monetary Authority is adopted for illustrative purpose. The adjustment also reflects the corresponding profit tax effect calculated at 17.5%.

The following is the text of a report, prepared for the sole purpose of inclusion in this circular, received from the independent reporting accountants, KPMG, Certified Public Accountants, Hong Kong. As described in the section headed "Documents available for inspection" in Appendix V, a copy of the following report is available for inspection.

KPMG

8th Floor
Prince's Building
10 Chater Road
Central
Hong Kong

29 December 2006

The Board of Directors
CITIC International Financial Holdings Limited
Suites 1801-1802 Bank of America Tower
12 Harcourt Road Central
Hong Kong

Dear Sirs

CITIC International Financial Holdings Limited ("the Company")
Circular in connection with the Very Substantial Acquisition for
the Proposed Acquisition of further interest in China CITIC Bank (the "Circular")

Dear Sirs,

We report on the unaudited pro forma combined consolidated income statement, pro forma combined consolidated balance sheet and pro forma combined condensed consolidated cash flow statement ("the Pro Forma Financial Information") of the Company and its subsidiaries ("the Group") set out on pages 352 to 359 in Appendix IV of the Circular dated 29 December 2006, which has been prepared by the Directors of the Company solely for illustrative purposes to provide information about the following proposed transactions which might have affected the financial information presented. The proposed transactions are as follows:

- the proposed acquisition of a 19.9% equity stake in China CITIC Bank ("CNCB") contemplated under the Original Agreement entered into with CITIC Group on 13 April 2006 ("CIFH's investment in CNCB");

- the proposed acquisition of further interest in CNCB contemplated under the Top Up Agreement entered into with CNCB and CITIC Group on 22 November 2006, which is a continuation of CIFH's investment in CNCB. The purpose of this transaction is to ensure that the Group's interest in CNCB, on a fully diluted basis, will continue to be maintained at least 15% ("CIFH's Top Up investment in CNCB"); and

- the proposed share subscription in CIFH by Banco Bilbao Vizcaya Argentaria, S.A. with cash consideration of HK$3,897,788,600 for 668,574,374 Shares at a price of HK$5.83 each ("BBVA's share subscription in CIFH").

The basis of preparation of the Pro Forma Financial Information is set out on pages 352 to 359 of the Circular.

Responsibilities

It is the sole responsibility of the Directors of the Company to prepare the unaudited Pro Forma Financial Information in accordance with Paragraph 4.29 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and with reference to Accounting Guideline 7 "Preparation of Pro Forma Financial Information for inclusion in Investment Circulars" issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA").

It is our responsibility to form an opinion, as required by paragraph 4.29 of the Listing Rules, on the unaudited Pro Forma Financial Information and to report our opinion to you. We do not accept any responsibility for any reports previously given by us on any financial information used in the compilation of the unaudited Pro Forma Financial Information beyond that owed to those to whom those reports were addressed by us at the dates of their issue.

Basis of opinion

We conducted our work in accordance with Hong Kong Standard on Investment Circular Reporting Engagements 300 "Accountants' Reports on Pro Forma Financial Information in Investment Circulars" issued by the HKICPA. Our work consisted primarily of comparing the unadjusted financial information with source documents, considering the evidence supporting the adjustments and discussing the Pro Forma Financial Information with the Directors of the Company. The engagement did not involve independent examination of any of the underlying financial information.

Our work did not constitute an audit or review made in accordance with Hong Kong Standards on Auditing or Hong Kong Standards on Review Engagements issued by the HKICPA, and accordingly, we do not express any such audit or review assurance on the Pro Forma Financial Information.

We planned and performed our work so as to obtain the information and explanations we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Pro Forma Financial Information has been properly compiled by the Directors of the Company on the basis stated, that such basis is consistent with the accounting policies of the Group and that the adjustments are appropriate for the purposes of the unaudited Pro Forma Financial Information as disclosed pursuant to paragraph 4.29(1) of the Listing Rules.

The unaudited Pro Forma Financial Information is for illustrative purposes only, based on the judgements and assumptions of the Directors of the Company, and because of its hypothetical nature, it does not provide any assurance or indication that any event will take place in the future and may not be indicative of

- the financial position of the Group as at 30 June 2006 or any future date; or
- the earnings per share and results of the Group for the six months ended 30 June 2006 or any future periods.

Opinion

In our opinion:

(a) the unaudited Pro Forma Financial Information has been properly compiled on the basis stated;

(b) such basis is consistent with the accounting policies of the Group, and

(c) the adjustments are appropriate for the purposes of the unaudited Pro Forma Financial Information as disclosed pursuant to Paragraph 4.29(1) of the Listing Rules.

Yours faithfully
KPMG
Certified Public Accountants
Hong Kong

RESPONSIBILITY STATEMENT

This circular includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Group. The Directors collectively and individually accept full responsibility for the accuracy of the information contained in this circular and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief, statements of fact expressed herein are true, accurate and not misleading, statements of opinion expressed herein have been arrived at after due and careful consideration and there are no other facts not contained in this circular the omission of which would make any statement herein misleading.

SHARE CAPITAL

Authorised and issued share capital

The authorised and issued share capital of the Company as at the Latest Practicable Date were as follows:

Authorised:		*HK$*
Ordinary Shares		
6,000,000,000	Shares	6,000,000,000.00
Issued and fully paid:		
Ordinary Shares		
3,468,912,372	Shares	3,468,912,372.00

All the existing issued Shares rank pari passu in all respects including all rights as to dividends, voting and return of capital.

As at the Latest Practicable Date, save for the Convertible Bonds and options granted pursuant to share option scheme of the Company, the Group did not have any outstanding options, warrants or other securities carrying rights of conversion into or exchange or subscription for Shares.

DISCLOSURE OF INTERESTS

As at the Latest Practicable Date, the interests and short positions of the Directors and the chief executive of the Company in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which were required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have taken under such provisions of the SFO); or were required, pursuant to Section 352 of the SFO, to be entered in the register kept by the Company, or were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Companies in the Listing Rules, to be notified to the Company and the Stock Exchange were as follows:

1. Long positions in shares of the Company:

Name of Director	Capacity	Number of ordinary shares held	Percentage of issued share capital
Mrs. Chan Hui Dor Lam Doreen	Beneficial owner	2,074,689	0.060%
Mr. Zhao Shengbiao	Beneficial owner	2,014,114	0.058%

2. Long positions (in respect of equity derivatives) in underlying shares of the Company:

Share options, being unlisted physically settled equity derivatives, to subscribe for the ordinary shares of the Company were granted to Mr. Kong Dan, Mr. Dou Jianzhong, Mrs. Chan Hui Dor Lam Doreen, Mr. Lo Wing Yat Kelvin, Mr. Roger Clark Spyer and Mr. Zhao Shengbiao pursuant to the share option scheme of the Company. Details of these options are as follows:

Name of Director	Date of Options granted	Number of Options granted	Exercise Price	Vesting Period	Exercisable Period	Outstanding Options
Mr. Kong Dan	17/11/2003	400,000	HK$3.540	17/11/2003–16/11/2005	17/11/2005–16/11/2013	400,000
	06/04/2004	400,000	HK$3.775	06/04/2004–05/04/2006	06/04/2006–05/04/2014	400,000
	13/06/2005	400,000	HK$2.925	13/06/2005–12/06/2007	13/06/2007–12/06/2015	400,000
	18/05/2006	400,000	HK$4.275	18/05/2006–17/05/2008	18/05/2008–17/05/2016	400,000

Name of Director	Date of Options granted	Number of Options granted	Exercise Price	Vesting Period	Exercisable Period	Outstanding Options
Mr. Dou Jianzhong	18/05/2006	400,000	HK$4.275	18/05/2006–17/05/2008	18/05/2008–17/05/2016	400,000
Mrs. Chan Hui Dor Lam Doreen	17/11/2003	300,000	HK$3.540	17/11/2003–16/11/2005	17/11/2005–16/11/2013	300,000
	06/04/2004	300,000	HK$3.775	06/04/2004–05/04/2006	06/04/2006–05/04/2014	300,000
	13/06/2005	300,000	HK$2.925	13/06/2005–12/06/2007	13/06/2007–12/06/2015	300,000
	18/05/2006	300,000	HK$4.275	18/05/2006–17/05/2008	18/05/2008–17/05/2016	300,000
Mr. Lo Wing Yat Kelvin	17/11/2003	200,000	HK$3.540	17/11/2003–16/11/2005	17/11/2005–16/11/2013	200,000
	06/04/2004	200,000	HK$3.775	06/04/2004–05/04/2006	06/04/2006–05/04/2014	200,000
	13/06/2005	200,000	HK$2.925	13/06/2005–12/06/2007	13/06/2007–12/06/2015	200,000
	18/05/2006	200,000	HK$4.275	18/05/2006–17/05/2008	18/05/2008–17/05/2016	200,000
Mr. Roger Clark Spyer	18/05/2006	140,000	HK$4.275	18/05/2006–17/05/2008	18/05/2008–17/05/2016	140,000
Mr. Zhao Shengbiao	17/11/2003	40,000	HK$3.540	17/11/2003–16/11/2005	17/11/2005–16/11/2013	40,000
	06/04/2004	40,000	HK$3.775	06/04/2004–05/04/2006	06/04/2006–05/04/2014	40,000
	13/06/2005	40,000	HK$2.925	13/06/2005–12/06/2007	13/06/2007–12/06/2015	40,000
	18/05/2006	40,000	HK$4.275	18/05/2006–17/05/2008	18/05/2008–17/05/2016	40,000

In addition, the Equity Linked Deferred Award (the "**ELDA**") was granted by CKWB to the following Directors:

Name of Director	Offer date	Number of ordinary shares notionally subject to ELDA	ELDA price per share *(HK$)*
Mrs. Chan Hui Dor Lam Doreen	24/03/2005	150,000	2.00
	28/04/2006	250,000	2.00
Mr. Lo Wing Yat Kelvin	24/03/2005	80,000	2.00
Mr. Roger Clark Spyer	28/04/2006	100,000	2.00

3. Short positions in shares and (in respect of equity derivatives) underlying shares of the Company:

None.

4. Long and short positions in shares of associated corporations of the Company:

None.

5. Long positions (in respect of equity derivatives) in underlying shares of associated corporations of the Company:

Share options, being unlisted physically settled equity derivatives, to subscribe for the ordinary shares of CITIC Capital Holdings Limited ("**CCHL**"), an associated company of the Company, were granted by CCHL to the following Directors:–

Name of Director	Capacity	Number of CCHL's ordinary shares involved	Exercisable period
Mr. Kong Dan	Beneficial owner	30,000	02/03/2007 to 01/03/2010
	Beneficial owner	25,000	04/04/2008 to 03/04/2011
Mr. Dou Jianzhong	Beneficial owner	15,000	02/03/2007 to 01/03/2010
	Beneficial owner	10,000	04/04/2008 to 03/04/2011
Mrs. Chan Hui Dor Lam Doreen	Beneficial owner	15,000	02/03/2007 to 01/03/2010
	Beneficial owner	10,000	04/04/2008 to 03/04/2011
Mr. Wang Dongming	Beneficial owner	15,000	02/03/2007 to 01/03/2010
	Beneficial owner	10,000	04/04/2008 to 03/04/2011

6. Short positions (in respect of equity derivatives) in underlying shares of associated corporations of the Company:

None.

7. Interests in debentures of the Company:

None.

8. Interests in debentures of the associated corporations of the Company:

None

Save as disclosed above, as at the Latest Practicable Date, none of the Directors or chief executive of the Company were aware that they had any interests or short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) which are required and are due to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are deemed or taken to have under such provisions of the SFO) or which are required, pursuant to section 352 of the SFO to be entered in the register referred to therein or which are required and are due, pursuant to the Model Code for Securities Transactions by Directors of Listed Companies, to be notified to the Company and the Stock Exchange.

SUBSTANTIAL SHAREHOLDER

So far as the Directors are aware, other than a Director or chief executive of the Company, the following persons had an interest of 5% or more of the issued share capital of the Company as at the Latest Practicable Date:

1. Long positions in shares of the Company:

Name of Shareholder	**Capacity**	**Number of ordinary Shares held**	**Percentage of issued share capital** *(Note 3)*
CITIC Group	Beneficial owner *(Note 1)*	2,771,104,674	79.88%
	Interest of controlled corporations	1,376,770	0.04%

Name of Shareholder	Capacity	Number of ordinary shares held	Percentage of issued share capital *(Note 3)*
	Interests of any parties to an agreement to acquire interests in a particular listed corporation required to be disclosed under Section 317(1)(a) and Section 318 of the SFO *(Note 2)*	982,056,454	28.31%
BBVA	Beneficial owner	835,717,967	24.09%
	Other	1,769,800,884	51.02%

Note 1: These interests include the 1,789,048,220 Shares in the Company held by CITIC Group as at the Latest Practicable Date and the Shares in the Company which may be acquired by CITIC Group in exercise of its pre-emption rights over the Shares in the Company of BBVA pursuant to the share purchase agreement dated 22 November 2006 between CITIC Group and BBVA.

Note 2: These interests include the 668,574,374 Shares in the Company to be issued to BBVA and any additional Shares which may fall to be issued to BBVA in respect of the anti-dilution right of BBVA under the subscription agreement entered into between the Company and BBVA dated 22 November 2006.

Note 3: The percentage interest is calculated on the basis of an issued share capital of the Company of 3,468,912,372 Shares as at the Latest Practicable Date.

2. Short positions in shares of the Company:

Name of Shareholder	Capacity	Number of ordinary shares held	Percentage of issued share capital *(Note)*
CITIC Group	Beneficial owner	167,143,593	4.82%
BBVA	Beneficial owner	835,717,967	24.09%

Note: The percentage interest is calculated on the basis of an issued share capital of the Company of 3,468,912,372 Shares as at the Latest Practicable Date.

3. Long and short positions in (in respect of equity derivative) underlying shares of the Company:

None.

Save as disclosed above, the Directors or chief executive of the Company are not aware of any person (other than a Director or chief executive of the Company), who, as at the Latest Practicable Date, had interests or short positions in the shares or underlying shares of the Company which are required to be disclosed to the Company under the provision of Divisions 2 and 3 of Part XV of the SFO, or, who is expected, directly or indirectly, to be interested in 10% or more of the nominal value of any class of share capital carrying rights to vote in all circumstances at general meetings of any other member of the Group.

RELATIONSHIP WITH CNCB

CITIC Group has been the controlling shareholder of the Company since 1986 and has wholly-owned CNCB since its establishment. The Company has operated as CITIC Group's Hong Kong based international banking arm whilst CNCB is the domestic banking platform of CITIC Group. Although under common control, the Company and CNCB are operated and managed independently. Mr. Kong Dan and Mr. Chen Xiaoxian, Directors of the Company, are also directors of CNCB and Mr. Chen Xiaoxian is also its president.

The Company, through its subsidiary CKWB, and CNCB are in the process of agreeing business plans and strategies that will be complementary and supportive to each other's businesses. The Company does not believe that there is significant overlap or competition between CKWB and CNCB. CKWB has signified its intention to concentrate on developing crossborder services, offshore financing and overseas business with CITIC Group's corporate and industrial clients. CKWB will also develop relationships with large regional and international corporations and institutions looking to develop their businesses in the PRC, linking with CNCB to provide the onshore product and service requirements where CKWB is unable to do so. Accordingly, the focus of CKWB's Shanghai branch office, its representative and presence in the PRC, will be to meet the cross-border needs of its international customers as well as providing cross-border services to PRC customers with business needs in Hong Kong and elsewhere. CNCB will provide domestic banking, trade and other PRC based products and services which link in as appropriate with CKWB.

Given the cooperative and supplementary nature of the business relationship and the clear delineation of business between CNCB and CKWB, and as both banks are under the supervision of a number of regulators, the Directors believe that the interests of minority shareholders of the Company are adequately protected.

DIRECTORS' INTERESTS IN POTENTIALLY COMPETING BUSINESS

As at the Latest Practicable Date, the interests of the Directors and their respective associates required to be disclosed pursuant to Rule 8.10 of the Listing Rules were as follows:

1. Mr. Kong Dan is the chairman, Mr. Chang Zhenming is the vice chairman and president and Mr. Dou Jianzhong, Mr. Chen Xiaoxian, Mr. Ju Weimin and Mr. Wang Dongming are directors of CITIC Group, a conglomerate with businesses (through its subsidiaries) in the area of money lending and securities services;

2. Mr. Kong Dan and Mr. Chen Xiaoxian are directors of CNCB, a subsidiary of CITIC Group, engaged in the provision of banking and financing services;

3. Mr. Dou Jianzhong is a director of China Investment and Finance Limited, a subsidiary of CNCB, engaged in the provision of money lending services; and

4. Mr. Wang Dongming is the chairman and Mr. Ju Weimin is a director of CITIC Securities Co., Ltd., an associate company of CITIC Group, engaged in the provision of securities services.

SERVICE CONTRACTS

As at the Latest Practicable Date, none of the Directors have entered into any service contract with the Company or any members of the Group which will not expire or is not determinable by the employer within one year without payment of compensation (other than statutory compensation).

INTERESTS IN ASSETS AND/OR CONTRACTS AND OTHER INTERESTS

As at the Latest Practicable Date, none of the Directors had any direct or indirect interest in any assets which had been, since 31 December 2005, being the date to which the latest published audited accounts of the Company were made up, acquired or disposed of by or leased to any member of the Group, or are proposed to be acquired or disposed of by or leased to any member of the Group.

As at the Latest Practicable Date, none of the Directors was materially interested in any contract or arrangement which is significant in relation to the business of the Group.

EXPERTS' QUALIFICATIONS AND CONSENTS

The following are the qualifications of the experts whose letters and reports (as the case may be) are contained in this circular:

Name	Qualification
Somerley Limited	a licensed corporation under the SFO to conduct type 1 (dealing in securities), type 4 (advising on securities), type 6 (advising on corporate finance) and type 9 (asset management) regulated activities under the SFO
KPMG	Certified Public Accountants

Each of Somerley Limited and KPMG has given and has not withdrawn its written consent to the issue of this circular with the inclusion of its letter and/or report (as the case may be) and the references to its name, in the form and context in which they are included.

As at the Latest Practicable Date, none of Somerley Limited and KPMG had any shareholding in any member of the Group or the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group.

As at the Latest Practicable Date, none of Somerley Limited and KPMG had any direct or indirect interest in any assets which had been, since 31 December 2005, being the date to which the latest published audited accounts of the Company were made up, acquired or disposed of by or leased to any member of the Group, or are proposed to be acquired or disposed of by or leased to any member of the Group.

LITIGATION

As at the Latest Practicable Date, there was no litigation or claims of material importance pending or threatened against any member of the Group.

MATERIAL CONTRACTS

As at the Latest Practicable Date, the following are the material contracts (not being contracts entered into in the ordinary course of business) entered into by members of the Group within the two years immediately preceding the Latest Practicable Date:

1. the Original Agreement;
2. the Subscription Agreement;
3. the Cooperation MOU;
4. the Top Up Agreement;
5. the CNCB Cooperation MOU; and
6. the share transfer and subscription agreement dated 4 December 2006 entered into between the Company, CIAM and Asset Managers Co., Ltd., Ithmaar Bank B.S.C. and Mega Rider Offshore Ltd. (as investors) in relation to the purchase and subscription of shares in CIAM by the investors.

GENERAL

(a) The secretary of the Company is Ms. Kyna Y.C. Wong, Associate Member of The Institute of Chartered Secretaries & Administrators and The Hong Kong Institute of Company Secretaries.

(b) The qualified accountant of the Company appointed pursuant to Rule 3.24 of the Listing Rules is Mr. Wong Ho Sing Steve, Fellow Member of The Association of Chartered Certified Accountants and The Hong Kong Institute of Certified Public Accountants, and Associate Member of The Institute of Chartered Secretaries & Administrators and The Hong Kong Institute of Company Secretaries.

(c) The registered office of the Company is at Suites 1801-2, Bank of America Tower, 12 Harcourt Road, Central, Hong Kong.

(d) In the event of inconsistency, the English language text of this circular shall prevail over the Chinese language text.

DOCUMENTS AVAILABLE FOR INSPECTION

Copies of the following documents will be available for inspection during normal business hours at 20th Floor, Alexandra House, 16 – 20 Chater Road, Central, Hong Kong from the date of this circular up to and including the date of the EGM:

(a) the Subscription Agreement;

(b) the Cooperation MOU;

(c) the Top Up Agreement;

(d) the CNCB Cooperation MOU (including the CNCB Cooperation Agreement);

(e) the Original Agreement;

(f) the promoters' agreement dated 22 November 2006 between CNCB, CITIC Group and the Company;

(g) the memorandum and articles of association of the Company;

(h) the material contract (other then (a), (b), (c), (d) and (e) above) referred to in the section headed "Material Contracts" in this Appendix;

(i) the annual report of the Company for each of the two years ended 31 December 2004 and 31 December 2005;

(j) the accountants' report on CNCB from KPMG dated 29 December 2006, the text of which is set out in Appendix III to this circular;

(k) the letter on the unaudited pro forma financial information of the Company after Completion from KPMG dated 29 December 2006, the text of which is set out in Appendix IV to this circular;

(l) the letter from the Independent Board Committee, the text of which is set out on page 29 of this circular;

(m) the letter of Somerley Limited, the text of which is set out on pages 30 to 54 of this circular; and

(n) the letters of consent referred to in the section headed "Experts' Qualifications and Consents" in this Appendix.

中信國際金融控股有限公司
CITIC INTERNATIONAL FINANCIAL HOLDINGS LIMITED
(Incorporated in Hong Kong with limited liability under the Companies Ordinance)
(Stock Code: 183)

NOTICE IS HEREBY GIVEN THAT an Extraordinary General Meeting (the "Meeting") of the members of CITIC International Financial Holdings Limited (the "Company") will be held at Salon 5, Level 3, JW Marriott Hotel Hong Kong, Pacific Place, 88 Queensway, Hong Kong on Friday, 9 February 2007 at 10:00 a.m. for the purposes of considering and, if thought fit, passing with or without modification, the following resolutions as ordinary resolutions of the Company:

ORDINARY RESOLUTIONS

1. "**THAT** the authorized share capital of the Company be increased from HK$6,000,000,000 to HK$8,000,000,000 by the creation of additional 2,000,000,000 shares of HK$1.00 each."

2. "**THAT**:

(A) the terms of the subscription agreement (the "Subscription Agreement") (a copy of which has been produced to this Meeting marked "A" and initialed by the chairman of the Meeting for identification) dated 22 November 2006, between the Company and Banco Bilbao Vizcaya Argentaria, S.A. ("BBVA") pursuant to which, inter alia, subject to the fulfillment of the conditions set out therein, the Company has agreed to issue and allot 668,574,374 shares (the "Consideration Shares") of HK$1.00 each (each a "Share") at a price of HK$5.83 per Consideration Share, subject to the terms as set out in the Subscription Agreement, the details of which are described in the circular of the Company dated 29 December 2006, be and are hereby approved;

(B) the allotment and issue by the Company of the Consideration Shares in accordance with the Subscription Agreement be and is hereby approved;

(C) the allotment and issue by the Company of up to 33,353,587 new Shares at HK$5.83 per Share to BBVA during the period commencing from the date of completion of the Subscription Agreement and ending on 10 business days after 31 December 2007 which may fall to be issued as a result of the exercise by BBVA of its top up rights pursuant to the Subscription Agreement in connection with the conversion of the outstanding convertible bonds of the Company, the details of which are described in the circular of the Company dated 29 December 2006, be and is hereby approved;

(D) the Directors be and are hereby authorized to exercise all powers of the Company to deal with the allotment and issue by the Company of up to 112,984,900 new Shares to BBVA at a price equivalent to the average closing price of the Company for the twenty trading days immediately before the date of the notice of exercise by BBVA of its anti-dilution top up right (the "Anti-Dilution Top Up Right") pursuant to the Subscription Agreement if, during the period commencing from the date of completion of the Subscription Agreement and ending on 31 October 2007, BBVA exercises such rights in accordance with the terms of the Subscription Agreement , subject always to the conditions that:

(i) the pricing of any new Shares in respect of which BBVA is entitled to exercise its Anti-Dilution Top Up Right must be approved by the directors of the Company (the "Directors") (including the independent non-executive Directors) who do not have a direct interest in the transaction and who are not connected with BBVA or its associates;

(ii) where the Shares to be issued pursuant to the exercise of the Anti-Dilution Top Up Right is at a discount of more than 10% to the bench mark price, being the higher of:

(a) the closing price on the date of exercise relating to the proposed issue of Shares in respect of the Anti-Dilution Top Up Right; and

(b) the average closing price in the five trading days immediately prior to the earliest of:

(i) the date of the announcement in respect of the proposed issuance of Shares in respect of the Anti-Dilution Top Up Right (if any);

(ii) the date of the relevant exercise of the Anti-Dilution Top Up Right; and

(iii) the date on which the subscription price in respect of the exercise of the Anti-Dilution Top Up Right is fixed,

an independent financial adviser's opinion on the fairness of the price or value at which new Shares are to be issued to BBVA will be required, in addition to the approval of the Directors described above, and the Company will be required to include reference to this opinion in any announcement to be issued by the Company in relation to the issue of new Shares pursuant to the exercise of the Anti-Dilution Top Up Right by BBVA;

(iii) where the new Shares to be issued pursuant to the exercise of the Anti-Dilution Top Up Right by BBVA is at a discount of 20% or more to the benchmark price (described above), the approval of the independent shareholders of the Company will be required in advance of such issue; and

(iv) the issue price to BBVA upon the exercise of the Anti-Dilution Top Up Right should be no less than the price offered to independent third parties whose transaction gives rise to BBVA being entitled to exercise the Anti-Dilution Top Up Right;

(E) the Directors be and are hereby authorized to exercise all the powers of the Company and take all steps as might in their opinion be desirable or necessary in connection with the Subscription Agreement including, without limitation to:

(i) the execution, amendment, supplement, delivery, submission and implementation of any further documents or agreements with BBVA or any other parties in relation to the issue and allotment of the Subscription Shares or the Shares to be issued pursuant to the exercise of the anti-dilution rights in (C) and (D) of Resolution 2 above; and

(ii) the taking of all necessary actions to implement the transaction contemplated under the Subscription Agreement."

3. "**THAT**:

(A) the terms of the subscription agreement (the "Top Up Agreement") (a copy of which has been produced to this Meeting marked "B" and initialed by the chairman of the Meeting for identification) dated 22 November 2006, among the Company, China CITIC Bank ("CNCB") and CITIC Group pursuant to which, inter alia, subject to the fulfillment of the conditions set out therein, the Company agreed to subscribe for, and CNCB (or its successor, a joint stock company to be restructured from CNCB) agreed to issue to the Company such number of shares so that the percentage of equity interest of the Company in the joint stock company will be no less than 15% and the consideration for each share in the joint stock company will be the final Hong Kong dollar price per H-share of the joint stock company at which they are to be offered to the pubic and is to be satisfied in cash, provided that such consideration (on the basis that it is not aggregated to the transaction under the sale and purchase agreement between the Company and CITIC Group dated 13 April 2006) shall not result in any of the Company's "percentage ratios" under Rule 14.07 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited to exceed 25%, the details of which are described in the circular of the Company dated 29 December 2006, be and are hereby approved;

(B) the terms of the memorandum of understanding (the "CNCB Cooperation MOU") together with the agreement (the "CNCB Cooperation Agreement") to be entered into among CITIC Group, CNCB and the Company pursuant to the CNCB Cooperation MOU (a copy of which has been produced to this Meeting marked "C" and initialed by the chairman of the Meeting for identification) dated 22 November 2006, between the Company, CNCB and CITIC Group, be and are hereby approved and that the entering into by the Company of the CNCB Cooperation Agreement subject to such comments and amendments as may be required by the relevant regulatory authorities be and is hereby approved;

(C) a committee of Directors (comprising at least two independent non-executive Directors) be and are hereby authorized to exercise all the powers of the Company and take all steps as might in their opinion be desirable or necessary in connection with the Top Up Agreement, the CNCB Cooperation MOU and the CNCB Cooperation Agreement including, without limitation to:

(i) the execution, amendment, supplement, delivery, submission and implementation of any further documents or agreements with CNCB and/or CITIC Group or any other parties in relation to the Top Up Agreement, the CNCB Cooperation MOU and the CNCB Cooperation Agreement;

(ii) the amendment of the terms of the CNCB Cooperation Agreement to such extent as they consider necessary or desirable to take into account comments and amendments as may be required by the relevant regulatory authorities;

(ii) the taking of all necessary actions to implement the transaction contemplated under the Top Up Agreement, the CNCB Cooperation MOU and the CNCB Cooperation Agreement."

By Order of the Board
CITIC International Financial Holdings Limited
Kyna Y. C. Wong
Company Secretary

Dated 29 December 2006

Notes:

1. Every member entitled to attend and vote at the Meeting convened by the above notice is entitled to appoint one or more proxies to attend and vote in his stead provided that if more than one person is authorised, the proxy/authorisation must specify the number of Shares in respect of which each such person is so authorised. The proxy need not be a member of the Company.

2. A form of proxy for use at the Meeting convened by the above notice is enclosed herewith. To be valid, the form of proxy and the power of attorney or other authority (if any) under which it is signed (or a notarially certified copy of such power of attorney or authority) must be completed, signed and deposited to the Company's share registrar, Computershare Hong Kong Investor Services Limited, at 46th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong not less than 48 hours before the time appointed for holding the Meeting or any adjournment thereof.

3. The instrument appointing a proxy shall be in writing in any usual or common form or in any other form which the Directors may accept (provided that this shall not preclude the use of the two-way form), and shall be deemed, subject to the proviso described in note 4 below, to confer authority upon the proxy to vote on any resolution (or amendment thereto) put to the Meeting for which it is given as the proxy thinks fit.

4. Provided that any form issued to a Shareholder for him/her for appointing a proxy to attend at the Meeting at which special business is to be transacted shall be such as to enable the Shareholder according to his intention to instruct the proxy to vote in favour of or against (or, in default of instructions, to exercise his discretion in respect of) each resolution dealing with any such special business and shall, unless the contrary is stated therein, be valid as well for any adjournment of the Meeting and for the Meeting to which it relates.

5. Delivery of an instrument appointing a proxy shall not preclude a Shareholder from attending and voting in person at the Meeting or poll concerned and, in such event, the instrument appointing a proxy shall be deemed to be revoked.

6. Where two or more persons are registered as the holder of any Share, the Company shall be at liberty to treat the person whose name stands first in the register of members as one of the joint holders of any Shares as solely entitled to attend or vote at the Meeting, but any one of such joint holders may be appointed the proxy of the persons entitled to vote on behalf of such joint holders, and as such proxy to attend and vote at the Meeting of the Company, but if more than one of such joint holders be present at any meeting personally or by proxy that one so present whose name stands first in the register of member in respect of such Shares shall alone be entitled to vote in respect thereof.