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**中銀香港(控股)有限公司**

**BOC HONG KONG (HOLDINGS) LIMITED**

*(Incorporated in Hong Kong with limited liability)*

**(the “Company”, Stock Code: 2388)**

## **2010 INTERIM RESULTS ANNOUNCEMENT**

The Board of Directors of the Company (the “Board”) is pleased to announce the unaudited results of the Company and its subsidiaries for the six months period ended 30 June 2010. This announcement, containing the full text of the 2010 Interim Report of the Company, complies with the relevant requirements of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited in relation to information to accompany preliminary announcements of interim results. Printed version of the Company’s 2010 Interim Report will be delivered to the Company’s shareholders who have not indicated their preference to receive corporate communication by electronic means and will also be available for viewing on the websites of Hong Kong Exchanges and Clearing Limited at [www.hkex.com.hk](http://www.hkex.com.hk) and of the Company at [www.bochk.com](http://www.bochk.com) in mid September 2010.

# FINANCIAL HIGHLIGHTS

|                                                                                                          | Half-year ended<br>30 June<br>2010<br>HK\$'m | Half-year ended<br>30 June<br>2009<br>HK\$'m | Year ended<br>31 December<br>2009<br>HK\$'m |
|----------------------------------------------------------------------------------------------------------|----------------------------------------------|----------------------------------------------|---------------------------------------------|
| Net operating income before impairment allowances                                                        | 12,541                                       | 13,028                                       | 26,055                                      |
| Operating profit                                                                                         | 8,168                                        | 7,719                                        | 15,104                                      |
| Profit before taxation                                                                                   | 8,767                                        | 8,244                                        | 16,724                                      |
| Profit for the period/year                                                                               | 7,353                                        | 6,875                                        | 14,046                                      |
| Profit attributable to the equity holders<br>of the Company                                              | 7,190                                        | 6,691                                        | 13,725                                      |
|                                                                                                          | HK\$                                         | HK\$                                         | HK\$                                        |
| Earnings per share                                                                                       | 0.6800                                       | 0.6329                                       | 1.2981                                      |
| Dividend per share                                                                                       | 0.4000                                       | 0.2850                                       | 0.8550                                      |
|                                                                                                          | HK\$'m                                       | HK\$'m                                       | HK\$'m                                      |
| Capital and reserves attributable to<br>the equity holders of the Company                                | 106,711                                      | 94,149                                       | 102,902                                     |
| Issued and fully paid share capital                                                                      | 52,864                                       | 52,864                                       | 52,864                                      |
| Total assets                                                                                             | 1,302,176                                    | 1,146,150                                    | 1,212,791                                   |
| <b>Financial ratios</b>                                                                                  | %                                            | %                                            | %                                           |
| Return on average total assets <sup>1</sup>                                                              | 1.17                                         | 1.23                                         | 1.19                                        |
| Return on average capital and reserves attributable<br>to the equity holders of the Company <sup>2</sup> | 13.72                                        | 15.13                                        | 14.79                                       |
| Cost to income ratio                                                                                     | 36.15                                        | 32.19                                        | 46.60                                       |
| Loan to deposit ratio <sup>3</sup>                                                                       | 64.02                                        | 57.66                                        | 60.98                                       |
| Average liquidity ratio <sup>4</sup>                                                                     | 37.81                                        | 39.70                                        | 40.18                                       |
| Capital adequacy ratio <sup>5</sup>                                                                      | 16.17                                        | 16.10                                        | 16.85                                       |

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

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

3. Loan to deposit ratio is calculated as at 30 June 2010, 30 June 2009 and 31 December 2009. Loan represents gross advances to customers. Deposit also includes structured deposits reported as "Financial liabilities at fair value through profit or loss".

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

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

## CHAIRMAN'S STATEMENT

For the first six months of 2010, the Group maintained its growth momentum in its core businesses and a strong financial position. Despite continued improvement in the economic environment, overall operating conditions remained challenging, especially in the competitive landscape. We remained focused on executing our strategy and managed to capture quality growth opportunities by capitalising on our core strengths. The Group's operating income before impairment allowances decreased mildly by 3.7% year-on-year to HK\$12,541 million. Operating profit before impairment allowances declined by 9.4% to HK\$8,007 million. The Group's profit attributable to shareholders increased by 7.5% year-on-year to HK\$7,190 million or HK\$0.68 per share. The increase in our profit was helped by the improvement in the impairment allowances of securities investments compared to the same period last year. The Board has declared an interim dividend of HK\$0.40 per share, representing an increase of 40.4% compared to HK\$0.285 per share for the same period last year.

During the period, we continued to manage our balance sheet prudently. As at end June 2010, total assets grew 7.4% to HK\$1,302.2 billion. Our loan book grew 11.0% while loan quality remained strong with classified or impaired loan ratio further improving to 0.23% from 0.34% at end 2009. We continued to manage our treasury investments proactively as the global markets remained volatile. We adopted a flexible deposit strategy to support the growth of our business. As at end June 2010, our customer deposits grew 5.7% and loan-to-deposit ratio increased to 64.02% from 60.98% as at end 2009. We maintained a solid capital base with our consolidated capital adequacy ratio standing comfortably at 16.17% and a core capital ratio of 11.33%. Our liquidity position remained solid at 37.81%.

With China's increasing importance in the global economy, we believe the offshore RMB market will continue to expand in an incremental and orderly manner. The RMB business will become an important growth driver for the banking industry in Hong Kong in the longer term. The launch of the Pilot RMB Trade Settlement Scheme in July 2009 marked an important milestone in the development of the RMB business. By enabling the use of RMB in global trades, it has extended the scope of RMB business beyond personal transactions in Hong Kong which was first started in 2004. To further enhance the flexibility of Hong Kong banks to conduct RMB businesses, the Hong Kong Monetary Authority elucidated supervisory principles and operational arrangements regarding RMB business in February 2010. In June, the trade settlement scheme was further expanded to cover the major economic regions of the Mainland and its global trading partners beyond the ASEAN countries. Lately, the use of RMB in foreign direct investment into the Mainland is also allowed, subject to relevant regulatory approval. Moreover, BOCHK was appointed by People's Bank of China as the Clearing Bank of RMB cashnotes business for Taiwan. This new service will further facilitate exchanges between people and businesses across the strait and strengthen economic and commercial ties between the Mainland and Taiwan. All these positive developments will enhance the use and circulation of RMB offshore. As the Clearing Bank of RMB business in Hong Kong, we will continue to work closely with the regulators and are committed to supporting and contributing to the steady and healthy growth of the offshore RMB market.

The RMB business is an important strategic focus for the Group. With the increasing significance of RMB in the global economy, we believe there will be increasing demand for RMB products and services. We will focus on

developing a wide spectrum of RMB products and services to meet the needs of our customers. We will also closely collaborate with BOC, our parent bank, to enhance the Group's overall RMB service capability and to consolidate the Group's leading position.

Over the past years, we have been strengthening our franchise and demonstrated our ability to grow and steer our business through different phases of the economic cycle. On a positive note, the global financial crisis in 2008 provided BOCHK a valuable opportunity to deepen our relationship with customers. This was demonstrated in our 2009 performance, especially in our corporate lending business. Capitalising on our strong balance sheet, we were able to support our customers through tough times. Our efforts and support were greatly appreciated by our customers and we continued to explore new business opportunities with them. We also invested judiciously in our strategic focuses to maintain our core competitiveness and to enhance our capabilities to better serve our customers. Looking ahead, we will continue to capitalise on our fundamental strengths and strong cooperation with BOC to capture the emerging growth opportunities in China and the Asia Pacific region.

The global economy is gradually recovering from the financial crisis but there are still uncertainties about the shape and pace of the recovery. Taking into account the magnitude of this unprecedented crisis, headwinds should still be expected across the path to recovery. We have already seen some volatility in the global financial market since the second quarter, triggered by the sovereign debt crisis in Europe. As for the Chinese economy, it is maintaining respectable growth via domestic growth impetus, which in turn provides solid support to the Hong Kong economy. We will closely monitor the market

developments and take proactive measures to safeguard our financial strengths, so we can respond swiftly and continue to lead. Amid market uncertainties and volatilities, prudent and efficient risk management is key to ensure the Group's quality growth. We remain confident that given our capital strength and enhanced business capabilities, this will allow us to deliver sustainable growth and create greater values for our shareholders in the long term.

While we are pleased with our progress to date, we are aware that there is still a lot more we can achieve. My colleagues and I are deeply committed to our vision to be our customers' premier bank and to striving for continual improvement. I also wish to thank our customers and shareholders for their continuous support and the Board for their wisdom and counsel. Lastly, with effect on 21 May 2010, Madam Yang Linda Tsao has retired as an Independent Non-Executive Director of the Company and its principal operating subsidiary, Bank of China (Hong Kong) Limited. On behalf of the Board, I would like to take this opportunity to thank Madam Yang Linda Tsao for her valuable contributions to the Group during her tenure of office since 2003 and wish her a happy retirement.



**XIAO Gang**

*Chairman*

26 August 2010

# CHIEF EXECUTIVE'S REPORT

The operating environment for the banking industry in Hong Kong continued to stabilise in the first half of 2010. We witnessed strong economic growth spurred by the rise in domestic consumption, business investment, export of goods, inbound tourism as well as investment in property. These gave rise to demand for credit and banking services. However, the recovery of major economies from the global financial crisis was still far from smooth. International financial markets remained volatile. Interest rates stayed at an exceptionally low level, which had a direct impact on banks' net interest income. Competition intensified and the cost of operation escalated with inflation.

Despite these challenges, we focused on growing our traditional businesses by capitalising on our solid foundations and unique competitiveness. In the first six months, we maintained our growth momentum for core businesses and solidified our market lead in key areas. Of equal, if not more, importance, we have succeeded in capturing various new business opportunities. In particular, we made significant headway in expanding the scope and geographical reach of our RMB-related business. We also further strengthened our leading position in offering cross-border banking services. In view of the uncertainties that still prevailed in the market, we took effective steps to further enhance our risk management, boost our capital strength and ensure our liquidity position.

## Business Highlights

Our key business results in the first half of 2010 are highlighted as follows:

- By taking advantage of the reviving economy to drive business growth and improve profitability, we continued to grow our profit attributable to shareholders by a healthy margin. We recorded robust growth in total assets.
- We managed to maintain our net interest income in an unfavourable interest rate environment.
- Our lending business registered strong broad-based growth, led by corporate lending, trade finance, residential mortgage and our Mainland operation. In view of the changes in the market, we have proactively adjusted our lending strategy in the latter part of this reporting period in order to strike a better balance among growth, return and risks.
- Despite fierce competition in the market, we achieved an inspiring increase in customers' deposits with strong performance of RMB deposits.
- We maintained our leading market positions in corporate lending, loan syndication, residential mortgage and RMB-related business in Hong Kong. Our life insurance business recorded significant growth in the first half.
- We made various breakthroughs in our RMB banking business. An important milestone is that we have extended our reach beyond Hong Kong to the world. In line with the steady opening of RMB business, we pioneered a significant number of new RMB services in trade settlement and finance, corporate lending and corporate bonds. Our launch of the CNY HIBOR as a reference rate for RMB trade settlement and commercial loans in Hong Kong was applauded by the market.
- Our ability to innovate in cross-border financial services is apparent. We broadened our custody services to QDIIs in China and offered an increasing number of wealth management solutions for corporate and individual clients in the Mainland.
- We made considerable progress in our collaboration with BOC which resulted in major achievements in such key areas as offering global service for major corporate clients of both banks, extension of credit card business for BOC's overseas branches, providing support to these branches by our call centre, as well as IT cooperation on many business fronts.
- The Group's asset quality has proved to be excellent. Our classified or impaired loan ratio kept improving to the best level in the local market.
- We successfully issued two subordinated notes in February and April of this year respectively to repay the USD Subordinated Credit Facility provided by BOC in 2008, which broadened our investor base, established a market benchmark, diversified our funding channels and enhanced our international profile. Our capital adequacy ratio stayed at a level which is strong for sustaining our growth and development.

## Financial Performance

In the first six months of 2010, profit attributable to the Company's shareholders increased by 7.5% to HK\$7,190 million, which was due primarily to the stable contributions from most of our core business earnings and a net reversal of impairment allowances on securities investments.

The Group's net operating income before impairment allowances was HK\$12,541 million, down 3.7% year-on-year. Operating profit before impairment allowances was HK\$8,007 million, 9.4% lower as compared with the first half of 2009 but improved significantly by 57.6% from the second half of the year. Return on average total assets (ROA) and return on average capital and reserves attributable to the equity holders (ROE) were 1.17% and 13.72% respectively, versus 1.23% and 15.13% respectively for the first half of 2009.

Net interest income was stable at HK\$8,964 million as the net interest margin (NIM) narrowed by 21 basis points year-on-year to 1.58%. This decrease was, however, largely offset by a growth of 12.6% in the Group's average interest-earning assets which reached HK\$1,142,383 million. It should be noted that we have taken initiatives to improve the pricing of new corporate loans during the period.

Net fee and commission income grew by 15.3% year-on-year to HK\$3,397 million. This was led mainly by the hefty rise in loan commissions of 56.5%, made possible by the Group's expanded lending. Fees from our credit card business increased by an impressive 28.1%. Satisfactory growth was also recorded in fee income from other traditional banking businesses such as bills, payments services and currency exchange. Compared to the second half of 2009, net fee and commission income dropped slightly by 4.6% due to the decline in stock brokerage fee income in a less buoyant market.

There was a net trading loss of HK\$36 million in the first half versus a net trading gain of HK\$804 million in the same period of 2009. This was caused mainly by foreign exchange (FX) losses on foreign exchange swap contracts and a mark-to-market loss on interest rate swap contracts, which will be reversed upon maturity of the contracts. FX swap contracts were used for the Group's funding activities and liquidity management; despite FX losses, there were interest differentials generated from these contracts and reflected in higher net interest income.

Riding on the growth momentum built up last year in our lending business, total loans and advances to customers grew by 20.2% year-on-year and 11.0% half-on-half to HK\$571,486 million. Over the interim period, corporate loans increased by 14.3%, trade finance by 34.0% and residential mortgage loans by 3.4%. Loans for use in Hong Kong were up 9.4% whereas loans for use outside Hong Kong were up 10.3%.

The Group's total assets increased by 7.4% over the 6-month period to HK\$1,302,176 million by 30 June 2010. Our effective risk management ensured the high quality of our assets. The classified or impaired loan ratio as at end-June of 2010 was 0.23%, versus 0.34% six months ago and 0.37% twelve months ago.

On the expenditure side, we continued to be highly cost-conscious throughout the period under review. Total operating expenses increased by 8.1% to HK\$4,534 million, which was primarily due to the rise in staff costs connected with higher accrual of performance-linked remuneration and increased human resources inputs in our Mainland operation. Business growth and development, including marketing and promotion in both the local and Mainland markets, also accounted for part of the total increase.

Our capital and liquidity positions remained strong. Consolidated capital adequacy ratio (CAR) as at 30 June 2010 was 16.17%, versus 16.10% as at 30 June and 16.85% as at the end of 2009. Core capital ratio was at 11.33%. The average liquidity ratio stayed at a healthy level of 37.81%, compared to 39.70% a year ago.

## Business Review

Our operating performance in the first two quarters duly reflects our competence and incessant effort in driving business growth and development.

### Personal Banking

During the first half of 2010, Personal Banking took full advantage of the improved market environment to grow its core segments, including residential mortgage, life insurance, wealth management, RMB banking and credit card business. It recorded an operating income of HK\$5,316 million and a profit before taxation of HK\$2,230 million, up 4.9% and 0.6% year-on-year respectively.

Through product innovation and strategic alliance with property developers, we grew our underwriting of new mortgages and maintained our market lead in the first half of the year. The Group's outstanding mortgage loans were up 3.4% versus the end of 2009. The quality of mortgage loans remained sound under rigorous risk assessment and control. The delinquency and rescheduled loan ratio stood at a low 0.03% by 30 June 2010.

In the interim period, sentiment in the local stock market was adversely affected by the external environment, in particular the sovereign debt crisis in Europe. This inevitably had a negative impact on our stock brokerage business and related fee income. Despite that, we attached great importance to enhance our products and services and put emphasis on acquiring new customers in both Hong Kong and the Mainland, thus effectively enlarging our stock-trading customer base.

Our Bancassurance business recorded significant growth in the period under review as a result of an expanded product spectrum. This not only led to a strong growth in sales income but reinforced our prominent position in the local life insurance market.

We continued to broaden our wealth management customer base by means of service differentiation and customisation. New promotional offers were launched to attract and retain high net-worth customers. By collaborating with BOC, we further expanded our cross-border wealth management services and provided more tailor-made services to customers in the Mainland and Hong Kong. In the first six months of 2010, the total number of wealth management customers and the amount of assets under our management increased by 6.7% and 1.5% respectively from the end of 2009.

The performance of the Group's credit card business was highly satisfactory in the interim period. Encouraging growth was recorded in card issuance (up by 9.3% compared with end-2009), cardholder spending and merchant acquiring (up by 21.4% and 41.8% respectively compared with the first half of 2009). The loan quality of card advances stayed excellent with the annualised charge-off ratio standing at 1.56%.

We reinforced our leading position in RMB banking services in Hong Kong by focusing on RMB integrated services, "RMB Remittance Express" and "RMB Exchange Express". Our RMB deposit-taking business in Hong Kong continued to flourish. We also remained the market leader in the RMB credit card business with the number of China Union Pay ("CUP") Dual Currency Credit Card issued by us grew by 45.5% versus six months ago, reaching a total of about 530,000 by the end of June. We are glad to witness that the Group was well ahead of the market in CUP merchant acquiring business through a host of merchant offers in Hong Kong, Macau and the Mainland, with merchant acquiring volume and cardholder spending up by 69.3% and 157.5% respectively year-on-year. Meanwhile, we launched the first RMB life insurance product in Hong Kong which was well-received by customers.

### **Corporate Banking**

The Group's Corporate Banking business experienced robust growth, solidified its market position in key segments and expanded its service range during the interim period. Operating income was HK\$4,459 million, up 16.1% year-on-year. Profit before taxation was HK\$3,358 million, up 14.4%.

By meeting the rise in demand in Hong Kong while stepping up the development of cross-border financial services for Mainland corporate clients, we recorded a solid growth of 14.3% in our corporate loan portfolio as compared to end-2009. We also maintained our position as the top mandated arranger in the Hong Kong-Macau syndicated loan market. These enabled us to increase our loan commission income substantially.

We expanded our SME business by actively promoting both the "SME Loan Guarantee Scheme" and "Special SME Loan Guarantee Scheme" in support of the HKSAR Government's initiatives to help SMEs. Meanwhile, we worked closely with BOC, NCB (China) and major trade associations to promote our SME services. We took great pleasure in receiving the "SME's Best Partner Award" for the third consecutive year granted by the Hong Kong Chamber of Small and Medium Business Limited.

We made considerable advancement in our RMB-related banking services following the announcement by the Hong Kong Monetary Authority (HKMA) of the "Elucidation of Supervisory Principles and Operational Arrangements Regarding RMB Business in Hong Kong" in February this year, which allowed a greater degree of flexibility in conducting RMB banking business. The Group then took the initiative in introducing a new range of RMB-related services to the market to meet the demand of our customers. We extended the first RMB export invoice finance, the first RMB import invoice finance, the first RMB working capital loan, as well as RMB remittance service for dividend payout. We also took advantage of the geographical expansion of the Cross-border RMB Trade Settlement Services Pilot Programme from 5 cities to 20 cities and provinces by enlarging our services to corporate clients in all the pilot cities.

Benefiting from the revival of global trade, our trade finance business experienced an impressive half-year growth of 34.0% while bills commission rose by 19.7% year-on-year. We retained our market share in the trade finance business amid fierce competition.

Meanwhile, our custody services continued to thrive and are now spread to a number of Mainland clients, including major banks and other financial institutions. By 30 June 2010, total assets under our custody reached HK\$384 billion. Through service enhancement, our cash management business also prospered by attracting a large number of customers. With the linkage with BOC and its overseas branches, our cash management service platform greatly facilitated customers in fund transfers between Hong Kong, the Mainland and a number of countries in the region.

### **Mainland Business**

The Group's Mainland business recorded satisfactory growth in the first half of the year. Customer deposits increased by 60.6% while total advances to customers grew by 18.2%. Total operating income increased by 11.8% to HK\$521 million, driven mainly by the rise in net interest income. Profit before taxation was HK\$256 million, down 16.9% as a result of higher operating expenses, necessitated by inputs for business development, and lower contribution from recoveries as compared with the first half of 2009. The asset quality remained good, with the classified loan ratio standing at 0.37% versus 0.44% at 31 December 2009.

Our branch network in China kept expanding. NCB (China)'s Wuxi branch was opened for operation in July and approval has been obtained for NCB (China) to open new sub-branches in Shanghai and Beijing respectively.

### **Treasury**

Fully alert to the volatile situation in the global investment market, we have been pursuing a prudent yet proactive approach in managing our investment portfolio in order to guard against risks while maximising return. Having regard to the market situation, in the first quarter we increased our investments in fixed rate debt securities, including government-related securities and higher quality bonds issued by financial institutions and corporates, to optimise interest return. In the second quarter, in view of the sovereign debt crisis in Europe, we chose to focus more on quality corporate bonds.

In terms of business development, we continued to concentrate on traditional products related to foreign exchange and precious metals which yielded good results. Hedging products linked to foreign exchange were offered to offshore customers. We also deepened our cooperation with BOC's overseas branches to conduct RMB exchange business.

In the interim period, the Treasury segment recorded an operating income of HK\$2,376 million, down 36.6%. Of which, net interest income dropped as part of the residual funds were redeployed to lending, whereas non-interest income was affected by factors as explained earlier in the paragraph of net trading gain. Profit before taxation was down 3.0% to HK\$2,118 million.

### **Insurance**

The Group's Insurance business recorded a profit before taxation of HK\$106 million, down 31.6% year-on-year because of higher commission expenses resulting from the substantial increase in new business.

We continued to expand our product range which led directly to the continuous growth in premium income in the first half. In line with the further opening of RMB business, we introduced new RMB insurance products which are settled in RMB or HKD. The demand for such products was encouraging which contributed to reinforcing our lead in the local RMB insurance market.

## Outlook

For the global economy, the road to full recovery after the 2008 financial crisis is expected to be long and uneven. We are also aware of the uncertainties that still prevail in the global financial markets. Despite the solid economic growth witnessed in Hong Kong in the past year or so, we cannot assume that it can be entirely immune from the uncertainties and potential pitfalls in the external environment. For banks, interest rates are still likely to stay at the current low level for longer than originally expected, which means that the pressure on net interest margin and net interest income will not be lifted in the foreseeable future. The competition for business is therefore expected to intensify.

In view of these challenges, we will continue to adopt a proactive but prudent approach in conducting our business in the remainder of the year. On the one hand, we will leverage our competitive advantages to capture new opportunities in order to grow our core businesses. On the other hand, we will remain extremely vigilant over our capital strength, the maintenance of liquidity, risk management and cost control. While striving for business growth, we will focus not just on volume but also on quality and sustainability to ensure risk-adjusted return.

With the increasing significance of RMB in the global economy, RMB-related banking business is now becoming a growth engine for Hong Kong's banking sector in general and our Group in particular. As can be expected, the "Supplementary Memorandum of Cooperation on RMB Business" signed between the HKMA and the People's Bank of China (PBoC) as well as the revised "Settlement Agreement on the Clearing of RMB Businesses" signed between BOCHK and PBoC on 19 July this year will be

highly conducive to the robust development of Hong Kong's RMB banking business. Given our unrivalled status as the sole RMB clearing bank in Hong Kong, our strong track record in conducting RMB business, our close relationship with BOC and extensive connection in the Mainland, we believe we are in a superior position to broaden the scope of our RMB banking services for both corporate and individual customers as well as financial institutions on both sides of the border and across the world.

Right at the beginning of the second half of 2010, we marked a number of new milestones in our RMB business, namely, acting as the Sole Bookrunner and Lead Manager of the first RMB corporate bonds issued in Hong Kong, conducting the first CNY deliverable forwards transaction for our corporate clients, launching BOC Wealth Express Card and BOC CUP Dual Currency Credit Card Shenzhen-Hong Kong Cross Border Autopay Service, and the like. While solidifying our strong RMB branding, we are now able to provide a comprehensive range of professional RMB services to meet the diverse needs of customers, thus ensuring the premier choices for them.

We are currently providing RMB clearing service to over 100 participating banks. Now that the scope of RMB business clearing service has been extended from Hong Kong, Macau and ASEAN countries to the world, we will, as always, continue to provide impartial, timely, accurate and professional RMB clearing services to all the participating banks in Hong Kong and overseas. The latest development is that in July this year, we signed the Agreement on Provision of Clearing Service for RMB Cashnotes Business for Taiwan with PBoC, which allows us to extend our RMB clearing service for the Taiwan region.

We have entered a new horizon which will help, together with other developments, promote Hong Kong's status as an offshore RMB centre.

Against the backdrop of uncertainties in western economies, the Mainland of China remains the most rapidly growing market and is the bright spot in the eyes of global investors. Benefiting from the "Framework Agreement on Hong Kong-Guangdong Cooperation" signed in April this year, we expect business opportunities in the neighbouring Pearl River Delta (PRD) to proliferate. The demand will rise among affluent customers for wealth management services. We will continue to build up our high net-worth customer base by offering and customising wealth management solutions. At the same time, the demand among commercial clients for more extensive financial services that cover the whole region or beyond is also expected to increase rapidly. Capitalising on our strong franchise and close connection with our parent, we will provide a full suite of service for these clients with enormous potentials.

To sustain the growth and leading marketing positions in our core traditional businesses, we strive to enhance our business service platform, optimise our distribution channel, heighten our product development capabilities and expand our customer base. Among others, the recent launch of BOCHK Mobile Banking offers a secure and reliable banking service platform for our customers. Our dynamic, brand-new flagship model branches will also help strengthen our strong brand franchise and integrated service capabilities for customers. All these will enable us to better serve as BOC Group's product manufacturing centre and service supporting centre in the Asia-Pacific region.

Apart from business development, we will endeavour to fulfill our corporate social responsibility, which has become an integral part of the Group's long-term development strategy. We are pleased that the Company has been recently selected as a constituent stock for the Hang Seng Corporate Sustainability Index. We also won the Hong Kong Community Chest Top Donor of the Year Award in July. I am sure the Group and its staff will be further committed on that score in the time ahead.

To conclude, I believe the Group has been coping well with the challenges of the operating environment and positioning itself strategically for the long-term sustainable growth and development, for which I must extend my heartfelt thanks to the Board, our shareholders, our customers and all my colleagues.



**HE Guangbei**

*Vice Chairman & Chief Executive*

26 August 2010

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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

## FINANCIAL PERFORMANCE AND CONDITION IN BRIEF

The following table is a summary of the Group's key financial results for the first half of 2010 with a comparison with the previous two half-yearly periods.

| Financial Indicators                                                                                             |                                                                                                                                             | 2010 First Half Performance                                                                                                                                                                                                                                                                   |
|------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1. Profit Attributable to Shareholders                                                                           | <div>HK\$m</div> <div><div>6,691</div><div>7,034</div><div>7,190</div></div> <div><div>1H2009</div><div>2H2009</div><div>1H2010</div></div> | <div>Profit attributable to shareholders</div> <div><div><div>The Group’s profit continued to grow. Profit attributable to shareholders was HK\$7,190 million, up HK\$499 million, or 7.5%, year-on-year.</div></div></div>                                                                   |
| 2. Return on Average Capital and Reserves Attributable to the Equity Holders of the Company (“ROE”) <sup>1</sup> | <div>%</div> <div><div>15.13</div><div>14.28</div><div>13.72</div></div> <div><div>1H2009</div><div>2H2009</div><div>1H2010</div></div>     | <div>ROE</div> <div><div><div>ROE was 13.72%, down 1.41 percentage points year-on-year as the increase in reserves outpaced that of the Group’s profit.</div></div></div>                                                                                                                     |
| 3. Return on Average Total Assets (“ROA”) <sup>2</sup>                                                           | <div>%</div> <div><div>1.23</div><div>1.16</div><div>1.17</div></div> <div><div>1H2009</div><div>2H2009</div><div>1H2010</div></div>        | <div>ROA</div> <div><div><div>ROA was 1.17%, down 0.06 percentage point year-on-year.</div></div></div>                                                                                                                                                                                       |
| 4. Net Interest Margin (“NIM”)                                                                                   | <div>%</div> <div><div>1.79</div><div>1.61</div><div>1.58</div></div> <div><div>1H2009</div><div>2H2009</div><div>1H2010</div></div>        | <div>NIM</div> <div><div><div>NIM was 1.58%, down 21 basis points year-on-year due to lower market interest rates and intense pricing competition.</div></div></div>                                                                                                                          |
| 5. Cost-to-Income Ratio (“CIR”)                                                                                  | <div>%</div> <div><div>32.19</div><div>61.00</div><div>36.15</div></div> <div><div>1H2009</div><div>2H2009</div><div>1H2010</div></div>     | <div>CIR</div> <div><div><div>CIR was 36.15%, up 3.96 percentage points year-on-year mainly due to the increase in operating expenses.</div><div>CIR was lower than in the second half of 2009 when significant expenses were incurred on Lehman Brothers-related products.</div></div></div> |

| Financial Indicators                                          |                                                                                                                                                                                | 2010 First Half Performance                                                                                                                                                                                                                                                            |
|---------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 6. Deposits from Customers<br>(including structured deposits) | <div>HK\$'bn</div> <div><div><div>824.7</div><div>2009.06.30</div></div><div><div>844.5</div><div>2009.12.31</div></div><div><div>892.7</div><div>2010.06.30</div></div></div> | <div>Deposits from Customers</div> <div><div>Total deposits increased by 5.7% from the end of 2009, with strong performance of RMB deposits.</div></div>                                                                                                                               |
|                                                               |                                                                                                                                                                                |                                                                                                                                                                                                                                                                                        |
| 7. Advances to Customers                                      | <div>HK\$'bn</div> <div><div><div>475.6</div><div>2009.06.30</div></div><div><div>515.0</div><div>2009.12.31</div></div><div><div>571.5</div><div>2010.06.30</div></div></div> | <div>Advances to Customers</div> <div><div>Advances to customers continued its growth momentum and rose by 11.0% from the end of 2009. The Group has also made progress in improving pricing of loans this year with market demand.</div></div>                                        |
|                                                               |                                                                                                                                                                                |                                                                                                                                                                                                                                                                                        |
| 8. Classified or Impaired Loan Ratio <sup>3</sup>             | <div>%</div> <div><div><div>0.37</div><div>2009.06.30</div></div><div><div>0.34</div><div>2009.12.31</div></div><div><div>0.23</div><div>2010.06.30</div></div></div>          | <div>Classified or Impaired Loan Ratio</div> <div><div>Classified or impaired loan ratio was 0.23%, down 0.11 percentage point from the end of 2009.</div><div>Formation of new classified loans remained at a low level, representing approximately 0.03% of total loans.</div></div> |
|                                                               |                                                                                                                                                                                |                                                                                                                                                                                                                                                                                        |
| 9. Capital Adequacy Ratio ("CAR")                             | <div>%</div> <div><div><div>16.10</div><div>2009.06.30</div></div><div><div>16.85</div><div>2009.12.31</div></div><div><div>16.17</div><div>2010.06.30</div></div></div>       | <div>CAR</div> <div><div>CAR was maintained at a high level of 16.17%.</div><div>Core capital ratio was at a solid level of 11.33%.</div></div>                                                                                                                                        |
|                                                               |                                                                                                                                                                                |                                                                                                                                                                                                                                                                                        |
| 10. Average Liquidity Ratio                                   | <div>%</div> <div><div><div>39.70</div><div>1H2009</div></div><div><div>40.66</div><div>2H2009</div></div><div><div>37.81</div><div>1H2010</div></div></div>                   | <div>Average Liquidity Ratio</div> <div><div>Average liquidity ratio was at a comfortable level of 37.81%.</div></div>                                                                                                                                                                 |
|                                                               |                                                                                                                                                                                |                                                                                                                                                                                                                                                                                        |

<sup>1</sup> Return on Average Capital and Reserves Attributable to the Equity Holders of the Company as defined in "Financial Highlights".

<sup>2</sup> Return on Average Total Assets as defined in "Financial Highlights".

<sup>3</sup> Classified or impaired loans represent advances which have been classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

## ECONOMIC BACKGROUND AND OPERATING ENVIRONMENT

The recovery of the global economy extended to the first half of 2010. Among the world's major economies, China continued with its strong growth in 2010 despite the tightening of its monetary policy. The Hong Kong economy achieved an impressive annualised GDP growth of 8.2% in the first quarter of the year spurred by an increase in retail sales as well as higher exports of goods and services. The unemployment rate dropped to 4.6% in the second quarter of the year. The pressure on inflation was becoming more visible due to the rise in wages and import prices. Hong Kong's Composite Consumer Price Index grew by 2.8% in June 2010 over the same month a year earlier. Meanwhile, the recent European sovereign debt crisis and the potential tightening of monetary policies by major central banks added uncertainties to the market.

Market interest rates remained at a low level with ample liquidity in the market. Average 1-month HIBOR and LIBOR stayed close to zero in the first half of 2010.

Investors' sentiments in the Hong Kong stock market turned less positive in the first half of 2010. The risk appetite of investors was further weakened towards the end of the first half of 2010 in light of the worsening of the European debt crisis and the tightening of the Mainland's policy. After reaching 22,417 on 6 January 2010, the Hang Seng Index closed at 20,129 on 30 June 2010.

The local residential property market remained buoyant in the first half of 2010 as property prices and transaction volume continued to rise. The number of sales and

purchase agreements of all building units registered a 31.3% increase versus the same period in 2009, while the prices of private domestic properties showed an increase of 8.1% from end-2009.

During the first half of 2010, the competition for both loans and deposits continued to intensify. Despite the higher demand for mortgage loans, particularly those in HIBOR-based as customers take advantage of the low interbank rates, banks had to offer lower rates to attract customers. On the other hand, higher rates were being offered to depositors to attract funds from the market.

On 11 February 2010, Hong Kong Monetary Authority announced the "Elucidation of Supervisory Principles and Operational Arrangements Regarding Renminbi Business in Hong Kong" ("Elucidation"), with an aim to increase the flexibility in developing diversified RMB-denominated financial services. The Elucidation helped simplifying, enhancing and providing convenient operational procedures for the business of cross-border trade settlement in RMB, and thus leading to greater flexibility and offering more favourable development prospects for the RMB business.

In summary, the operating environment of the banking industry improved in general alongside the revival of both the global and local economies. However, it remained highly challenging as banks were faced with persistent pressure on their net interest margin in the low interest rate environment, intensifying competition on pricing, greater inflationary pressure on operating cost and uncertainties triggered by the recent European sovereign debt crisis.

## CONSOLIDATED FINANCIAL REVIEW

### Financial Performance

The economic recovery in Hong Kong gathered pace in the first half of 2010. However, the market interest rate still stood at an exceptionally low level and competition remained intense in the banking industry. By capitalising on its core competencies and competitive advantages, the Group managed to seize opportunities arising from the recovering economy and achieved business growth. Meanwhile, it continued to exercise stringent risk management in view of the economic uncertainties arising from the debt crisis in Europe and the potential tightening of monetary policies in certain countries.

Compared to the first half of 2009, the core earnings<sup>1</sup> of the Group remained stable. However, substantial mark-to-market losses led to a drop in operating income of HK\$487 million or 3.7%. Meanwhile, operating expenses rose from a relatively low level in the first half of 2009. As a result, the Group's operating profit before impairment allowances declined by HK\$827 million or 9.4%. The Group recorded a net reversal of impairment allowances

on securities investments versus a significant net charge in the first half of 2009. The net reversal of impairment allowances on loans remained at a low level. The Group's profit attributable to shareholders increased by HK\$499 million, or 7.5%, to HK\$7,190 million. Earnings per share were HK\$0.68, up HK\$0.0471 from the same period last year. ROA was 1.17% while ROE was 13.72%.

As compared to the second half of 2009, the Group's profit attributable to shareholders increased by HK\$156 million, or 2.2%. During the period, net interest income rose slightly. However, both net trading gain and net fee and commission income registered a decline. Operating expenses declined as significant expenses were incurred on Lehman Brothers-related products in the second half of 2009. The Group also recorded a net gain on the disposal of securities investments. Meanwhile, net reversal of impairment allowances on securities investments dropped substantially while a modest amount of net reversal of impairment allowances on loans was recorded as opposed to a net charge in the second half of 2009.

1 Core earnings include net interest income, net fee and commission income and net trading gain of the banking business which excludes mark-to-market gain or loss but includes foreign exchange gain or loss from foreign exchange swap contracts.

### Financial Highlights

|                                                                                          | Half-year ended<br>30 June<br>2010 | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|------------------------------------------------------------------------------------------|------------------------------------|----------------------------------------|------------------------------------|
| HK\$m, except percentage amounts                                                         |                                    |                                        |                                    |
| Net interest income                                                                      | 8,964                              | 8,918                                  | 9,014                              |
| Other operating income                                                                   | 3,577                              | 4,109                                  | 4,014                              |
| Operating income                                                                         | 12,541                             | 13,027                                 | 13,028                             |
| Operating expenses                                                                       | (4,534)                            | (7,947)                                | (4,194)                            |
| Operating profit before impairment allowances                                            | 8,007                              | 5,080                                  | 8,834                              |
| Net reversal/(charge) of impairment allowances                                           | 161                                | 2,305                                  | (1,115)                            |
| Others                                                                                   | 599                                | 1,095                                  | 525                                |
| Profit before taxation                                                                   | 8,767                              | 8,480                                  | 8,244                              |
| Profit attributable to equity holders of the Company                                     | 7,190                              | 7,034                                  | 6,691                              |
| Earnings per share (HK\$)                                                                | 0.6800                             | 0.6652                                 | 0.6329                             |
| Return on average total assets                                                           | 1.17%                              | 1.16%                                  | 1.23%                              |
| Return on average capital and reserves attributable to the equity holders of the Company | 13.72%                             | 14.28%                                 | 15.13%                             |
| Net interest margin (NIM)                                                                | 1.58%                              | 1.61%                                  | 1.79%                              |
| Non-interest income ratio                                                                | 28.52%                             | 31.54%                                 | 30.81%                             |
| Cost-to-income ratio                                                                     | 36.15%                             | 61.00%                                 | 32.19%                             |

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

### **Net Interest Income and Margin**

|                                  | <b>Half-year ended<br/>30 June<br/>2010</b> | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|----------------------------------|---------------------------------------------|----------------------------------------|------------------------------------|
| HK\$m, except percentage amounts |                                             |                                        |                                    |
| Interest income                  | <b>10,671</b>                               | 10,353                                 | 11,331                             |
| Interest expense                 | <b>(1,707)</b>                              | (1,435)                                | (2,317)                            |
| Net interest income              | <b>8,964</b>                                | 8,918                                  | 9,014                              |
| Average interest-earning assets  | <b>1,142,383</b>                            | 1,101,861                              | 1,014,954                          |
| Net interest spread              | <b>1.53%</b>                                | 1.56%                                  | 1.73%                              |
| Net interest margin              | <b>1.58%</b>                                | 1.61%                                  | 1.79%                              |

In the first half of 2010, short-term market interest rates remained at a low level, which could be attributed to ongoing accommodative monetary policies rates in major economies and ample liquidity in the interbank market. Compared to the first half of 2009, average one-month HIBOR and average one-month LIBOR fell by 8 basis points and 15 basis points to 0.13% and 0.27% respectively, while average three-month HIBOR and average three-month LIBOR declined by 53 basis points and 69 basis points to 0.19% and 0.35% respectively. The Group's average HKD Prime rate remained at 5.00% thus widening the HKD Prime-to-one-month HIBOR spread by 8 basis points to 4.87%.

Compared to the first half of 2009, the Group's net interest income decreased slightly by HK\$50 million, or 0.6% to HK\$8,964 million. The decline was mainly due to the narrowing of the net interest margin by 21 basis points to 1.58%, which was mostly offset by the 12.6% growth in average interest-earning assets. The contribution of net free fund fell by 1 basis point.

Average yield of interest-earning assets fell by 37 basis points while the average rate of interest-bearing liabilities dropped by 17 basis points. As a result, the net interest spread decreased by 20 basis points under the low interest rate environment.

The narrowing of spread was primarily due to the decline in the average yield of total interest-earning assets. Average gross yield on loans and advances to customers and debt securities were down by 37 and 34 basis points respectively. Loan yield was compressed by the decline in market rates and greater pricing pressure, particularly on mortgage loans, as a result of intense market competition. In addition, there was a bigger proportion of HIBOR-based residential mortgage loans and large corporate loans the pricing of which was based on interbank market rates (hereafter called "market rate-based loans"). This exerted pressure on the average yield of the Group's loans as market rate-based loans bore a lower gross yield relative to Prime-based loans amid the current interest rate environment. Nevertheless, the Group focused on enhancing the pricing of its corporate lending and improved the pricing of new corporate loans during the period. Gross yield of debt securities declined following their repricing at lower interest rates. Meanwhile, the average rate of interest-bearing liabilities dropped by a lesser extent as deposit costs were already close to zero.

On the other hand, the Group's assets and liabilities mix improved. The increase in higher-yielding assets such as loans and advances to customers as well as debt securities investments, coupled with the increase in the proportion of demand, current and savings deposits in average total deposits partly offset the decline in interest spread.

|                                                                              | Half-year ended<br>30 June 2010 |                       | Half-year ended<br>31 December 2009* |                       | Half-year ended<br>30 June 2009* |                       |
|------------------------------------------------------------------------------|---------------------------------|-----------------------|--------------------------------------|-----------------------|----------------------------------|-----------------------|
|                                                                              | Average<br>balance<br>HK\$'m    | Average<br>yield<br>% | Average<br>balance<br>HK\$'m         | Average<br>yield<br>% | Average<br>balance<br>HK\$'m     | Average<br>yield<br>% |
| <b>ASSETS</b>                                                                |                                 |                       |                                      |                       |                                  |                       |
| Cash, balances and placements with<br>banks and other financial institutions | 211,521                         | 0.95                  | 253,525                              | 0.91                  | 230,145                          | 1.55                  |
| Debt securities investments                                                  | 369,306                         | 2.28                  | 338,254                              | 2.30                  | 322,004                          | 2.62                  |
| Loans and advances to customers                                              | 547,281                         | 2.00                  | 495,723                              | 2.07                  | 451,694                          | 2.37                  |
| Other interest-earning assets                                                | 14,275                          | 1.26                  | 14,359                               | 1.17                  | 11,111                           | 1.09                  |
| Total interest-earning assets                                                | 1,142,383                       | 1.88                  | 1,101,861                            | 1.86                  | 1,014,954                        | 2.25                  |
| Non interest-earning assets                                                  | 116,018                         | –                     | 130,059                              | –                     | 106,807                          | –                     |
| Total assets                                                                 | 1,258,401                       | 1.71                  | 1,231,920                            | 1.67                  | 1,121,761                        | 2.04                  |

|                                                                          | Half-year ended<br>30 June 2010 |                      | Half-year ended<br>31 December 2009* |                      | Half-year ended<br>30 June 2009* |                      |
|--------------------------------------------------------------------------|---------------------------------|----------------------|--------------------------------------|----------------------|----------------------------------|----------------------|
|                                                                          | Average<br>balance<br>HK\$'m    | Average<br>rate<br>% | Average<br>balance<br>HK\$'m         | Average<br>rate<br>% | Average<br>balance<br>HK\$'m     | Average<br>rate<br>% |
| <b>LIABILITIES</b>                                                       |                                 |                      |                                      |                      |                                  |                      |
| Deposits and balances of banks and<br>other financial institutions       | 105,914                         | 0.58                 | 76,382                               | 0.63                 | 73,058                           | 0.78                 |
| Current, savings and fixed deposits                                      | 807,886                         | 0.27                 | 821,150                              | 0.19                 | 763,867                          | 0.39                 |
| Certificates of deposit issued                                           | –                               | –                    | 198                                  | 4.04                 | 845                              | 4.07                 |
| Subordinated liabilities                                                 | 26,373                          | 2.10                 | 27,001                               | 2.90                 | 27,185                           | 3.91                 |
| Other interest-bearing liabilities                                       | 39,572                          | 0.31                 | 31,879                               | 0.13                 | 27,745                           | 0.24                 |
| Total interest-bearing liabilities                                       | 979,745                         | 0.35                 | 956,610                              | 0.30                 | 892,700                          | 0.52                 |
| Non interest-bearing deposits                                            | 57,847                          | –                    | 68,806                               | –                    | 44,193                           | –                    |
| Shareholders' funds <sup>#</sup> and<br>non interest-bearing liabilities | 220,809                         | –                    | 206,504                              | –                    | 184,868                          | –                    |
| Total liabilities                                                        | 1,258,401                       | 0.27                 | 1,231,920                            | 0.23                 | 1,121,761                        | 0.42                 |

\* Interest income and expense for interest rate derivatives held for trading have been reclassified from "Net interest income" to "Net trading (loss)/gain". The comparative figures have been reclassified to conform with the current period's presentation.

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

Compared to the second half of 2009, average one-month HIBOR increased by 4 basis points to 0.13% while average one-month LIBOR increased by 2 basis points to 0.27%. The Group's net interest income increased slightly by HK\$46 million or 0.5%. Net interest margin and net interest spread each narrowed by 3 basis points.

Net interest income increased as average interest-earning assets recorded a growth of 3.7%. However net interest spread narrowed mainly due to an increase in deposit costs amid acute competition. The negative effects were partly offset by the improvement in the assets mix with the growth in loans and advances to customers and debt securities investments.

**Net Fee and Commission Income**

| HK\$'m                              | Half-year ended<br>30 June<br>2010 | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|-------------------------------------|------------------------------------|----------------------------------------|------------------------------------|
| Investment and insurance fee income | <b>1,748</b>                       | 2,145                                  | 1,741                              |
| Securities brokerage (Stockbroking) | <b>1,506</b>                       | 2,013                                  | 1,625                              |
| Securities brokerage (Bonds)        | <b>3</b>                           | 35                                     | 4                                  |
| Funds distribution                  | <b>67</b>                          | 59                                     | 38                                 |
| Life insurance*                     | <b>172</b>                         | 38                                     | 74                                 |
| Credit cards                        | <b>903</b>                         | 806                                    | 705                                |
| Loan commissions                    | <b>623</b>                         | 524                                    | 398                                |
| Bills commissions                   | <b>371</b>                         | 317                                    | 310                                |
| Payment services                    | <b>272</b>                         | 268                                    | 227                                |
| Account services                    | <b>136</b>                         | 144                                    | 132                                |
| Currency exchange                   | <b>125</b>                         | 126                                    | 87                                 |
| Trust services                      | <b>98</b>                          | 96                                     | 82                                 |
| General insurance                   | <b>48</b>                          | 52                                     | 48                                 |
| Correspondent banking               | <b>24</b>                          | 24                                     | 21                                 |
| Custody                             | <b>17</b>                          | 21                                     | 15                                 |
| IPO-related business                | <b>9</b>                           | 40                                     | 1                                  |
| Others                              | <b>107</b>                         | 89                                     | 117                                |
| Fee and commission income           | <b>4,481</b>                       | 4,652                                  | 3,884                              |
| Fee and commission expenses         | <b>(1,084)</b>                     | (1,091)                                | (937)                              |
| Net fee and commission income       | <b>3,397</b>                       | 3,561                                  | 2,947                              |

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

Net fee and commission income recorded a broad-based growth of HK\$450 million or 15.3% year-on-year to HK\$3,397 million, mainly driven by the strong growth of HK\$225 million or 56.5% in loan commissions. Fee from the credit card business grew by HK\$198 million or 28.1% with the increase in cardholder spending and merchant acquiring volume by 21.4% and 41.8% respectively. Fee and commission income arising from bills, payment services and currency exchange recorded satisfactory growth due to higher transaction volumes amid the economic recovery. Investment and insurance fee income, which is discussed in the next section "Investment and Insurance Business", remained largely the same. Meanwhile, fee and commission expenses rose by HK\$147 million or 15.7%, mainly due to the increase in fee expenses in credit cards.

Compared to the second half of 2009, net fee and commission income dropped by HK\$164 million or 4.6%, mainly because of the HK\$507 million or 25.2% decrease in fee income from stock broking. On the other hand, fee income from life insurance rose by HK\$134 million or 352.6% and loan commissions grew by HK\$99 million or 18.9%. Fee income from credit cards increased by HK\$97 million or 12.0% while bills commissions registered a growth of HK\$54 million or 17.0%. Meanwhile, fee and commission expenses decreased slightly by HK\$7 million or 0.6%, as the drop in fee expenses on stock broking was mostly offset by an increase in credit cards expenses.

**Investment and Insurance Business**

|                                                                                             | Half-year ended<br>30 June<br>2010 | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|---------------------------------------------------------------------------------------------|------------------------------------|----------------------------------------|------------------------------------|
| HK\$'m                                                                                      |                                    |                                        |                                    |
| Investment and insurance fee income                                                         |                                    |                                        |                                    |
| Securities brokerage (Stockbroking)                                                         | 1,506                              | 2,013                                  | 1,625                              |
| Securities brokerage (Bonds)                                                                | 3                                  | 35                                     | 4                                  |
| Funds distribution                                                                          | 67                                 | 59                                     | 38                                 |
| Life insurance*                                                                             | 172                                | 38                                     | 74                                 |
|                                                                                             | 1,748                              | 2,145                                  | 1,741                              |
| Net operating income of BOC Life#                                                           |                                    |                                        |                                    |
| Net insurance premium income                                                                | 2,798                              | 5,483                                  | 2,261                              |
| Interest income                                                                             | 724                                | 709                                    | 562                                |
| Net gain/(loss) on financial instruments<br>designated at fair value through profit or loss | 591                                | 636                                    | (1,575)                            |
| Net gain on investment in securities                                                        | 118                                | –                                      | –                                  |
| Others                                                                                      | 4                                  | 5                                      | 5                                  |
|                                                                                             | 4,235                              | 6,833                                  | 1,253                              |
| Gross operating income of BOC Life#                                                         |                                    |                                        |                                    |
| Less: net insurance benefits and claims                                                     | (3,875)                            | (6,367)                                | (919)                              |
|                                                                                             | 360                                | 466                                    | 334                                |
| Total investment and insurance income                                                       | 2,108                              | 2,611                                  | 2,075                              |
| Of which: Life insurance fee income*                                                        | 172                                | 38                                     | 74                                 |
| Net operating income of BOC Life#                                                           | 360                                | 466                                    | 334                                |
| Total life insurance income                                                                 | 532                                | 504                                    | 408                                |
| Investment fee income                                                                       | 1,576                              | 2,107                                  | 1,667                              |
| Total investment and insurance income                                                       | 2,108                              | 2,611                                  | 2,075                              |

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

# Before commission expenses.

The Group's total investment and insurance income registered an increase of HK\$33 million or 1.6% to HK\$2,108 million compared to the same period last year. The increase was mainly attributable to the increase in the fee income from life insurance of HK\$98 million or 132.4% which was driven by the increase in transaction volumes. Fee income from fund distribution also increased by HK\$29 million or 76.3%. They were, however, partially

offset by the HK\$119 million or 7.3% decrease in fee income from stock broking.

Owing to the European debt crisis and the tightening of the Mainland's policy, investment sentiments in the local stock market turned less bullish in the second quarter of 2010. This had a negative impact on the Group's stock broking business and related fee income.

The increase in net operating income of BOC Life was mainly attributable to the increase in net insurance premium income. Following the launch of the new financial planning team and the "Need-based Selling" approach in 2009, the Group successfully boosted the sales of its insurance products with an increase of HK\$537 million or 23.8% in net insurance premium income. Meanwhile, it recorded a net gain on financial instruments designated at fair value through profit and loss versus a net loss in the same period last year. The increase was substantially offset by an increase in net insurance benefits and claims which was set aside to support policyholders' benefits under the

new business, as well as the movement in reserve caused by the drop of long-term interest rates.

Compared to the second half of 2009, total investment and insurance income dropped by HK\$503 million or 19.3%. The decline was caused by a significant drop in fee income from stock broking by HK\$507 million or 25.2% from a comparatively high level in the second half of 2009 when the equity market was buoyant. Income from BOC Life also decreased by HK\$106 million or 22.7% from the second half of 2009 when its investment income benefited from the narrowing of credit spread.

### Net Trading (Loss)/Gain

| HK\$'m                                                        | Half-year ended<br>30 June<br>2010 | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|---------------------------------------------------------------|------------------------------------|----------------------------------------|------------------------------------|
| Foreign exchange and foreign exchange products                | 350                                | 483                                    | 790                                |
| Interest rate instruments and items under fair value<br>hedge | (424)                              | 119                                    | (57)                               |
| Equity instruments                                            | (20)                               | 9                                      | 17                                 |
| Commodities                                                   | 58                                 | 70                                     | 54                                 |
| Net trading (loss)/gain                                       | (36)                               | 681                                    | 804                                |

Net trading loss was HK\$36 million, representing a HK\$840 million decline from a net trading gain of HK\$804 million in the first half of 2009, primarily due to the decrease in net trading gain from foreign exchange and related products, and the increase in net trading loss from interest rate instruments.

Net trading gain from foreign exchange and related products fell by HK\$440 million or 55.7%, which was mainly attributable to the foreign exchange loss on foreign exchange swap contracts\* compared to a gain in the first half of 2009. Should the impact of loss on foreign exchange swap contracts be excluded, the gain from other foreign exchange activities would have increased by 19.0%. As the signs of economic recovery became more apparent and the appreciation of RMB was expected, the demand for foreign exchange rebounded and the

Group recorded a year-on-year growth in related gain. Net trading loss from interest rate instruments and items under fair value hedge increased by HK\$367 million or 643.9%, mainly due to the mark-to-market loss on certain interest rate instruments. Net trading loss from equity instruments stood at HK\$20 million as opposed to a gain of HK\$17 million, mainly as a result of the mark-to-market loss on certain equity investments.

Compared to the second half of 2009, net trading gain declined by HK\$717 million, which was mainly attributable to the mark-to-market loss on certain interest rate instruments. Meanwhile, trading gain from foreign exchange and related products fell by HK\$133 million, or 27.5%, mainly due to the foreign exchange loss on foreign exchange swap contracts\*.

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

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

|                                                                                             | <b>Half-year ended<br/>30 June<br/>2010</b> | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|---------------------------------------------------------------------------------------------|---------------------------------------------|----------------------------------------|------------------------------------|
| HK\$m                                                                                       |                                             |                                        |                                    |
| Banking business of the Group                                                               | <b>49</b>                                   | 81                                     | 180                                |
| BOC Life                                                                                    | <b>591</b>                                  | 636                                    | (1,575)                            |
| Net gain/(loss) on financial instruments designated<br>at fair value through profit or loss | <b>640</b>                                  | 717                                    | (1,395)                            |

Compared to the net loss of HK\$1,395 million recorded in the first half of 2009, the Group recorded a net gain of HK\$640 million on financial instruments designated at fair value through profit or loss in the first half of 2010. This resulted mainly from the mark-to-market gain on certain debt securities of BOC Life caused by the drop of market interest rates. The loss in the first half of 2009 was caused by mark-to-market loss on its debt investments portfolio due to increase in long-term market interest rates. These mark-to-market changes were substantially offset by the corresponding changes in policy reserves, as reflected in

the changes in net insurance benefits and claims which were attributable to market interest rate movement.

Compared to the second half of 2009, net gain on financial instruments designated at fair value through profit or loss decreased by HK\$77 million or 10.7% to HK\$640 million. The gain in the second half of 2009 was mainly attributable to the mark-to-market gain of certain debt securities investments of BOC Life caused by the narrowing of credit spread as the capital market stabilised.

**Operating Expenses**

|                                                          | <b>Half-year ended<br/>30 June<br/>2010</b> | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|----------------------------------------------------------|---------------------------------------------|----------------------------------------|------------------------------------|
| HK\$m, except percentage amounts                         |                                             |                                        |                                    |
| Staff costs                                              | <b>2,526</b>                                | 2,835                                  | 2,256                              |
| Premises and equipment expenses (excluding depreciation) | <b>574</b>                                  | 622                                    | 538                                |
| Depreciation on owned fixed assets                       | <b>556</b>                                  | 522                                    | 496                                |
| Other operating expenses                                 | <b>878</b>                                  | 3,968                                  | 904                                |
| Total operating expenses                                 | <b>4,534</b>                                | 7,947                                  | 4,194                              |
| Cost-to-income ratio                                     | <b>36.15%</b>                               | 61.00%                                 | 32.19%                             |

The Group's total operating expenses increased by HK\$340 million, or 8.1%, to HK\$4,534 million. Since 2008, the Group had implemented a number of cost containment measures in view of the weakening local economy and intensifying global financial crisis. As a result, the Group had been able to maintain comparatively lower operating expenses. As the market showed clearer signs of improvement since the second half of 2009, the Group gradually incurred additional costs on marketing and promotion as well as business expansion in areas of its

strategic focus such as the Mainland market. Nevertheless, the Group remained focused on operational efficiency and cost control in the first half of 2010.

Staff costs increased by HK\$270 million or 12.0%, primarily due to higher accrual of performance-related remuneration and the increase in human resources for the Mainland operation. Compared to 30 June 2009, headcount measured in full-time equivalents rose by 220 to 13,429 as at 30 June 2010.

Premises and equipment expenses increased by HK\$36 million or 6.7% as a result of higher IT costs and higher rental for branches in Hong Kong and new branches in the Mainland. Depreciation on owned fixed assets rose by HK\$60 million or 12.1%, which was attributable to larger depreciation charge on premises and computer equipment.

Other operating expenses decreased by HK\$26 million or 2.9% mainly due to expenses incurred on Lehman Brothers-related products in the first half of 2009

amounted to HK\$222 million. Meanwhile, in the first half of 2010, the Group incurred higher marketing and promotion expenses as well as expenses connected with the improved business volume.

Compared to the second half of 2009, operating expenses decreased by HK\$3,413 million or 42.9%. This was largely due to expenses incurred for Lehman Brothers-related products amounted to HK\$3,056 million, as well as higher staff costs and promotional expenses in the second half of 2009.

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

| HK\$'m                                                                           | Half-year ended<br>30 June<br>2010 | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|----------------------------------------------------------------------------------|------------------------------------|----------------------------------------|------------------------------------|
| Individual assessment<br>– net reversal/(charge) of allowances before recoveries | 56                                 | (165)                                  | (76)                               |
| Collective assessment<br>– net charge of allowances before recoveries            | (256)                              | (319)                                  | (24)                               |
| Recoveries                                                                       | 294                                | 321                                    | 160                                |
| Net reversal/(charge) of loan impairment allowances                              | 94                                 | (163)                                  | 60                                 |

The Group's loan quality continued to improve. Loan impairment allowances recorded a net reversal of HK\$94 million in the first half of 2010. There was a net reversal of HK\$56 million and a net charge of HK\$256 million of loan impairment allowances before recoveries from individual and collective assessment respectively. Meanwhile, total recoveries stood at HK\$294 million.

The net reversal of individual impairment allowances before recoveries in the current period as opposed to the net charge of HK\$76 million in the first half of 2009 was mainly due to improved loan quality under the economic

recovery. Meanwhile net charge of collective impairment allowances before recoveries increased by HK\$232 million as a result of the refinement of the collective assessment methodology since the second half of 2009 and higher loan growth in the first half of 2010.

Compared to the second half of 2009, loan impairment allowances improved from a net charge of HK\$163 million to a net reversal of HK\$94 million. The higher net charge of individual impairment allowances before recoveries in the second half of 2009 was attributable to the downgrade of certain customers during the period.

**Net Reversal/(Charge) of Impairment Allowances on Securities Investments**

|                                                                          | <b>Half-year ended<br/>30 June<br/>2010</b> | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|--------------------------------------------------------------------------|---------------------------------------------|----------------------------------------|------------------------------------|
| HK\$'m                                                                   |                                             |                                        |                                    |
| Held-to-maturity securities                                              | <b>32</b>                                   | 1,129                                  | (439)                              |
| Available-for-sale securities                                            | <b>40</b>                                   | 1,341                                  | (729)                              |
| Net reversal/(charge) of impairment allowances on securities investments | <b>72</b>                                   | 2,470                                  | (1,168)                            |

The reviving economy and stable capital market had a positive impact on the Group's securities investments portfolio. Following the disposal and repayment of securities, the Group recorded a net reversal of impairment allowances of HK\$72 million. The table below illustrates

the breakdown of the Group's net reversal or charge of impairment allowances against its securities investments in the first half of 2010 and the corresponding periods in 2009.

|                                                                                       | <b>Half-year ended<br/>30 June<br/>2010</b> | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|---------------------------------------------------------------------------------------|---------------------------------------------|----------------------------------------|------------------------------------|
| HK\$'m                                                                                |                                             |                                        |                                    |
| <b>US non-agency residential mortgage-backed securities</b>                           |                                             |                                        |                                    |
| Subprime                                                                              | <b>10</b>                                   | 53                                     | (23)                               |
| Alt-A                                                                                 | <b>6</b>                                    | 189                                    | (173)                              |
| Prime                                                                                 | <b>29</b>                                   | 2,156                                  | (1,016)                            |
|                                                                                       | <b>45</b>                                   | 2,398                                  | (1,212)                            |
| <b>Other debt securities</b>                                                          | <b>27</b>                                   | 72                                     | 44                                 |
| <b>Total net reversal/(charge) of impairment allowances on securities investments</b> | <b>72</b>                                   | 2,470                                  | (1,168)                            |

For details about the composition of the Group's investment securities portfolio, please refer to Note 24 to the Interim Financial Information.

Compared to the second half of 2009, the Group recorded a significantly lower reversal of impairment allowances in the first half of 2010. The balance of impairment allowances had decreased considerably as a result of the Group's active disposal of US non-agency residential mortgage-backed securities ("RMBS") in the second half of 2009.

**Property Revaluation**

| HK\$'m                                                                 | Half-year ended<br>30 June<br>2010 | Half-year ended<br>31 December<br>2009 | Half-year ended<br>30 June<br>2009 |
|------------------------------------------------------------------------|------------------------------------|----------------------------------------|------------------------------------|
| Net gain on fair value adjustments on investment properties            | 601                                | 1,027                                  | 527                                |
| Deferred tax charge                                                    | (99)                               | (155)                                  | (82)                               |
| Net gain on fair value adjustments on investment properties, after tax | 502                                | 872                                    | 445                                |
| Net gain on revaluation of premises                                    | 1                                  | 11                                     | 4                                  |
| Deferred tax charge                                                    | –                                  | (1)                                    | (1)                                |
| Net gain on revaluation of premises, after tax                         | 1                                  | 10                                     | 3                                  |

The aggregate impact of property revaluation before tax on the income statement in the first half of 2010 was a gain of HK\$602 million, which arose mainly from a net gain of HK\$601 million from the revaluation of investment properties and a net gain of HK\$1 million from the revaluation of premises. The related deferred tax charge on revaluation of investment properties amounted to HK\$99 million. As a result, the net impact of fair value

adjustments on investment properties on the Group's profit attributable to equity holders in the first half of 2010 was a gain of HK\$502 million.

Compared to the second half of 2009, the net gain on property revaluation in the first half of 2010 was milder, which was in line with the trend of property prices.

**Financial Position**

| HK\$m, except percentage amounts                                                              | At 30 June<br>2010 | At 31 December<br>2009 |
|-----------------------------------------------------------------------------------------------|--------------------|------------------------|
| Cash and balances with banks and other financial institutions                                 | 169,554            | 160,788                |
| Placements with banks and other financial institutions maturing between one and twelve months | 35,958             | 60,282                 |
| Hong Kong SAR Government certificates of indebtedness                                         | 41,950             | 38,310                 |
| Securities investments <sup>1</sup>                                                           | 383,609            | 358,349                |
| Advances and other accounts                                                                   | 597,306            | 527,135                |
| Fixed assets and investment properties                                                        | 37,558             | 35,650                 |
| Other assets <sup>2</sup>                                                                     | 36,241             | 32,277                 |
| Total assets                                                                                  | 1,302,176          | 1,212,791              |
| Hong Kong SAR currency notes in circulation                                                   | 41,950             | 38,310                 |
| Deposits and balances of banks and other financial institutions                               | 110,786            | 99,647                 |
| Deposits from customers                                                                       | 892,211            | 842,321                |
| Insurance contract liabilities                                                                | 35,050             | 33,408                 |
| Other accounts and provisions <sup>3</sup>                                                    | 85,450             | 66,694                 |
| Subordinated liabilities <sup>4</sup>                                                         | 27,192             | 26,776                 |
| Total liabilities                                                                             | 1,192,639          | 1,107,156              |
| Non-controlling interests                                                                     | 2,826              | 2,733                  |
| Capital and reserves attributable to the equity holders of the Company                        | 106,711            | 102,902                |
| Total liabilities and equity                                                                  | 1,302,176          | 1,212,791              |
| Loan-to-deposit ratio <sup>5</sup>                                                            | 64.02%             | 60.98%                 |

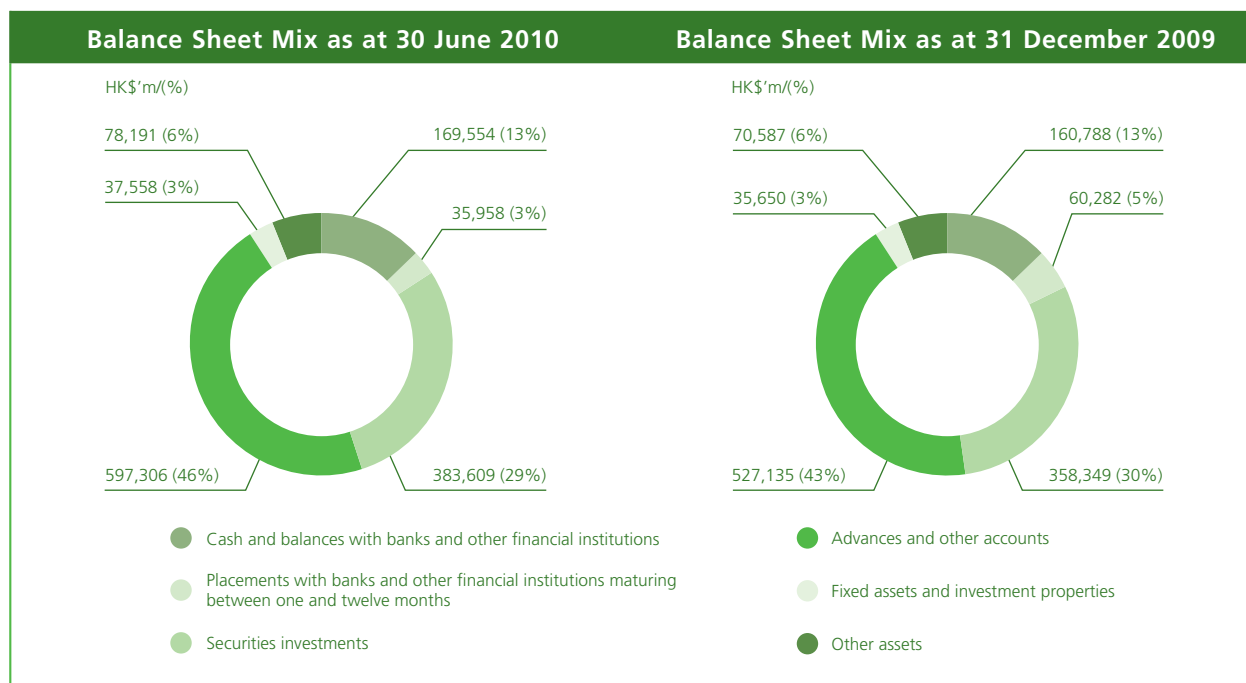
1 Securities investments comprise investment in securities and financial assets at fair value through profit or loss.

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

3 Financial liabilities at fair value through profit or loss, derivative financial liabilities, current tax liabilities and deferred tax liabilities are included in other accounts and provisions.

4 Subordinated liabilities as at 31 December 2009 represent USD and EUR subordinated loans granted by BOC (the "Loans"). During the first half of 2010, the Group issued USD subordinated notes (the "Notes"), the proceeds of which were applied to repay the USD Loans. Accordingly, subordinated liabilities as at 30 June 2010 comprise the Notes and the EUR Loans.

5 Of which deposits from customers also include structured deposits reported as "Financial liabilities at fair value through profit or loss".



The Group's total assets were HK\$1,302,176 million as at 30 June 2010, up HK\$89,385 million or 7.4% from the end of 2009. The overall assets structure of the Group improved further with a growth in higher-yielding assets such as advances to customers as well as securities investments. Key changes include:

- Placements with banks and other financial institutions maturing between one and twelve months decreased by HK\$24,324 million, or 40.4%, as the Group redeployed its funds for advances to customers and debt securities investments.
- Securities investments increased by HK\$25,260 million or 7.0%. The Group expanded its investments in government-related securities, and high-quality financial institution bonds and corporate bonds.
- Advances and other accounts increased by HK\$70,171 million, or 13.3%, which was mainly attributable to the growth in advances to customers by HK\$56,514 million or 11.0%, and trade bills by HK\$15,563 million or 171.0%.

In February and April 2010, the Group successfully completed the issue of Subordinated Notes (the "Notes") of US\$1,600 million and US\$900 million respectively to global debt investors. The proceeds of the Notes were used to repay the subordinated credit facility provided by BOC in December 2008. Pursuant to the regulatory requirements of the HKMA, the Notes qualify as Tier 2 Capital. The issue of the Notes broadened the Group's investor base and established a market benchmark for the Group to tap the debt market as an alternative source of future funding for its growth and development.

### Advances to Customers

| HK\$m, except percentage amounts     | At 30 June 2010 |       | At 31 December 2009 |       |
|--------------------------------------|-----------------|-------|---------------------|-------|
|                                      |                 | %     |                     | %     |
| Loans for use in Hong Kong           | 417,181         | 73.0  | 381,394             | 74.1  |
| Industrial, commercial and financial | 256,389         | 44.9  | 224,261             | 43.6  |
| Individuals                          | 160,792         | 28.1  | 157,133             | 30.5  |
| Trade finance                        | 39,285          | 6.9   | 29,321              | 5.7   |
| Loans for use outside Hong Kong      | 115,020         | 20.1  | 104,257             | 20.2  |
| Total advances to customers          | 571,486         | 100.0 | 514,972             | 100.0 |

The Group continued to implement proactive business strategies and strengthened its collaboration with BOC to capture new business opportunities in the recovering economy. As a result, the Group's advances to customers grew by HK\$56,514 million or 11.0% to HK\$571,486 million as at 30 June 2010.

Loans for use in Hong Kong grew by HK\$35,787 million or 9.4%.

- Lending to the industrial, commercial and financial sectors increased by HK\$32,128 million, or 14.3%, to HK\$256,389 million, covering a wide range of industries. Notable growth was recorded in the lending to property development, financial concerns, wholesale and retail trade as well as manufacturing industries.
- Residential mortgage loans (excluding those under the Government-sponsored Home Ownership Scheme) were up HK\$4,283 million, or 3.4%, to HK\$131,491 million. The proportion of total new drawdown in HIBOR-based residential mortgage loans showed a significant increase as customers inclined to take advantage of the low interbank rates.

Trade finance rose strongly by HK\$9,964 million or 34.0%, which was in tandem with the growth in Hong Kong's merchandised trade in the first half of 2010. Meanwhile, loans for use outside Hong Kong grew by HK\$10,763 million or 10.3%, which was driven by the increase in lending recorded by the Group's Mainland operation.

#### **Deposits from Customers\***

| HK\$m, except percentage amounts     | At 30 June |       | At 31 December |       |
|--------------------------------------|------------|-------|----------------|-------|
|                                      | 2010       | %     | 2009           | %     |
| Demand deposits and current accounts | 67,122     | 7.5   | 65,440         | 7.7   |
| Savings deposits                     | 473,492    | 53.0  | 495,512        | 58.7  |
| Time, call and notice deposits       | 351,597    | 39.4  | 281,369        | 33.3  |
|                                      | 892,211    | 99.9  | 842,321        | 99.7  |
| Structured deposits                  | 526        | 0.1   | 2,132          | 0.3   |
| Deposits from customers              | 892,737    | 100.0 | 844,453        | 100.0 |

\* including structured deposits

In the first half of 2010, market competition for customer deposits was intense. Despite this, the Group's deposits from customers increased by HK\$48,284 million, or 5.7%, to HK\$892,737 million as a result of effective promotion strategies. The balance of time, call and notice deposits rose by HK\$70,228 million or 25.0% to HK\$351,597 million. Savings deposits recorded a drop of HK\$22,020 million or 4.4%, while demand deposits and current accounts increased by HK\$1,682 million, or 2.6%. Customers skewed their funds towards fixed deposits as the interest rates on fixed deposits were moving up gradually. Structured deposits, a hybrid of retail deposit and derivatives offering a higher nominal interest rate, dropped by HK\$1,606 million, or 75.3%. The Group's loan-to-deposit ratio was up 3.04 percentage points to 64.02% at the end of June 2010.

**Loan Quality**

| HK\$m, except percentage amounts                                                              | At 30 June<br>2010 | At 31 December<br>2009 |
|-----------------------------------------------------------------------------------------------|--------------------|------------------------|
| Advances to customers                                                                         | <b>571,486</b>     | 514,972                |
| Classified or impaired loan ratio <sup>1</sup>                                                | <b>0.23%</b>       | 0.34%                  |
| Impairment allowances                                                                         | <b>2,289</b>       | 2,269                  |
| Regulatory reserve for general banking risks                                                  | <b>4,611</b>       | 4,040                  |
| Total allowances and regulatory reserve                                                       | <b>6,900</b>       | 6,309                  |
| Total allowances as a percentage of advances to customers                                     | <b>0.40%</b>       | 0.44%                  |
| Total allowances and regulatory reserve as a percentage of advances to customers              | <b>1.21%</b>       | 1.23%                  |
| Impairment allowances <sup>2</sup> on classified or impaired loan ratio                       | <b>40.70%</b>      | 39.57%                 |
| Residential mortgage loans <sup>3</sup> – delinquency and rescheduled loan ratio <sup>4</sup> | <b>0.03%</b>       | 0.04%                  |
| Card advances – delinquency ratio <sup>4,5</sup>                                              | <b>0.18%</b>       | 0.23%                  |

|                                                 | Half-year ended<br>30 June<br>2010 | Half-year ended<br>30 June<br>2009 |
|-------------------------------------------------|------------------------------------|------------------------------------|
| Card advances – charge-off ratio <sup>5,6</sup> | <b>1.56%</b>                       | 3.14%                              |

1 Classified or impaired loans represent advances which have been classified as “substandard”, “doubtful” or “loss” under the Group’s classification of loan quality, or individually assessed to be impaired.

2 Referring to impairment allowances on loans classified as “substandard”, “doubtful” or “loss” under the Group’s classification of loan quality, or individually assessed to be impaired.

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

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

5 Excluding Great Wall cards and computed according to the HKMA’s definition.

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

The Group’s loan quality further improved with the classified or impaired loan ratio falling by 0.11 percentage point to 0.23%. Classified or impaired loans decreased by approximately HK\$452 million, or 25.6%, to HK\$1,317 million mainly due to collections and fewer new classified loans. New classified loans in the first half of 2010 represented approximately 0.03% of total loans outstanding.

Total impairment allowances, including both individual assessment and collective assessment, amounted to HK\$2,289 million. Total impairment allowances in respect of the classified or impaired loans as a percentage of total classified or impaired loans accounted for 40.70%.

The quality of the Group’s residential mortgage loans remained sound with the combined delinquency and rescheduled loan ratio standing at a low level of 0.03% at the end of June 2010. As compared to the first half of 2009, the charge-off ratio of card advances dropped by 1.58 percentage points to 1.56%, mainly due to the cardholders’ improved debt servicing capability as economic conditions improved.

**Capital and Liquidity Ratios**

| HK\$m, except percentage amounts             | At 30 June<br>2010 | At 31 December<br>2009 |
|----------------------------------------------|--------------------|------------------------|
| Core capital                                 | <b>76,012</b>      | 72,465                 |
| Deductions                                   | <b>(715)</b>       | (334)                  |
| Core capital after deductions                | <b>75,297</b>      | 72,131                 |
| Supplementary capital                        | <b>32,944</b>      | 32,638                 |
| Deductions                                   | <b>(715)</b>       | (334)                  |
| Supplementary capital after deductions       | <b>32,229</b>      | 32,304                 |
| Total capital base after deductions          | <b>107,526</b>     | 104,435                |
| Risk-weighted assets                         |                    |                        |
| Credit risk                                  | <b>618,503</b>     | 578,374                |
| Market risk                                  | <b>18,501</b>      | 12,023                 |
| Operational risk                             | <b>47,898</b>      | 47,352                 |
| Deductions                                   | <b>(20,126)</b>    | (17,954)               |
| Total risk-weighted assets                   | <b>664,776</b>     | 619,795                |
| Capital adequacy ratios (consolidated basis) |                    |                        |
| Core capital ratio                           | <b>11.33%</b>      | 11.64%                 |
| Capital adequacy ratio                       | <b>16.17%</b>      | 16.85%                 |

|                         | Half-year ended<br>30 June<br>2010 | Half-year ended<br>30 June<br>2009 |
|-------------------------|------------------------------------|------------------------------------|
| Average liquidity ratio | <b>37.81%</b>                      | 39.70%                             |

The Group adopted the Standardised Approach in calculating capital adequacy ratios.

Consolidated capital adequacy ratio of the banking group at 30 June 2010 was 16.17%, 0.68 percentage point lower than that at the end of 2009. The Group's total capital base expanded by 3.0% to HK\$107,526

million mainly due to the increase in retained earnings. Meanwhile, risk-weighted assets for credit risk increased by 6.9% to HK\$618,503 million, as a result of the growth in advances to customers.

The average liquidity ratio in the first half of 2010 remained strong at 37.81%.

## BUSINESS REVIEW

## PERSONAL BANKING

| HK\$m, except percentage amounts              | Half-year ended<br>30 June<br>2010 | Half-year ended<br>30 June<br>2009 | Increase/<br>(decrease) |
|-----------------------------------------------|------------------------------------|------------------------------------|-------------------------|
| Net interest income                           | 2,932                              | 2,849                              | +2.9%                   |
| Other operating income                        | 2,384                              | 2,218                              | +7.5%                   |
| Operating income                              | 5,316                              | 5,067                              | +4.9%                   |
| Operating expenses                            | (3,044)                            | (2,771)                            | +9.9%                   |
| Operating profit before impairment allowances | 2,272                              | 2,296                              | -1.0%                   |
| Net charge of loan impairment allowances      | (37)                               | (74)                               | -50.0%                  |
| Others                                        | (5)                                | (6)                                | -16.7%                  |
| Profit before taxation                        | 2,230                              | 2,216                              | +0.6%                   |

|                     | At 30 June<br>2010 | At 31 December<br>2009 | Increase/<br>(decrease) |
|---------------------|--------------------|------------------------|-------------------------|
| Segment assets      | 191,760            | 178,026                | +7.7%                   |
| Segment liabilities | 612,200            | 570,566                | +7.3%                   |

Note: For additional segmental information, see Note 41 to the Interim Financial Information.

## Financial Results

Personal Banking recorded a profit before taxation of HK\$2,230 million in the first half of 2010. Operating income rose by 4.9%, driven by an increase in both net interest income and net fee income. Operating expenses rose by 9.9%. Operating profit before impairment allowances stood at HK\$2,272 million.

Net interest income increased by 2.9% due to the growth in both the average interest-earning assets and customers deposits, as well as improved deposit mix. The increase was partly offset by narrower loan spread and deposit spread under the low interest rate environment. Other operating income rose by 7.5% on account of the strong

growth in fee income from insurance and payment services. However, the increase was partially offset by the decline in fee income from stock brokerage.

Operating expenses rose by 9.9% mainly due to higher staff costs, rental expenses and IT costs.

Net charge of loan impairment allowances fell by HK\$37 million or 50.0%, as customers' debt servicing capability improved with the economic recovery.

Advances and other accounts, including mortgage loans and card advances, increased by 9.3% to HK\$177,488 million.

### **Business operation**

In the first half of 2010, the Group solidified its premier position in RMB business and maintained its market leadership in residential mortgage business. It also continued to drive the development of its stock trading business. The Group expanded its customer base by extending its reach to high net-worth customers in the Mainland and other potential customer segments in Hong Kong. At the same time, its service platform was revamped to better meet customers' needs for investment services and traditional banking services.

#### ***Maintaining steady growth in residential mortgages***

With the growth of the local property market in the first half of 2010, the Group achieved satisfactory results in the underwriting of new mortgages through effective marketing and the offering of a wide array of mortgage products. It continued to expand and strengthen its strategic partnership with major property developers and participated in joint promotions in most of the prime property development projects. In response to the launch of the "Sandwich Class Housing Scheme" by the Hong Kong Housing Society, the Group offered tailor-made mortgage plans to meet customers' needs. These initiatives helped maintain the Group's leading position in the underwriting of new mortgages. In recognition of its outstanding performance in the mortgage business, the Group received the "Sing Tao Excellent Services Brand Award 2009 – Mortgage Services" from Sing Tao Daily. By the end of June 2010, the Group's outstanding residential mortgage loans grew by 3.4% from the end of 2009. Meanwhile, the Group continued to strengthen its risk assessment and control over its mortgage business. The credit quality of residential mortgages remained sound with the delinquency and rescheduled loan ratio standing at a low level of 0.03% at the end of June 2010.

#### ***Promoting stock brokerage business and maintaining competitive edge in insurance***

Overshadowed by the European debt crisis and the Mainland's tightening policy, sentiments in the stock market were weakened. This had an adverse impact on the Group's stock brokerage business. Despite this, the Group continued to enhance its products and services and focused on acquiring new customers. During the period, the Group launched a series of promotion and marketing

campaigns and investment seminars in order to attract targeted customers. Meanwhile, the Group extended a bundled range of promotional offers to its stock-trading customers and embarked on a number of acquisition campaigns to attract new customers. The Group also introduced the "Big-Ticket Customer Programme" and "Incremental Turnover Usage Programme" for selected segments of existing customers to further expand its customer base and boost its stock brokerage business.

Regarding its Bancassurance business, the Group recorded significant sales growth by broadening its product spectrum, launching extensive marketing campaigns and implementing a multi-channel distribution strategy. The Group was the first in the Hong Kong market to launch RMB insurance products. It introduced RMB insurance products with settlement being made in Hong Kong Dollars, namely the "Target 8 Years Insurance Plan Series" and the "Target 5 Years Insurance Plan Series". These products offered greater flexibility to customers while capturing the capital gain potential from the appreciation of RMB. Meanwhile, the Group launched a life insurance savings plan, the "Glorious Life Savings Insurance Plan", and revamped existing insurance products to enhance the overall competitiveness in its product shelf. The Group continued to extend its financial planning model and rolled out large scale marketing campaigns to promote its customer oriented services. These initiatives helped expand its foothold in the market and boost the sales of insurance products significantly during the period.

#### ***Enhancing relationship with high net-worth customers***

The Group strived to maintain long-term relationship with its wealth management customers by providing differentiated services and tailor-made wealth management solutions through different service channels. During the first half of 2010, the Group continued to strengthen its customer segmentation strategy and expand its high net-worth customer base. In order to further broaden its wealth management customer base, the Group launched the "Grow Your Wealth with Every Opportunity" campaign, "Wealth Management Customer Referral Programme" and "New Wealth Management Customer Loyalty Building Programme".

Besides, the Group introduced the Capital Investment Entrant Scheme ("CIES") Services promotion campaign to provide a wide range of banking services to CIES customers. It also continued to work closely with BOC in providing cross-border wealth management services. Meanwhile, a mobile sales team was established to enhance the collaboration with BOC branches and strengthened the business development of NCB (China). At the end of June 2010, the total number of wealth management customers and their assets maintained with the Group grew by 6.7% and 1.5% respectively from the end of 2009.

#### ***Steady growth in credit card business***

The Group's card business sustained its growth momentum in the first half of 2010. The total number of cards issued increased by 9.3% compared to the end of 2009 while cardholder spending and merchant acquiring volume rose by 21.4% and 41.8% respectively year-on-year. The Group maintained its leadership in the China UnionPay ("CUP") merchant acquiring business and CUP card issuing business, with merchant acquiring and cardholder spending volume surging by 69.3% and 157.5% respectively compared to the first half of 2009.

Riding on the competitive edge of the "BOC CUP Dual Currency Credit Card" in the market, the Group continued to extend appealing merchant offer programmes to customers through its comprehensive merchant network covering Hong Kong, Macau and the Mainland.

The Group's success in credit card business gained extensive market recognition, as evidenced by a total of 28 awards received from VISA International, MasterCard and China UnionPay respectively.

The Group managed to safeguard its asset quality. The annualised charge-off ratio of credit cards for the six-month period to 30 June 2010 was 1.56%.

#### ***Maintaining market leadership in RMB banking business in Hong Kong***

The Group remained the market leader in RMB banking business in Hong Kong. In the first half of 2010, the Group focused on the RMB integrated services, "RMB Remittance Express" and "RMB Exchange Express" and launched

promotional offers to boost RMB deposits with satisfactory results. The Group also secured its leading position in the RMB card issuing business, with an increase of 45.5% in the number of RMB-HKD dual currency credit cards from the end of 2009. Meanwhile, the Group pioneered the first RMB life insurance product in Hong Kong with settlement being made in Hong Kong Dollars. This new product was well-received by customers. The Group also made significant progress in the RMB corporate banking business. For details, please refer to Corporate Banking section below.

#### ***Channel rationalisation and e-channel development***

In response to the changing needs of customers, the Group revamped its branch network to strengthen its offering of investment services and traditional banking services. Customers can obtain specialised investment advices as well as comprehensive traditional banking services at designated branches. Service quality and customer experience were enhanced by a series of well-structured staff training programmes. At the end of June 2010, the Group's service network in Hong Kong comprised 269 branches.

The Group continued to enhance the functions of its e-Banking platform and improve its investment service quality. It introduced the credit card payment service for insurance premiums and remittance, which was the first of its kind in the market. At the same time, the launch of the new 24-hour scheduled electronic transfer functions provided customers with more efficient e-Banking services. It also strengthened the security measures such as a conversion to a new e-certificate storage device with higher security and notification of unusual transactions to customers by SMS. In the first half of 2010, the number of internet banking customer increased by 5.5% while stock trading transactions carried out through e-channels accounted for 77.1% of total transactions. The Group also enhanced the quality of telephone banking services by consolidating its services into four specialised hotline numbers, namely personal, corporate, investment and wealth management, with the aim of providing one-stop and more user-friendly phone banking services to customers. The Group also opened a new call centre in Shenzhen to provide cross-border service support for Hong Kong as well as Mainland customers.

To encourage more customers to use its automated banking services, the Group added new ATMs to its ATM network and increased the number of cheque deposit machines and cash deposit machines. At the same time,

the Group enhanced its promotion of the dual currency cash withdrawal services, which aimed at providing convenient RMB cash withdrawal services to customers.

## CORPORATE BANKING

| HK\$m, except percentage amounts              | Half-year ended<br>30 June<br>2010 | Half-year ended<br>30 June<br>2009 | Increase/<br>(decrease) |
|-----------------------------------------------|------------------------------------|------------------------------------|-------------------------|
| Net interest income                           | 2,995                              | 2,644                              | +13.3%                  |
| Other operating income                        | 1,464                              | 1,197                              | +22.3%                  |
| Operating income                              | 4,459                              | 3,841                              | +16.1%                  |
| Operating expenses                            | (1,232)                            | (1,039)                            | +18.6%                  |
| Operating profit before impairment allowances | 3,227                              | 2,802                              | +15.2%                  |
| Net release of loan impairment allowance      | 131                                | 134                                | -2.2%                   |
| Others                                        | –                                  | (1)                                | –                       |
| Profit before taxation                        | 3,358                              | 2,935                              | +14.4%                  |

|                     | At 30 June<br>2010 | At 31 December<br>2009 | Increase/<br>(decrease) |
|---------------------|--------------------|------------------------|-------------------------|
| Segment assets      | 427,618            | 372,443                | +14.8%                  |
| Segment liabilities | 313,592            | 304,882                | +2.9%                   |

Note: For additional segmental information, see Note 41 to the Interim Financial Information.

### Financial Results

Corporate Banking performed particularly well with profit before taxation rising by HK\$423 million or 14.4% to HK\$3,358 million in the first half of 2010. Operating profit before impairment allowance increased by 15.2% to HK\$3,227 million. The increase was mainly driven by the growth in net interest income and other operating income.

Net interest income increased by 13.3%, which was mainly attributable to the increase in the average balance

of loans and advances. The increase was partly offset by narrower loan spread. Other operating income rose by 22.3%, primarily driven by the growth in fee income from the lending business, currency exchange and bills commission.

Operating expenses rose by 18.6% mainly due to higher staff costs, rental expenses and IT costs.

Advances and other accounts increased by 14.9% to HK\$425,589 million.

### **Business Operation**

The corporate banking business posted steady development during the first half of 2010. Corporate loans registered double-digit growth. The Group continued to provide comprehensive cross-border financing services for large corporate clients with overseas expansion plans. The Group succeeded in improving the pricing of new corporate loans during the period. Boosted by active marketing and product innovation, the Group stayed as the market leader in the cross-border RMB business in Hong Kong, pioneering a number of first transactions in new business areas. As for the Mainland business, the Group registered satisfactory growth in both loans and deposits.

#### ***Corporate loans sustained continuous growth***

Against the backdrop of a reviving economy, the Group stepped up the provision and development of cross-border financial services for corporate clients in the Mainland using Hong Kong as a financial platform. As a result, corporate loans witnessed rapid growth. At the end of June 2010, the Group's overall corporate loans surged by 14.3% over the end of last year. It remained the top mandated arranger in the Hong Kong-Macau syndicated loan market.

#### ***Steady development of SME business***

The Group gave further and active support to local enterprises with sound financial strength through the "SME Loan Guarantee Scheme" and "Special SME Loan Guarantee Scheme" launched by the government. In close collaboration with BOC and NCB (China) on the one hand, and by deepening cooperation with major trade associations on the other, the Group succeeded in reaching out to new customers. In recognition of its quality services and contribution to the SME business, the Group was honoured with the "SME's Best Partner Award" for the third consecutive year by the Hong Kong Chamber of Small and Medium Business Limited.

#### ***Pioneering new business areas in RMB banking***

Leveraging its unique position as the Hong Kong's RMB clearing bank, the Group achieved a number of

milestones in the development of the RMB banking business. Following the announcement of the "Elucidation of Supervisory Principles and Operational Arrangements Regarding Renminbi Business in Hong Kong" by the Hong Kong Monetary Authority on 11 February, the Group pioneered a number of first transactions in new areas of RMB business in Hong Kong, such as the granting of the first RMB export invoice finance, the first RMB import invoice finance, the first RMB working capital loan and the first RMB remittance service for dividend payout. In June 2010, the number of cities covered by the pilot programme of Cross-border RMB Trade Settlement Services was further expanded. BOCHK took the lead in conducting 34 cross-border RMB trade settlement transactions on the first day of the expanded pilot programme. In July 2010, the Group underwrote the first RMB corporate bond in Hong Kong as the sole bookrunner and lead manager.

The Group launched the CNY HIBOR as a pricing benchmark for RMB trade finance and commercial loans in Hong Kong. It also signed various agreements with more financial institutions across the globe for the provision of RMB clearing services. On 13 July, the People's Bank of China and BOCHK signed the "Agreement on Provision of Clearing Service for RMB Cashnotes Business for Taiwan" which authorises BOCHK as the Clearing Bank of RMB cashnotes business for Taiwan.

#### ***Trade finance registering strong growth***

The Group's balance of trade finance surged notably by 34.0% over the end of 2009. This was partly fuelled by the rapid recovery in global trade and partly as a result of closer cooperation with BOC. Innovative products with cross-border features have been launched to enhance the Group's trade finance services. In April 2010, BOCHK received "The Asian Banker Achievement Award for Trade Finance in Hong Kong" from The Asian Banker magazine in recognition of its outstanding performance and contribution in trade finance.

**Expanding foothold in custody services**

Riding on its growth momentum in 2009, the custody business continued to flourish in the first half of 2010. The Group has successfully secured mandates to provide global custody services to various Qualified Domestic Institutional Investors, including major banks, fund houses and securities companies in the Mainland. Furthermore, with continuous communication and sales effort coupled with outstanding service track record, clients were increasingly aware of the Group's strengths and capabilities in the global custody arena. The Group continued to work closely with BOC to expand its customer base. At the end of June 2010, total assets under the Group's custody were valued at HK\$384 billion.

**Cash management making solid progress**

The Group made solid progress in its cash management business in the first half of 2010. In April, the Group launched a remittance service via credit card, enabling BOCHK credit card holders to send remittance overseas with their BOCHK Credit Cards, which was the first of its kind in the market. A new Premium Savings Account product was launched in May, which provided competitive product features to corporate customers and attracted new savings deposits. The Group continued to strengthen the linkage of its cash management service platform with those of BOC and its overseas branches. With effective marketing, the remittance transaction volume increased by 14.0% year-on-year, while the number of Corporate Banking Services Online ("CBS Online") customers increase by 10.7% over the end of 2009.

**Proactive measures in risk management**

In view of the still uncertain global economic environment, the Group remained vigilant over risk management. To safeguard asset quality, the Group closely monitored those corporate customers which were adversely affected by rising production costs in the Mainland, RMB appreciation, the recent upsurge in commodity prices, and emerging

risks in the Euro region. With a forward-looking credit control system in place, the Group was able to implement more stringent credit control in those segments with higher risks.

**MAINLAND BUSINESS****Steady growth of Mainland business**

The Group's Mainland business recorded satisfactory growth in the first half of 2010. Total operating income increased by 11.8% year-on-year, driven by a rapid growth in income which more than offset the increase in operating expenses following the Group's further investment in the Mainland. Total advances to customers grew by 18.2% over the end of 2009, while the deposits balance leaped by 60.6%. NCB (China) launched various RMB wealth management products, such as "Floating Yield Product with Flexible Maturity", "Yi An Investment-Supported Products" and "Structured Deposits Linked with Exchange Rate". The customer base was further enlarged, with considerable increase in the number of high net worth customers. Since the launch of debit cards in late 2009, the Group continued to enhance their features to provide more convenient financial services to cross-border customers. The Group's asset quality in the Mainland remained sound with the classified loan ratio dropping by 0.07 of a percentage point from the end of 2009 to 0.37%.

**Further expansion of Mainland branch network**

The Group's total number of branches and sub-branches in the Mainland was 23 at the end of June 2010. The expansion of the Group's network in the Mainland continued. During the first half of 2010, NCB (China) received approval from the China Banking Regulatory Commission ("CBRC") for establishing the Shanghai Hongqiao sub-branch and Beijing Zhongguancun sub-branch. Meanwhile, Wuxi branch of NCB (China) commenced business on 19 July 2010.

## TREASURY

| HK\$'m, except percentage amounts                                       | Half-year ended<br>30 June<br>2010 | Half-year ended<br>30 June<br>2009 | Increase/<br>(decrease) |
|-------------------------------------------------------------------------|------------------------------------|------------------------------------|-------------------------|
| Net interest income                                                     | 2,341                              | 2,999                              | -21.9%                  |
| Other operating income                                                  | 35                                 | 747                                | -95.3%                  |
| Operating income                                                        | 2,376                              | 3,746                              | -36.6%                  |
| Operating expenses                                                      | (330)                              | (394)                              | -16.2%                  |
| Operating profit before impairment allowances                           | 2,046                              | 3,352                              | -39.0%                  |
| Net release/(charge) of impairment allowances on securities investments | 72                                 | (1,168)                            | +106.2%                 |
| Profit before taxation                                                  | 2,118                              | 2,184                              | -3.0%                   |

|                     | At 30 June<br>2010 | At 31 December<br>2009 | Increase/<br>(decrease) |
|---------------------|--------------------|------------------------|-------------------------|
| Segment assets      | 608,925            | 593,807                | +2.5%                   |
| Segment liabilities | 227,112            | 195,956                | +15.9%                  |

Note: For additional segmental information, see Note 41 to the Interim Financial Information.

## Financial Results

In the first half of 2010, the Treasury segment's profit before taxation fell by 3.0% to HK\$2,118 million. Operating profit before impairment allowances decreased by 39.0% to HK\$2,046 million, which was mainly caused by the decrease in net interest income and other operating income.

Net interest income fell by 21.9% mainly due to the decline in the average balance of residual funds as funds were redeployed for advances to customers. Meanwhile, the decrease in net yield of debt securities due to repricing also led to the decline in net interest income.

Other operating income dropped by 95.3% on account of the foreign exchange loss on foreign exchange swap contracts and mark-to-market loss on certain interest rate instruments.

## Business Operation

*Pursuing proactive investment strategy*

In light of the gradual economic revival and uncertainties in capital markets, the Group proactively managed its banking book investments and adopted a prudent approach in asset and liability management. In the first quarter of 2010, the Group took advantage of the steepening yield curve and expanded its investments in

fixed rate debt securities with increases in government-related securities as well as high quality financial institution bonds and corporate bonds in order to maximise the net interest margin of its investment portfolio. Starting from the second quarter, in spite of the sturdy growth in financial performance of financial institutions and corporations in the Asia-Pacific and the USA, credit spread widened as a result of the European sovereign debt crisis. While avoiding high-risk entities and regions, the Group seized the opportunity to increase its exposures to financial institution bonds and corporate bonds with robust fundamentals. Meanwhile, it also continued to provide clearing services to participating banks in Hong Kong and overseas regions.

As at the end of June 2010, the carrying value of the Group's exposure to US non-agency RMBS was HK\$3.0 billion (versus HK\$3.8 billion at the end of 2009). In respect of the exposure to the European countries which were affected by the debt crisis, namely Portugal, Ireland, Italy, Greece and Spain, the Group only had exposure to debt securities issued by financial institutions of Ireland and Italy amounting to a total of HK\$1,806 million as at the end of June 2010 (versus HK\$3,217 million at the end of 2009). There were no signs of impairment on these debt securities.

**Focusing on traditional business and internal control**

The European sovereign debt crisis had weakened market sentiments and investors' confidence. Despite this unfavorable factor, the Group's strategy of focusing on traditional products relating to foreign exchange and precious metals yielded promising results. Meanwhile, the Group also provided offshore customers with hedging products linked to foreign exchange and interest rate

to meet their hedging needs. As a result, the trading volumes of RMB foreign exchange derivatives and interest rate swaps registered satisfactory growth. The Group also expanded business cooperation with BOC's overseas branches to conduct RMB exchange business. Meanwhile, the Group closely monitored and exercised stringent control on the sale procedures and risk of its structured products.

**INSURANCE**

| HK\$m, except percentage amounts  | Half-year ended<br>30 June<br>2010 | Half-year ended<br>30 June<br>2009 | Increase/<br>(decrease) |
|-----------------------------------|------------------------------------|------------------------------------|-------------------------|
| Net interest income               | 724                                | 562                                | +28.8%                  |
| Other operating income            | 3,361                              | 573                                | +486.6%                 |
| Operating income                  | 4,085                              | 1,135                              | +259.9%                 |
| Net insurance benefits and claims | (3,875)                            | (919)                              | +321.7%                 |
| Net operating income              | 210                                | 216                                | -2.8%                   |
| Operating expenses                | (104)                              | (61)                               | +70.5%                  |
| Profit before taxation            | 106                                | 155                                | -31.6%                  |

|                     | At 30 June<br>2010 | At 31 December<br>2009 | Increase/<br>(decrease) |
|---------------------|--------------------|------------------------|-------------------------|
| Segment assets      | 40,153             | 37,963                 | +5.8%                   |
| Segment liabilities | 37,459             | 35,355                 | +6.0%                   |

Note: For additional segmental information, see Note 41 to the Interim Financial Information.

**Financial Results**

The Group's Insurance segment recorded a profit before taxation of HK\$106 million. The segment's profit dropped 31.6% year-on-year mainly due to the new business strain caused by the substantial increase in the regular premium business. This phenomenon is normal as new business, in particular the growth of regular premium, inevitably causes an immediate downward pressure on the current year's profit because higher commission expenses are recognised as incurred in the first year the policies are being written. The benefit of the new business to the Insurance segment's profit will be duly reflected in the years ahead.

Net interest income rose by 28.8% due to the increase in debt securities investments made for the new premiums received. Other operating income increased significantly

by 486.6% due to the growth of net insurance premium income and a net gain on financial instruments designated at fair value through profit or loss. During the first half of 2010, net insurance premium income rose considerably by 23.6% year-on-year. Net gain on financial instruments designated at fair value through profit or loss was attributable to the mark-to-market gain of debt securities investment caused by the decrease in market interest rates. The change in market interest rates also led to a corresponding increase of net insurance benefits and claims.

The net insurance benefits and claims rose significantly following the increase in policy reserves caused by the growth of the insurance business and the decrease in interest rates.

Operating expenses increased by 70.5% which were primarily due to the increase in staff costs following the expansion of the financial planning team, and the increase in resources to strengthen the business support.

Assets in the insurance segment grew by 5.8% because of the increase in both debt and equity securities investments made for the new income. Liabilities rose by 6.0% reflected the corresponding increase in insurance contractual liabilities.

### **Business Operation**

#### ***Further improvement in product mix and market share***

Following the launch of the new financial planning team and "Need-based Selling" approach in 2009, the Group continued to make good progress in growing its insurance business. Total premium income increased with product mix improved. Regular premium received improved by 250.9% as the Group continued to emphasise on sale of regular-premium products.

#### ***Introducing new RMB insurance products***

The Group intensified its effort in product innovation to fulfill customers' needs. In the first half of 2010, the Group introduced a broader range of RMB insurance products with settlement being made in Hong Kong Dollars. These new products, including the RMB "Target 8 Years Insurance Plan Series" and the RMB "Target 5 Years Insurance Plan Series", were highly receptive to customers. This reinforced the Group's leadership position in the RMB insurance business in Hong Kong.

## **RISK MANAGEMENT**

### ***Banking Group***

#### **Overview**

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

### **Risk Management Governance Structure**

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

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

The Chief Executive ("CE") is responsible for managing the Group's various types of risks, approving detailed risk management policies, and approving material risk exposures or transactions within his authority delegated by the Board of Directors. The Chief Risk Officer ("CRO") assists the CE in fulfilling his responsibilities for the day-to-day management of risks. The CRO is responsible for initiating new risk management strategies, projects and measures that will enable the Group to better monitor and manage new risk issues or areas that may arise from time to time from new businesses, products and changes in the operating environment. He may also take appropriate initiatives in response to regulatory changes. The CRO is also responsible for reviewing material risk exposures or

transactions within his delegated authority and exercising his power of veto if he believes that any transaction should not proceed.

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

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

### Credit Risk Management

Credit risk is the risk that a customer or counterparty will be unable to or unwilling to meet its obligations under a contract. It arises principally from lending, trade finance and treasury businesses, and covers inter-bank transactions, foreign exchange and derivative transactions as well as investments in bonds and securities. The Chief Credit Officer reports directly to the CRO and is responsible for the management of credit risk and for the formulation of all credit policies and procedures. The Chief Analytics Officer who reports directly to the CRO is responsible for the development and maintenance of internal rating models and rating criteria. Different credit approval and control procedures are adopted according to the level of risk associated with the customer, counterparty or transaction. Corporate and financial institution credit applications are independently reviewed, objectively assessed and monitored by risk management units and credit rating models/scorecards are used in the process of credit approval whenever they are applicable. A credit scoring system is used to process retail credit transactions, including residential mortgage loans, personal loans and credit cards. The Credit Risk Assessment Committee comprising experts from the Group's credit and other functions is responsible for making an independent assessment of all credit facilities which require the approval of a Deputy Chief Executive or above.

The Group's internal loan grading system divides credit assets into 5 categories with reference to HKMA's guidelines. The Risk Management Department ("RMD") provides regular credit management information reports and ad hoc reports to the Management Committee, RC and Board of Directors to facilitate their continuous monitoring of credit risk.

For investments in debt securities and securitisation assets, the external credit rating and assessment on credit quality of the underlying assets are used for managing the credit risk involved. Credit limits are established on a customer and security issuer basis. For derivatives, the Group sets customer limits to manage the credit risk involved and follows the same approval and control processes as loans and advances. Ongoing monitoring procedures are established.

The Group adopts a comprehensive methodology in determining whether a particular asset/mortgage-backed security ("ABS/MBS") is impaired. Under the methodology, the Group will take into consideration not only the mark-to-market (MTM) price of the issue and its external credit rating, but also additional factors such as FICO score, vintage, location, adjustable rate mortgage ("ARM") status, delinquencies, level of collateral protection, loan to value ratio and prepayment speed of the underlying assets. Furthermore, having considered these factors, the ABS/MBS issue has to further pass the required credit enhancement coverage ratio set by the Group. This ratio is determined by applying assumptions regarding the default rates based on the available delinquency, foreclosure and real estate owned ("REO") data of the ABS/MBS issue.

### Interest Rate Risk Management

The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

- Repricing risk – mismatches in the maturity or repricing periods of assets and liabilities
- Basis risk – different pricing basis for different transactions so that the yield on assets and cost of liabilities may change by different amounts within the same repricing period

- Yield curve risk – non-parallel shifts in the yield curve, e.g. steepening or flattening of the yield curve that may have an adverse impact on net interest income or economic value
- Option risk – exercise of the options embedded in assets, liabilities or off-balance sheet items that can cause a change in the cashflows of assets and liabilities

The ALCO exercises its oversight of interest rate risk and ensures the business operations of the Group are conducted within the risk appetite and controls as set by RC. The Asset & Liability Management Department ("ALMD") assists the ALCO to manage and optimise the asset-liability structure of which the interest rate characteristics are key factors that affect the interest rate risk profile. RMD is the independent unit responsible for overseeing the interest rate risk according to the established policies and limits and reporting the results to RC and ALCO regularly.

The interest rate risk is identified and measured on a daily basis. Gap analysis is one of the tools used to measure the Group's exposure to repricing risk. This provides the Group with a static view of the maturity and repricing characteristics of its balance sheet positions. As the risk is complicated by having optionality embedded in certain products, behavioural assumptions are made to reflect more accurately the interest rate risk exposures. The key assumption in gap analysis includes the replacement of contractual maturity of fixed rate mortgage-backed (US prime and Alt-A) securities by behavioural maturity. The Group uses interest rate derivatives to hedge its interest rate exposures and in most cases, plain vanilla interest rate swaps are used.

Sensitivities of earnings and economic value to interest rate changes (Earnings at Risk and Economic Value at Risk) are assessed through a hypothetical interest rate shock of 200 basis points across the yield curve on both sides. Earnings at Risk and Economic Value at Risk are controlled within an approved percentage of the projected net interest income for the year and the latest capital base respectively and these limits are sanctioned by RC. Moreover, sensitivity limits like PVBP and Option Greeks limits are adopted as daily control measures to monitor the repricing risk and option risk of the investment portfolio.

The impact of basis risk is gauged by the projected change in net interest income under scenarios of imperfect correlation in the adjustment of the rates earned and paid on different instruments. In addition, ratios of assets to liabilities with similar pricing basis are established to monitor such risk.

Apart from the above, regular stress tests and scenario analysis are conducted to assess the impact of different types of interest rate risk on the Group's earnings and economic value under both normal and stress conditions.

Before launching a new product or business, the relevant departments are required to go through a risk assessment process, which includes assessment of underlying interest rate risk and consideration of the adequacy of current risk management mechanism. Any material impact on interest rate risk noted during the risk assessment process will be reported to RC.

### Market Risk Management

Market risk is the risk of loss that results from movements in market rates and prices. The Group's market risk in the trading book arises from customer-related business and proprietary trading. Trading positions are subject to daily mark-to-market valuation. The risk includes potential losses arising from a change in foreign exchange and interest rates as well as the prices of equities and commodities.

The major market risk in the banking book arises from the Group's investment portfolio. The risk includes potential losses arising from changes in market parameters such as credit, liquidity, and interest rate risk. These positions are subject to monthly mark-to-market valuation and various control measures in relevant risk areas.

#### *Market risk management framework*

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

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

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

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

The Group uses backtesting to monitor the predictive power of the VAR measure. Backtesting compares the calculated VAR figure of those trading positions of each business day with the actual revenues arising on those positions on the next business day. These actual revenues exclude non-trading income, such as fee and commission. If backtesting revenues are negative and exceeding the VAR, a "backtesting exception" is noted. The Group will assess the magnitude of the backtesting exceptions, and revise its VAR model (including the parameters and

assumptions) accordingly. Backtesting results are reported to the Group's senior management, including CE and CRO.

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

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

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

#### **Liquidity Risk Management**

The aim of liquidity management is to enable the Group to meet, even under adverse market conditions, all its maturing repayment obligations on time, and to fund all its asset growth and strategic opportunities with reasonable costs.

The primary objective of the Group's asset and liability management strategy is to achieve optimal returns while ensuring adequate levels of liquidity and capital within an effective risk control framework. The Group funds its operations principally by accepting deposits from retail and corporate depositors. In addition, the Group may issue certificates of deposit or debt instruments to secure long-term funds. Besides, the Group may obtain funds from the interbank market when necessary. Funding may also be secured through adjusting the asset mix in the Group's investment portfolio. The Group uses the majority of funds raised to extend loans, to purchase debt securities or to conduct interbank placements.

Liquidity management is carried out at both the Group and the subsidiary level. BOCHK and its subsidiaries are required to maintain a strong daily liquidity position and a healthy cash flow profile that can align the risk-taking incentives with the liquidity exposures and make sure all funding obligations are met when due. Subsidiaries are required to report their respective liquidity position to BOCHK on a regular basis to facilitate group-wide management.

The ALCO exercises its oversight of liquidity risk and ensures the daily operations of the Group are conducted within the risk appetite and controls as set by RC. ALMD assists the ALCO to manage and optimise the asset-liability structure of which the maturity profile is a key factor that affects the liquidity risk profile. RMD is the independent unit responsible for overseeing the liquidity risk according to the established policies and limits on a daily basis and reports the results to RC and ALCO regularly.

Liquidity risk management tools adopted include cash flow analysis (under normal and stress conditions), such as Maximum Cumulative Outflow, liquidity buffer asset portfolio, and balance sheet management ratios, deposits maturity structure, concentration risk, liquidity ratio, loan-to-deposit ratio, etc. Apart from these, regular stress tests (bank-specific crisis and general-market crisis) and scenario analysis are conducted to assess the Group's capability to withstand various severe liquidity crises.

Before launching a new product or business, the relevant departments are required to go through a risk assessment process, which includes the assessment of underlying liquidity risk and consideration of the adequacy of the current risk management mechanism. Any material impact

on liquidity risk noted during the risk assessment process will be reported to RC.

### Operational Risk Management

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. The risk is inherent in every aspect of business operations and confronted by the Bank in its day to day operational activities.

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

The Group has adopted the "Three Lines of Defence" model for its operational risk management framework. All departments and business units are the first line of defence, responsible for managing and reporting operational risks specific to their business/functional areas by applying the respective tools such as key risk indicators, self assessment and operational risk events reporting mechanism to identify, assess and control the risks inherent in their business/functional processes, activities and products. OR&CD together with certain operational risk-related functional departments within the Group are the second line of defence. In addition to formulating the operational risk management policies and procedures, OR&CD is also responsible for developing and introducing operational risk management tools, monitoring the performance and result of operational risk management in various units, assessing operational risk profile, recording operational risk data and reporting operational risk events to RC and the senior management in order to assist the overall management of the Group's operational risk. Certain functional departments including the Human Resources Department, Informational Technology Department, Corporate Services Department, Financial Management Department, General Accounting & Accounting Policy Department and OR&CD, are required to carry out the corporate-level operational risk management for the risk areas that are under their functional responsibilities and to provide other units with professional advice/training in respect of certain operational risk categories. The Audit

Department is the third line of defence, responsible for conducting independent audit of the operational risk management activities to evaluate their compliance and effectiveness.

The Group also takes out insurance to mitigate unforeseeable operational risks. Business continuity plans are in place to support business operations in the event of an emergency or disaster. Adequate backup facilities are maintained and periodic drills are conducted.

### **Reputation Risk Management**

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

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

In the Lehman Brothers minibonds incident, the Group has handled customer complaints in accordance with regulatory guidelines and completed the repurchase of most of the outstanding minibonds under the Repurchase Scheme and its complaint handling process to minimise the reputation risk.

### **Legal and Compliance Risk Management**

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

### **Strategic Risk Management**

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

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

### **Capital Management**

The major objective of capital management is to maximise shareholders' total return while maintaining a capital adequacy position commensurate with the Group's overall risk profile. The Group periodically reviews its capital structure and adjusts the capital mix where appropriate. ALCO monitors the Group's capital adequacy position. The Group has complied with all the statutory capital standards for all the periods in the first half of 2010.

To comply with HKMA's requirements as stated in the Supervisory Policy Manual "Supervisory Review Process", the Group has established the internal capital adequacy assessment process (ICAAP) and reviews it annually. Using the statutory minimum CAR, 8%, as a starting point, extra capital (capital add-on) needed to cover the risks not captured under Pillar I is assessed. A Scorecard approach based on HKMA's compliance guidance on Pillar II has been used to evaluate the Group's risk profile in order to assess the add-on capital in Pillar II to the minimum regulatory capital calculated under Pillar I to determine the minimum CAR. An Operating CAR Range has also been established which incorporates the need for future business growth and efficiency of capital utilisation. In view of the envisaged adoption of Foundation internal ratings-based approach ("FIRB"), the minimum CAR and the Operating CAR Range for 2010 are determined based on both Standardised approach and FIRB approach.

### Stress Testing

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

### BOC Life Insurance

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

#### Insurance Risk Management

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

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

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

For in-force insurance contracts, most of the underlying insurance liabilities are related to endowment and unit-linked insurance products. For most of the insurance policies issued, BOC Life has a retention limit on any single life insured. BOC Life cedes the excess of the insured benefit over the limit for standard risks (from a medical point of view) to reinsurer under an excess of loss reinsurance arrangement.

Uncertainty in the estimation of future benefit payments and premium receipts for long-term insurance contracts arises from the unpredictability of long-term changes in overall levels of mortality and persistency. In order to assess the uncertainty due to the mortality assumption and lapse assumption, BOC Life conducts mortality study and lapse study in order to determine the appropriate assumptions. In these studies, consistent results are reflected in both assumptions with appropriate margins.

#### Interest Rate Risk Management

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

#### Liquidity Risk Management

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

### Credit Risk Management

BOC Life has exposure to credit risk, which is the risk that a customer or counterparty will be unable to or unwilling to meet a commitment that it has entered into. Key areas to which BOC Life's insurance business is exposed include:

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

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

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

# CONDENSED CONSOLIDATED INCOME STATEMENT

|                                                                                             | Notes | (Unaudited)<br>Half-year ended<br>30 June 2010<br>HK\$'m | (Unaudited)<br>Half-year ended<br>30 June 2009<br>HK\$'m |
|---------------------------------------------------------------------------------------------|-------|----------------------------------------------------------|----------------------------------------------------------|
| Interest income                                                                             |       | 10,671                                                   | 11,331                                                   |
| Interest expense                                                                            |       | (1,707)                                                  | (2,317)                                                  |
| <b>Net interest income</b>                                                                  | 4     | <b>8,964</b>                                             | 9,014                                                    |
| Fee and commission income                                                                   |       | 4,481                                                    | 3,884                                                    |
| Fee and commission expense                                                                  |       | (1,084)                                                  | (937)                                                    |
| <b>Net fee and commission income</b>                                                        | 5     | <b>3,397</b>                                             | 2,947                                                    |
| Net trading (loss)/gain                                                                     | 6     | (36)                                                     | 804                                                      |
| Net gain/(loss) on financial instruments designated<br>at fair value through profit or loss |       | 640                                                      | (1,395)                                                  |
| Net gain on investment in securities                                                        | 7     | 404                                                      | 67                                                       |
| Net insurance premium income                                                                | 8     | 2,798                                                    | 2,261                                                    |
| Other operating income                                                                      | 9     | 249                                                      | 249                                                      |
| <b>Total operating income</b>                                                               |       | <b>16,416</b>                                            | 13,947                                                   |
| Net insurance benefits and claims                                                           | 10    | (3,875)                                                  | (919)                                                    |
| <b>Net operating income before impairment allowances</b>                                    |       | <b>12,541</b>                                            | 13,028                                                   |
| Net reversal/(charge) of impairment allowances                                              | 11    | 161                                                      | (1,115)                                                  |
| <b>Net operating income</b>                                                                 |       | <b>12,702</b>                                            | 11,913                                                   |
| Operating expenses                                                                          | 12    | (4,534)                                                  | (4,194)                                                  |
| <b>Operating profit</b>                                                                     |       | <b>8,168</b>                                             | 7,719                                                    |
| Net gain from disposal of/fair value adjustments<br>on investment properties                | 13    | 601                                                      | 525                                                      |
| Net loss from disposal/revaluation of properties,<br>plant and equipment                    | 14    | (1)                                                      | (1)                                                      |
| Share of profits less losses after tax of associates                                        |       | (1)                                                      | 1                                                        |
| <b>Profit before taxation</b>                                                               |       | <b>8,767</b>                                             | 8,244                                                    |
| Taxation                                                                                    | 15    | (1,414)                                                  | (1,369)                                                  |
| <b>Profit for the period</b>                                                                |       | <b>7,353</b>                                             | 6,875                                                    |
| <b>Profit attributable to:</b>                                                              |       |                                                          |                                                          |
| Equity holders of the Company                                                               |       | 7,190                                                    | 6,691                                                    |
| Non-controlling interests                                                                   |       | 163                                                      | 184                                                      |
|                                                                                             |       | <b>7,353</b>                                             | 6,875                                                    |
| <b>Dividends</b>                                                                            | 16    | <b>4,229</b>                                             | 3,013                                                    |
|                                                                                             |       | HK\$                                                     | HK\$                                                     |
| <b>Earnings per share for profit attributable to<br/>the equity holders of the Company</b>  | 17    | <b>0.6800</b>                                            | 0.6329                                                   |

The notes on pages 49 to 118 are an integral part of this interim financial information.

# CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

|                                                                                                       | Notes | (Unaudited)<br>Half-year ended<br>30 June 2010<br>HK\$'m | (Unaudited)<br>Half-year ended<br>30 June 2009<br>HK\$'m |
|-------------------------------------------------------------------------------------------------------|-------|----------------------------------------------------------|----------------------------------------------------------|
| <b>Profit for the period</b>                                                                          |       | <b>7,353</b>                                             | 6,875                                                    |
| Change in fair value of available-for-sale securities                                                 |       | <b>1,681</b>                                             | 3,449                                                    |
| Change in fair value of cash flow hedges                                                              |       | <b>(1)</b>                                               | –                                                        |
| Revaluation of premises                                                                               |       | <b>1,953</b>                                             | 1,415                                                    |
| Currency translation difference                                                                       |       | <b>25</b>                                                | (6)                                                      |
| Net deferred tax effect                                                                               | 32    | <b>(568)</b>                                             | (747)                                                    |
| Reclassification adjustments                                                                          |       |                                                          |                                                          |
| Release upon disposal of available-for-sale securities                                                |       | <b>(380)</b>                                             | (64)                                                     |
| Net impairment (release)/charge on available-for-sale securities transferred to income statement      | 11    | <b>(40)</b>                                              | 729                                                      |
| Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities |       | <b>(22)</b>                                              | (37)                                                     |
| <b>Other comprehensive income for the period, net of tax</b>                                          |       | <b>2,648</b>                                             | 4,739                                                    |
| <b>Total comprehensive income for the period</b>                                                      |       | <b>10,001</b>                                            | 11,614                                                   |
| <b>Total comprehensive income attributable to:</b>                                                    |       |                                                          |                                                          |
| Equity holders of the Company                                                                         |       | <b>9,836</b>                                             | 11,430                                                   |
| Non-controlling interests                                                                             |       | <b>165</b>                                               | 184                                                      |
|                                                                                                       |       | <b>10,001</b>                                            | 11,614                                                   |

The notes on pages 49 to 118 are an integral part of this interim financial information.

# CONDENSED CONSOLIDATED BALANCE SHEET

|                                                                                                  |       | (Unaudited)<br>At 30 June<br>2010<br>HK\$'m | (Audited)<br>At 31 December<br>2009<br>HK\$'m |
|--------------------------------------------------------------------------------------------------|-------|---------------------------------------------|-----------------------------------------------|
|                                                                                                  | Notes |                                             |                                               |
| <b>ASSETS</b>                                                                                    |       |                                             |                                               |
| Cash and balances with banks and other financial institutions                                    | 20    | 169,554                                     | 160,788                                       |
| Placements with banks and other financial institutions<br>maturing between one and twelve months |       | 35,958                                      | 60,282                                        |
| Financial assets at fair value through profit or loss                                            | 21    | 70,372                                      | 44,594                                        |
| Derivative financial instruments                                                                 | 22    | 19,140                                      | 17,584                                        |
| Hong Kong SAR Government certificates of indebtedness                                            |       | 41,950                                      | 38,310                                        |
| Advances and other accounts                                                                      | 23    | 597,306                                     | 527,135                                       |
| Investment in securities                                                                         | 24    | 313,237                                     | 313,755                                       |
| Interests in associates                                                                          |       | 213                                         | 217                                           |
| Investment properties                                                                            | 25    | 9,323                                       | 9,364                                         |
| Properties, plant and equipment                                                                  | 26    | 28,235                                      | 26,286                                        |
| Deferred tax assets                                                                              | 32    | 128                                         | 149                                           |
| Other assets                                                                                     | 27    | 16,760                                      | 14,327                                        |
| Total assets                                                                                     |       | 1,302,176                                   | 1,212,791                                     |
| <b>LIABILITIES</b>                                                                               |       |                                             |                                               |
| Hong Kong SAR currency notes in circulation                                                      |       | 41,950                                      | 38,310                                        |
| Deposits and balances of banks and other financial institutions                                  |       | 110,786                                     | 99,647                                        |
| Financial liabilities at fair value through profit or loss                                       | 28    | 26,876                                      | 16,288                                        |
| Derivative financial instruments                                                                 | 22    | 15,771                                      | 13,967                                        |
| Deposits from customers                                                                          | 29    | 892,211                                     | 842,321                                       |
| Other accounts and provisions                                                                    | 30    | 34,690                                      | 29,930                                        |
| Current tax liabilities                                                                          |       | 2,955                                       | 1,918                                         |
| Deferred tax liabilities                                                                         | 32    | 5,158                                       | 4,591                                         |
| Insurance contract liabilities                                                                   | 33    | 35,050                                      | 33,408                                        |
| Subordinated liabilities                                                                         | 34    | 27,192                                      | 26,776                                        |
| Total liabilities                                                                                |       | 1,192,639                                   | 1,107,156                                     |
| <b>EQUITY</b>                                                                                    |       |                                             |                                               |
| Share capital                                                                                    | 35    | 52,864                                      | 52,864                                        |
| Reserves                                                                                         | 36    | 53,847                                      | 50,038                                        |
| Capital and reserves attributable to the equity holders of<br>the Company                        |       | 106,711                                     | 102,902                                       |
| Non-controlling interests                                                                        |       | 2,826                                       | 2,733                                         |
| Total equity                                                                                     |       | 109,537                                     | 105,635                                       |
| Total liabilities and equity                                                                     |       | 1,302,176                                   | 1,212,791                                     |

The notes on pages 49 to 118 are an integral part of this interim financial information.

# CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

|                                                                                     | (Unaudited)                                       |                                             |                                                                                       |                                     |                                 |                                 |                               |                |                                           |                       |
|-------------------------------------------------------------------------------------|---------------------------------------------------|---------------------------------------------|---------------------------------------------------------------------------------------|-------------------------------------|---------------------------------|---------------------------------|-------------------------------|----------------|-------------------------------------------|-----------------------|
|                                                                                     | Attributable to the equity holders of the Company |                                             |                                                                                       |                                     |                                 |                                 |                               |                |                                           |                       |
|                                                                                     | Share capital<br>HK\$m                            | Premises<br>revaluation<br>reserve<br>HK\$m | Reserve for<br>fair value<br>changes of<br>available-for-<br>sale securities<br>HK\$m | Cash flow<br>hedge reserve<br>HK\$m | Regulatory<br>reserve*<br>HK\$m | Translation<br>reserve<br>HK\$m | Retained<br>earnings<br>HK\$m | Total<br>HK\$m | Non-<br>controlling<br>interests<br>HK\$m | Total equity<br>HK\$m |
| At 1 January 2009                                                                   | 52,864                                            | 8,214                                       | (4,125)                                                                               | –                                   | 4,503                           | 226                             | 21,037                        | 82,719         | 1,813                                     | 84,532                |
| Comprehensive income                                                                | –                                                 | 1,216                                       | 3,566                                                                                 | –                                   | –                               | (6)                             | 6,654                         | 11,430         | 184                                       | 11,614                |
| Release upon disposal of premises                                                   | –                                                 | (1)                                         | –                                                                                     | –                                   | –                               | –                               | 1                             | –              | –                                         | –                     |
| Transfer from retained earnings                                                     | –                                                 | –                                           | –                                                                                     | –                                   | 115                             | –                               | (115)                         | –              | –                                         | –                     |
| Dividends paid                                                                      | –                                                 | –                                           | –                                                                                     | –                                   | –                               | –                               | –                             | –              | (180)                                     | (180)                 |
| At 30 June 2009                                                                     | 52,864                                            | 9,429                                       | (559)                                                                                 | –                                   | 4,618                           | 220                             | 27,577                        | 94,149         | 1,817                                     | 95,966                |
| Company and subsidiaries                                                            | 52,864                                            | 9,429                                       | (559)                                                                                 | –                                   | 4,618                           | 220                             | 27,529                        | 94,101         |                                           |                       |
| Associates                                                                          | –                                                 | –                                           | –                                                                                     | –                                   | –                               | –                               | 48                            | 48             |                                           |                       |
|                                                                                     | 52,864                                            | 9,429                                       | (559)                                                                                 | –                                   | 4,618                           | 220                             | 27,577                        | 94,149         |                                           |                       |
| At 1 July 2009                                                                      | 52,864                                            | 9,429                                       | (559)                                                                                 | –                                   | 4,618                           | 220                             | 27,577                        | 94,149         | 1,817                                     | 95,966                |
| Comprehensive income                                                                | –                                                 | 2,314                                       | 2,439                                                                                 | –                                   | –                               | 5                               | 7,008                         | 11,766         | 198                                       | 11,964                |
| Release upon disposal of premises                                                   | –                                                 | (184)                                       | –                                                                                     | –                                   | –                               | –                               | 184                           | –              | –                                         | –                     |
| Transfer to retained earnings                                                       | –                                                 | –                                           | –                                                                                     | –                                   | (578)                           | –                               | 578                           | –              | –                                         | –                     |
| Dividends paid                                                                      | –                                                 | –                                           | –                                                                                     | –                                   | –                               | –                               | (3,013)                       | (3,013)        | (17)                                      | (3,030)               |
| Increase in non-controlling interests arising from capital issuance of a subsidiary | –                                                 | –                                           | –                                                                                     | –                                   | –                               | –                               | –                             | –              | 735                                       | 735                   |
| At 31 December 2009                                                                 | 52,864                                            | 11,559                                      | 1,880                                                                                 | –                                   | 4,040                           | 225                             | 32,334                        | 102,902        | 2,733                                     | 105,635               |
| Company and subsidiaries                                                            | 52,864                                            | 11,559                                      | 1,880                                                                                 | –                                   | 4,040                           | 225                             | 32,279                        | 102,847        |                                           |                       |
| Associates                                                                          | –                                                 | –                                           | –                                                                                     | –                                   | –                               | –                               | 55                            | 55             |                                           |                       |
|                                                                                     | 52,864                                            | 11,559                                      | 1,880                                                                                 | –                                   | 4,040                           | 225                             | 32,334                        | 102,902        |                                           |                       |
| At 1 January 2010                                                                   | 52,864                                            | 11,559                                      | 1,880                                                                                 | –                                   | 4,040                           | 225                             | 32,334                        | 102,902        | 2,733                                     | 105,635               |
| Comprehensive income                                                                | –                                                 | 1,628                                       | 974                                                                                   | (1)                                 | –                               | 66                              | 7,169                         | 9,836          | 165                                       | 10,001                |
| Release upon disposal of premises                                                   | –                                                 | (30)                                        | –                                                                                     | –                                   | –                               | –                               | 30                            | –              | –                                         | –                     |
| Transfer from retained earnings                                                     | –                                                 | –                                           | –                                                                                     | –                                   | 571                             | –                               | (571)                         | –              | –                                         | –                     |
| Dividends paid                                                                      | –                                                 | –                                           | –                                                                                     | –                                   | –                               | –                               | (6,027)                       | (6,027)        | (72)                                      | (6,099)               |
| At 30 June 2010                                                                     | 52,864                                            | 13,157                                      | 2,854                                                                                 | (1)                                 | 4,611                           | 291                             | 32,935                        | 106,711        | 2,826                                     | 109,537               |
| Company and subsidiaries                                                            | 52,864                                            | 13,157                                      | 2,854                                                                                 | (1)                                 | 4,611                           | 291                             | 32,884                        | 106,660        |                                           |                       |
| Associates                                                                          | –                                                 | –                                           | –                                                                                     | –                                   | –                               | –                               | 51                            | 51             |                                           |                       |
|                                                                                     | 52,864                                            | 13,157                                      | 2,854                                                                                 | (1)                                 | 4,611                           | 291                             | 32,935                        | 106,711        |                                           |                       |
| Representing:                                                                       |                                                   |                                             |                                                                                       |                                     |                                 |                                 |                               |                |                                           |                       |
| 2010 interim dividend proposed (Note 16)                                            |                                                   |                                             |                                                                                       |                                     |                                 |                                 | 4,229                         |                |                                           |                       |
| Others                                                                              |                                                   |                                             |                                                                                       |                                     |                                 |                                 | 28,706                        |                |                                           |                       |
| Retained earnings as at 30 June 2010                                                |                                                   |                                             |                                                                                       |                                     |                                 |                                 | 32,935                        |                |                                           |                       |

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

The notes on pages 49 to 118 are an integral part of this interim financial information.

# CONDENSED CONSOLIDATED CASH FLOW STATEMENT

|                                                            | Notes | (Unaudited)<br>Half-year ended<br>30 June 2010<br>HK\$'m | (Unaudited)<br>Half-year ended<br>30 June 2009<br>HK\$'m |
|------------------------------------------------------------|-------|----------------------------------------------------------|----------------------------------------------------------|
| <b>Cash flows from operating activities</b>                |       |                                                          |                                                          |
| Operating cash inflow/(outflow) before taxation            | 37(a) | 21,742                                                   | (25,354)                                                 |
| Hong Kong profits tax paid                                 |       | (325)                                                    | (126)                                                    |
| Overseas profits tax paid                                  |       | (32)                                                     | (59)                                                     |
| <b>Net cash inflow/(outflow) from operating activities</b> |       | <b>21,385</b>                                            | <b>(25,539)</b>                                          |
| <b>Cash flows from investing activities</b>                |       |                                                          |                                                          |
| Purchase of properties, plant and equipment                |       | (162)                                                    | (149)                                                    |
| Purchase of investment properties                          |       | (2)                                                      | –                                                        |
| Proceeds from disposal of properties, plant and equipment  |       | 93                                                       | 4                                                        |
| Proceeds from disposal of investment properties            |       | 163                                                      | 23                                                       |
| Dividends received from associates                         |       | 3                                                        | 3                                                        |
| <b>Net cash inflow/(outflow) from investing activities</b> |       | <b>95</b>                                                | <b>(119)</b>                                             |
| <b>Cash flows from financing activities</b>                |       |                                                          |                                                          |
| Dividends paid to the equity holders of the Company        |       | (6,027)                                                  | –                                                        |
| Dividends paid to non-controlling interests                |       | (72)                                                     | (180)                                                    |
| Proceeds from issuance of subordinated notes               |       | 19,261                                                   | –                                                        |
| Repayment of subordinated loans                            |       | (19,418)                                                 | –                                                        |
| Interest paid for subordinated loans                       |       | (156)                                                    | (552)                                                    |
| <b>Net cash outflow from financing activities</b>          |       | <b>(6,412)</b>                                           | <b>(732)</b>                                             |
| Increase/(decrease) in cash and cash equivalents           |       | 15,068                                                   | (26,390)                                                 |
| Cash and cash equivalents at 1 January                     |       | 182,708                                                  | 174,926                                                  |
| <b>Cash and cash equivalents at 30 June</b>                | 37(b) | <b>197,776</b>                                           | <b>148,536</b>                                           |

The notes on pages 49 to 118 are an integral part of this interim financial information.

# NOTES TO THE INTERIM FINANCIAL INFORMATION

## 1. Basis of preparation and accounting policies

### *Basis of preparation*

The unaudited interim report has been prepared in accordance with HKAS 34 “Interim Financial Reporting” issued by the HKICPA.

### *Accounting policies*

Except as described below, the accounting policies and methods of computation used in the preparation of the unaudited interim report are consistent with those used in the Group’s financial statements for the year ended 31 December 2009 and should be read in conjunction with the Group’s Annual Report for 2009.

### **Financial liabilities issued at amortised cost with fair value hedge adjustment**

The Group issued fixed rate subordinated notes in the first half of 2010 which are measured at amortised cost. The Group uses interest rate swaps to hedge the fixed rate subordinated notes, which change their interest rate repricing characteristics into those of floating rate financial liabilities. The hedge of fixed rate subordinated notes with interest rate swaps are designated as fair value hedge when the criteria for hedge accounting are fulfilled at the inception of the hedge and the hedge relationship last while the criteria are continued to be fulfilled on an on-going basis.

When fair value hedge accounting is applied to fixed rate financial liabilities, the carrying values of the financial liabilities are adjusted for changes in fair value that are attributable to the interest rate risk being hedged with the derivative instruments rather than carried at amortised cost, such carrying value adjustment is recognised in the income statement together with the changes in fair value of the hedging derivatives.

If the hedge relationship is terminated for reasons other than the derecognition, e.g. due to repayment of the hedged item, the unamortised carrying value adjustment (the difference between the carrying value of the hedged item at the time of termination and the value at which it would have been carried had the hedge never existed) is amortised to the income statement over the remaining life of the hedged item. If the hedged item is derecognised, the unamortised carrying value adjustment is recognised immediately in the income statement.

### **Revised standards and amendments to standards that are mandatory for the first time for the financial year beginning 1 January 2010**

- HKFRS 3 (Revised), ‘Business combinations’ and consequential amendments to HKAS 27, ‘Consolidated and separate financial statements’, HKAS 28, ‘Investments in associates’, and HKAS 31, ‘Interests in joint ventures’, are effective prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009.

The revised standard continues to apply the acquisition method to business combinations, with some significant changes. For example, all payments to purchase a business are to be recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently re-measured through the consolidated income statement. There is a choice on an acquisition-by-acquisition basis to measure the non-controlling interest in the acquiree either at fair value or at the non-controlling interest’s proportionate share of the acquiree’s net assets. All acquisition-related costs should be expensed. The adoption of HKFRS 3 (Revised) and consequential amendments to HKAS 27, HKAS 28 and HKAS 31 do not have an impact on the financial statements of the Group as there is no business combination conducted in the first half of 2010.

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

### *Accounting policies (continued)*

#### **Revised standards and amendments to standards that are mandatory for the first time for the financial year beginning 1 January 2010 (continued)**

- HKAS 17 (Amendment), 'Leases'. The amendment, which is part of an improvement to HKFRSs in 2009, has been made to delete a guidance stating that a lease of land with an indefinite economic life normally is classified as an operating lease, unless at the end of the lease term title is expected to pass to the lessee. The amendment requires the classification of leasehold land to be based on the general principles set out in HKAS 17, that are based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee.

As the transaction values in the Hong Kong property market have typically demonstrated that the market believes the lease term specified in land leases will be capable of extension for a nominal amount, risks and rewards of leaseholds land have already been substantially transferred to the lessee. Split of the land and buildings elements is no longer necessary as both of them are finance lease. The adoption of this amendment does not have an impact on the Group as the Group has not separately accounted for its land and buildings in the financial statements for the reason given in Note 2.18 shown in the Group's Annual Report for 2009.

- HKAS 27 (Revised), 'Consolidated and separate financial statements'. The revised standard requires changes in a parent's ownership interest in a subsidiary that do not result in the loss of control are accounted for within other comprehensive income and these transactions will no longer result in goodwill or gains and losses. The standard also specifies the accounting when control is lost. Any remaining interest in the entity is re-measured to fair value and a gain or loss is recognised in income statement. There has been no impact of HKAS 27 (Revised) on the current period as there have been no transactions with non-controlling interests.
- Other improvements to HKFRSs made in 2009 contain numerous amendments to HKFRSs which the HKICPA consider non-urgent but necessary. It comprises amendments that result in accounting changes for presentation, recognition or measurement purpose as well as terminology or editorial amendments related to a variety of individual HKFRS. Most of the amendments are effective for annual periods beginning on or after 1 January 2010, with earlier application permitted. No material changes to accounting policies are expected as a result of these amendments.

#### **Standards and amendments issued that are relevant to the Group but not yet effective and have not been early adopted by the Group in 2010**

| Standard          | Content                                                      | Applicable for financial years beginning on/after |
|-------------------|--------------------------------------------------------------|---------------------------------------------------|
| HKAS 24 (Revised) | Related Party Disclosures                                    | 1 January 2011                                    |
| HKFRS 9           | Financial Instruments Part 1: Classification and Measurement | 1 January 2013                                    |

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

### *Accounting policies (continued)*

#### **Standards and amendments issued that are relevant to the Group but not yet effective and have not been early adopted by the Group in 2010 (continued)**

- HKAS 24, 'Related Party Disclosures (Revised)'. The Group early adopted the partial exemption regarding disclosure requirements for transactions with government-related entities in its annual financial statements for the year ended 31 December 2009. The application of the remainder of the revised standard which amending the definition of related parties will not have significant impact on the Group.
- HKFRS 9, 'Financial Instruments Part 1: Classification and Measurement'. The application of HKFRS 9 is expected to have an effect on the classification and measurement of financial assets of the Group and a related impact on the Group's financial statements.
- Annual Improvements 2010 were issued in May 2010. This annual improvements process provides a vehicle for making non-urgent but necessary amendments to HKFRSs. Most of the amendments are effective for annual periods beginning on or after 1 January 2011, no material changes to accounting policies are expected as a result of these improvements.

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

The nature and assumptions related to the Group's accounting estimates are consistent with those used in the Group's financial statements for the year ended 31 December 2009.

As disclosed in the Group's financial statements for the year ended 31 December 2009, the Group entered into an agreement dated 22 July 2009 among the Securities and Futures Commission, the HKMA and 13 other distributing banks, pursuant to which the Group has repurchased from eligible customers their holdings in outstanding Lehman Brothers minibonds ("Minibonds"). The amount recoverable by the Group from the Minibonds remains uncertain and is dependent on a number of factors including resolution of certain legal matters, which may result in a wide range of recovery outcomes.

The final amount recovered by the Group could be different from the assessment made for the purposes of the Group's financial statements, and may result in a considerable credit being recognised in the income statement in the period when it is realised.

### 3. Financial risk management

The Group is exposed to financial risks as a result of engaging in a variety of business activities. The principal financial risks are credit risk, market risk (including currency risk and interest rate risk) and liquidity risk. This note summarises the Group's exposures to these risks.

#### 3.1 Credit Risk

##### A. Gross loans and advances

###### (a) Impaired advances

A financial asset is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred and that loss event(s) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

If there is objective evidence that an impairment loss on loans has been incurred, the amount of loss is measured as the difference between the carrying amount and the present value of estimated future cash flows generated by the financial asset. Objective evidence that a financial asset is impaired includes observable data that comes to the attention of the holder of the asset about the loss events.

|                                                                                              | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|----------------------------------------------------------------------------------------------|------------------------------|----------------------------------|
| Gross impaired advances to customers                                                         | 699                          | 1,023                            |
| Individually assessed loan impairment allowances made in respect of such advances            | 512                          | 671                              |
| Current market value of collateral held against the covered portion of advances to customers | 150                          | 227                              |
| Covered portion of advances to customers                                                     | 145                          | 192                              |
| Uncovered portion of advances to customers                                                   | 554                          | 831                              |
| Gross impaired advances to customers as a percentage of gross advances to customers          | 0.12%                        | 0.20%                            |

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

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### A. Gross loans and advances (continued)

###### (a) Impaired advances (continued)

Classified or impaired advances to customers are analysed as follows:

|                                                                                                   | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|---------------------------------------------------------------------------------------------------|------------------------------|----------------------------------|
| Gross classified or impaired advances to customers                                                | 1,317                        | 1,769                            |
| Gross classified or impaired advances to customers as a percentage of gross advances to customers | 0.23%                        | 0.34%                            |

Classified or impaired advances to customers follow the definitions set out in the Banking (Disclosure) Rules and represent advances which are either classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

###### (b) Advances overdue for more than 3 months

Advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid. Advances repayable by regular instalments are classified as overdue when an instalment payment is past due and remains unpaid. Advances repayable on demand are classified as overdue either when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instruction or when the advances have remained continuously outside the approved limit that was advised to the borrower.

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### A. Gross loans and advances (continued)

##### (b) Advances overdue for more than 3 months (continued)

The gross amount of advances overdue for more than 3 months is analysed as follows:

|                                                                                   | At 30 June 2010  |                                        | At 31 December 2009 |                                        |
|-----------------------------------------------------------------------------------|------------------|----------------------------------------|---------------------|----------------------------------------|
|                                                                                   | Amount<br>HK\$'m | % of gross<br>advances to<br>customers | Amount<br>HK\$'m    | % of gross<br>advances to<br>customers |
| Gross advances to customers which have been overdue for:                          |                  |                                        |                     |                                        |
| – six months or less but over three months                                        | 75               | 0.01%                                  | 103                 | 0.02%                                  |
| – one year or less but over six months                                            | 89               | 0.02%                                  | 154                 | 0.03%                                  |
| – over one year                                                                   | 558              | 0.10%                                  | 569                 | 0.11%                                  |
| Advances overdue for over three months                                            | 722              | 0.13%                                  | 826                 | 0.16%                                  |
| Individually assessed loan impairment allowances made in respect of such advances | 310              |                                        | 393                 |                                        |

|                                                                                              | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|----------------------------------------------------------------------------------------------|------------------------------|----------------------------------|
| Current market value of collateral held against the covered portion of advances to customers | 968                          | 977                              |
| Covered portion of advances to customers                                                     | 424                          | 459                              |
| Uncovered portion of advances to customers                                                   | 298                          | 367                              |

Collateral held against overdue or impaired loans is principally represented by charges over business assets such as commercial and residential premises for corporate loans and mortgages over residential properties for personal loans.

As at 30 June 2010 and 31 December 2009, there were no advances to banks and other financial institutions overdue for more than three months.

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### A. Gross loans and advances (continued)

##### (c) Rescheduled advances

|                                                                                                      | At 30 June 2010  |                                        | At 31 December 2009 |                                        |
|------------------------------------------------------------------------------------------------------|------------------|----------------------------------------|---------------------|----------------------------------------|
|                                                                                                      | Amount<br>HK\$'m | % of gross<br>advances to<br>customers | Amount<br>HK\$'m    | % of gross<br>advances to<br>customers |
| Rescheduled advances to customers net of amounts included in advances overdue for more than 3 months | 392              | 0.07%                                  | 573                 | 0.11%                                  |

As at 30 June 2010 and 31 December 2009, there were no rescheduled advances to banks and other financial institutions.

Rescheduled advances are those advances that have been restructured or renegotiated because of deterioration in the financial position of the borrower or of the inability of the borrower to meet the original repayment schedule and for which the revised repayment terms, either of interest or of repayment period, are non-commercial. Rescheduled advances, which have been overdue for more than three months under the revised repayment terms, are included in overdue advances.

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### A. Gross loans and advances (continued)

##### (d) Concentration of advances to customers

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

The information concerning gross advances to customers has been analysed into loans used inside or outside Hong Kong by industry sectors of the borrowers as follows:

|                                                                                                                                         | At 30 June 2010             |                      |                           |          |                                    |                                    |
|-----------------------------------------------------------------------------------------------------------------------------------------|-----------------------------|----------------------|---------------------------|----------|------------------------------------|------------------------------------|
|                                                                                                                                         | % Covered<br>by collateral  |                      | Classified or<br>impaired | Overdue* | Individually<br>assessed           | Collectively<br>assessed           |
|                                                                                                                                         | Gross<br>Advances<br>HK\$'m | or other<br>security |                           |          | impairment<br>allowances<br>HK\$'m | impairment<br>allowances<br>HK\$'m |
| Loans for use in Hong Kong                                                                                                              |                             |                      |                           |          |                                    |                                    |
| Industrial, commercial<br>and financial                                                                                                 |                             |                      |                           |          |                                    |                                    |
| – Property development                                                                                                                  | 31,588                      | 29.54%               | 3                         | 5        | –                                  | 93                                 |
| – Property investment                                                                                                                   | 69,525                      | 89.45%               | 142                       | 284      | 12                                 | 373                                |
| – Financial concerns                                                                                                                    | 19,754                      | 7.68%                | –                         | 1        | –                                  | 73                                 |
| – Stockbrokers                                                                                                                          | 1,291                       | 86.33%               | –                         | –        | –                                  | 6                                  |
| – Wholesale and retail trade                                                                                                            | 27,309                      | 41.68%               | 110                       | 160      | 44                                 | 129                                |
| – Manufacturing                                                                                                                         | 27,833                      | 38.54%               | 94                        | 277      | 42                                 | 134                                |
| – Transport and transport<br>equipment                                                                                                  | 26,519                      | 22.59%               | 89                        | 88       | 5                                  | 82                                 |
| – Recreational activities                                                                                                               | 429                         | 9.63%                | –                         | –        | –                                  | 1                                  |
| – Information technology                                                                                                                | 15,140                      | 0.82%                | –                         | –        | –                                  | 43                                 |
| – Others                                                                                                                                | 37,001                      | 28.97%               | 61                        | 266      | 11                                 | 118                                |
| Individuals                                                                                                                             |                             |                      |                           |          |                                    |                                    |
| – Loans for the purchase of flats<br>in Home Ownership Scheme,<br>Private Sector Participation<br>Scheme and Tenants<br>Purchase Scheme | 11,572                      | 99.95%               | 69                        | 395      | 1                                  | 9                                  |
| – Loans for purchase of other<br>residential properties                                                                                 | 131,491                     | 99.97%               | 112                       | 1,149    | –                                  | 62                                 |
| – Credit card advances                                                                                                                  | 7,143                       | –                    | 21                        | 178      | –                                  | 73                                 |
| – Others                                                                                                                                | 10,586                      | 69.06%               | 61                        | 239      | 33                                 | 17                                 |
| Total loans for use in Hong Kong                                                                                                        | 417,181                     | 63.15%               | 762                       | 3,042    | 148                                | 1,213                              |
| Trade finance                                                                                                                           | 39,285                      | 20.75%               | 141                       | 161      | 84                                 | 165                                |
| Loans for use outside Hong Kong                                                                                                         | 115,020                     | 31.98%               | 414                       | 174      | 280                                | 399                                |
| Gross advances to customers                                                                                                             | 571,486                     | 53.96%               | 1,317                     | 3,377    | 512                                | 1,777                              |

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### A. Gross loans and advances (continued)

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

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

|                                                                                                                                         | At 31 December 2009         |                      |                           |          |                                    |                                    |
|-----------------------------------------------------------------------------------------------------------------------------------------|-----------------------------|----------------------|---------------------------|----------|------------------------------------|------------------------------------|
|                                                                                                                                         | % Covered<br>by collateral  |                      | Classified or<br>impaired | Overdue* | Individually<br>assessed           | Collectively<br>assessed           |
|                                                                                                                                         | Gross<br>advances<br>HK\$'m | or other<br>security |                           |          | impairment<br>allowances<br>HK\$'m | impairment<br>allowances<br>HK\$'m |
| Loans for use in Hong Kong                                                                                                              |                             |                      |                           |          |                                    |                                    |
| Industrial, commercial<br>and financial                                                                                                 |                             |                      |                           |          |                                    |                                    |
| – Property development                                                                                                                  | 23,002                      | 38.08%               | 3                         | 5        | 1                                  | 68                                 |
| – Property investment                                                                                                                   | 72,686                      | 86.03%               | 206                       | 475      | 10                                 | 359                                |
| – Financial concerns                                                                                                                    | 11,596                      | 8.02%                | –                         | 5        | –                                  | 53                                 |
| – Stockbrokers                                                                                                                          | 301                         | 32.90%               | –                         | –        | –                                  | 2                                  |
| – Wholesale and retail trade                                                                                                            | 19,231                      | 53.38%               | 154                       | 225      | 61                                 | 96                                 |
| – Manufacturing                                                                                                                         | 21,388                      | 46.46%               | 117                       | 178      | 47                                 | 108                                |
| – Transport and transport<br>equipment                                                                                                  | 26,951                      | 16.39%               | 91                        | 14       | 3                                  | 80                                 |
| – Recreational activities                                                                                                               | 309                         | 14.41%               | –                         | –        | –                                  | 1                                  |
| – Information technology                                                                                                                | 15,581                      | 0.79%                | –                         | 1        | –                                  | 45                                 |
| – Others                                                                                                                                | 33,216                      | 22.10%               | 62                        | 203      | 15                                 | 106                                |
| Individuals                                                                                                                             |                             |                      |                           |          |                                    |                                    |
| – Loans for the purchase of flats<br>in Home Ownership Scheme,<br>Private Sector Participation<br>Scheme and Tenants<br>Purchase Scheme | 11,932                      | 99.94%               | 77                        | 457      | 1                                  | 10                                 |
| – Loans for purchase of other<br>residential properties                                                                                 | 127,208                     | 99.99%               | 125                       | 1,368    | 1                                  | 68                                 |
| – Credit card advances                                                                                                                  | 7,348                       | –                    | 27                        | 183      | –                                  | 76                                 |
| – Others                                                                                                                                | 10,645                      | 73.48%               | 68                        | 174      | 36                                 | 18                                 |
| Total loans for use in Hong Kong                                                                                                        | 381,394                     | 65.91%               | 930                       | 3,288    | 175                                | 1,090                              |
| Trade finance                                                                                                                           | 29,321                      | 23.03%               | 237                       | 224      | 175                                | 128                                |
| Loans for use outside Hong Kong                                                                                                         | 104,257                     | 25.54%               | 602                       | 240      | 321                                | 380                                |
| Gross advances to customers                                                                                                             | 514,972                     | 55.30%               | 1,769                     | 3,752    | 671                                | 1,598                              |

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

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### A. Gross loans and advances (continued)

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

##### (ii) Geographical analysis of gross advances to customers and overdue advances

The following geographical analysis of gross advances to customers and overdue advances is based on the location of the counterparties, after taking into account the transfer of risk in respect of such advances where appropriate.

##### Gross advances to customers

|                                                                                                                   | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|-------------------------------------------------------------------------------------------------------------------|------------------------------|----------------------------------|
| Hong Kong                                                                                                         | 433,779                      | 409,564                          |
| Mainland China                                                                                                    | 102,387                      | 72,556                           |
| Others                                                                                                            | 35,320                       | 32,852                           |
|                                                                                                                   | <b>571,486</b>               | <b>514,972</b>                   |
| <b>Collectively assessed loan<br/>impairment allowances<br/>in respect of the gross<br/>advances to customers</b> |                              |                                  |
| Hong Kong                                                                                                         | 1,293                        | 1,205                            |
| Mainland China                                                                                                    | 375                          | 290                              |
| Others                                                                                                            | 109                          | 103                              |
|                                                                                                                   | <b>1,777</b>                 | <b>1,598</b>                     |

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### A. Gross loans and advances (continued)

(d) Concentration of advances to customers (continued)

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

##### Overdue advances

|                                                                                                    | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|----------------------------------------------------------------------------------------------------|------------------------------|----------------------------------|
| Hong Kong                                                                                          | 3,144                        | 3,470                            |
| Mainland China                                                                                     | 216                          | 253                              |
| Others                                                                                             | 17                           | 29                               |
|                                                                                                    | <b>3,377</b>                 | <b>3,752</b>                     |
| <b>Individually assessed loan<br/>impairment allowances in<br/>respect of the overdue advances</b> |                              |                                  |
| Hong Kong                                                                                          | 229                          | 297                              |
| Mainland China                                                                                     | 83                           | 154                              |
| Others                                                                                             | 6                            | 6                                |
|                                                                                                    | <b>318</b>                   | <b>457</b>                       |
| <b>Collectively assessed loan<br/>impairment allowances in<br/>respect of the overdue advances</b> |                              |                                  |
| Hong Kong                                                                                          | 54                           | 57                               |
| Mainland China                                                                                     | 8                            | 9                                |
|                                                                                                    | <b>62</b>                    | <b>66</b>                        |

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### A. Gross loans and advances (continued)

(d) Concentration of advances to customers (continued)

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

##### Classified or impaired advances

|                                                                                                                       | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|-----------------------------------------------------------------------------------------------------------------------|------------------------------|----------------------------------|
| Hong Kong                                                                                                             | 916                          | 1,153                            |
| Mainland China                                                                                                        | 188                          | 260                              |
| Others                                                                                                                | 213                          | 356                              |
|                                                                                                                       | <b>1,317</b>                 | <b>1,769</b>                     |
| <b>Individually assessed loan<br/>impairment allowances in<br/>respect of the classified or<br/>impaired advances</b> |                              |                                  |
| Hong Kong                                                                                                             | 264                          | 316                              |
| Mainland China                                                                                                        | 86                           | 191                              |
| Others                                                                                                                | 162                          | 164                              |
|                                                                                                                       | <b>512</b>                   | <b>671</b>                       |
| <b>Collectively assessed loan<br/>impairment allowances in<br/>respect of the classified or<br/>impaired advances</b> |                              |                                  |
| Hong Kong                                                                                                             | 18                           | 23                               |
| Mainland China                                                                                                        | 6                            | 6                                |
|                                                                                                                       | <b>24</b>                    | <b>29</b>                        |

##### B. Repossessed assets

The estimated market value of repossessed assets held by the Group as at 30 June 2010 amounted to HK\$88 million (31 December 2009: HK\$137 million). They comprise properties in respect of which the Group has acquired access or control (e.g. through court proceedings or voluntary actions by the borrowers concerned) for release in full or in part of the obligations of the borrowers.

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

##### C. Debt securities

The table below represents an analysis of the carrying value of debt securities by credit rating and credit risk characteristic, based on Moody's ratings or their equivalent to the respective issues of the debt securities.

|                                                                      | At 30 June 2010 |                     |                   |                           |                                                        |        |                                                       |                |
|----------------------------------------------------------------------|-----------------|---------------------|-------------------|---------------------------|--------------------------------------------------------|--------|-------------------------------------------------------|----------------|
|                                                                      |                 |                     |                   |                           | Unrated                                                |        |                                                       | Total<br>HK\$m |
|                                                                      |                 |                     |                   |                           | Hong Kong<br>government<br>and<br>government<br>bodies |        | Other<br>governments<br>and<br>government<br>agencies |                |
|                                                                      | Aaa<br>HK\$m    | Aa1 to Aa3<br>HK\$m | A1 to A3<br>HK\$m | Lower<br>than A3<br>HK\$m |                                                        |        | Other<br>HK\$m                                        |                |
| <b>Investment in securities</b>                                      |                 |                     |                   |                           |                                                        |        |                                                       |                |
| US non-agency residential<br>mortgage-backed                         |                 |                     |                   |                           |                                                        |        |                                                       |                |
| – Subprime                                                           | 420             | 19                  | –                 | –                         | –                                                      | –      | –                                                     | 439            |
| – Alt-A                                                              | 102             | 127                 | 41                | 48                        | –                                                      | –      | –                                                     | 318            |
| – Prime                                                              | 463             | 92                  | 257               | 1,400                     | –                                                      | –      | –                                                     | 2,212          |
| Fannie Mae                                                           |                 |                     |                   |                           |                                                        |        |                                                       |                |
| – mortgage-backed<br>securities                                      | –               | –                   | –                 | –                         | –                                                      | 28     | –                                                     | 28             |
| Freddie Mac                                                          |                 |                     |                   |                           |                                                        |        |                                                       |                |
| – issued debt securities                                             | 79              | 160                 | –                 | –                         | –                                                      | –      | –                                                     | 239            |
| – mortgage-backed<br>securities                                      | –               | –                   | –                 | –                         | –                                                      | 823    | –                                                     | 823            |
| Other MBS/ABS                                                        | 2,789           | 372                 | –                 | –                         | –                                                      | 3,680  | –                                                     | 6,841          |
| Other debt securities                                                | 100,236         | 71,241              | 46,887            | 5,220                     | 8,252                                                  | 30,674 | 36,779                                                | 299,289        |
| Subtotal                                                             | 104,089         | 72,011              | 47,185            | 6,668                     | 8,252                                                  | 35,205 | 36,779                                                | 310,189        |
| <b>Financial assets at<br/>fair value through<br/>profit or loss</b> |                 |                     |                   |                           |                                                        |        |                                                       |                |
| Other MBS/ABS                                                        | 22              | –                   | –                 | –                         | –                                                      | –      | –                                                     | 22             |
| Other debt securities                                                | 978             | 10,941              | 17,369            | 1,309                     | 32,032                                                 | 157    | 2,282                                                 | 65,068         |
| Subtotal                                                             | 1,000           | 10,941              | 17,369            | 1,309                     | 32,032                                                 | 157    | 2,282                                                 | 65,090         |
| Total                                                                | 105,089         | 82,952              | 64,554            | 7,977                     | 40,284                                                 | 35,362 | 39,061                                                | 375,279        |

## 3. Financial risk management (continued)

## 3.1 Credit Risk (continued)

## C. Debt securities (continued)

|                                                                      | At 31 December 2009 |                     |                   |                           |                                                        |        |                                                       |                |
|----------------------------------------------------------------------|---------------------|---------------------|-------------------|---------------------------|--------------------------------------------------------|--------|-------------------------------------------------------|----------------|
|                                                                      |                     |                     |                   |                           | Unrated                                                |        |                                                       | Total<br>HK\$m |
|                                                                      |                     |                     |                   |                           | Hong Kong<br>government<br>and<br>government<br>bodies |        | Other<br>governments<br>and<br>government<br>agencies |                |
|                                                                      | Aaa<br>HK\$m        | Aa1 to Aa3<br>HK\$m | A1 to A3<br>HK\$m | Lower<br>than A3<br>HK\$m |                                                        |        | Other<br>HK\$m                                        |                |
| <b>Investment in securities</b>                                      |                     |                     |                   |                           |                                                        |        |                                                       |                |
| US non-agency residential<br>mortgage-backed                         |                     |                     |                   |                           |                                                        |        |                                                       |                |
| – Subprime                                                           | 504                 | 31                  | 12                | –                         | –                                                      | –      | –                                                     | 547            |
| – Alt-A                                                              | 138                 | 191                 | 44                | 11                        | –                                                      | –      | –                                                     | 384            |
| – Prime                                                              | 635                 | 242                 | 632               | 1,344                     | –                                                      | –      | –                                                     | 2,853          |
| Fannie Mae                                                           |                     |                     |                   |                           |                                                        |        |                                                       |                |
| – issued debt securities                                             | 1,348               | –                   | –                 | –                         | –                                                      | –      | –                                                     | 1,348          |
| – mortgage-backed<br>securities                                      | –                   | –                   | –                 | –                         | –                                                      | 51     | –                                                     | 51             |
| Freddie Mac                                                          |                     |                     |                   |                           |                                                        |        |                                                       |                |
| – issued debt securities                                             | 79                  | 160                 | –                 | –                         | –                                                      | –      | –                                                     | 239            |
| – mortgage-backed<br>securities                                      | –                   | –                   | –                 | –                         | –                                                      | 1,164  | –                                                     | 1,164          |
| Other MBS/ABS                                                        | 3,481               | 416                 | 25                | –                         | –                                                      | 2,695  | –                                                     | 6,617          |
| Other debt securities                                                | 84,843              | 71,964              | 39,499            | 6,824                     | 9,609                                                  | 39,437 | 45,119                                                | 297,295        |
| Subtotal                                                             | 91,028              | 73,004              | 40,212            | 8,179                     | 9,609                                                  | 43,347 | 45,119                                                | 310,498        |
| <b>Financial assets at<br/>fair value through<br/>profit or loss</b> |                     |                     |                   |                           |                                                        |        |                                                       |                |
| Fannie Mae                                                           |                     |                     |                   |                           |                                                        |        |                                                       |                |
| – issued debt securities                                             | 260                 | –                   | –                 | –                         | –                                                      | –      | –                                                     | 260            |
| Other MBS/ABS                                                        | 25                  | –                   | –                 | –                         | –                                                      | –      | –                                                     | 25             |
| Other debt securities                                                | 1,039               | 7,941               | 14,630            | 1,639                     | 13,902                                                 | 290    | 602                                                   | 40,043         |
| Subtotal                                                             | 1,324               | 7,941               | 14,630            | 1,639                     | 13,902                                                 | 290    | 602                                                   | 40,328         |
| Total                                                                | 92,352              | 80,945              | 54,842            | 9,818                     | 23,511                                                 | 43,637 | 45,721                                                | 350,826        |

The total amount of unrated issues amounted to HK\$114,707 million (31 December 2009: HK\$112,869 million) as at 30 June 2010, of which only HK\$3,950 million (31 December 2009: HK\$3,868 million) were without issuer ratings. For details, please refer to page 63.

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

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

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

|                                                          | At 30 June 2010 |                         |                       |                            |                   |                 |
|----------------------------------------------------------|-----------------|-------------------------|-----------------------|----------------------------|-------------------|-----------------|
|                                                          | Aaa<br>HK\$'m   | Aa1<br>to Aa3<br>HK\$'m | A1<br>to A3<br>HK\$'m | Lower<br>than A3<br>HK\$'m | Unrated<br>HK\$'m | Total<br>HK\$'m |
| Available-for-sale securities                            | 35,156          | 9,861                   | 8,056                 | 3,909                      | 2,561             | 59,543          |
| Held-to-maturity securities                              | 680             | 6,435                   | 1,683                 | –                          | 200               | 8,998           |
| Loans and receivables                                    | –               | 8,865                   | 2,830                 | –                          | –                 | 11,695          |
| Financial assets at fair value<br>through profit or loss | 157             | 32,032                  | 1,093                 | –                          | 1,189             | 34,471          |
| Total                                                    | 35,993          | 57,193                  | 13,662                | 3,909                      | 3,950             | 114,707         |

|                                                          | At 31 December 2009 |                         |                       |                            |                   |                 |
|----------------------------------------------------------|---------------------|-------------------------|-----------------------|----------------------------|-------------------|-----------------|
|                                                          | Aaa<br>HK\$'m       | Aa1<br>to Aa3<br>HK\$'m | A1<br>to A3<br>HK\$'m | Lower<br>than A3<br>HK\$'m | Unrated<br>HK\$'m | Total<br>HK\$'m |
| Available-for-sale securities                            | 30,333              | 28,233                  | 6,683                 | 3,089                      | 2,468             | 70,806          |
| Held-to-maturity securities                              | 697                 | 9,687                   | 3,039                 | 155                        | 988               | 14,566          |
| Loans and receivables                                    | –                   | 9,768                   | 2,935                 | –                          | –                 | 12,703          |
| Financial assets at fair value<br>through profit or loss | 156                 | 13,903                  | 323                   | –                          | 412               | 14,794          |
| Total                                                    | 31,186              | 61,591                  | 12,980                | 3,244                      | 3,868             | 112,869         |

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

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

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

|                                               | At 30 June 2010 |            |          |                  |         |       |                                                              |
|-----------------------------------------------|-----------------|------------|----------|------------------|---------|-------|--------------------------------------------------------------|
|                                               | Carrying values |            |          |                  |         |       | Of which<br>accumulated<br>impairment<br>allowances<br>HK\$m |
|                                               | Aaa             | Aa1 to Aa3 | A1 to A3 | Lower<br>than A3 | Unrated | Total |                                                              |
|                                               | HK\$m           | HK\$m      | HK\$m    | HK\$m            | HK\$m   | HK\$m |                                                              |
| <b>Investment in securities</b>               |                 |            |          |                  |         |       |                                                              |
| US non-agency residential<br>mortgage-backed  |                 |            |          |                  |         |       |                                                              |
| – Subprime                                    | 401             | 5          | –        | –                | –       | 406   | 45                                                           |
| – Alt-A                                       | –               | 38         | 41       | 48               | –       | 127   | 57                                                           |
| – Prime                                       | 48              | –          | 198      | 1,300            | –       | 1,546 | 292                                                          |
| Other MBS/ABS                                 | –               | 79         | –        | –                | –       | 79    | 9                                                            |
| Other debt securities                         | –               | –          | –        | –                | –       | –     | 281                                                          |
| Total                                         | 449             | 122        | 239      | 1,348            | –       | 2,158 | 684                                                          |
| Of which accumulated<br>impairment allowances | 64              | 25         | 97       | 217              | 281     | 684   |                                                              |

|                                               | At 31 December 2009 |                     |                   |                           |                  |                |                                                              |
|-----------------------------------------------|---------------------|---------------------|-------------------|---------------------------|------------------|----------------|--------------------------------------------------------------|
|                                               | Carrying values     |                     |                   |                           |                  |                | Of which<br>accumulated<br>impairment<br>allowances<br>HK\$m |
|                                               | Aaa<br>HK\$m        | Aa1 to Aa3<br>HK\$m | A1 to A3<br>HK\$m | Lower<br>than A3<br>HK\$m | Unrated<br>HK\$m | Total<br>HK\$m |                                                              |
| <b>Investment in securities</b>               |                     |                     |                   |                           |                  |                |                                                              |
| US non-agency residential<br>mortgage-backed  |                     |                     |                   |                           |                  |                |                                                              |
| – Subprime                                    | 467                 | –                   | 12                | –                         | –                | 479            | 55                                                           |
| – Alt-A                                       | –                   | 91                  | 44                | 11                        | –                | 146            | 66                                                           |
| – Prime                                       | 50                  | 188                 | 231               | 839                       | –                | 1,308          | 348                                                          |
| Other MBS/ABS                                 | –                   | 75                  | –                 | –                         | –                | 75             | 38                                                           |
| Other debt securities                         | –                   | –                   | 32                | –                         | –                | 32             | 281                                                          |
| Total                                         | 517                 | 354                 | 319               | 850                       | –                | 2,040          | 788                                                          |
| Of which accumulated<br>impairment allowances | 74                  | 117                 | 130               | 186                       | 281              | 788            |                                                              |

As at 30 June 2010 and 31 December 2009, there were no debt securities overdue for more than 3 months.

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

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

##### MBS/ABS

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

|                                           | At 30 June 2010 |                                  |                                                               |
|-------------------------------------------|-----------------|----------------------------------|---------------------------------------------------------------|
|                                           | Carrying values |                                  | Of which<br>accumulated<br>impairment<br>allowances<br>HK\$'m |
|                                           | Total<br>HK\$'m | Impaired<br>securities<br>HK\$'m |                                                               |
| <b>US MBS/ABS</b>                         |                 |                                  |                                                               |
| Non-agency residential<br>mortgage-backed |                 |                                  |                                                               |
| – Subprime                                | 439             | 406                              | 45                                                            |
| – Alt-A                                   | 318             | 127                              | 57                                                            |
| – Prime                                   | 2,212           | 1,546                            | 292                                                           |
| Ginnie Mae                                | 3,680           | –                                | –                                                             |
| Fannie Mae                                | 28              | –                                | –                                                             |
| Freddie Mac                               | 823             | –                                | –                                                             |
| Others                                    | 1,115           | –                                | –                                                             |
|                                           | <b>8,615</b>    | <b>2,079</b>                     | <b>394</b>                                                    |
| <b>Other countries MBS/ABS</b>            |                 |                                  |                                                               |
| Residential mortgage-backed               | 1,922           | 79                               | 9                                                             |
| Commercial mortgage-backed                | 146             | –                                | –                                                             |
|                                           | <b>2,068</b>    | <b>79</b>                        | <b>9</b>                                                      |
| <b>Total MBS/ABS</b>                      | <b>10,683</b>   | <b>2,158</b>                     | <b>403</b>                                                    |

## 3. Financial risk management (continued)

## 3.1 Credit Risk (continued)

## C. Debt securities (continued)

MBS/ABS (continued)

|                                        | At 31 December 2009 |                      |                                                               |
|----------------------------------------|---------------------|----------------------|---------------------------------------------------------------|
|                                        | Carrying values     |                      | Of which<br>accumulated<br>impairment<br>allowances<br>HK\$'m |
|                                        | Total               | Impaired             |                                                               |
|                                        | HK\$'m              | securities<br>HK\$'m |                                                               |
| <b>US MBS/ABS</b>                      |                     |                      |                                                               |
| Non-agency residential mortgage-backed |                     |                      |                                                               |
| – Subprime                             | 547                 | 479                  | 55                                                            |
| – Alt-A                                | 384                 | 146                  | 66                                                            |
| – Prime                                | 2,853               | 1,308                | 348                                                           |
| Ginnie Mae                             | 2,695               | –                    | –                                                             |
| Fannie Mae                             | 51                  | –                    | –                                                             |
| Freddie Mac                            | 1,164               | –                    | –                                                             |
| Others                                 | 1,534               | –                    | –                                                             |
|                                        | 9,228               | 1,933                | 469                                                           |
| <b>Other countries MBS/ABS</b>         |                     |                      |                                                               |
| Residential mortgage-backed            | 2,253               | 75                   | 38                                                            |
| Commercial mortgage-backed             | 160                 | –                    | –                                                             |
|                                        | 2,413               | 75                   | 38                                                            |
| <b>Total MBS/ABS</b>                   | <b>11,641</b>       | <b>2,008</b>         | <b>507</b>                                                    |

|                                                                                                                                                                                            | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------|----------------------------------|
| Increase in fair value taken to available-for-sale securities reserve on MBS/ABS for the period/ year (net of impairment releases taken to income statement excluding deferred tax impact) | <b>182</b>                            | 1,617                            |
| Closing balance of available-for-sale securities reserve relating to MBS/ABS (excluding deferred tax impact)                                                                               | <b>92</b>                             | (90)                             |

### 3. Financial risk management (continued)

#### 3.1 Credit Risk (continued)

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

MBS/ABS (continued)

The table below represents an analysis of impairment charges/(releases) for the period/year for MBS/ABS held as at 30 June 2010 and 31 December 2009.

|                                        | At 30 June 2010 |                         |                       |                            |                   |                 |
|----------------------------------------|-----------------|-------------------------|-----------------------|----------------------------|-------------------|-----------------|
|                                        | Aaa<br>HK\$'m   | Aa1 to<br>Aa3<br>HK\$'m | A1 to<br>A3<br>HK\$'m | Lower<br>than A3<br>HK\$'m | Unrated<br>HK\$'m | Total<br>HK\$'m |
| <b>US MBS/ABS</b>                      |                 |                         |                       |                            |                   |                 |
| Non-agency residential mortgage-backed |                 |                         |                       |                            |                   |                 |
| – Subprime                             | (8)             | (1)                     | –                     | –                          | –                 | (9)             |
| – Alt-A                                | –               | (1)                     | (2)                   | (2)                        | –                 | (5)             |
| – Prime                                | (2)             | –                       | (6)                   | 27                         | –                 | 19              |
|                                        | (10)            | (2)                     | (8)                   | 25                         | –                 | 5               |
| <b>Other countries MBS/ABS</b>         |                 |                         |                       |                            |                   |                 |
| Residential mortgage-backed            | –               | (27)                    | –                     | –                          | –                 | (27)            |
| Total MBS/ABS                          | (10)            | (29)                    | (8)                   | 25                         | –                 | (22)            |

|                                        | At 31 December 2009 |                         |                       |                            |                   |                 |
|----------------------------------------|---------------------|-------------------------|-----------------------|----------------------------|-------------------|-----------------|
|                                        | Aaa<br>HK\$'m       | Aa1 to<br>Aa3<br>HK\$'m | A1 to<br>A3<br>HK\$'m | Lower<br>than A3<br>HK\$'m | Unrated<br>HK\$'m | Total<br>HK\$'m |
| <b>US MBS/ABS</b>                      |                     |                         |                       |                            |                   |                 |
| Non-agency residential mortgage-backed |                     |                         |                       |                            |                   |                 |
| – Subprime                             | (15)                | –                       | (3)                   | –                          | –                 | (18)            |
| – Alt-A                                | –                   | 10                      | 20                    | (3)                        | –                 | 27              |
| – Prime                                | 22                  | 15                      | (2)                   | 139                        | –                 | 174             |
|                                        | 7                   | 25                      | 15                    | 136                        | –                 | 183             |
| <b>Other countries MBS/ABS</b>         |                     |                         |                       |                            |                   |                 |
| Residential mortgage-backed            | –                   | 8                       | –                     | –                          | –                 | 8               |
| Total MBS/ABS                          | 7                   | 33                      | 15                    | 136                        | –                 | 191             |

Note: The impairment charges/(releases) for MBS/ABS disposed during the period/year are excluded.

### 3. Financial risk management (continued)

#### 3.2 Market Risk

##### A. VAR

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

The Group uses a historical simulation approach, a 99% confidence level and a one day holding period to calculate portfolio and individual risk-product VAR. Historical movements in market prices are calculated by reference to market data from the last two years.

The following table sets out the VAR for all trading market risk exposure<sup>1</sup> of BOCHK.

| HK\$'m                                    |            | Minimum for<br>the first half<br>of year | Maximum for<br>the first half<br>of year | Average for<br>the first half<br>of year |
|-------------------------------------------|------------|------------------------------------------|------------------------------------------|------------------------------------------|
|                                           | At 30 June |                                          |                                          |                                          |
| VAR for all market risk                   | – 2010     | 7.4                                      | 6.9                                      | 15.7                                     |
|                                           | – 2009     | 11.6                                     | 9.0                                      | 16.3                                     |
| VAR for foreign exchange<br>risk products | – 2010     | 5.6                                      | 2.3                                      | 11.2                                     |
|                                           | – 2009     | 12.3                                     | 9.2                                      | 15.8                                     |
| VAR for interest rate risk<br>products    | – 2010     | 6.0                                      | 5.1                                      | 13.6                                     |
|                                           | – 2009     | 4.2                                      | 2.1                                      | 5.4                                      |
| VAR for equity risk products              | – 2010     | 0.0                                      | 0.0                                      | 1.7                                      |
|                                           | – 2009     | 0.1                                      | 0.1                                      | 2.5                                      |
| VAR for commodity risk<br>products        | – 2010     | 0.0                                      | 0.0                                      | 0.2                                      |
|                                           | – 2009     | 0.0                                      | 0.0                                      | 0.0                                      |

In the first half of 2010, the average daily revenue<sup>2</sup> of BOCHK earned from market risk-related trading activities was HK\$4.5 million (first half of 2009: HK\$3.9 million).

The Group uses backtesting to monitor the predictive power of the VAR measure. Backtesting compares the calculated VAR figure of those trading positions of each business day with the actual revenues arising on those positions on the next business day. These actual revenues exclude non-trading income, such as fee and commission. If backtesting revenues are negative and exceeding the VAR, a “backtesting exception” is noted. The Group will assess the magnitude of the backtesting exceptions, and revise its VAR model (including the parameters and assumptions) accordingly. Backtesting results are reported to the Group’s senior management, including CE and CRO.

<sup>1</sup> Structural FX positions have been excluded.

<sup>2</sup> Revenues from structural FX positions and back to back transactions have been excluded.

### 3. Financial risk management (continued)

#### 3.2 Market Risk (continued)

##### B. Currency risk

The tables below summarise the Group's exposure to foreign currency exchange rate risk as at 30 June 2010 and 31 December 2009. Included in the tables are the assets and liabilities at carrying amounts in HK\$ equivalent, categorised by the original currency.

|                                                                                               | At 30 June 2010    |                      |                      |                |                           |                             |                  |                  |
|-----------------------------------------------------------------------------------------------|--------------------|----------------------|----------------------|----------------|---------------------------|-----------------------------|------------------|------------------|
|                                                                                               | Renminbi<br>HK\$'m | US Dollars<br>HK\$'m | HK Dollars<br>HK\$'m | Euro<br>HK\$'m | Japanese<br>Yen<br>HK\$'m | Pound<br>Sterling<br>HK\$'m | Others<br>HK\$'m | Total<br>HK\$'m  |
| <b>Assets</b>                                                                                 |                    |                      |                      |                |                           |                             |                  |                  |
| Cash and balances with banks and other financial institutions                                 | 95,506             | 33,067               | 33,643               | 1,663          | 301                       | 356                         | 5,018            | 169,554          |
| Placements with banks and other financial institutions maturing between one and twelve months | 3,697              | 19,237               | 11,868               | 8              | -                         | 647                         | 501              | 35,958           |
| Financial assets at fair value through profit or loss                                         | 573                | 14,956               | 54,693               | 89             | -                         | -                           | 61               | 70,372           |
| Derivative financial instruments                                                              | 69                 | 2,827                | 16,205               | 20             | -                         | -                           | 19               | 19,140           |
| Hong Kong SAR Government certificates of indebtedness                                         | -                  | -                    | 41,950               | -              | -                         | -                           | -                | 41,950           |
| Advances and other accounts                                                                   | 21,406             | 158,163              | 404,262              | 4,616          | 1,274                     | 45                          | 7,540            | 597,306          |
| Investment in securities                                                                      |                    |                      |                      |                |                           |                             |                  |                  |
| – Available-for-sale securities                                                               | 2,616              | 138,678              | 31,507               | 21,808         | 1,689                     | 1,790                       | 39,836           | 237,924          |
| – Held-to-maturity securities                                                                 | 1,779              | 27,505               | 22,152               | 2,796          | 1,864                     | 36                          | 7,486            | 63,618           |
| – Loans and receivables                                                                       | -                  | 8,837                | 2,858                | -              | -                         | -                           | -                | 11,695           |
| Interests in associates                                                                       | -                  | -                    | 213                  | -              | -                         | -                           | -                | 213              |
| Investment properties                                                                         | 58                 | -                    | 9,265                | -              | -                         | -                           | -                | 9,323            |
| Properties, plant and equipment                                                               | 350                | -                    | 27,885               | -              | -                         | -                           | -                | 28,235           |
| Other assets (including deferred tax assets)                                                  | 337                | 860                  | 14,967               | 254            | 335                       | 64                          | 71               | 16,888           |
| <b>Total assets</b>                                                                           | <b>126,391</b>     | <b>404,130</b>       | <b>671,468</b>       | <b>31,254</b>  | <b>5,463</b>              | <b>2,938</b>                | <b>60,532</b>    | <b>1,302,176</b> |
| <b>Liabilities</b>                                                                            |                    |                      |                      |                |                           |                             |                  |                  |
| Hong Kong SAR currency notes in circulation                                                   | -                  | -                    | 41,950               | -              | -                         | -                           | -                | 41,950           |
| Deposits and balances of banks and other financial institutions                               | 59,638             | 30,029               | 16,582               | 397            | 438                       | 375                         | 3,327            | 110,786          |
| Financial liabilities at fair value through profit or loss                                    | -                  | 177                  | 26,443               | -              | -                         | -                           | 256              | 26,876           |
| Derivative financial instruments                                                              | 73                 | 3,325                | 11,492               | 758            | 2                         | -                           | 121              | 15,771           |
| Deposits from customers                                                                       | 57,117             | 181,970              | 570,464              | 14,588         | 1,763                     | 15,667                      | 50,642           | 892,211          |
| Other accounts and provisions (including current and deferred tax liabilities)                | 3,782              | 10,714               | 25,530               | 662            | 49                        | 510                         | 1,556            | 42,803           |
| Insurance contract liabilities                                                                | 185                | 6,408                | 28,457               | -              | -                         | -                           | -                | 35,050           |
| Subordinated liabilities                                                                      | -                  | 20,915               | -                    | 6,277          | -                         | -                           | -                | 27,192           |
| <b>Total liabilities</b>                                                                      | <b>120,795</b>     | <b>253,538</b>       | <b>720,918</b>       | <b>22,682</b>  | <b>2,252</b>              | <b>16,552</b>               | <b>55,902</b>    | <b>1,192,639</b> |
| Net on-balance sheet position                                                                 | 5,596              | 150,592              | (49,450)             | 8,572          | 3,211                     | (13,614)                    | 4,630            | 109,537          |
| Off-balance sheet net notional position*                                                      | 544                | (142,101)            | 148,944              | (8,735)        | (3,169)                   | 13,698                      | (4,560)          | 4,621            |
| Contingent liabilities and commitments                                                        | 9,167              | 90,268               | 209,478              | 4,363          | 430                       | 927                         | 3,273            | 317,906          |

## 3. Financial risk management (continued)

## 3.2 Market Risk (continued)

## B. Currency risk (continued)

|                                                                                               | At 31 December 2009 |                      |                      |                |                           |                             |                  |                  |
|-----------------------------------------------------------------------------------------------|---------------------|----------------------|----------------------|----------------|---------------------------|-----------------------------|------------------|------------------|
|                                                                                               | Renminbi<br>HK\$'m  | US Dollars<br>HK\$'m | HK Dollars<br>HK\$'m | Euro<br>HK\$'m | Japanese<br>Yen<br>HK\$'m | Pound<br>Sterling<br>HK\$'m | Others<br>HK\$'m | Total<br>HK\$'m  |
| <b>Assets</b>                                                                                 |                     |                      |                      |                |                           |                             |                  |                  |
| Cash and balances with banks and other financial institutions                                 | 59,001              | 45,058               | 51,024               | 2,066          | 317                       | 623                         | 2,699            | 160,788          |
| Placements with banks and other financial institutions maturing between one and twelve months | 1,782               | 34,514               | 19,365               | 3,083          | 43                        | 125                         | 1,370            | 60,282           |
| Financial assets at fair value through profit or loss                                         | 700                 | 10,884               | 32,948               | –              | –                         | –                           | 62               | 44,594           |
| Derivative financial instruments                                                              | 5                   | 1,201                | 16,238               | 48             | –                         | –                           | 92               | 17,584           |
| Hong Kong SAR Government certificates of indebtedness                                         | –                   | –                    | 38,310               | –              | –                         | –                           | –                | 38,310           |
| Advances and other accounts                                                                   | 15,810              | 112,386              | 386,259              | 3,352          | 1,170                     | 46                          | 8,112            | 527,135          |
| Investment in securities                                                                      |                     |                      |                      |                |                           |                             |                  |                  |
| – Available-for-sale securities                                                               | 2,414               | 115,645              | 36,176               | 24,365         | 13,261                    | 1,882                       | 34,870           | 228,613          |
| – Held-to-maturity securities                                                                 | 1,761               | 26,623               | 25,291               | 6,749          | 2,725                     | 362                         | 8,928            | 72,439           |
| – Loans and receivables                                                                       | –                   | 5,873                | 6,661                | –              | –                         | –                           | 169              | 12,703           |
| Interests in associates                                                                       | –                   | –                    | 217                  | –              | –                         | –                           | –                | 217              |
| Investment properties                                                                         | 59                  | –                    | 9,305                | –              | –                         | –                           | –                | 9,364            |
| Properties, plant and equipment                                                               | 350                 | –                    | 25,936               | –              | –                         | –                           | –                | 26,286           |
| Other assets (including deferred tax assets)                                                  | 125                 | 614                  | 13,497               | 11             | 110                       | 54                          | 65               | 14,476           |
| <b>Total assets</b>                                                                           | <b>82,007</b>       | <b>352,798</b>       | <b>661,227</b>       | <b>39,674</b>  | <b>17,626</b>             | <b>3,092</b>                | <b>56,367</b>    | <b>1,212,791</b> |
| <b>Liabilities</b>                                                                            |                     |                      |                      |                |                           |                             |                  |                  |
| Hong Kong SAR currency notes in circulation                                                   | –                   | –                    | 38,310               | –              | –                         | –                           | –                | 38,310           |
| Deposits and balances of banks and other financial institutions                               | 38,104              | 24,930               | 35,539               | 18             | 28                        | 13                          | 1,015            | 99,647           |
| Financial liabilities at fair value through profit or loss                                    | –                   | 599                  | 15,229               | –              | –                         | –                           | 460              | 16,288           |
| Derivative financial instruments                                                              | 7                   | 2,056                | 10,921               | 869            | 3                         | –                           | 111              | 13,967           |
| Deposits from customers                                                                       | 38,714              | 158,094              | 564,319              | 15,517         | 2,199                     | 14,645                      | 48,833           | 842,321          |
| Other accounts and provisions (including current and deferred tax liabilities)                | 1,194               | 8,304                | 24,229               | 617            | 56                        | 528                         | 1,511            | 36,439           |
| Insurance contract liabilities                                                                | 1                   | 6,202                | 27,205               | –              | –                         | –                           | –                | 33,408           |
| Subordinated liabilities                                                                      | –                   | 19,399               | –                    | 7,377          | –                         | –                           | –                | 26,776           |
| <b>Total liabilities</b>                                                                      | <b>78,020</b>       | <b>219,584</b>       | <b>715,752</b>       | <b>24,398</b>  | <b>2,286</b>              | <b>15,186</b>               | <b>51,930</b>    | <b>1,107,156</b> |
| Net on-balance sheet position                                                                 | 3,987               | 133,214              | (54,525)             | 15,276         | 15,340                    | (12,094)                    | 4,437            | 105,635          |
| Off-balance sheet net notional position*                                                      | 462                 | (120,753)            | 149,934              | (15,284)       | (15,284)                  | 11,849                      | (4,728)          | 6,196            |
| Contingent liabilities and commitments                                                        | 5,940               | 61,833               | 197,945              | 4,341          | 569                       | 835                         | 4,961            | 276,424          |

\* Off-balance sheet net notional position represents the net notional amounts of foreign currency derivative financial instruments, which are principally used to reduce the Group's exposure to currency movements.

### 3. Financial risk management (continued)

#### 3.2 Market Risk (continued)

##### C. Interest rate risk

The tables below summarise the Group's exposure to interest rate risk as at 30 June 2010 and 31 December 2009. Included in the tables are the assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

|                                                                                               | At 30 June 2010            |                         |                          |                        |                           |                                   |                  |
|-----------------------------------------------------------------------------------------------|----------------------------|-------------------------|--------------------------|------------------------|---------------------------|-----------------------------------|------------------|
|                                                                                               | Up to 1<br>month<br>HK\$'m | 1-3<br>months<br>HK\$'m | 3-12<br>months<br>HK\$'m | 1-5<br>years<br>HK\$'m | Over 5<br>years<br>HK\$'m | Non-interest<br>bearing<br>HK\$'m | Total<br>HK\$'m  |
| <b>Assets</b>                                                                                 |                            |                         |                          |                        |                           |                                   |                  |
| Cash and balances with banks and other financial institutions                                 | 159,565                    | -                       | -                        | -                      | -                         | 9,989                             | 169,554          |
| Placements with banks and other financial institutions maturing between one and twelve months | -                          | 18,653                  | 17,305                   | -                      | -                         | -                                 | 35,958           |
| Financial assets at fair value through profit or loss                                         | 12,490                     | 21,349                  | 4,272                    | 12,573                 | 14,406                    | 5,282                             | 70,372           |
| Derivative financial instruments                                                              | -                          | -                       | -                        | -                      | -                         | 19,140                            | 19,140           |
| Hong Kong SAR Government certificates of indebtedness                                         | -                          | -                       | -                        | -                      | -                         | 41,950                            | 41,950           |
| Advances and other accounts                                                                   | 466,575                    | 90,265                  | 35,376                   | 1,164                  | 122                       | 3,804                             | 597,306          |
| Investment in securities                                                                      |                            |                         |                          |                        |                           |                                   |                  |
| – Available-for-sale securities                                                               | 24,283                     | 31,702                  | 25,435                   | 124,919                | 28,537                    | 3,048                             | 237,924          |
| – Held-to-maturity securities                                                                 | 11,351                     | 19,887                  | 8,697                    | 15,669                 | 8,014                     | -                                 | 63,618           |
| – Loans and receivables                                                                       | 1,190                      | 1,077                   | 9,428                    | -                      | -                         | -                                 | 11,695           |
| Interests in associates                                                                       | -                          | -                       | -                        | -                      | -                         | 213                               | 213              |
| Investment properties                                                                         | -                          | -                       | -                        | -                      | -                         | 9,323                             | 9,323            |
| Properties, plant and equipment                                                               | -                          | -                       | -                        | -                      | -                         | 28,235                            | 28,235           |
| Other assets (including deferred tax assets)                                                  | -                          | -                       | -                        | -                      | -                         | 16,888                            | 16,888           |
| <b>Total assets</b>                                                                           | <b>675,454</b>             | <b>182,933</b>          | <b>100,513</b>           | <b>154,325</b>         | <b>51,079</b>             | <b>137,872</b>                    | <b>1,302,176</b> |
| <b>Liabilities</b>                                                                            |                            |                         |                          |                        |                           |                                   |                  |
| Hong Kong SAR currency notes in circulation                                                   | -                          | -                       | -                        | -                      | -                         | 41,950                            | 41,950           |
| Deposits and balances of banks and other financial institutions                               | 93,137                     | 3,958                   | 1,975                    | -                      | -                         | 11,716                            | 110,786          |
| Financial liabilities at fair value through profit or loss                                    | 8,168                      | 15,375                  | 3,212                    | 121                    | -                         | -                                 | 26,876           |
| Derivative financial instruments                                                              | -                          | -                       | -                        | -                      | -                         | 15,771                            | 15,771           |
| Deposits from customers                                                                       | 693,177                    | 88,169                  | 60,026                   | 1,262                  | -                         | 49,577                            | 892,211          |
| Other accounts and provisions (including current and deferred tax liabilities)                | 10,393                     | 575                     | 2,288                    | 303                    | -                         | 29,244                            | 42,803           |
| Insurance contract liabilities                                                                | -                          | -                       | -                        | -                      | -                         | 35,050                            | 35,050           |
| Subordinated liabilities                                                                      | -                          | -                       | 6,277                    | -                      | 20,915                    | -                                 | 27,192           |
| <b>Total liabilities</b>                                                                      | <b>804,875</b>             | <b>108,077</b>          | <b>73,778</b>            | <b>1,686</b>           | <b>20,915</b>             | <b>183,308</b>                    | <b>1,192,639</b> |
| Interest sensitivity gap                                                                      | (129,421)                  | 74,856                  | 26,735                   | 152,639                | 30,164                    | (45,436)                          | 109,537          |

## 3. Financial risk management (continued)

## 3.2 Market Risk (continued)

## C. Interest rate risk (continued)

|                                                                                               | At 31 December 2009        |                         |                          |                        |                           |                                   |                 |
|-----------------------------------------------------------------------------------------------|----------------------------|-------------------------|--------------------------|------------------------|---------------------------|-----------------------------------|-----------------|
|                                                                                               | Up to 1<br>month<br>HK\$'m | 1-3<br>months<br>HK\$'m | 3-12<br>months<br>HK\$'m | 1-5<br>years<br>HK\$'m | Over 5<br>years<br>HK\$'m | Non-interest<br>bearing<br>HK\$'m | Total<br>HK\$'m |
| <b>Assets</b>                                                                                 |                            |                         |                          |                        |                           |                                   |                 |
| Cash and balances with banks and other financial institutions                                 | 132,002                    | –                       | –                        | –                      | –                         | 28,786                            | 160,788         |
| Placements with banks and other financial institutions maturing between one and twelve months | –                          | 26,170                  | 34,112                   | –                      | –                         | –                                 | 60,282          |
| Financial assets at fair value through profit or loss                                         | 10,862                     | 2,567                   | 2,223                    | 11,269                 | 13,407                    | 4,266                             | 44,594          |
| Derivative financial instruments                                                              | –                          | –                       | –                        | –                      | –                         | 17,584                            | 17,584          |
| Hong Kong SAR Government certificates of indebtedness                                         | –                          | –                       | –                        | –                      | –                         | 38,310                            | 38,310          |
| Advances and other accounts                                                                   | 437,386                    | 66,229                  | 17,878                   | 1,491                  | 164                       | 3,987                             | 527,135         |
| Investment in securities                                                                      |                            |                         |                          |                        |                           |                                   |                 |
| – Available-for-sale securities                                                               | 24,086                     | 42,303                  | 15,488                   | 119,124                | 24,355                    | 3,257                             | 228,613         |
| – Held-to-maturity securities                                                                 | 16,968                     | 28,856                  | 11,241                   | 10,920                 | 4,454                     | –                                 | 72,439          |
| – Loans and receivables                                                                       | 169                        | 1,774                   | 10,760                   | –                      | –                         | –                                 | 12,703          |
| Interests in associates                                                                       | –                          | –                       | –                        | –                      | –                         | 217                               | 217             |
| Investment properties                                                                         | –                          | –                       | –                        | –                      | –                         | 9,364                             | 9,364           |
| Properties, plant and equipment                                                               | –                          | –                       | –                        | –                      | –                         | 26,286                            | 26,286          |
| Other assets (including deferred tax assets)                                                  | –                          | –                       | –                        | –                      | –                         | 14,476                            | 14,476          |
| <b>Total assets</b>                                                                           | 621,473                    | 167,899                 | 91,702                   | 142,804                | 42,380                    | 146,533                           | 1,212,791       |
| <b>Liabilities</b>                                                                            |                            |                         |                          |                        |                           |                                   |                 |
| Hong Kong SAR currency notes in circulation                                                   | –                          | –                       | –                        | –                      | –                         | 38,310                            | 38,310          |
| Deposits and balances of banks and other financial institutions                               | 78,388                     | 1,751                   | 3,475                    | –                      | –                         | 16,033                            | 99,647          |
| Financial liabilities at fair value through profit or loss                                    | 13,375                     | 1,974                   | 846                      | 93                     | –                         | –                                 | 16,288          |
| Derivative financial instruments                                                              | –                          | –                       | –                        | –                      | –                         | 13,967                            | 13,967          |
| Deposits from customers                                                                       | 681,049                    | 76,187                  | 36,107                   | 1,073                  | –                         | 47,905                            | 842,321         |
| Other accounts and provisions (including current and deferred tax liabilities)                | 9,685                      | 265                     | 274                      | 305                    | –                         | 25,910                            | 36,439          |
| Insurance contract liabilities                                                                | –                          | –                       | –                        | –                      | –                         | 33,408                            | 33,408          |
| Subordinated liabilities                                                                      | –                          | –                       | 26,776                   | –                      | –                         | –                                 | 26,776          |
| <b>Total liabilities</b>                                                                      | 782,497                    | 80,177                  | 67,478                   | 1,471                  | –                         | 175,533                           | 1,107,156       |
| Interest sensitivity gap                                                                      | (161,024)                  | 87,722                  | 24,224                   | 141,333                | 42,380                    | (29,000)                          | 105,635         |

### 3. Financial risk management (continued)

#### 3.3 Liquidity Risk

##### A. Liquidity ratio

|                         | Half-year ended<br>30 June 2010 | Half-year ended<br>30 June 2009 |
|-------------------------|---------------------------------|---------------------------------|
| Average liquidity ratio | 37.81%                          | 39.70%                          |

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

The liquidity ratio is computed on the solo basis (the Hong Kong offices only) and is in accordance with the Fourth Schedule to the Banking Ordinance.

### 3. Financial risk management (continued)

#### 3.3 Liquidity Risk (continued)

##### B. Maturity analysis

Tables below analyse assets and liabilities of the Group as at 30 June 2010 and 31 December 2009 into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

|                                                                                               | At 30 June 2010     |                         |                      |                       |                     |                        |                      |                  |
|-----------------------------------------------------------------------------------------------|---------------------|-------------------------|----------------------|-----------------------|---------------------|------------------------|----------------------|------------------|
|                                                                                               | On demand<br>HK\$'m | Up to 1 month<br>HK\$'m | 1-3 Months<br>HK\$'m | 3-12 Months<br>HK\$'m | 1-5 years<br>HK\$'m | Over 5 Years<br>HK\$'m | Indefinite<br>HK\$'m | Total<br>HK\$'m  |
| <b>Assets</b>                                                                                 |                     |                         |                      |                       |                     |                        |                      |                  |
| Cash and balances with banks and other financial institutions                                 | 97,748              | 71,806                  | -                    | -                     | -                   | -                      | -                    | 169,554          |
| Placements with banks and other financial institutions maturing between one and twelve months | -                   | -                       | 18,653               | 17,305                | -                   | -                      | -                    | 35,958           |
| Financial assets at fair value through profit or loss                                         |                     |                         |                      |                       |                     |                        |                      |                  |
| – debt securities held for trading                                                            | -                   | -                       | -                    | 782                   | 200                 | -                      | -                    | 982              |
| – certificates of deposit held                                                                | -                   | 12,289                  | 20,228               | 3,407                 | 2,195               | 4,937                  | -                    | 43,056           |
| – debt securities designated at fair value through profit or loss                             |                     |                         |                      |                       |                     |                        |                      |                  |
| – certificates of deposit held                                                                | -                   | -                       | -                    | 155                   | 1,769               | 730                    | -                    | 2,654            |
| – others                                                                                      | -                   | -                       | 58                   | 630                   | 8,949               | 8,761                  | -                    | 18,398           |
| – fund and equity securities                                                                  | -                   | -                       | -                    | -                     | -                   | -                      | 5,282                | 5,282            |
| Derivative financial instruments                                                              | 14,013              | 541                     | 591                  | 1,119                 | 1,219               | 1,657                  | -                    | 19,140           |
| Hong Kong SAR Government certificates of indebtedness                                         | 41,950              | -                       | -                    | -                     | -                   | -                      | -                    | 41,950           |
| Advances and other accounts                                                                   |                     |                         |                      |                       |                     |                        |                      |                  |
| – advances to customers                                                                       | 34,925              | 14,177                  | 32,302               | 106,516               | 225,339             | 155,054                | 884                  | 569,197          |
| – trade bills                                                                                 | 1                   | 8,487                   | 8,348                | 7,821                 | 6                   | -                      | -                    | 24,663           |
| – advances to banks and other financial institutions                                          | 15                  | 213                     | 167                  | 1,425                 | 1,626               | -                      | -                    | 3,446            |
| Investment in securities                                                                      |                     |                         |                      |                       |                     |                        |                      |                  |
| – debt securities held for available-for-sale                                                 |                     |                         |                      |                       |                     |                        |                      |                  |
| – certificates of deposit held                                                                | -                   | 1,189                   | 1,655                | 3,122                 | 11,658              | -                      | -                    | 17,624           |
| – others                                                                                      | -                   | 7,795                   | 4,960                | 27,782                | 141,319             | 33,746                 | 1,650                | 217,252          |
| – debt securities held for held-to-maturity                                                   |                     |                         |                      |                       |                     |                        |                      |                  |
| – certificates of deposit held                                                                | -                   | 58                      | -                    | 1,798                 | 2,838               | 377                    | -                    | 5,071            |
| – others                                                                                      | -                   | 1,260                   | 4,116                | 15,431                | 27,309              | 9,923                  | 508                  | 58,547           |
| – debt securities held for loans and receivables                                              | -                   | 1,190                   | 1,077                | 9,428                 | -                   | -                      | -                    | 11,695           |
| – equity securities                                                                           | -                   | -                       | -                    | -                     | -                   | -                      | 3,048                | 3,048            |
| Interests in associates                                                                       | -                   | -                       | -                    | -                     | -                   | -                      | 213                  | 213              |
| Investment properties                                                                         | -                   | -                       | -                    | -                     | -                   | -                      | 9,323                | 9,323            |
| Properties, plant and equipment                                                               | -                   | -                       | -                    | -                     | -                   | -                      | 28,235               | 28,235           |
| Other assets (including deferred tax assets)                                                  | 3,650               | 12,672                  | 30                   | 219                   | 151                 | -                      | 166                  | 16,888           |
| <b>Total assets</b>                                                                           | <b>192,302</b>      | <b>131,677</b>          | <b>92,185</b>        | <b>196,940</b>        | <b>424,578</b>      | <b>215,185</b>         | <b>49,309</b>        | <b>1,302,176</b> |

### 3. Financial risk management (continued)

#### 3.3 Liquidity Risk (continued)

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

|                                                                                | At 30 June 2010 |                |                |               |               |               |            |                  |
|--------------------------------------------------------------------------------|-----------------|----------------|----------------|---------------|---------------|---------------|------------|------------------|
|                                                                                | On demand       | Up to 1 month  | 1-3 months     | 3-12 months   | 1-5 years     | Over 5 years  | Indefinite | Total            |
|                                                                                | HK\$'m          | HK\$'m         | HK\$'m         | HK\$'m        | HK\$'m        | HK\$'m        | HK\$'m     | HK\$'m           |
| <b>Liabilities</b>                                                             |                 |                |                |               |               |               |            |                  |
| Hong Kong SAR currency notes in circulation                                    | 41,950          | -              | -              | -             | -             | -             | -          | 41,950           |
| Deposits and balances of banks and other financial institutions                | 85,049          | 19,804         | 3,958          | 1,975         | -             | -             | -          | 110,786          |
| Financial liabilities at fair value through profit or loss                     |                 |                |                |               |               |               |            |                  |
| – certificates of deposit issued                                               | -               | -              | -              | -             | -             | -             | -          | -                |
| – others                                                                       | -               | 8,168          | 15,375         | 3,212         | 121           | -             | -          | 26,876           |
| Derivative financial instruments                                               | 9,299           | 417            | 360            | 1,368         | 3,117         | 1,210         | -          | 15,771           |
| Deposits from customers                                                        | 542,176         | 200,574        | 88,169         | 59,684        | 1,608         | -             | -          | 892,211          |
| Other accounts and provisions (including current and deferred tax liabilities) | 19,640          | 11,264         | 746            | 5,913         | 5,240         | -             | -          | 42,803           |
| Insurance contract liabilities                                                 | 1,511           | 177            | 3              | 3,121         | 22,508        | 7,730         | -          | 35,050           |
| Subordinated liabilities                                                       | -               | -              | 347            | 1             | -             | 26,844        | -          | 27,192           |
| <b>Total liabilities</b>                                                       | <b>699,625</b>  | <b>240,404</b> | <b>108,958</b> | <b>75,274</b> | <b>32,594</b> | <b>35,784</b> | <b>-</b>   | <b>1,192,639</b> |
| Net liquidity gap                                                              | (507,323)       | (108,727)      | (16,773)       | 121,666       | 391,984       | 179,401       | 49,309     | 109,537          |

## 3. Financial risk management (continued)

## 3.3 Liquidity Risk (continued)

## B. Maturity analysis (continued)

|                                                                                               | At 31 December 2009 |                         |                      |                       |                     |                        |                      |                  |
|-----------------------------------------------------------------------------------------------|---------------------|-------------------------|----------------------|-----------------------|---------------------|------------------------|----------------------|------------------|
|                                                                                               | On demand<br>HK\$'m | Up to 1 month<br>HK\$'m | 1-3 months<br>HK\$'m | 3-12 months<br>HK\$'m | 1-5 years<br>HK\$'m | Over 5 years<br>HK\$'m | Indefinite<br>HK\$'m | Total<br>HK\$'m  |
| <b>Assets</b>                                                                                 |                     |                         |                      |                       |                     |                        |                      |                  |
| Cash and balances with banks and other financial institutions                                 | 91,290              | 69,498                  | –                    | –                     | –                   | –                      | –                    | 160,788          |
| Placements with banks and other financial institutions maturing between one and twelve months | –                   | –                       | 26,170               | 34,112                | –                   | –                      | –                    | 60,282           |
| Financial assets at fair value through profit or loss                                         |                     |                         |                      |                       |                     |                        |                      |                  |
| – debt securities held for trading                                                            | –                   | –                       | –                    | –                     | –                   | –                      | –                    | –                |
| – certificates of deposit held                                                                | –                   | 10,793                  | 2,051                | 2,018                 | 1,266               | 2,467                  | –                    | 18,595           |
| – debt securities designated at fair value through profit or loss                             |                     |                         |                      |                       |                     |                        |                      |                  |
| – certificates of deposit held                                                                | –                   | –                       | –                    | 53                    | 1,845               | 687                    | –                    | 2,585            |
| – others                                                                                      | –                   | 69                      | 80                   | 228                   | 8,493               | 10,278                 | –                    | 19,148           |
| – fund and equity securities                                                                  | –                   | –                       | –                    | –                     | –                   | –                      | 4,266                | 4,266            |
| Derivative financial instruments                                                              | 13,825              | 606                     | 1,082                | 845                   | 995                 | 231                    | –                    | 17,584           |
| Hong Kong SAR Government certificates of indebtedness                                         | 38,310              | –                       | –                    | –                     | –                   | –                      | –                    | 38,310           |
| Advances and other accounts                                                                   |                     |                         |                      |                       |                     |                        |                      |                  |
| – advances to customers                                                                       | 28,490              | 10,667                  | 31,118               | 76,503                | 216,468             | 148,265                | 1,192                | 512,703          |
| – trade bills                                                                                 | –                   | 3,820                   | 5,130                | 150                   | –                   | –                      | –                    | 9,100            |
| – advances to banks and other financial institutions                                          | 10                  | –                       | –                    | 3,044                 | 2,278               | –                      | –                    | 5,332            |
| Investment in securities                                                                      |                     |                         |                      |                       |                     |                        |                      |                  |
| – debt securities held for available-for-sale                                                 |                     |                         |                      |                       |                     |                        |                      |                  |
| – certificates of deposit held                                                                | –                   | 3,250                   | 1,247                | 4,588                 | 10,023              | –                      | –                    | 19,108           |
| – others                                                                                      | –                   | 7,625                   | 15,721               | 16,775                | 134,620             | 30,152                 | 1,355                | 206,248          |
| – debt securities held for held-to-maturity                                                   |                     |                         |                      |                       |                     |                        |                      |                  |
| – certificates of deposit held                                                                | –                   | 1,679                   | 922                  | 2,695                 | 3,924               | 613                    | –                    | 9,833            |
| – others                                                                                      | –                   | 2,433                   | 2,942                | 23,351                | 26,331              | 6,864                  | 685                  | 62,606           |
| – debt securities held for loans and receivables                                              | –                   | 169                     | 1,774                | 10,760                | –                   | –                      | –                    | 12,703           |
| – equity securities                                                                           | –                   | –                       | –                    | –                     | –                   | –                      | 3,257                | 3,257            |
| Interests in associates                                                                       | –                   | –                       | –                    | –                     | –                   | –                      | 217                  | 217              |
| Investment properties                                                                         | –                   | –                       | –                    | –                     | –                   | –                      | 9,364                | 9,364            |
| Properties, plant and equipment                                                               | –                   | –                       | –                    | –                     | –                   | –                      | 26,286               | 26,286           |
| Other assets (including deferred tax assets)                                                  | 2,917               | 11,187                  | 4                    | 75                    | 162                 | –                      | 131                  | 14,476           |
| <b>Total assets</b>                                                                           | <b>174,842</b>      | <b>121,796</b>          | <b>88,241</b>        | <b>175,197</b>        | <b>406,405</b>      | <b>199,557</b>         | <b>46,753</b>        | <b>1,212,791</b> |

### 3. Financial risk management (continued)

#### 3.3 Liquidity Risk (continued)

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

|                                                                                | At 31 December 2009 |                |               |               |               |               |            |                  |
|--------------------------------------------------------------------------------|---------------------|----------------|---------------|---------------|---------------|---------------|------------|------------------|
|                                                                                | On demand           | Up to 1 month  | 1-3 months    | 3-12 months   | 1-5 years     | Over 5 years  | Indefinite | Total            |
|                                                                                | HK\$'m              | HK\$'m         | HK\$'m        | HK\$'m        | HK\$'m        | HK\$'m        | HK\$'m     | HK\$'m           |
| <b>Liabilities</b>                                                             |                     |                |               |               |               |               |            |                  |
| Hong Kong SAR currency notes in circulation                                    | 38,310              | -              | -             | -             | -             | -             | -          | 38,310           |
| Deposits and balances of banks and other financial institutions                | 76,858              | 17,563         | 1,751         | 3,475         | -             | -             | -          | 99,647           |
| Financial liabilities at fair value through profit or loss                     |                     |                |               |               |               |               |            |                  |
| – certificates of deposit issued                                               | -                   | -              | -             | -             | -             | -             | -          | -                |
| – others                                                                       | -                   | 13,166         | 864           | 2,159         | 99            | -             | -          | 16,288           |
| Derivative financial instruments                                               | 9,389               | 570            | 152           | 536           | 2,514         | 806           | -          | 13,967           |
| Deposits from customers                                                        | 564,595             | 164,327        | 74,942        | 37,384        | 1,073         | -             | -          | 842,321          |
| Other accounts and provisions (including current and deferred tax liabilities) | 15,657              | 12,653         | 901           | 2,353         | 4,875         | -             | -          | 36,439           |
| Insurance contract liabilities                                                 | 1,704               | 663            | 13            | 1,321         | 23,012        | 6,695         | -          | 33,408           |
| Subordinated liabilities                                                       | -                   | -              | -             | 13            | -             | 26,763        | -          | 26,776           |
| <b>Total liabilities</b>                                                       | <b>706,513</b>      | <b>208,942</b> | <b>78,623</b> | <b>47,241</b> | <b>31,573</b> | <b>34,264</b> | <b>-</b>   | <b>1,107,156</b> |
| Net liquidity gap                                                              | (531,671)           | (87,146)       | 9,618         | 127,956       | 374,832       | 165,293       | 46,753     | 105,635          |

The above maturity classifications have been prepared in accordance with relevant provisions under the Banking (Disclosure) Rules. The Group has reported assets such as advances and debt securities which have been overdue for not more than one month as “Repayable on demand”. In the case of an asset that is repayable by different payments or instalments, only that portion of the asset that is actually overdue is reported as overdue. Any part of the asset that is not due is reported according to the residual maturity unless the repayment of the asset is in doubt in which case the amount is reported as “Indefinite”. The above assets are stated after deduction of provisions, if any.

The analysis of debt securities by remaining period to maturity is disclosed in order to comply with relevant provisions under the Banking (Disclosure) Rules. The disclosure does not imply that the securities will be held to maturity.

The above analysis in respect of insurance contract liabilities represents the estimated timing of net cash outflows resulting from recognised insurance contract liabilities on the balance sheet as at 30 June 2010 and 31 December 2009.

### 3. Financial risk management (continued)

#### 3.4 Insurance Risk

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

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

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

For the in-force insurance contracts, most of the underlying insurance liabilities are related to endowment and unit-linked insurance products. For most of the insurance policies issued, the Group has a retention limit on any single life insured. The Group cedes the excess of the insured benefit over the limit for standard risks (from a medical point of view) to reinsurer under an excess of loss reinsurance arrangement.

Uncertainty in the estimation of future benefit payments and premium receipts for long-term insurance contracts arises from the unpredictability of long-term changes in overall levels of mortality and persistency. In order to assess the uncertainty due to the mortality assumption and lapse assumption, the Group conducts mortality study and lapse study in order to determine the appropriate assumptions. In these studies, consistent results are reflected in both assumptions with appropriate margins.

#### 3.5 Capital Management

##### (a) Capital adequacy ratio

|                        | At 30 June<br>2010 | At 31 December<br>2009 |
|------------------------|--------------------|------------------------|
| Capital adequacy ratio | 16.17%             | 16.85%                 |
| Core capital ratio     | 11.33%             | 11.64%                 |

The capital ratios are computed on the consolidated basis that comprises the positions of BOCHK and certain subsidiaries specified by the HKMA for its regulatory purposes and in accordance with the Banking (Capital) Rules.

The differences between the basis of consolidation for accounting and regulatory purposes are described in "Appendix – Subsidiaries of the Company" on page 131.

### 3. Financial risk management (continued)

#### 3.5 Capital Management (continued)

##### (b) Components of capital base after deductions

The consolidated capital base after deductions used in the calculation of the above capital adequacy ratio as at 30 June 2010 and 31 December 2009 and reported to the HKMA is analysed as follows:

|                                                                                                            | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|------------------------------------------------------------------------------------------------------------|------------------------------|----------------------------------|
| Core capital:                                                                                              |                              |                                  |
| Paid up ordinary share capital                                                                             | 43,043                       | 43,043                           |
| Reserves                                                                                                   | 27,639                       | 26,154                           |
| Profit and loss account                                                                                    | 4,036                        | 2,039                            |
| Minority interests                                                                                         | 1,294                        | 1,229                            |
|                                                                                                            | 76,012                       | 72,465                           |
| Deductions from core capital                                                                               | (715)                        | (334)                            |
| Core capital                                                                                               | 75,297                       | 72,131                           |
| Supplementary capital:                                                                                     |                              |                                  |
| Fair value gains arising from holdings<br>of available-for-sale securities                                 | 889                          | 237                              |
| Fair value gains arising from holdings<br>of securities designated at fair value<br>through profit or loss | 15                           | –                                |
| Collective loan impairment allowances                                                                      | 1,777                        | 1,598                            |
| Regulatory reserve                                                                                         | 4,611                        | 4,040                            |
| Term subordinated debt                                                                                     | 25,652                       | 26,763                           |
|                                                                                                            | 32,944                       | 32,638                           |
| Deductions from supplementary capital                                                                      | (715)                        | (334)                            |
| Supplementary capital                                                                                      | 32,229                       | 32,304                           |
| Total capital base after deductions                                                                        | 107,526                      | 104,435                          |

Subsidiaries which are not included in the consolidation group for the calculation of capital adequacy ratios are denoted in “Appendix – Subsidiaries of the Company” on pages 128 to 131. Investment costs in such subsidiaries are deducted from the capital base.

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

#### 4. Net interest income

|                                                          | Half-year ended<br>30 June 2010<br>HK\$m | Half-year ended<br>30 June 2009<br>HK\$m |
|----------------------------------------------------------|------------------------------------------|------------------------------------------|
| <b>Interest income</b>                                   |                                          |                                          |
| Cash and due from banks and other financial institutions | 996                                      | 1,772                                    |
| Advances to customers                                    | 5,419                                    | 5,316                                    |
| Listed investments                                       | 1,934                                    | 1,320                                    |
| Unlisted investments                                     | 2,233                                    | 2,862                                    |
| Others                                                   | 89                                       | 61                                       |
|                                                          | <b>10,671</b>                            | <b>11,331</b>                            |
| <b>Interest expense</b>                                  |                                          |                                          |
| Due to banks, customers and other financial institutions | (1,371)                                  | (1,722)                                  |
| Debt securities in issue                                 | –                                        | (19)                                     |
| Subordinated liabilities                                 | (275)                                    | (546)                                    |
| Others                                                   | (61)                                     | (30)                                     |
|                                                          | <b>(1,707)</b>                           | <b>(2,317)</b>                           |
| <b>Net interest income</b>                               | <b>8,964</b>                             | <b>9,014</b>                             |

Included within interest income is HK\$5 million (first half of 2009: HK\$8 million) of interest with respect to income recognised on advances classified as impaired for the first half of 2010. Interest income accrued on impaired investment in securities amounted to HK\$50 million (first half of 2009: HK\$315 million).

Included within interest income and interest expense are HK\$10,593 million (first half of 2009: HK\$10,951 million) and HK\$1,906 million (first half of 2009: HK\$2,270 million) for financial assets and financial liabilities that are not recognised at fair value through profit or loss respectively.

Interest income and expense for interest rate derivatives held for trading have been reclassified from “Net interest income” to “Net trading (loss)/gain”. The comparative figures have been reclassified to conform with the current period’s presentation.

## 5. Net fee and commission income

|                                                                                         | Half-year ended<br>30 June 2010<br>HK\$'m | Half-year ended<br>30 June 2009<br>HK\$'m |
|-----------------------------------------------------------------------------------------|-------------------------------------------|-------------------------------------------|
| <b>Fee and commission income</b>                                                        |                                           |                                           |
| Securities brokerage                                                                    |                                           |                                           |
| – Stockbroking                                                                          | 1,506                                     | 1,625                                     |
| – Bonds                                                                                 | 3                                         | 4                                         |
| Credit cards                                                                            | 903                                       | 705                                       |
| Loan commissions                                                                        | 623                                       | 398                                       |
| Bills commissions                                                                       | 371                                       | 310                                       |
| Payment services                                                                        | 272                                       | 227                                       |
| Insurance                                                                               | 220                                       | 122                                       |
| Currency exchange                                                                       | 125                                       | 87                                        |
| Safe deposit box                                                                        | 103                                       | 98                                        |
| Trust services                                                                          | 98                                        | 82                                        |
| Funds distribution                                                                      | 67                                        | 38                                        |
| Others                                                                                  | 190                                       | 188                                       |
|                                                                                         | <b>4,481</b>                              | <b>3,884</b>                              |
| <b>Fee and commission expense</b>                                                       |                                           |                                           |
| Credit cards                                                                            | (668)                                     | (500)                                     |
| Securities brokerage                                                                    | (234)                                     | (255)                                     |
| Payment services                                                                        | (42)                                      | (39)                                      |
| Others                                                                                  | (140)                                     | (143)                                     |
|                                                                                         | <b>(1,084)</b>                            | <b>(937)</b>                              |
| <b>Net fee and commission income</b>                                                    | <b>3,397</b>                              | <b>2,947</b>                              |
| Of which arise from                                                                     |                                           |                                           |
| – financial assets or financial liabilities not at fair value<br>through profit or loss |                                           |                                           |
| – Fee and commission income                                                             | 725                                       | 452                                       |
| – Fee and commission expense                                                            | (4)                                       | (11)                                      |
|                                                                                         | <b>721</b>                                | <b>441</b>                                |
| – trust and other fiduciary activities                                                  |                                           |                                           |
| – Fee and commission income                                                             | 213                                       | 201                                       |
| – Fee and commission expense                                                            | (3)                                       | (4)                                       |
|                                                                                         | <b>210</b>                                | <b>197</b>                                |

**6. Net trading (loss)/gain**

|                                                              | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|--------------------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| Net (loss)/gain from:                                        |                                                    |                                           |
| – foreign exchange and foreign exchange products             | <b>350</b>                                         | 790                                       |
| – interest rate instruments and items under fair value hedge | <b>(424)</b>                                       | (57)                                      |
| – equity instruments                                         | <b>(20)</b>                                        | 17                                        |
| – commodities                                                | <b>58</b>                                          | 54                                        |
|                                                              | <b>(36)</b>                                        | 804                                       |

Interest income and expense for interest rate derivatives held for trading have been reclassified from “Net interest income” to “Net trading (loss)/gain”. The comparative figures have been reclassified to conform with the current period’s presentation.

**7. Net gain on investment in securities**

|                                                         | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|---------------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| Net gain from disposal of available-for-sale securities | <b>404</b>                                         | 64                                        |
| Net gain from redemption of held-to-maturity securities | –                                                  | 3                                         |
|                                                         | <b>404</b>                                         | 67                                        |

**8. Net insurance premium income**

|                                                  | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|--------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| Gross earned premiums                            | <b>2,809</b>                                       | 2,266                                     |
| Less: Gross written premiums ceded to reinsurers | <b>(11)</b>                                        | (5)                                       |
| Net insurance premium income                     | <b>2,798</b>                                       | 2,261                                     |

**9. Other operating income**

|                                                     | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|-----------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| Dividend income from investment in securities       |                                                    |                                           |
| – listed investments                                | <b>41</b>                                          | 2                                         |
| – unlisted investments                              | <b>13</b>                                          | 11                                        |
| Gross rental income from investment properties      | <b>164</b>                                         | 179                                       |
| Less: Outgoings in respect of investment properties | <b>(30)</b>                                        | (23)                                      |
| Others                                              | <b>61</b>                                          | 80                                        |
|                                                     | <b>249</b>                                         | 249                                       |

Included in the “Outgoings in respect of investment properties” is HK\$7 million (first half of 2009: HK\$3 million) of direct operating expenses related to investment properties that were not let during the period.

**10. Net insurance benefits and claims**

|                                                                                             | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|---------------------------------------------------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| Claims, benefits and surrenders paid                                                        | <b>2,239</b>                                       | 1,682                                     |
| Movement in liabilities                                                                     | <b>1,641</b>                                       | (762)                                     |
| Gross claims, benefits and surrenders paid and movement in liabilities                      | <b>3,880</b>                                       | 920                                       |
| Less: Reinsurers' share of claims, benefits and surrenders paid and movement in liabilities | <b>(5)</b>                                         | (1)                                       |
| Net insurance claims, benefits and surrenders paid and movement in liabilities              | <b>3,875</b>                                       | 919                                       |

**11. Net reversal/(charge) of impairment allowances**

|                                                                                  | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|----------------------------------------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| <b>Advances to customers</b>                                                     |                                                    |                                           |
| Individually assessed                                                            |                                                    |                                           |
| – new allowances                                                                 | <b>(46)</b>                                        | (163)                                     |
| – releases                                                                       | <b>102</b>                                         | 87                                        |
| – recoveries                                                                     | <b>277</b>                                         | 142                                       |
| Net reversal of individually assessed loan impairment allowances                 | <b>333</b>                                         | 66                                        |
| Collectively assessed                                                            |                                                    |                                           |
| – new allowances                                                                 | <b>(265)</b>                                       | (198)                                     |
| – releases                                                                       | <b>9</b>                                           | 174                                       |
| – recoveries                                                                     | <b>17</b>                                          | 18                                        |
| Net charge of collectively assessed loan impairment allowances                   | <b>(239)</b>                                       | (6)                                       |
| Net reversal of loan impairment allowances                                       | <b>94</b>                                          | 60                                        |
| <b>Available-for-sale securities</b>                                             |                                                    |                                           |
| Net reversal/(charge) of impairment losses on<br>available-for-sale securities   |                                                    |                                           |
| – Individually assessed                                                          | <b>40</b>                                          | (729)                                     |
| <b>Held-to-maturity securities</b>                                               |                                                    |                                           |
| Net reversal/(charge) of impairment allowances on<br>held-to-maturity securities |                                                    |                                           |
| – Individually assessed                                                          | <b>32</b>                                          | (439)                                     |
| <b>Others</b>                                                                    | <b>(5)</b>                                         | (7)                                       |
| <b>Net reversal/(charge) of impairment allowances</b>                            | <b>161</b>                                         | (1,115)                                   |

**12. Operating expenses**

|                                                          | Half-year ended<br>30 June 2010<br>HK\$'m | Half-year ended<br>30 June 2009<br>HK\$'m |
|----------------------------------------------------------|-------------------------------------------|-------------------------------------------|
| Staff costs (including directors' emoluments)            |                                           |                                           |
| – salaries and other costs                               | 2,332                                     | 2,057                                     |
| – termination benefit                                    | –                                         | 5                                         |
| – pension cost                                           | 194                                       | 194                                       |
|                                                          | 2,526                                     | 2,256                                     |
| Premises and equipment expenses (excluding depreciation) |                                           |                                           |
| – rental of premises                                     | 249                                       | 241                                       |
| – information technology                                 | 183                                       | 161                                       |
| – others                                                 | 142                                       | 136                                       |
|                                                          | 574                                       | 538                                       |
| Depreciation                                             | 556                                       | 496                                       |
| Auditor's remuneration                                   |                                           |                                           |
| – audit services                                         | 4                                         | 4                                         |
| – non-audit services                                     | 6                                         | 2                                         |
| Other operating expenses                                 | 868                                       | 898                                       |
|                                                          | 4,534                                     | 4,194                                     |

**13. Net gain from disposal of/fair value adjustments on investment properties**

|                                                             | Half-year ended<br>30 June 2010<br>HK\$'m | Half-year ended<br>30 June 2009<br>HK\$'m |
|-------------------------------------------------------------|-------------------------------------------|-------------------------------------------|
| Net loss on disposal of investment properties               | –                                         | (2)                                       |
| Net gain on fair value adjustments on investment properties | 601                                       | 527                                       |
|                                                             | 601                                       | 525                                       |

**14. Net loss from disposal/revaluation of properties, plant and equipment**

|                                            | Half-year ended<br>30 June 2010<br>HK\$'m | Half-year ended<br>30 June 2009<br>HK\$'m |
|--------------------------------------------|-------------------------------------------|-------------------------------------------|
| Net loss on disposal of other fixed assets | (2)                                       | (5)                                       |
| Net gain on revaluation of premises        | 1                                         | 4                                         |
|                                            | (1)                                       | (1)                                       |

**15. Taxation**

Taxation in the condensed consolidated income statement represents:

|                           | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|---------------------------|----------------------------------------------------|-------------------------------------------|
| Hong Kong profits tax     |                                                    |                                           |
| – current period taxation | <b>1,341</b>                                       | 1,169                                     |
| Deferred tax charge       | <b>20</b>                                          | 127                                       |
| Hong Kong profits tax     | <b>1,361</b>                                       | 1,296                                     |
| Overseas taxation         | <b>53</b>                                          | 73                                        |
|                           | <b>1,414</b>                                       | 1,369                                     |

Hong Kong profits tax has been provided at the rate of 16.5% (2009: 16.5%) on the estimated assessable profits arising in Hong Kong for the first half of 2010. Taxation on overseas profits has been calculated on the estimated assessable profits for the first half of 2010 at the rates of taxation prevailing in the countries in which the Group operates.

The taxation on the Group's profit before taxation that differs from the theoretical amount that would arise using the taxation rate of Hong Kong is as follows:

|                                                       | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|-------------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| Profit before taxation                                | <b>8,767</b>                                       | 8,244                                     |
| Calculated at a taxation rate of 16.5% (2009: 16.5%)  | <b>1,447</b>                                       | 1,360                                     |
| Effect of different taxation rates in other countries | <b>14</b>                                          | 3                                         |
| Income not subject to taxation                        | <b>(97)</b>                                        | (39)                                      |
| Expenses not deductible for taxation purposes         | <b>47</b>                                          | 43                                        |
| Tax losses not recognised                             | <b>3</b>                                           | 2                                         |
| Taxation charge                                       | <b>1,414</b>                                       | 1,369                                     |
| Effective tax rate                                    | <b>16.1%</b>                                       | 16.6%                                     |

**16. Dividends**

|                  | <b>Half-year ended<br/>30 June 2010</b> |                        | Half-year ended<br>30 June 2009 |                |
|------------------|-----------------------------------------|------------------------|---------------------------------|----------------|
|                  | <b>Per share<br/>HK\$</b>               | <b>Total<br/>HK\$m</b> | Per share<br>HK\$               | Total<br>HK\$m |
| Interim dividend | <b>0.400</b>                            | <b>4,229</b>           | 0.285                           | 3,013          |

At a meeting held on 26 August 2010, the Board declared an interim dividend of HK\$0.4 per ordinary share for the first half of 2010 amounting to approximately HK\$4,229 million. This declared dividend is not reflected as a dividend payable in this interim financial information, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2010.

**17. Earnings per share for profit attributable to the equity holders of the Company**

The calculation of basic earnings per share is based on the consolidated profit attributable to the equity holders of the Company for the first half of 2010 of approximately HK\$7,190 million (first half of 2009: HK\$6,691 million) and on the ordinary shares in issue of 10,572,780,266 shares (2009: 10,572,780,266 ordinary shares).

There was no dilution of earnings per share as no potential ordinary shares were in issue for the first half of 2010 (first half of 2009: Nil).

**18. Retirement benefit costs**

The principal defined contribution schemes for the Group's employees are ORSO schemes exempted under the MPF Schemes Ordinance and the BOC-Prudential Easy Choice MPF Scheme. Under the ORSO schemes, employees make monthly contributions to the ORSO schemes equal to 5% of their basic salaries, while the employer makes monthly contributions equal to 5% to 15% of the employees' monthly basic salaries, depending on years of service. The employees are entitled to receive 100% of the employer's contributions upon termination of employment after completing 20 years of service, or at a scale ranging from 20% to 95% for employees who have completed between 3 to 20 years of service, on conditions of retirement, early retirement, permanent incapacity and ill-health or termination of employment other than summary dismissal.

With the implementation of the MPF Schemes Ordinance on 1 December 2000, the Group also participates in the BOC-Prudential Easy Choice MPF Scheme, of which the trustee is BOCI-Prudential Trustee and the investment manager is BOCI-Prudential Manager, which are related parties of the Company.

The Group's total contributions made to the ORSO schemes for the first half of 2010 amounted to approximately HK\$155 million (first half of 2009: approximately HK\$161 million), after a deduction of forfeited contributions of approximately HK\$5.9 million (first half of 2009: approximately HK\$2.3 million). For the MPF Scheme, the Group contributed approximately HK\$22 million (first half of 2009: approximately HK\$18 million) for the first half of 2010.

**19. Share option schemes****(a) *Share Option Scheme and Sharesave Plan***

The principal terms of the Share Option Scheme and the Sharesave Plan were approved and adopted by written resolutions of all the shareholders of the Company dated 10 July 2002.

The purpose of the Share Option Scheme is to provide the participants with the opportunity to acquire proprietary interests in the Company. The Board may, in its absolute discretion, offer to grant options under the Share Option Scheme to any person as the Board may select. The subscription price for the shares shall be determined on the date of grant by the Board as an amount per share calculated on the basis of established rules. An option may be exercised in whole or in part at any time after the date prescribed by the Board and from time to time as specified in the offer and on or before the termination date prescribed by the Board.

The purpose of the Sharesave Plan is to encourage broad-based employee ownership of the shares of the Company. The amount of the monthly contribution under the savings contract to be made in connection with an option shall be the amount which the relevant eligible employee is willing to contribute, which amount shall not be less than 1% and not more than 10% of the eligible employee's monthly salary as at the date of application or such other maximum or minimum amounts as permitted by the Board. When an option is exercised during an exercise period, it may be exercised in whole or in part.

No options were granted pursuant to the Share Option Scheme or the Sharesave Plan during the first half of 2010 (first half of 2009: Nil).

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

On 5 July 2002, several directors together with approximately 60 senior management personnel of the Group and employees of BOC were granted options by BOC (BVI), the immediate holding company of the Company, pursuant to a Pre-Listing Share Option Scheme to purchase from BOC (BVI) an aggregate of 31,132,600 existing issued shares of the Company. The Group has taken advantage of the transitional provisions set out in paragraph 53 of HKFRS 2 under which the new recognition and measurement policies have not been applied to all options granted to employees on or before 7 November 2002.

**19. Share option schemes (continued)****(b) Pre-Listing Share Option Scheme (continued)**

Details of the share options outstanding as at 30 June 2010 and 31 December 2009 are disclosed as follows:

|                                                 | Directors   | Senior management | Others*     | Total number of share options | Average exercise price (HK\$ per share) |
|-------------------------------------------------|-------------|-------------------|-------------|-------------------------------|-----------------------------------------|
| At 1 January 2010                               | 3,976,500   | 1,074,300         | –           | 5,050,800                     | 8.5                                     |
| Less: Share options exercised during the period | –           | (437,000)         | –           | (437,000)                     | 8.5                                     |
| At 30 June 2010                                 | 3,976,500   | 637,300           | –           | 4,613,800                     | 8.5                                     |
| Exercisable at 30 June 2010                     | 3,976,500   | 637,300           | –           | 4,613,800                     | 8.5                                     |
| At 1 January 2009                               | 6,290,100   | 1,361,200         | –           | 7,651,300                     | 8.5                                     |
| Transfer                                        | (1,590,600) | –                 | 1,590,600   | –                             | 8.5                                     |
| Less: Share options exercised during the year   | (723,000)   | (286,900)         | (1,590,600) | (2,600,500)                   | 8.5                                     |
| At 31 December 2009                             | 3,976,500   | 1,074,300         | –           | 5,050,800                     | 8.5                                     |
| Exercisable at 31 December 2009                 | 3,976,500   | 1,074,300         | –           | 5,050,800                     | 8.5                                     |

\* Represented share options held by ex-directors of the Group.

Share options were exercised on a regular basis throughout the period, the weighted average share price during the period was HK\$18.34 (31 December 2009: HK\$16.83).

The options granted under this scheme can be exercised at HK\$8.50 per share in respect of the option price of HK\$1.00. These options have a vesting period of four years from the date on which dealings in the shares commenced on the Stock Exchange with a valid exercise period of ten years. No offer to grant any options under the Pre-Listing Share Option Scheme will be made on or after the date on which dealings in the shares commenced on the Stock Exchange.

**20. Cash and balances with banks and other financial institutions**

|                                                                                  | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|----------------------------------------------------------------------------------|---------------------------------------|----------------------------------|
| Cash                                                                             | <b>3,754</b>                          | 3,409                            |
| Balances with central banks                                                      | <b>85,926</b>                         | 81,790                           |
| Balances with banks and other financial institutions                             | <b>8,068</b>                          | 6,091                            |
| Placements with banks and other financial institutions maturing within one month | <b>71,806</b>                         | 69,498                           |
|                                                                                  | <b>169,554</b>                        | 160,788                          |

**21. Financial assets at fair value through profit or loss**

|                            | Trading securities           |                                  | Financial assets<br>designated at fair value<br>through profit or loss |                                  | Total                        |                                  |
|----------------------------|------------------------------|----------------------------------|------------------------------------------------------------------------|----------------------------------|------------------------------|----------------------------------|
|                            | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m | At 30 June<br>2010<br>HK\$'m                                           | At 31 December<br>2009<br>HK\$'m | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|                            |                              |                                  |                                                                        |                                  |                              |                                  |
| At fair value              |                              |                                  |                                                                        |                                  |                              |                                  |
| Debt securities            |                              |                                  |                                                                        |                                  |                              |                                  |
| – Listed in Hong Kong      | <b>656</b>                   | 333                              | <b>839</b>                                                             | 1,063                            | <b>1,495</b>                 | 1,396                            |
| – Listed outside Hong Kong | <b>5,146</b>                 | 2,408                            | <b>3,080</b>                                                           | 3,264                            | <b>8,226</b>                 | 5,672                            |
|                            | <b>5,802</b>                 | 2,741                            | <b>3,919</b>                                                           | 4,327                            | <b>9,721</b>                 | 7,068                            |
| – Unlisted                 | <b>38,236</b>                | 15,854                           | <b>17,133</b>                                                          | 17,406                           | <b>55,369</b>                | 33,260                           |
|                            | <b>44,038</b>                | 18,595                           | <b>21,052</b>                                                          | 21,733                           | <b>65,090</b>                | 40,328                           |
| Fund                       |                              |                                  |                                                                        |                                  |                              |                                  |
| – Unlisted                 | –                            | –                                | <b>3,555</b>                                                           | 2,757                            | <b>3,555</b>                 | 2,757                            |
| Equity securities          |                              |                                  |                                                                        |                                  |                              |                                  |
| – Listed in Hong Kong      | <b>19</b>                    | 37                               | <b>1,532</b>                                                           | 1,361                            | <b>1,551</b>                 | 1,398                            |
| – Listed outside Hong Kong | –                            | –                                | <b>89</b>                                                              | –                                | <b>89</b>                    | –                                |
| – Unlisted                 | <b>87</b>                    | 111                              | –                                                                      | –                                | <b>87</b>                    | 111                              |
|                            | <b>106</b>                   | 148                              | <b>1,621</b>                                                           | 1,361                            | <b>1,727</b>                 | 1,509                            |
| Total                      | <b>44,144</b>                | 18,743                           | <b>26,228</b>                                                          | 25,851                           | <b>70,372</b>                | 44,594                           |

**21. Financial assets at fair value through profit or loss (continued)**

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

|                                        | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|----------------------------------------|---------------------------------------|-------------------------------------------|
| Sovereigns                             | <b>37,326</b>                         | 15,970                                    |
| Public sector entities                 | <b>1,377</b>                          | 1,496                                     |
| Banks and other financial institutions | <b>24,390</b>                         | 21,853                                    |
| Corporate entities                     | <b>7,279</b>                          | 5,275                                     |
|                                        | <b>70,372</b>                         | 44,594                                    |

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

|                                                             | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|-------------------------------------------------------------|---------------------------------------|-------------------------------------------|
| Treasury bills                                              | <b>35,534</b>                         | 14,419                                    |
| Certificates of deposit held                                | <b>3,636</b>                          | 2,585                                     |
| Other financial assets at fair value through profit or loss | <b>31,202</b>                         | 27,590                                    |
|                                                             | <b>70,372</b>                         | 44,594                                    |

**22. Derivative financial instruments**

The Group enters into the following equity, foreign exchange, interest rate and precious metal related derivative financial instruments for trading and risk management purposes:

Currency forwards represent commitments to purchase and sell foreign currency on a future date. Interest rate futures are contractual obligations to receive or pay a net amount based on changes in interest rates or buy or sell interest rate financial instruments on a future date at an agreed price in the financial market under the administration of the stock exchange. Forward rate agreements are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contracted rate of interest and the current market rate, based on a notional principal amount.

Currency, interest rate and precious metal swaps are commitments to exchange one set of cash flows or commodity for another. Swaps result in an exchange of currencies, interest rates (for example, fixed rate for floating rate), or precious metals (for example, silver swaps) or a combination of all these (for example, cross-currency interest rate swaps). Except for certain currency swap contracts, no exchange of principal takes place.

Foreign currency, interest rate, equity and precious metal options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of the financial instrument at a predetermined price. In consideration for the assumption of foreign exchange and interest rate risk, the seller receives a premium from the purchaser. Options are negotiated over-the-counter ("OTC") between the Group and its counterparty or traded through the stock exchange (for example, exchange-traded stock option).

**22. Derivative financial instruments (continued)**

The contract/notional amounts and fair values of derivative financial instruments held by the Group are set out in the following tables. The contract/notional amounts of these instruments indicate the volume of transactions outstanding at the balance sheet dates and certain of them provide a basis for comparison with fair value instruments recognised on the condensed consolidated balance sheet. However, they do not necessarily indicate the amounts of future cash flows involved or the current fair values of the instruments and, therefore, do not indicate the Group's exposure to credit or market risks. The derivative financial instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates, foreign exchange rates or equity and metal prices relative to their terms. The aggregate fair values of derivative financial instruments assets and liabilities can fluctuate significantly from time to time.

The following tables summarise the contract/notional amounts of each significant type of derivative financial instrument as at 30 June 2010 and 31 December 2009:

|                                   | At 30 June 2010   |                   |                                                     |                 |
|-----------------------------------|-------------------|-------------------|-----------------------------------------------------|-----------------|
|                                   | Trading<br>HK\$'m | Hedging<br>HK\$'m | Not qualified<br>for hedge<br>accounting*<br>HK\$'m | Total<br>HK\$'m |
| Exchange rate contracts           |                   |                   |                                                     |                 |
| Spot and forwards                 | 329,577           | –                 | 2,270                                               | 331,847         |
| Swaps                             | 254,584           | 1,716             | –                                                   | 256,300         |
| Foreign currency option contracts |                   |                   |                                                     |                 |
| – Options purchased               | 1,463             | –                 | –                                                   | 1,463           |
| – Options written                 | 1,747             | –                 | –                                                   | 1,747           |
|                                   | 587,371           | 1,716             | 2,270                                               | 591,357         |
| Interest rate contracts           |                   |                   |                                                     |                 |
| Futures                           | 5,334             | –                 | –                                                   | 5,334           |
| Swaps                             | 211,445           | 49,445            | 15,485                                              | 276,375         |
| Interest rate option contracts    |                   |                   |                                                     |                 |
| – Swaptions written               | 156               | –                 | –                                                   | 156             |
| – Bond options written            | 2,647             | –                 | –                                                   | 2,647           |
|                                   | 219,582           | 49,445            | 15,485                                              | 284,512         |
| Bullion contracts                 | 10,859            | –                 | –                                                   | 10,859          |
| Equity contracts                  | 92                | –                 | –                                                   | 92              |
| Other contracts                   | 107               | –                 | –                                                   | 107             |
| Total                             | 818,011           | 51,161            | 17,755                                              | 886,927         |

\* Derivative transactions which do not qualify as hedges for accounting purposes but are managed in conjunction with the financial instruments designated at fair value through profit or loss are separately disclosed in compliance with the requirements set out in the Banking (Disclosure) Rules.

**22. Derivative financial instruments (continued)**

|                                   | At 31 December 2009 |                   |                                                    |                 |
|-----------------------------------|---------------------|-------------------|----------------------------------------------------|-----------------|
|                                   | Trading<br>HK\$'m   | Hedging<br>HK\$'m | Not qualified<br>for hedge<br>accounting<br>HK\$'m | Total<br>HK\$'m |
| Exchange rate contracts           |                     |                   |                                                    |                 |
| Spot and forwards                 | 264,014             | –                 | 3,718                                              | 267,732         |
| Swaps                             | 269,978             | 1,112             | 68                                                 | 271,158         |
| Foreign currency option contracts |                     |                   |                                                    |                 |
| – Options purchased               | 1,387               | –                 | –                                                  | 1,387           |
| – Options written                 | 1,603               | –                 | –                                                  | 1,603           |
|                                   | 536,982             | 1,112             | 3,786                                              | 541,880         |
| Interest rate contracts           |                     |                   |                                                    |                 |
| Futures                           | 655                 | –                 | –                                                  | 655             |
| Swaps                             | 140,088             | 32,471            | 23,665                                             | 196,224         |
| Interest rate option contracts    |                     |                   |                                                    |                 |
| – Bond options written            | 853                 | –                 | –                                                  | 853             |
|                                   | 141,596             | 32,471            | 23,665                                             | 197,732         |
| Bullion contracts                 | 8,290               | –                 | –                                                  | 8,290           |
| Equity contracts                  | 209                 | –                 | –                                                  | 209             |
| Other contracts                   | 117                 | –                 | –                                                  | 117             |
| Total                             | 687,194             | 33,583            | 27,451                                             | 748,228         |

**22. Derivative financial instruments (continued)**

The following tables summarise the fair values of each class of derivative financial instrument as at 30 June 2010 and 31 December 2009:

|                                   | At 30 June 2010         |                   |                      |                 |                         |                   |                      |                 |
|-----------------------------------|-------------------------|-------------------|----------------------|-----------------|-------------------------|-------------------|----------------------|-----------------|
|                                   | Fair value assets       |                   |                      |                 | Fair value liabilities  |                   |                      |                 |
|                                   | Not qualified for hedge |                   |                      |                 | Not qualified for hedge |                   |                      |                 |
|                                   | Trading<br>HK\$'m       | Hedging<br>HK\$'m | accounting<br>HK\$'m | Total<br>HK\$'m | Trading<br>HK\$'m       | Hedging<br>HK\$'m | accounting<br>HK\$'m | Total<br>HK\$'m |
| Exchange rate contracts           |                         |                   |                      |                 |                         |                   |                      |                 |
| Spot and forwards                 | 13,899                  | –                 | 1                    | 13,900          | (9,377)                 | –                 | (6)                  | (9,383)         |
| Swaps                             | 1,210                   | –                 | –                    | 1,210           | (933)                   | (12)              | –                    | (945)           |
| Foreign currency option contracts |                         |                   |                      |                 |                         |                   |                      |                 |
| – Options purchased               | 13                      | –                 | –                    | 13              | –                       | –                 | –                    | –               |
| – Options written                 | –                       | –                 | –                    | –               | (10)                    | –                 | –                    | (10)            |
|                                   | 15,122                  | –                 | 1                    | 15,123          | (10,320)                | (12)              | (6)                  | (10,338)        |
| Interest rate contracts           |                         |                   |                      |                 |                         |                   |                      |                 |
| Futures                           | 2                       | –                 | –                    | 2               | (2)                     | –                 | –                    | (2)             |
| Swaps                             | 1,704                   | 1,352             | 13                   | 3,069           | (2,431)                 | (2,129)           | (129)                | (4,689)         |
| Interest rate option contracts    |                         |                   |                      |                 |                         |                   |                      |                 |
| – Swaptions written               | –                       | –                 | –                    | –               | (4)                     | –                 | –                    | (4)             |
| – Bond options written            | –                       | –                 | –                    | –               | (116)                   | –                 | –                    | (116)           |
|                                   | 1,706                   | 1,352             | 13                   | 3,071           | (2,553)                 | (2,129)           | (129)                | (4,811)         |
| Bullion contracts                 | 944                     | –                 | –                    | 944             | (622)                   | –                 | –                    | (622)           |
| Equity contracts                  | 2                       | –                 | –                    | 2               | –                       | –                 | –                    | –               |
| Total                             | 17,774                  | 1,352             | 14                   | 19,140          | (13,495)                | (2,141)           | (135)                | (15,771)        |

## 22. Derivative financial instruments (continued)

|                                   | At 31 December 2009                |                   |                      |                 |                                    |                   |                      |                 |
|-----------------------------------|------------------------------------|-------------------|----------------------|-----------------|------------------------------------|-------------------|----------------------|-----------------|
|                                   | Fair value assets                  |                   |                      |                 | Fair value liabilities             |                   |                      |                 |
|                                   | Not qualified for hedge accounting |                   |                      |                 | Not qualified for hedge accounting |                   |                      |                 |
|                                   | Trading<br>HK\$'m                  | Hedging<br>HK\$'m | accounting<br>HK\$'m | Total<br>HK\$'m | Trading<br>HK\$'m                  | Hedging<br>HK\$'m | accounting<br>HK\$'m | Total<br>HK\$'m |
| Exchange rate contracts           |                                    |                   |                      |                 |                                    |                   |                      |                 |
| Spot and forwards                 | 13,472                             | –                 | –                    | 13,472          | (9,268)                            | –                 | (3)                  | (9,271)         |
| Swaps                             | 2,083                              | 17                | 5                    | 2,105           | (741)                              | (20)              | (6)                  | (767)           |
| Foreign currency option contracts |                                    |                   |                      |                 |                                    |                   |                      |                 |
| – Options purchased               | 10                                 | –                 | –                    | 10              | –                                  | –                 | –                    | –               |
| – Options written                 | –                                  | –                 | –                    | –               | (9)                                | –                 | –                    | (9)             |
|                                   | 15,565                             | 17                | 5                    | 15,587          | (10,018)                           | (20)              | (9)                  | (10,047)        |
| Interest rate contracts           |                                    |                   |                      |                 |                                    |                   |                      |                 |
| Futures                           | 2                                  | –                 | –                    | 2               | –                                  | –                 | –                    | –               |
| Swaps                             | 1,255                              | 92                | 15                   | 1,362           | (2,246)                            | (1,203)           | (92)                 | (3,541)         |
| Interest rate option contracts    |                                    |                   |                      |                 |                                    |                   |                      |                 |
| – Bond options written            | –                                  | –                 | –                    | –               | (4)                                | –                 | –                    | (4)             |
|                                   | 1,257                              | 92                | 15                   | 1,364           | (2,250)                            | (1,203)           | (92)                 | (3,545)         |
| Bullion contracts                 | 631                                | –                 | –                    | 631             | (374)                              | –                 | –                    | (374)           |
| Equity contracts                  | 2                                  | –                 | –                    | 2               | (1)                                | –                 | –                    | (1)             |
| Total                             | 17,455                             | 109               | 20                   | 17,584          | (12,643)                           | (1,223)           | (101)                | (13,967)        |

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

|                                   | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|-----------------------------------|------------------------------|----------------------------------|
| Exchange rate contracts           |                              |                                  |
| Forwards                          | 1,090                        | 580                              |
| Swaps                             | 1,354                        | 1,728                            |
| Foreign currency option contracts |                              |                                  |
| – Options purchased               | 2                            | 1                                |
| Interest rate contracts           |                              |                                  |
| Swaps                             | 1,262                        | 737                              |
| Bullion contracts                 | 2                            | 1                                |
|                                   | 3,710                        | 3,047                            |

**22. Derivative financial instruments (continued)**

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

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

**23. Advances and other accounts**

|                                                    | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|----------------------------------------------------|---------------------------------------|-------------------------------------------|
| Personal loans and advances                        | <b>167,447</b>                        | 161,439                                   |
| Corporate loans and advances                       | <b>404,039</b>                        | 353,533                                   |
| Advances to customers                              | <b>571,486</b>                        | 514,972                                   |
| Loan impairment allowances                         |                                       |                                           |
| – Individually assessed                            | <b>(512)</b>                          | (671)                                     |
| – Collectively assessed                            | <b>(1,777)</b>                        | (1,598)                                   |
|                                                    | <b>569,197</b>                        | 512,703                                   |
| Trade bills                                        | <b>24,663</b>                         | 9,100                                     |
| Advances to banks and other financial institutions | <b>3,446</b>                          | 5,332                                     |
| <b>Total</b>                                       | <b>597,306</b>                        | 527,135                                   |

As at 30 June 2010, advances to customers included accrued interest on gross advances of HK\$759 million (31 December 2009: HK\$619 million).

As at 30 June 2010 and 31 December 2009, no impairment allowance was made in respect of trade bills and advances to banks and other financial institutions.

**24. Investment in securities**

|                                                    | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
|----------------------------------------------------|------------------------------|----------------------------------|
| <b>(a) Available-for-sale securities</b>           |                              |                                  |
| Debt securities, at fair value                     |                              |                                  |
| – Listed in Hong Kong                              | 10,488                       | 8,439                            |
| – Listed outside Hong Kong                         | 100,129                      | 84,389                           |
|                                                    | 110,617                      | 92,828                           |
| – Unlisted                                         | 124,259                      | 132,528                          |
|                                                    | 234,876                      | 225,356                          |
| Equity securities, at fair value                   |                              |                                  |
| – Listed in Hong Kong                              | 2,494                        | 2,630                            |
| – Unlisted                                         | 554                          | 627                              |
|                                                    | 3,048                        | 3,257                            |
|                                                    | 237,924                      | 228,613                          |
| <b>(b) Held-to-maturity securities</b>             |                              |                                  |
| Listed, at amortised cost                          |                              |                                  |
| – in Hong Kong                                     | 1,122                        | 1,693                            |
| – outside Hong Kong                                | 20,313                       | 21,167                           |
|                                                    | 21,435                       | 22,860                           |
| Unlisted, at amortised cost                        | 42,252                       | 49,691                           |
|                                                    | 63,687                       | 72,551                           |
| Impairment allowances                              | (69)                         | (112)                            |
|                                                    | 63,618                       | 72,439                           |
| <b>(c) Loans and receivables</b>                   |                              |                                  |
| Unlisted, at amortised cost                        | 11,695                       | 12,703                           |
| <b>Total</b>                                       | <b>313,237</b>               | <b>313,755</b>                   |
| Market value of listed held-to-maturity securities | 21,422                       | 22,711                           |

**24. Investment in securities (continued)**

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

|                                        | At 30 June 2010                      |                                    |                          |                |
|----------------------------------------|--------------------------------------|------------------------------------|--------------------------|----------------|
|                                        | Available-<br>for-sale<br>securities | Held-to-<br>maturity<br>securities | Loans and<br>receivables | Total          |
|                                        | HK\$'m                               | HK\$'m                             | HK\$'m                   | HK\$'m         |
| Sovereigns                             | 51,650                               | 4,581                              | –                        | 56,231         |
| Public sector entities                 | 29,737                               | 6,625                              | –                        | 36,362         |
| Banks and other financial institutions | 142,657                              | 46,734                             | 11,695                   | 201,086        |
| Corporate entities                     | 13,880                               | 5,678                              | –                        | 19,558         |
|                                        | <b>237,924</b>                       | <b>63,618</b>                      | <b>11,695</b>            | <b>313,237</b> |

|                                        | At 31 December 2009                  |                                    |                          |                |
|----------------------------------------|--------------------------------------|------------------------------------|--------------------------|----------------|
|                                        | Available-<br>for-sale<br>securities | Held-to-<br>maturity<br>securities | Loans and<br>receivables | Total          |
|                                        | HK\$'m                               | HK\$'m                             | HK\$'m                   | HK\$'m         |
| Sovereigns                             | 57,583                               | 3,271                              | –                        | 60,854         |
| Public sector entities                 | 27,902                               | 5,131                              | –                        | 33,033         |
| Banks and other financial institutions | 129,629                              | 56,806                             | 12,703                   | 199,138        |
| Corporate entities                     | 13,499                               | 7,231                              | –                        | 20,730         |
|                                        | <b>228,613</b>                       | <b>72,439</b>                      | <b>12,703</b>            | <b>313,755</b> |

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

|                              | Available-for-sale<br>securities |                        | Held-to-maturity<br>securities |                        |
|------------------------------|----------------------------------|------------------------|--------------------------------|------------------------|
|                              | At 30 June<br>2010               | At 31 December<br>2009 | At 30 June<br>2010             | At 31 December<br>2009 |
|                              | HK\$'m                           | HK\$'m                 | HK\$'m                         | HK\$'m                 |
| Treasury bills               | 7,404                            | 22,955                 | 700                            | 1,041                  |
| Certificates of deposit held | 17,624                           | 19,108                 | 5,071                          | 9,833                  |
| Others                       | 212,896                          | 186,550                | 57,847                         | 61,565                 |
|                              | <b>237,924</b>                   | <b>228,613</b>         | <b>63,618</b>                  | <b>72,439</b>          |

**25. Investment properties**

|                                                                      | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|----------------------------------------------------------------------|---------------------------------------|----------------------------------|
| At 1 January                                                         | <b>9,364</b>                          | 7,727                            |
| Additions                                                            | <b>2</b>                              | –                                |
| Disposals                                                            | <b>(163)</b>                          | (77)                             |
| Fair value gains                                                     | <b>601</b>                            | 1,554                            |
| Reclassification (to)/from properties, plant and equipment (Note 26) | <b>(481)</b>                          | 160                              |
| At period/year end                                                   | <b>9,323</b>                          | 9,364                            |

**26. Properties, plant and equipment**

|                                                            | <b>Premises<br/>HK\$'m</b> | <b>Equipment,<br/>fixtures and<br/>fittings<br/>HK\$'m</b> | <b>Total<br/>HK\$'m</b> |
|------------------------------------------------------------|----------------------------|------------------------------------------------------------|-------------------------|
| Net book value at 1 January 2010                           | <b>23,701</b>              | <b>2,585</b>                                               | <b>26,286</b>           |
| Additions                                                  | <b>15</b>                  | <b>147</b>                                                 | <b>162</b>              |
| Disposals                                                  | <b>(92)</b>                | <b>(3)</b>                                                 | <b>(95)</b>             |
| Revaluation                                                | <b>1,954</b>               | –                                                          | <b>1,954</b>            |
| Depreciation for the period (Note 12)                      | <b>(234)</b>               | <b>(322)</b>                                               | <b>(556)</b>            |
| Reclassification from/(to) investment properties (Note 25) | <b>494</b>                 | <b>(13)</b>                                                | <b>481</b>              |
| Transfer                                                   | <b>47</b>                  | <b>(47)</b>                                                | –                       |
| Exchange difference                                        | <b>2</b>                   | <b>1</b>                                                   | <b>3</b>                |
| Net book value at 30 June 2010                             | <b>25,887</b>              | <b>2,348</b>                                               | <b>28,235</b>           |
| At 30 June 2010                                            |                            |                                                            |                         |
| Cost or valuation                                          | <b>25,887</b>              | <b>6,514</b>                                               | <b>32,401</b>           |
| Accumulated depreciation and impairment                    | –                          | <b>(4,166)</b>                                             | <b>(4,166)</b>          |
| Net book value at 30 June 2010                             | <b>25,887</b>              | <b>2,348</b>                                               | <b>28,235</b>           |

**26. Properties, plant and equipment (continued)**

|                                                        | Premises<br>HK\$'m | Equipment,<br>fixtures and<br>fittings<br>HK\$'m | Total<br>HK\$'m |
|--------------------------------------------------------|--------------------|--------------------------------------------------|-----------------|
| Net book value at 1 January 2009                       | 20,105             | 2,690                                            | 22,795          |
| Additions                                              | 1                  | 573                                              | 574             |
| Disposals                                              | (140)              | (12)                                             | (152)           |
| Revaluation                                            | 4,247              | –                                                | 4,247           |
| Depreciation for the year                              | (386)              | (632)                                            | (1,018)         |
| Reclassification to investment properties<br>(Note 25) | (157)              | (3)                                              | (160)           |
| Transfer                                               | 31                 | (31)                                             | –               |
| Net book value at 31 December 2009                     | 23,701             | 2,585                                            | 26,286          |
| At 31 December 2009                                    |                    |                                                  |                 |
| Cost or valuation                                      | 23,701             | 6,531                                            | 30,232          |
| Accumulated depreciation and impairment                | –                  | (3,946)                                          | (3,946)         |
| Net book value at 31 December 2009                     | 23,701             | 2,585                                            | 26,286          |

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

|                     | Premises<br>HK\$'m | Equipment,<br>fixtures and<br>fittings<br>HK\$'m | Total<br>HK\$'m |
|---------------------|--------------------|--------------------------------------------------|-----------------|
| At 30 June 2010     |                    |                                                  |                 |
| At cost             | –                  | 6,514                                            | 6,514           |
| At valuation        | 25,887             | –                                                | 25,887          |
|                     | 25,887             | 6,514                                            | 32,401          |
| At 31 December 2009 |                    |                                                  |                 |
| At cost             | –                  | 6,531                                            | 6,531           |
| At valuation        | 23,701             | –                                                | 23,701          |
|                     | 23,701             | 6,531                                            | 30,232          |

**27. Other assets**

|                                     | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|-------------------------------------|---------------------------------------|----------------------------------|
| Reposessed assets                   | <b>41</b>                             | 95                               |
| Precious metals                     | <b>2,418</b>                          | 2,432                            |
| Accounts receivable and prepayments | <b>14,301</b>                         | 11,800                           |
|                                     | <b>16,760</b>                         | 14,327                           |

**28. Financial liabilities at fair value through profit or loss**

|                                                                       | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|-----------------------------------------------------------------------|---------------------------------------|----------------------------------|
| Trading liabilities                                                   |                                       |                                  |
| – Short positions in Exchange Fund Bills                              | <b>26,350</b>                         | 14,156                           |
| Financial liabilities designated at fair value through profit or loss |                                       |                                  |
| – Structured deposits (Note 29)                                       | <b>526</b>                            | 2,132                            |
|                                                                       | <b>26,876</b>                         | 16,288                           |

The carrying amount of financial liabilities designated at fair value through profit or loss as at 30 June 2010 is more than the amount that the Group would be contractually required to pay at maturity to the holders by HK\$2 million, and it was less than the amount that the Group would be contractually required to pay at maturity to the holders by HK\$1 million as at 31 December 2009. The amount of change in the fair values of financial liabilities at fair value through profit or loss, during the period and cumulatively, attributable to changes in credit risk is insignificant.

**29. Deposits from customers**

|                                                                                                         | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|---------------------------------------------------------------------------------------------------------|---------------------------------------|-------------------------------------------|
| Current, savings and other deposit accounts<br>(per condensed consolidated balance sheet)               | <b>892,211</b>                        | 842,321                                   |
| Structured deposits reported as financial liabilities<br>at fair value through profit or loss (Note 28) | <b>526</b>                            | 2,132                                     |
|                                                                                                         | <b>892,737</b>                        | 844,453                                   |
| Analysed by:                                                                                            |                                       |                                           |
| Demand deposits and current accounts                                                                    |                                       |                                           |
| – corporate customers                                                                                   | <b>52,541</b>                         | 51,043                                    |
| – individual customers                                                                                  | <b>14,581</b>                         | 14,397                                    |
|                                                                                                         | <b>67,122</b>                         | 65,440                                    |
| Savings deposits                                                                                        |                                       |                                           |
| – corporate customers                                                                                   | <b>133,195</b>                        | 141,560                                   |
| – individual customers                                                                                  | <b>340,297</b>                        | 353,952                                   |
|                                                                                                         | <b>473,492</b>                        | 495,512                                   |
| Time, call and notice deposits                                                                          |                                       |                                           |
| – corporate customers                                                                                   | <b>166,910</b>                        | 110,941                                   |
| – individual customers                                                                                  | <b>185,213</b>                        | 172,560                                   |
|                                                                                                         | <b>352,123</b>                        | 283,501                                   |
|                                                                                                         | <b>892,737</b>                        | 844,453                                   |

**30. Other accounts and provisions**

|                        | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|------------------------|---------------------------------------|-------------------------------------------|
| Other accounts payable | <b>34,418</b>                         | 29,592                                    |
| Provisions             | <b>272</b>                            | 338                                       |
|                        | <b>34,690</b>                         | 29,930                                    |

**31. Assets pledged as security**

As at 30 June 2010, liabilities of the Group amounting to HK\$26,041 million (31 December 2009: HK\$13,330 million) were secured by assets deposited with central depositories to facilitate settlement operations. In addition, the liabilities of the Group amounting to HK\$10,598 million (31 December 2009: Nil) were secured by debt securities related to sale and repurchase arrangements. The amount of assets pledged by the Group to secure these liabilities was HK\$40,557 million (31 December 2009: HK\$13,407 million) included in "Trading securities" and "Available-for-sale securities".

### 32. Deferred taxation

Deferred tax is recognised in respect of the temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in this interim financial information in accordance with HKAS 12 “Income Taxes”.

The major components of deferred tax (assets)/liabilities recorded in the condensed consolidated balance sheet, and the movements during the first half of 2010 and the year ended 31 December 2009 are as follows:

|                                                               | At 30 June 2010                    |                         |        |                         |                                   |        |
|---------------------------------------------------------------|------------------------------------|-------------------------|--------|-------------------------|-----------------------------------|--------|
|                                                               | Accelerated<br>tax<br>depreciation | Property<br>revaluation | Losses | Impairment<br>allowance | Other<br>temporary<br>differences | Total  |
|                                                               | HK\$'m                             | HK\$'m                  | HK\$'m | HK\$'m                  | HK\$'m                            | HK\$'m |
| At 1 January 2010                                             | 540                                | 4,359                   | (139)  | (274)                   | (44)                              | 4,442  |
| (Credited)/charged to condensed<br>income statement (Note 15) | (14)                               | 26                      | 24     | (28)                    | 12                                | 20     |
| Charged to other comprehensive<br>income                      | –                                  | 316                     | –      | –                       | 252                               | 568    |
| At 30 June 2010                                               | 526                                | 4,701                   | (115)  | (302)                   | 220                               | 5,030  |

|                                           | At 31 December 2009                |                         |        |                         |                                   |        |
|-------------------------------------------|------------------------------------|-------------------------|--------|-------------------------|-----------------------------------|--------|
|                                           | Accelerated<br>tax<br>depreciation | Property<br>revaluation | Losses | Impairment<br>allowance | Other<br>temporary<br>differences | Total  |
|                                           | HK\$'m                             | HK\$'m                  | HK\$'m | HK\$'m                  | HK\$'m                            | HK\$'m |
| At 1 January 2009                         | 545                                | 3,464                   | (126)  | (254)                   | (984)                             | 2,645  |
| (Credited)/charged to income<br>statement | (5)                                | 214                     | (13)   | (20)                    | 49                                | 225    |
| Charged to other comprehensive<br>income  | –                                  | 681                     | –      | –                       | 891                               | 1,572  |
| At 31 December 2009                       | 540                                | 4,359                   | (139)  | (274)                   | (44)                              | 4,442  |

**32. Deferred taxation (continued)**

Deferred tax assets and liabilities are offset on an individual entity basis when there is a legal right to set off current tax assets against current tax liabilities and when the deferred taxation relates to the same authority. The following amounts, determined after appropriate offsetting, are shown in the condensed consolidated balance sheet:

|                          | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|--------------------------|---------------------------------------|----------------------------------|
| Deferred tax assets      | <b>(128)</b>                          | (149)                            |
| Deferred tax liabilities | <b>5,158</b>                          | 4,591                            |
|                          | <b>5,030</b>                          | 4,442                            |

|                                                                      | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|----------------------------------------------------------------------|---------------------------------------|----------------------------------|
| Deferred tax assets to be recovered after more than twelve months    | <b>(112)</b>                          | (137)                            |
| Deferred tax liabilities to be settled after more than twelve months | <b>4,934</b>                          | 4,633                            |
|                                                                      | <b>4,822</b>                          | 4,496                            |

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

|                                                     | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|-----------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| Fair value changes of available-for-sale securities | <b>253</b>                                         | 552                                       |
| Revaluation of premises                             | <b>314</b>                                         | 195                                       |
| Non-controlling interests                           | <b>1</b>                                           | –                                         |
|                                                     | <b>568</b>                                         | 747                                       |

**33. Insurance contract liabilities**

|                                             | At 30 June 2010 |                       |               |
|---------------------------------------------|-----------------|-----------------------|---------------|
|                                             | Gross<br>HK\$'m | Reinsurance<br>HK\$'m | Net<br>HK\$'m |
| At 1 January 2010                           | 33,408          | –                     | 33,408        |
| Benefits paid                               | (2,119)         | –                     | (2,119)       |
| Claims incurred and movement in liabilities | 3,761           | (2)                   | 3,759         |
| At 30 June 2010                             | 35,050          | (2)                   | 35,048        |

|                                             | At 31 December 2009 |                       |               |
|---------------------------------------------|---------------------|-----------------------|---------------|
|                                             | Gross<br>HK\$'m     | Reinsurance<br>HK\$'m | Net<br>HK\$'m |
| At 1 January 2009                           | 28,274              | –                     | 28,274        |
| Benefits paid                               | (2,012)             | –                     | (2,012)       |
| Claims incurred and movement in liabilities | 7,146               | –                     | 7,146         |
| At 31 December 2009                         | 33,408              | –                     | 33,408        |

Amounts recoverable from reinsurance of insurance contract liabilities are included in the condensed consolidated balance sheet in "Other assets".

**34. Subordinated liabilities**

|                                                                                   | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|-----------------------------------------------------------------------------------|---------------------------------------|----------------------------------|
| <b>Subordinated loans, at amortised cost</b>                                      |                                       |                                  |
| EUR 660m*                                                                         | <b>6,277</b>                          | 7,377                            |
| USD2,500m**                                                                       | –                                     | 19,399                           |
|                                                                                   | <b>6,277</b>                          | 26,776                           |
| <b>Subordinated notes, at amortised cost with<br/>fair value hedge adjustment</b> |                                       |                                  |
| USD2,500m***                                                                      | <b>20,915</b>                         | –                                |
| Total                                                                             | <b>27,192</b>                         | 26,776                           |

BOCHK obtained floating-rate subordinated loans from BOC, the intermediate holding company in 2008. The subordinated loans are repayable prior to maturity after the first 5-year tenure at the option of the borrower.

During the period, BOCHK issued listed subordinated notes with an aggregate amount of US\$2,500 million and applied the proceeds to repay the USD subordinated loan provided by BOC in December 2008. HKMA has approved such early repayment of the USD subordinated loan provided by BOC. BOC and BOCHK entered into an agreement to provide for the same.

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

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

\*\* Interest rate at 6-month LIBOR plus 2.00% for the first 5 years, 6-month LIBOR plus 2.50% for the remaining tenure payable semi-annually, due December 2018. It has been fully repaid during the period by the proceeds from the offering of subordinated notes.

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

**35. Share capital**

|                                              | <b>At 30 June<br/>2010<br/>HK\$'m</b> | At 31 December<br>2009<br>HK\$'m |
|----------------------------------------------|---------------------------------------|----------------------------------|
| Authorised:                                  |                                       |                                  |
| 20,000,000,000 ordinary shares of HK\$5 each | <b>100,000</b>                        | 100,000                          |
| Issued and fully paid:                       |                                       |                                  |
| 10,572,780,266 ordinary shares of HK\$5 each | <b>52,864</b>                         | 52,864                           |

**36. Reserves**

The Group's reserves and the movements therein for the current and prior periods are presented in the condensed consolidated statement of changes in equity on page 47.

**37. Notes to condensed consolidated cash flow statement****(a) Reconciliation of operating profit to operating cash inflow/(outflow) before taxation**

|                                                                                                                  | Half-year ended<br>30 June 2010<br>HK\$'m | Half-year ended<br>30 June 2009<br>HK\$'m |
|------------------------------------------------------------------------------------------------------------------|-------------------------------------------|-------------------------------------------|
| Operating profit                                                                                                 | 8,168                                     | 7,719                                     |
| Depreciation                                                                                                     | 556                                       | 496                                       |
| Net (reversal)/charge of impairment allowances                                                                   | (161)                                     | 1,115                                     |
| Unwind of discount on impairment                                                                                 | (5)                                       | (8)                                       |
| Advances written off net of recoveries                                                                           | 115                                       | (213)                                     |
| Interest expense on subordinated liabilities                                                                     | 489                                       | 546                                       |
| Change in subordinated liabilities                                                                               | 240                                       | –                                         |
| Change in cash and balances with banks and other financial institutions with original maturity over three months | 5,726                                     | 13,201                                    |
| Change in placements with banks and other financial institutions with original maturity over three months        | 21,741                                    | (18,391)                                  |
| Change in financial assets at fair value through profit or loss                                                  | (17,019)                                  | 6,001                                     |
| Change in derivative financial instruments                                                                       | 247                                       | (5,318)                                   |
| Change in advances and other accounts                                                                            | (70,191)                                  | (15,582)                                  |
| Change in investment in securities                                                                               | (3,771)                                   | 193                                       |
| Change in other assets                                                                                           | (2,438)                                   | (5,961)                                   |
| Change in deposits and balances of banks and other financial institutions                                        | 11,139                                    | (11,663)                                  |
| Change in financial liabilities at fair value through profit or loss                                             | 10,588                                    | (11,076)                                  |
| Change in deposits from customers                                                                                | 49,890                                    | 18,400                                    |
| Change in debt securities in issue at amortised cost                                                             | –                                         | (906)                                     |
| Change in other accounts and provisions                                                                          | 4,760                                     | (3,328)                                   |
| Change in insurance contract liabilities                                                                         | 1,642                                     | (579)                                     |
| Exchange difference                                                                                              | 26                                        | –                                         |
| Operating cash inflow/(outflow) before taxation                                                                  | 21,742                                    | (25,354)                                  |
| Cash flows from operating activities included:                                                                   |                                           |                                           |
| – Interest received                                                                                              | 10,135                                    | 13,466                                    |
| – Interest paid                                                                                                  | 873                                       | 4,109                                     |
| – Dividend received                                                                                              | 54                                        | 13                                        |

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

|                                                                                                          | At 30 June<br>2010<br>HK\$'m | At 30 June<br>2009<br>HK\$'m |
|----------------------------------------------------------------------------------------------------------|------------------------------|------------------------------|
| Cash and balances with banks and other financial institutions with original maturity within three months | 158,378                      | 100,968                      |
| Placements with banks and other financial institutions with original maturity within three months        | 12,769                       | 27,156                       |
| Treasury bills with original maturity within three months                                                | 26,629                       | 19,412                       |
| Certificates of deposit held with original maturity within three months                                  | –                            | 1,000                        |
|                                                                                                          | 197,776                      | 148,536                      |

**38. Contingent liabilities and commitments**

The following is a summary of the contractual amounts of each significant class of contingent liability and commitment and the corresponding aggregate credit risk weighted amount:

|                                                                       | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|-----------------------------------------------------------------------|---------------------------------------|-------------------------------------------|
| Direct credit substitutes                                             | <b>4,218</b>                          | 2,065                                     |
| Transaction-related contingencies                                     | <b>6,544</b>                          | 9,055                                     |
| Trade-related contingencies                                           | <b>33,401</b>                         | 31,460                                    |
| Note issuance and revolving underwriting facilities                   | <b>1,148</b>                          | –                                         |
| Commitments that are unconditionally cancellable without prior notice | <b>193,457</b>                        | 165,829                                   |
| Other commitments with an original maturity of                        |                                       |                                           |
| – up to one year                                                      | <b>25,494</b>                         | 15,842                                    |
| – over one year                                                       | <b>53,644</b>                         | 52,173                                    |
|                                                                       | <b>317,906</b>                        | 276,424                                   |
| Credit risk weighted amount                                           | <b>37,950</b>                         | 35,229                                    |

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

**39. Capital commitments**

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

|                                                    | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|----------------------------------------------------|---------------------------------------|-------------------------------------------|
| Authorised and contracted for but not provided for | <b>187</b>                            | 96                                        |
| Authorised but not contracted for                  | <b>28</b>                             | 9                                         |
|                                                    | <b>215</b>                            | 105                                       |

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

**40. Operating lease commitments****(a) The Group as lessee**

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

|                                                     | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|-----------------------------------------------------|---------------------------------------|-------------------------------------------|
| Land and buildings                                  |                                       |                                           |
| – not later than one year                           | <b>408</b>                            | 435                                       |
| – later than one year but not later than five years | <b>390</b>                            | 450                                       |
| – later than five years                             | <b>20</b>                             | 13                                        |
|                                                     | <b>818</b>                            | 898                                       |

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

**(b) The Group as lessor**

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

|                                                     | <b>At 30 June<br/>2010<br/>HK\$'m</b> | <b>At 31 December<br/>2009<br/>HK\$'m</b> |
|-----------------------------------------------------|---------------------------------------|-------------------------------------------|
| Land and buildings                                  |                                       |                                           |
| – not later than one year                           | <b>280</b>                            | 275                                       |
| – later than one year but not later than five years | <b>224</b>                            | 193                                       |
|                                                     | <b>504</b>                            | 468                                       |

The Group leases its investment properties under operating lease arrangements, with leases typically for a period from one to three years. The terms of the leases generally require the tenants to pay security deposits and provide for periodic rent adjustments according to the prevailing market conditions. None of the leases include contingent rentals.

#### 41. Segmental reporting

The Group engages in many businesses in several regions. For segmental reporting purposes, information is solely provided in respect of business segments. Geographical segment information is not presented because over 90% of the Group's revenues, profits before tax and assets are derived from Hong Kong.

Information about the four business segments is provided in segmental reporting. They are Personal Banking, Corporate Banking, Treasury and Insurance. The classification of the Group's operating segments is based on customer segment and product type, which is aligned with the RPC (relationship, product and channel) management model of the Group.

In this period, customer segment of small business and social organisations was reclassified from Corporate Banking to Personal Banking to align with the corresponding change in the management of customer segment. No change has been made to the comparative figures.

Both Personal Banking and Corporate Banking segments provide general banking services. Personal Banking mainly serves individual customers while Corporate Banking mainly deals with non individual customers. The Treasury segment is responsible for managing the capital, liquidity, and the interest rate and foreign exchange positions of the Group in addition to proprietary trades. The Insurance segment shows business relates to the long-term life insurance products, including traditional and linked individual life insurance and group life insurance products. "Others" refers to those items related to the Group as a whole rather than directly attributable to the other four business segments, including the Group's holdings of premises, investment properties, equity investments and interests in associates.

Revenues, expenses, assets and liabilities of any business segment mainly include items directly attributable to the segment. In relation to occupation of the Group's premises, rentals are internally charged on market rates according to the areas occupied. For management overheads, allocations are made on reasonable bases. Inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group.

## 41. Segmental reporting (continued)

|                                                                                         | Personal<br>HK\$'m | Corporate<br>HK\$'m | Treasury<br>HK\$'m | Insurance<br>HK\$'m | Others<br>HK\$'m | Subtotal<br>HK\$'m | Eliminations<br>HK\$'m | Consolidated<br>HK\$'m |
|-----------------------------------------------------------------------------------------|--------------------|---------------------|--------------------|---------------------|------------------|--------------------|------------------------|------------------------|
| <b>Half-year ended 30 June 2010</b>                                                     |                    |                     |                    |                     |                  |                    |                        |                        |
| Net interest income/(expense)                                                           |                    |                     |                    |                     |                  |                    |                        |                        |
| – external                                                                              | 1,358              | 3,235               | 3,647              | 724                 | –                | 8,964              | –                      | 8,964                  |
| – inter-segment                                                                         | 1,574              | (240)               | (1,306)            | –                   | (28)             | –                  | –                      | –                      |
|                                                                                         | 2,932              | 2,995               | 2,341              | 724                 | (28)             | 8,964              | –                      | 8,964                  |
| Net fee and commission<br>income/(expense)                                              | 2,160              | 1,382               | (4)                | (154)               | 67               | 3,451              | (54)                   | 3,397                  |
| Net trading gain/(loss)                                                                 | 205                | 81                  | (296)              | (4)                 | (18)             | (32)               | (4)                    | (36)                   |
| Net gain on financial<br>instruments designated at fair<br>value through profit or loss | –                  | –                   | 49                 | 591                 | –                | 640                | –                      | 640                    |
| Net gain on investment in<br>securities                                                 | –                  | –                   | 286                | 118                 | –                | 404                | –                      | 404                    |
| Net insurance premium income                                                            | –                  | –                   | –                  | 2,802               | –                | 2,802              | (4)                    | 2,798                  |
| Other operating income                                                                  | 19                 | 1                   | –                  | 8                   | 968              | 996                | (747)                  | 249                    |
| <b>Total operating income</b>                                                           | <b>5,316</b>       | <b>4,459</b>        | <b>2,376</b>       | <b>4,085</b>        | <b>989</b>       | <b>17,225</b>      | <b>(809)</b>           | <b>16,416</b>          |
| Net insurance benefits and<br>claims                                                    | –                  | –                   | –                  | (3,875)             | –                | (3,875)            | –                      | (3,875)                |
| <b>Net operating income before<br/>impairment allowances</b>                            | <b>5,316</b>       | <b>4,459</b>        | <b>2,376</b>       | <b>210</b>          | <b>989</b>       | <b>13,350</b>      | <b>(809)</b>           | <b>12,541</b>          |
| Net (charge)/reversal of<br>impairment allowances                                       | (42)               | 131                 | 72                 | –                   | –                | 161                | –                      | 161                    |
| <b>Net operating income</b>                                                             | <b>5,274</b>       | <b>4,590</b>        | <b>2,448</b>       | <b>210</b>          | <b>989</b>       | <b>13,511</b>      | <b>(809)</b>           | <b>12,702</b>          |
| Operating expenses                                                                      | (3,044)            | (1,232)             | (330)              | (104)               | (633)            | (5,343)            | 809                    | (4,534)                |
| <b>Operating profit</b>                                                                 | <b>2,230</b>       | <b>3,358</b>        | <b>2,118</b>       | <b>106</b>          | <b>356</b>       | <b>8,168</b>       | <b>–</b>               | <b>8,168</b>           |
| Net gain from disposal of/<br>fair value adjustments on<br>investment properties        | –                  | –                   | –                  | –                   | 601              | 601                | –                      | 601                    |
| Net loss from disposal/<br>revaluation of properties,<br>plant and equipment            | –                  | –                   | –                  | –                   | (1)              | (1)                | –                      | (1)                    |
| Share of profits less losses after<br>tax of associates                                 | –                  | –                   | –                  | –                   | (1)              | (1)                | –                      | (1)                    |
| <b>Profit before taxation</b>                                                           | <b>2,230</b>       | <b>3,358</b>        | <b>2,118</b>       | <b>106</b>          | <b>955</b>       | <b>8,767</b>       | <b>–</b>               | <b>8,767</b>           |
| <b>At 30 June 2010</b>                                                                  |                    |                     |                    |                     |                  |                    |                        |                        |
| <b>Assets</b>                                                                           |                    |                     |                    |                     |                  |                    |                        |                        |
| Segment assets                                                                          | 191,760            | 427,618             | 608,925            | 40,153              | 44,727           | 1,313,183          | (11,220)               | 1,301,963              |
| Interests in associates                                                                 | –                  | –                   | –                  | –                   | 213              | 213                | –                      | 213                    |
|                                                                                         | 191,760            | 427,618             | 608,925            | 40,153              | 44,940           | 1,313,396          | (11,220)               | 1,302,176              |
| <b>Liabilities</b>                                                                      |                    |                     |                    |                     |                  |                    |                        |                        |
| Segment liabilities                                                                     | 612,200            | 313,592             | 227,112            | 37,459              | 13,496           | 1,203,859          | (11,220)               | 1,192,639              |
| <b>Half-year ended 30 June 2010</b>                                                     |                    |                     |                    |                     |                  |                    |                        |                        |
| <b>Other information</b>                                                                |                    |                     |                    |                     |                  |                    |                        |                        |
| Capital expenditure                                                                     | 1                  | 1                   | –                  | –                   | 162              | 164                | –                      | 164                    |
| Depreciation                                                                            | 154                | 78                  | 36                 | 2                   | 286              | 556                | –                      | 556                    |
| Amortisation of securities                                                              | –                  | –                   | 25                 | 47                  | –                | 72                 | –                      | 72                     |

## 41. Segmental reporting (continued)

|                                                                                          | Personal<br>HK\$'m | Corporate<br>HK\$'m | Treasury<br>HK\$'m | Insurance<br>HK\$'m | Others<br>HK\$'m | Subtotal<br>HK\$'m | Eliminations<br>HK\$'m | Consolidated<br>HK\$'m |
|------------------------------------------------------------------------------------------|--------------------|---------------------|--------------------|---------------------|------------------|--------------------|------------------------|------------------------|
| <b>Half-year ended 30 June 2009</b>                                                      |                    |                     |                    |                     |                  |                    |                        |                        |
| Net interest income/(expense)                                                            |                    |                     |                    |                     |                  |                    |                        |                        |
| – external                                                                               | 902                | 3,027               | 4,525              | 562                 | (2)              | 9,014              | –                      | 9,014                  |
| – inter-segment                                                                          | 1,947              | (383)               | (1,526)            | –                   | (38)             | –                  | –                      | –                      |
|                                                                                          | 2,849              | 2,644               | 2,999              | 562                 | (40)             | 9,014              | –                      | 9,014                  |
| Net fee and commission income/(expense)                                                  | 1,970              | 1,100               | (4)                | (124)               | 50               | 2,992              | (45)                   | 2,947                  |
| Net trading gain/(loss)                                                                  | 236                | 67                  | 502                | –                   | (1)              | 804                | –                      | 804                    |
| Net gain/(loss) on financial instruments designated at fair value through profit or loss | –                  | –                   | 180                | (1,575)             | –                | (1,395)            | –                      | (1,395)                |
| Net gain on investment in securities                                                     | –                  | –                   | 67                 | –                   | –                | 67                 | –                      | 67                     |
| Net insurance premium income                                                             | –                  | –                   | –                  | 2,267               | –                | 2,267              | (6)                    | 2,261                  |
| Other operating income                                                                   | 12                 | 30                  | 2                  | 5                   | 880              | 929                | (680)                  | 249                    |
| <b>Total operating income</b>                                                            | 5,067              | 3,841               | 3,746              | 1,135               | 889              | 14,678             | (731)                  | 13,947                 |
| Net insurance benefits and claims                                                        | –                  | –                   | –                  | (919)               | –                | (919)              | –                      | (919)                  |
| <b>Net operating income before impairment allowances</b>                                 | 5,067              | 3,841               | 3,746              | 216                 | 889              | 13,759             | (731)                  | 13,028                 |
| Net (charge)/reversal of impairment allowances                                           | (80)               | 133                 | (1,168)            | –                   | –                | (1,115)            | –                      | (1,115)                |
| <b>Net operating income</b>                                                              | 4,987              | 3,974               | 2,578              | 216                 | 889              | 12,644             | (731)                  | 11,913                 |
| Operating expenses                                                                       | (2,771)            | (1,039)             | (394)              | (61)                | (660)            | (4,925)            | 731                    | (4,194)                |
| <b>Operating profit</b>                                                                  | 2,216              | 2,935               | 2,184              | 155                 | 229              | 7,719              | –                      | 7,719                  |
| Net gain from disposal of/ fair value adjustments on investment properties               | –                  | –                   | –                  | –                   | 525              | 525                | –                      | 525                    |
| Net loss from disposal/ revaluation of properties, plant and equipment                   | –                  | –                   | –                  | –                   | (1)              | (1)                | –                      | (1)                    |
| Share of profits less losses after tax of associates                                     | –                  | –                   | –                  | –                   | 1                | 1                  | –                      | 1                      |
| <b>Profit before taxation</b>                                                            | 2,216              | 2,935               | 2,184              | 155                 | 754              | 8,244              | –                      | 8,244                  |
| <b>At 31 December 2009</b>                                                               |                    |                     |                    |                     |                  |                    |                        |                        |
| <b>Assets</b>                                                                            |                    |                     |                    |                     |                  |                    |                        |                        |
| Segment assets*                                                                          | 178,026            | 372,443             | 593,807            | 37,963              | 45,007           | 1,227,246          | (14,672)               | 1,212,574              |
| Interests in associates                                                                  | –                  | –                   | –                  | –                   | 217              | 217                | –                      | 217                    |
|                                                                                          | 178,026            | 372,443             | 593,807            | 37,963              | 45,224           | 1,227,463          | (14,672)               | 1,212,791              |
| <b>Liabilities</b>                                                                       |                    |                     |                    |                     |                  |                    |                        |                        |
| Segment liabilities*                                                                     | 570,566            | 304,882             | 195,956            | 35,355              | 15,069           | 1,121,828          | (14,672)               | 1,107,156              |
| <b>Half-year ended 30 June 2009</b>                                                      |                    |                     |                    |                     |                  |                    |                        |                        |
| <b>Other information</b>                                                                 |                    |                     |                    |                     |                  |                    |                        |                        |
| Capital expenditure                                                                      | 5                  | –                   | –                  | 1                   | 143              | 149                | –                      | 149                    |
| Depreciation                                                                             | 141                | 71                  | 52                 | 1                   | 231              | 496                | –                      | 496                    |
| Amortisation of securities                                                               | –                  | –                   | (310)              | 111                 | –                | (199)              | –                      | (199)                  |

\* Segment assets and liabilities of small business and social organisations amounted to HK\$9,624 million and HK\$39,677 million respectively as at 31 December 2009.

## 42. Significant related party transactions

Related parties are those parties that have the ability to control the other party or exercise significant influence over the other party in making financial or operating decisions. Parties are also considered to be related if they are subject to common control. Related parties may be individual or other entities.

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

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

#### (i) **General information of the parent companies**

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

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

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

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

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

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

- lending, provision of credits and guarantees, and deposit taking;
- inter-bank balance taking and placing;
- sales, purchase, underwriting and redemption of bonds issued by other state-controlled entities;
- rendering of foreign exchange, remittance and investment related services;
- provision of fiduciary activities; and
- purchase of utilities, transport, telecommunication and postage services.

**42. Significant related party transactions (continued)****(b) Summary of transactions entered into during the ordinary course of business with associates and other related parties**

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

|                                                  | Half-year ended 30 June 2010 |                                    |
|--------------------------------------------------|------------------------------|------------------------------------|
|                                                  | Associates<br>HK\$'m         | Other related<br>parties<br>HK\$'m |
| Income statement items:                          |                              |                                    |
| Administrative services fees received/receivable | –                            | 4                                  |
|                                                  |                              |                                    |
|                                                  | At 30 June 2010              |                                    |
|                                                  | Associates<br>HK\$'m         | Other related<br>parties<br>HK\$'m |
| Balance sheet items:                             |                              |                                    |
| Deposits from customers                          | 164                          | –                                  |
|                                                  |                              |                                    |
|                                                  | Half-year ended 30 June 2009 |                                    |
|                                                  | Associates<br>HK\$'m         | Other related<br>parties<br>HK\$'m |
| Income statement items:                          |                              |                                    |
| Administrative services fees received/receivable | –                            | 4                                  |
|                                                  |                              |                                    |
|                                                  | At 31 December 2009          |                                    |
|                                                  | Associates<br>HK\$'m         | Other related<br>parties<br>HK\$'m |
| Balance sheet items:                             |                              |                                    |
| Deposits from customers                          | 51                           | –                                  |

**42. Significant related party transactions (continued)****(c) Key management personnel**

Key management are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including directors and senior management. The Group accepts deposits from and grants loans and credit facilities to key management personnel in the ordinary course of business. During both the current and prior periods, no material transaction was conducted with key management personnel of BOCHK, its holding companies and parties related to them.

The key management compensation for the six months ended 30 June 2010 and 2009 is detailed as follows:

|                                                 | <b>Half-year ended<br/>30 June 2010<br/>HK\$'m</b> | Half-year ended<br>30 June 2009<br>HK\$'m |
|-------------------------------------------------|----------------------------------------------------|-------------------------------------------|
| Salaries and other short-term employee benefits | <b>23</b>                                          | 22                                        |
| Post-employment benefits                        | <b>1</b>                                           | 1                                         |
|                                                 | <b>24</b>                                          | 23                                        |

**43. Currency concentrations**

The following is a summary of the major foreign currency exposures arising from trading, non-trading and structural positions. The net options position is calculated based on the basis of delta-weighted positions of all foreign exchange options contracts.

|                           | <b>At 30 June 2010</b>               |                         |              |                               |                           |                 |               |              |
|---------------------------|--------------------------------------|-------------------------|--------------|-------------------------------|---------------------------|-----------------|---------------|--------------|
|                           | <b>Equivalent in million of HK\$</b> |                         |              |                               |                           |                 |               |              |
|                           | <b>US<br/>Dollars</b>                | <b>Japanese<br/>Yen</b> | <b>Euro</b>  | <b>Australian<br/>Dollars</b> | <b>Pound<br/>Sterling</b> | <b>Renminbi</b> | <b>Others</b> | <b>Total</b> |
| Spot assets               | 417,272                              | 5,427                   | 31,529       | 50,098                        | 3,265                     | 125,175         | 12,726        | 645,492      |
| Spot liabilities          | (266,155)                            | (2,214)                 | (22,447)     | (36,236)                      | (16,879)                  | (122,910)       | (21,898)      | (488,739)    |
| Forward purchases         | 433,536                              | 28,051                  | 24,041       | 24,741                        | 33,757                    | 119,941         | 33,469        | 697,536      |
| Forward sales             | (577,768)                            | (31,222)                | (33,297)     | (38,578)                      | (20,061)                  | (119,401)       | (24,294)      | (844,621)    |
| Net options position      | 36                                   | 1                       | –            | (47)                          | (1)                       | –               | (3)           | (14)         |
| Net long/(short) position | <b>6,921</b>                         | <b>43</b>               | <b>(174)</b> | <b>(22)</b>                   | <b>81</b>                 | <b>2,805</b>    | <b>–</b>      | <b>9,654</b> |
| Net structural position   | <b>296</b>                           | <b>–</b>                | <b>–</b>     | <b>–</b>                      | <b>–</b>                  | <b>3,223</b>    | <b>–</b>      | <b>3,519</b> |

|                           | <b>At 31 December 2009</b>           |                         |             |                               |                           |                 |               |               |
|---------------------------|--------------------------------------|-------------------------|-------------|-------------------------------|---------------------------|-----------------|---------------|---------------|
|                           | <b>Equivalent in million of HK\$</b> |                         |             |                               |                           |                 |               |               |
|                           | <b>US<br/>Dollars</b>                | <b>Japanese<br/>Yen</b> | <b>Euro</b> | <b>Australian<br/>Dollars</b> | <b>Pound<br/>Sterling</b> | <b>Renminbi</b> | <b>Others</b> | <b>Total</b>  |
| Spot assets               | 368,346                              | 17,647                  | 40,265      | 43,780                        | 3,486                     | 80,453          | 14,894        | 568,871       |
| Spot liabilities          | (234,622)                            | (2,304)                 | (24,465)    | (30,795)                      | (15,579)                  | (79,443)        | (23,456)      | (410,664)     |
| Forward purchases         | 419,917                              | 19,012                  | 21,741      | 23,307                        | 31,121                    | 71,103          | 34,469        | 620,670       |
| Forward sales             | (542,094)                            | (34,296)                | (37,537)    | (36,557)                      | (19,273)                  | (70,644)        | (25,910)      | (766,311)     |
| Net options position      | 233                                  | (2)                     | (5)         | (7)                           | 1                         | –               | 7             | 227           |
| Net long/(short) position | <b>11,780</b>                        | <b>57</b>               | <b>(1)</b>  | <b>(272)</b>                  | <b>(244)</b>              | <b>1,469</b>    | <b>4</b>      | <b>12,793</b> |
| Net structural position   | <b>295</b>                           | <b>–</b>                | <b>–</b>    | <b>–</b>                      | <b>–</b>                  | <b>2,958</b>    | <b>–</b>      | <b>3,253</b>  |

**44. Cross-border claims**

The information on cross-border claims discloses exposures to foreign counterparties on which the ultimate risk lies, and is derived according to the location of the counterparties after taking into account any transfer of risk. In general, such transfer of risk takes place if the claims are guaranteed by a party in a country, which is different from that of the counterparty, or if the claims are on an overseas branch of a bank whose head office is located in another country. Only regions constituting 10% or more of the aggregate cross-border claims are analysed by geographical areas and disclosed as follows:

|                            | <b>Banks</b>   | <b>Public sector</b> | <b>Others</b>  | <b>Total</b>   |
|----------------------------|----------------|----------------------|----------------|----------------|
|                            | <b>HK\$'m</b>  | <b>entities</b>      | <b>HK\$'m</b>  | <b>HK\$'m</b>  |
|                            |                | <b>HK\$'m</b>        |                |                |
| <b>At 30 June 2010</b>     |                |                      |                |                |
| Asia, other than Hong Kong |                |                      |                |                |
| – Mainland China           | <b>124,327</b> | <b>86,495</b>        | <b>68,269</b>  | <b>279,091</b> |
| – Others                   | <b>55,981</b>  | <b>9,403</b>         | <b>26,146</b>  | <b>91,530</b>  |
|                            | <b>180,308</b> | <b>95,898</b>        | <b>94,415</b>  | <b>370,621</b> |
| North America              |                |                      |                |                |
| – United States            | <b>5,951</b>   | <b>42,362</b>        | <b>34,937</b>  | <b>83,250</b>  |
| – Others                   | <b>13,530</b>  | <b>1,974</b>         | <b>1,504</b>   | <b>17,008</b>  |
|                            | <b>19,481</b>  | <b>44,336</b>        | <b>36,441</b>  | <b>100,258</b> |
| Western Europe             |                |                      |                |                |
| – United Kingdom           | <b>32,900</b>  | <b>2,514</b>         | <b>678</b>     | <b>36,092</b>  |
| – Others                   | <b>64,888</b>  | <b>13,268</b>        | <b>5,794</b>   | <b>83,950</b>  |
|                            | <b>97,788</b>  | <b>15,782</b>        | <b>6,472</b>   | <b>120,042</b> |
| <b>Total</b>               | <b>297,577</b> | <b>156,016</b>       | <b>137,328</b> | <b>590,921</b> |

**44. Cross-border claims (continued)**

|                            | Banks<br>HK\$'m | Public sector<br>entities<br>HK\$'m | Others<br>HK\$'m | Total<br>HK\$'m |
|----------------------------|-----------------|-------------------------------------|------------------|-----------------|
| At 31 December 2009        |                 |                                     |                  |                 |
| Asia, other than Hong Kong |                 |                                     |                  |                 |
| – Mainland China           | 90,168          | 58,893                              | 46,813           | 195,874         |
| – Others                   | 62,519          | 17,048                              | 24,187           | 103,754         |
|                            | 152,687         | 75,941                              | 71,000           | 299,628         |
| North America              |                 |                                     |                  |                 |
| – United States            | 7,231           | 39,587                              | 32,240           | 79,058          |
| – Others                   | 12,493          | 1,754                               | 1,425            | 15,672          |
|                            | 19,724          | 41,341                              | 33,665           | 94,730          |
| Western Europe             |                 |                                     |                  |                 |
| – United Kingdom           | 40,345          | 912                                 | 1,474            | 42,731          |
| – Others                   | 94,822          | 10,952                              | 5,613            | 111,387         |
|                            | 135,167         | 11,864                              | 7,087            | 154,118         |
| Total                      | 307,578         | 129,146                             | 111,752          | 548,476         |

**45. Non-bank Mainland China exposures**

Non-bank counterparties are identified in accordance with the definitions set out in the prudential return “Quarterly Analysis of Loans and Advances and Provisions” issued by the HKMA. Exposures in Mainland China arising from non-bank counterparties are summarised as follows:

|                                                                                                                 | At 30 June 2010                           |                                            |                             |                                                                |
|-----------------------------------------------------------------------------------------------------------------|-------------------------------------------|--------------------------------------------|-----------------------------|----------------------------------------------------------------|
|                                                                                                                 | On-balance<br>sheet<br>exposure<br>HK\$'m | Off-balance<br>sheet<br>exposure<br>HK\$'m | Total<br>exposure<br>HK\$'m | Individually<br>assessed<br>impairment<br>allowances<br>HK\$'m |
| Mainland China entities                                                                                         | 118,694                                   | 55,997                                     | 174,691                     | 74                                                             |
| Companies and individuals outside<br>Mainland China where the credit<br>is granted for use in Mainland<br>China | 31,350                                    | 16,203                                     | 47,553                      | 25                                                             |
| Other non-bank Mainland China<br>exposures                                                                      | 26,449                                    | 10,083                                     | 36,532                      | 42                                                             |
|                                                                                                                 | 176,493                                   | 82,283                                     | 258,776                     | 141                                                            |

**45. Non-bank Mainland China exposures (continued)**

|                                                                                                                 | At 31 December 2009                       |                                            |                             |                                                                |
|-----------------------------------------------------------------------------------------------------------------|-------------------------------------------|--------------------------------------------|-----------------------------|----------------------------------------------------------------|
|                                                                                                                 | On-balance<br>sheet<br>exposure<br>HK\$'m | Off-balance<br>sheet<br>exposure<br>HK\$'m | Total<br>exposure<br>HK\$'m | Individually<br>assessed<br>impairment<br>allowances<br>HK\$'m |
| Mainland China entities                                                                                         | 101,935                                   | 44,217                                     | 146,152                     | 73                                                             |
| Companies and individuals outside<br>Mainland China where the credit<br>is granted for use in Mainland<br>China | 26,176                                    | 18,260                                     | 44,436                      | 81                                                             |
| Other non-bank Mainland China<br>exposures                                                                      | 22,203                                    | 7,605                                      | 29,808                      | 42                                                             |
|                                                                                                                 | 150,314                                   | 70,082                                     | 220,396                     | 196                                                            |

**46. Compliance with HKAS 34**

The interim report for the first half of 2010 complies with HKAS 34 "Interim Financial Reporting" issued by the HKICPA.

**47. Statutory accounts**

The information in this interim report is unaudited and does not constitute statutory accounts. The statutory accounts for the year ended 31 December 2009 have been delivered to the Registrar of Companies and the HKMA. The auditor expressed an unqualified opinion on those statutory accounts in their report dated 23 March 2010.

# ADDITIONAL INFORMATION

## 1. Corporate information

### **Board of Directors**

|                      |                                                                                                                                                                                                                                                              |
|----------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Chairman</b>      | XIAO Gang <sup>#</sup>                                                                                                                                                                                                                                       |
| <b>Vice Chairmen</b> | LI Lihui <sup>#</sup><br>HE Guangbei                                                                                                                                                                                                                         |
| <b>Directors</b>     | LI Zaohang <sup>#</sup><br>ZHOU Zaiqun <sup>#</sup><br>ZHANG Yanling <sup>#</sup><br>GAO Yingxin<br>FUNG Victor Kwok King*<br>KOH Beng Seng*<br>SHAN Weijian*<br>TUNG Chee Chen*<br>TUNG Savio Wai-Hok*<br>YANG Linda Tsao*<br>(retired from<br>21 May 2010) |

<sup>#</sup> Non-executive Directors

\* Independent Non-executive Directors

### **Senior Management**

|                                  |                                                                                                                   |
|----------------------------------|-------------------------------------------------------------------------------------------------------------------|
| <b>Chief Executive</b>           | HE Guangbei                                                                                                       |
| <b>Deputy Chief Executive</b>    | LAM Yim Nam                                                                                                       |
| <b>Deputy Chief Executive</b>    | GAO Yingxin                                                                                                       |
| <b>Chief Financial Officer</b>   | ZHUO Chengwen                                                                                                     |
| <b>Deputy Chief Executive</b>    | WONG David See Hong                                                                                               |
| <b>Chief Risk Officer</b>        | LI Jiuzhong<br>(appointed on<br>1 March 2010)<br>CHEUNG Yau Shing<br>(term of office ceased<br>from 1 March 2010) |
| <b>Chief Operating Officer</b>   | LEE Alex Wing Kwai                                                                                                |
| <b>Assistant Chief Executive</b> | ZHU Yan Lai                                                                                                       |
| <b>Company Secretary</b>         | YEUNG Jason Chi Wai                                                                                               |

### **Registered Office**

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

### **Auditor**

PricewaterhouseCoopers

### **Share Registrar**

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

### **ADS Depositary Bank**

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

### **Credit Ratings (Long Term)**

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

### **Index Constituent**

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

### **Stock Codes**

|                                             |           |
|---------------------------------------------|-----------|
| Ordinary shares:                            |           |
| The Stock Exchange of<br>Hong Kong Limited: | 2388      |
| Reuters:                                    | 2388.HK   |
| Bloomberg:                                  | 2388 HK   |
| Level 1 ADR Programme:                      |           |
| CUSIP No.:                                  | 096813209 |
| OTC Symbol:                                 | BHKLY     |

### **Website**

www.bochk.com

## 2. Dividend and closure of register of members

The Board declared an interim dividend of HK\$0.40 per share (2009: HK\$0.285), payable on Friday, 24 September 2010 to shareholders whose names appear on the Register of Members of the Company on Thursday, 16 September 2010.

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to the interim dividend, from Monday, 13 September 2010 to Thursday, 16 September 2010 (both days inclusive), during which period no transfer of shares will be registered. In order to qualify for the interim dividend, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, not later than 4:30 p.m. on Friday, 10 September 2010. Shares of the Company will be traded ex-dividend as from Thursday, 9 September 2010.

## 3. Substantial interests in share capital

The register maintained by the Company pursuant to section 336 of the SFO recorded that, as at 30 June 2010, the following parties had the following interests (as defined in the SFO) in the Company set opposite their respective names:

| Name of Corporation | No. of shares of HK\$5 each in the Company<br>(% of total issued shares) |          |
|---------------------|--------------------------------------------------------------------------|----------|
| Central Huijin      | 6,984,274,213                                                            | (66.06%) |
| BOC                 | 6,984,274,213                                                            | (66.06%) |
| BOCHKG              | 6,984,175,056                                                            | (66.06%) |
| BOC (BVI)           | 6,984,175,056                                                            | (66.06%) |

Notes:

- Following the reorganisation of BOC in August 2004, Central Huijin holds the controlling equity capital of BOC on behalf of the State. Accordingly, for the purpose of the SFO, Central Huijin is deemed to have the same interests in the Company as BOC.
- BOC holds the entire issued share capital of BOCHKG, which in turn holds the entire issued share capital of BOC (BVI). Accordingly, BOC and BOCHKG are deemed to have the same interests in the Company as BOC (BVI) for the purpose of the SFO. BOC (BVI) beneficially holds 6,984,175,056 shares of the Company.
- BOC holds the entire issued share capital of BOCI, which in turn holds the entire issued share capital of BOCI Asia Limited and BOCI Financial Products Limited. Accordingly, BOC is deemed to have the same interests in the Company as BOCI Asia Limited and BOCI Financial Products Limited for the purpose of the SFO. BOCI Asia Limited had an interest in 24,479 shares of the Company and an interest in 72,000 shares held under physically settled equity derivatives while BOCI Financial Products Limited had an interest in 2,678 shares of the Company.

All the interests stated above represented long positions. Save as disclosed above, as at 30 June 2010, BOCI Financial Products Limited had an interest in 143,522 shares which represented short positions. BOC and Central Huijin are deemed to be interested in such amount of shares for the purpose of the SFO. Save as disclosed, no other interests or short positions were recorded in the register maintained by the Company under section 336 of the SFO as at 30 June 2010.

#### 4. Directors' rights to acquire shares

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

Particulars of the outstanding options granted to the Directors under the Pre-Listing Share Option Scheme as at 30 June 2010 are set out below:

| Name of Director | Date of grant | Exercise price (HK\$) | Exercisable period          | Number of share options |                               |                             |                               |                          |                             |
|------------------|---------------|-----------------------|-----------------------------|-------------------------|-------------------------------|-----------------------------|-------------------------------|--------------------------|-----------------------------|
|                  |               |                       |                             | Granted on 5 July 2002  | Balances as at 1 January 2010 | Exercised during the period | Surrendered during the period | Lapsed during the period | Balances as at 30 June 2010 |
| LI Zaohang       | 5 July 2002   | 8.50                  | 25 July 2003 to 4 July 2012 | 1,446,000               | 1,446,000                     | -                           | -                             | -                        | 1,446,000                   |
| ZHOU Zaiqun      | 5 July 2002   | 8.50                  | 25 July 2003 to 4 July 2012 | 1,446,000               | 1,084,500                     | -                           | -                             | -                        | 1,084,500                   |
| ZHANG Yanling    | 5 July 2002   | 8.50                  | 25 July 2003 to 4 July 2012 | 1,446,000               | 1,446,000                     | -                           | -                             | -                        | 1,446,000                   |
| Total            |               |                       |                             | 4,338,000               | 3,976,500                     | -                           | -                             | -                        | 3,976,500                   |

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

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

As at 30 June 2010, the Directors, the Chief Executive and their respective associates had the following interests in the shares and underlying shares of the Company, as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers:

| Name of Director | Number of shares/underlying shares held |                  |                     |                 |           | % of the issued share capital |
|------------------|-----------------------------------------|------------------|---------------------|-----------------|-----------|-------------------------------|
|                  | Personal interests                      | Family interests | Corporate interests | Other interests | Total     |                               |
| HE Guangbei      | 100,000                                 | -                | -                   | -               | 100,000   | 0.001%                        |
| LI Zaohang       | 1,446,000 <sup>1</sup>                  | -                | -                   | -               | 1,446,000 | 0.014%                        |
| ZHOU Zaiqun      | 1,084,500 <sup>1</sup>                  | -                | -                   | -               | 1,084,500 | 0.010%                        |
| ZHANG Yanling    | 1,446,000 <sup>1</sup>                  | -                | -                   | -               | 1,446,000 | 0.014%                        |
| Total            | 4,076,500                               | -                | -                   | -               | 4,076,500 | 0.039%                        |

Note:

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

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

Save as disclosed above, as at 30 June 2010, none of the Directors or the Chief Executive of the Company or their respective associates had any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

## 6. Changes to information in respect of Directors

In accordance with Rule 13.51B(1) of the Listing Rules, the changes to information required to be disclosed by Directors pursuant to paragraphs (a) to (e) and (g) of Rule 13.51(2) after the publication of the Company's Annual Report 2009 on 23 March 2010 up to 26 August 2010 (being the approval date of this Interim Report) are set out below:

### (a) Positions held with the Company and other members of the Group

- (i) Mr. HE Guangbei, an executive Director, ceased to be the chairman of Nanyang with effect from 28 April 2010;
- (ii) Mr. ZHOU Zaiqun, a non-executive Director, has become the chairman of the Strategy and Budget Committee of the Company since 21 May 2010. He was also appointed the chairman of Nanyang with effect from 28 April 2010 and the vice-chairman of NCB (China) with effect from 7 May 2010; and
- (iii) Madam YANG Linda Tsao has retired from the office of the independent non-executive Director since 21 May 2010. She ceased to be the chairlady of the Strategy and Budget Committee and a member of the Audit Committee and Nomination and Remuneration Committee upon her said retirement.

### (b) Experience including other directorships and major appointments

- (i) Mr. HE Guangbei was appointed a member of the Hong Kong/Japan Business Co-operation Committee with effect from 31 May 2010. Mr. HE ceased to be a board member of Airport Authority Hong Kong with effect from 1 June 2010;
- (ii) Madam ZHANG Yanling, a non-executive Director, ceased to be the executive vice president of BOC, a company listed on the Stock Exchange of Hong Kong and the Shanghai Stock Exchange and a controlling shareholder of the Company, with effect from 23 July 2010. Madam ZHANG had also ceased to be the vice chairman of BOCI, a subsidiary of BOC, with effect from 26 May 2010;
- (iii) Dr. FUNG Victor Kwok King, an independent non-executive Director, retired as an independent non-executive director of CapitaLand Limited, a company listed on Singapore Exchange Limited, with effect from 16 April 2010. Dr. FUNG has become Honorary Chairman of the International Chamber of Commerce since 1 July 2010 following two years as its Chairman. Further to the Gold Bauhinia Star awarded by the Hong Kong Government in 2003, Dr. FUNG has been granted the Grand Bauhinia Medal in 2010 for his distinguished contribution to the community;

## 6. Changes to information in respect of Directors (continued)

### (b) Experience including other directorships and major appointments (continued)

- (iv) Mr. SHAN Weijian, an independent non-executive Director, ceased to be a partner of TPG Capital with effect from 30 June 2010. Mr. SHAN was appointed the chairman and chief executive officer of Pacific Alliance Investment Management (HK) Ltd. with effect from 1 July 2010; and
- (v) Mr. TUNG Savio Wai-Hok, an independent non-executive Director, was appointed a director and a member of the audit committee of Tech Data Corporation, a company listed on NASDAQ, with effect from 2 June 2010. Further, Mr. TUNG ceased to be a director of Wireless Telecom Group, a company listed on AMEX, with effect from 12 May 2010.

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

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

## 8. Audit Committee

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

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

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

Note: Madam YANG Linda Tsao retired and resigned as Independent Non-executive Director and member of the Audit Committee with effect from 21 May 2010. The Independent Non-executive Directors nevertheless make up the majority of the Committee members, and the independence of the Committee is not affected by the relevant change.

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

The Company is committed to embrace and enhance good corporate governance principles and practices. The Company has been in full compliance with all the code provisions of the "Code on Corporate Governance Practices" contained in Appendix 14 of the Listing Rules (the "CG Code") save as disclosed in the paragraph headed "Directors' securities transactions" below, and it has also complied with nearly all the recommended best practices set out in the CG Code throughout the period under review. For further details, please refer to the section titled "Corporate Governance" contained in the Annual Report 2009 of the Company.

## 10. Directors' securities transactions

The Company has adopted the "Code for Securities Transactions by Directors" (the "Company's Code") to govern securities transactions by Directors. The terms of the Company's Code are more stringent than the mandatory standards set out in the "Model Code for Securities Transactions by Directors of Listed Issuers" contained in Appendix 10 of the Listing Rules ("Model Code"). Apart from the securities of the Company, the Company's Code applies equally to the Directors' dealings in the securities of BOC which was listed on the Stock Exchange of Hong Kong in June 2006. In this connection, the Company has made specific enquiry of all Directors, who confirmed that they had complied with the standards set out in both the Company's Code and the Model Code throughout the period under review, with the following exception. On 25 June 2010, without the knowledge of Mr. ZHOU Zaiquan who was on a business trip, or any prior consultation with him, his wife caused 500 shares in the Company held by him in an account jointly controlled by him and her to be sold. The number of shares sold represented only 0.05% of his interests in shares/underlying shares of the Company and only 0.000005% of the issued share capital of the Company. The sale did not take place during the "black out" period for Directors' dealing in securities in the Company. At the time Mr. ZHOU did not have any material non-public price-sensitive information relating to securities in the Company. As Mr. ZHOU was unaware of the sale of the 500 shares, he could not, and did not, seek any approval for the sale and did not disclose it pursuant to the requirements set out in the Company's Code (and the Model Code). Mr. ZHOU only learnt for the first time about the sale of the shares on 26 July 2010, whereupon he immediately brought the matter to the attention of the Management of the Company.

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

The unaudited interim report complies with the requirements set out in the Banking (Disclosure) Rules and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

## 12. Interim Report

This Interim Report is available in both English and Chinese. The Chinese version of this Interim Report is available by writing to the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong or email to [hkinfo@computershare.com.hk](mailto:hkinfo@computershare.com.hk). This Interim Report is also available (in both English and Chinese) on the Company's website at [www.bochk.com](http://www.bochk.com) and the Stock Exchange's website at [www.hkex.com.hk](http://www.hkex.com.hk). You are encouraged to access the corporate communications of the Company through these websites in lieu of receiving printed copies to help protect the environment. We believe that it is also the most efficient and convenient method of communication with our shareholders.

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

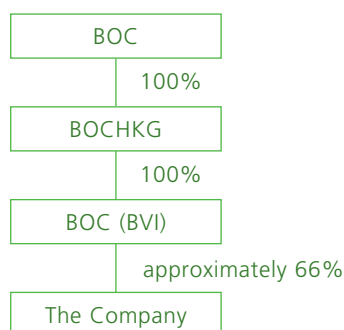
## 13. Reconciliation between HKFRSs vs IFRS/CAS

The Company understands that BOC, an intermediate holding company as well as controlling shareholder of the Company, will prepare and disclose consolidated financial information in accordance with IFRS and CAS for which the Company and its subsidiaries will form part of the interim financial information. CAS is the new set of PRC accounting standards that has been effective for annual periods beginning on or after 1 January 2007 for companies publicly listed in PRC. The requirements of CAS have substantially converged with IFRS and HKFRSs.

The consolidated financial information of "BOC Hong Kong Group" for the periods disclosed by BOC in its interim financial information is not the same as the consolidated financial information of the Group for the periods published by the Company pursuant to applicable laws and regulations in Hong Kong. There are two reasons for this.

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

First, the definitions of “BOC Hong Kong Group” (as adopted by BOC for the purpose of its own financial disclosure) and “Group” (as adopted by the Company in preparing and presenting its consolidated financial information) are different: “BOC Hong Kong Group” refers to BOCHKG and its subsidiaries, whereas “Group” refers to the Company and its subsidiaries (see the below organisation chart). Though there is difference in definitions between “BOC Hong Kong Group” and “Group”, their financial results for the periods presented are substantially the same. This is because BOCHKG and BOC (BVI) are holding companies only and have no substantive operations of their own.



Second, the Group has prepared its interim financial information in accordance with HK GAAP prior to 1 January 2005 and as from 1 January 2005 onwards in accordance with HKFRSs; whereas the consolidated financial information reported to BOC is prepared in accordance with IFRS and CAS respectively. Despite the fact that HKFRSs have converged with IFRS, there is a timing difference in the initial adoption of HKFRSs and IFRS by the Group and by BOC respectively.

The Board considers that the best way to ensure that shareholders and the investing public understand the material differences between the consolidated financial information of the Group published by the Company on the one hand, and the consolidated financial information of BOC Hong Kong Group disclosed by BOC in its interim financial information on the other hand, is to present reconciliations of the profit after tax/net assets of the Group prepared under HKFRSs to the profit after tax/net assets of the Group prepared under IFRS and CAS respectively for the periods presented.

The major differences between HKFRSs and IFRS/CAS, which arise from the difference in measurement basis in IFRS or CAS and the timing difference in the initial adoption of HKFRSs and IFRS relate to the following:

- re-measurement of carrying value of treasury products;
- restatement of carrying value of bank premises; and
- deferred taxation impact arising from the above different measurement basis.

#### (a) *Re-measurement of carrying value of treasury products*

Due to the difference in the timing of first adoption of HKFRSs and IFRS, classification and measurement of certain investment securities under HKFRSs and IFRS were different. Therefore, investment securities were reclassified and re-measured to align with the accounting policies of BOC for the relevant periods. Classification and measurement under IFRS and CAS is basically the same.

**13. Reconciliation between HKFRSs vs IFRS/CAS (continued)****(b) Restatement of carrying value of bank premises**

The Company has elected for a revaluation basis rather than cost basis to account for bank premises and investment properties under HKFRSs. On the contrary, BOC has elected for the cost convention for bank premises and revaluation basis for investment properties under IFRS and CAS. Therefore, adjustments have been made to the carrying value of bank premises as well as to re-calculate the depreciation charge and disposal gain/loss under IFRS and CAS.

**(c) Deferred tax adjustments**

These represent the deferred tax effect of the aforesaid adjustments.

Going forward, the differences relating to the restatement of carrying value of bank premises as a result of the election of the different measurement basis allowed under HKFRSs, IFRS and CAS will be recurring in the future, while the timing difference related to the measurement of investment securities will be reversed gradually and eliminated in future years.

**Profit after tax/Net assets reconciliation**  
**HKFRSs vs IFRS/CAS**

|                                                                                                | Profit after tax                             |                                              | Net assets                   |                                  |
|------------------------------------------------------------------------------------------------|----------------------------------------------|----------------------------------------------|------------------------------|----------------------------------|
|                                                                                                | Half-year ended<br>30 June<br>2010<br>HK\$'m | Half-year ended<br>30 June<br>2009<br>HK\$'m | At 30 June<br>2010<br>HK\$'m | At 31 December<br>2009<br>HK\$'m |
| <b>Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under HKFRSs</b>   | <b>7,353</b>                                 | 6,875                                        | <b>109,537</b>               | 105,635                          |
| Add: IFRS/CAS adjustments                                                                      |                                              |                                              |                              |                                  |
| Re-measurement of carrying value of treasury products                                          | (17)                                         | (73)                                         | (5)                          | (10)                             |
| Restatement of carrying value of bank premises                                                 | 172                                          | 65                                           | (14,966)                     | (13,218)                         |
| Deferred tax adjustments                                                                       | (40)                                         | 31                                           | 2,461                        | 2,186                            |
| <b>Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under IFRS/CAS</b> | <b>7,468</b>                                 | 6,898                                        | <b>97,027</b>                | 94,593                           |

# INDEPENDENT REVIEW REPORT

## REPORT ON REVIEW OF INTERIM FINANCIAL INFORMATION TO THE BOARD OF DIRECTORS OF BOC HONG KONG (HOLDINGS) LIMITED

(incorporated in Hong Kong with limited liability)

### Introduction

We have reviewed the interim financial information set out on pages 44 to 118, which comprises the condensed consolidated balance sheet of BOC Hong Kong (Holdings) Limited (the “Company”) and its subsidiaries (together, the “Group”) as at 30 June 2010 and the related condensed consolidated statements of income, comprehensive income, changes in equity and cash flows for the six-month period then ended, and a summary of significant accounting policies and other explanatory notes. The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and Hong Kong Accounting Standard 34 “Interim Financial Reporting” issued by the Hong Kong Institute of Certified Public Accountants. The directors of the Company are responsible for the preparation and presentation of this interim financial information in accordance with Hong Kong Accounting Standard 34 “Interim Financial Reporting”. Our responsibility is to express a conclusion on this interim financial information based on our review and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

### Scope of Review

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

### Conclusion

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



**PricewaterhouseCoopers**

Certified Public Accountants

Hong Kong, 26 August 2010

## Subsidiaries of the Company

The particulars of our subsidiaries are as follows:

| Name of company                                        | Country/place and date of incorporation/operation | Issued and fully paid up share capital/registered capital | Percentage of attributable equity interest | Principal activities            |
|--------------------------------------------------------|---------------------------------------------------|-----------------------------------------------------------|--------------------------------------------|---------------------------------|
| <b>Directly held:</b>                                  |                                                   |                                                           |                                            |                                 |
| Bank of China (Hong Kong) Limited                      | Hong Kong<br>16 October 1964                      | Ordinary shares<br>HK\$43,042,840,858                     | 100.00%                                    | Banking business                |
| BOC Group Life Assurance Company Limited*              | Hong Kong<br>12 March 1997                        | Ordinary shares<br>HK\$2,868,000,000                      | 51.00%                                     | Life insurance business         |
| <b>Indirectly held:</b>                                |                                                   |                                                           |                                            |                                 |
| Nanyang Commercial Bank, Limited                       | Hong Kong<br>2 February 1948                      | Ordinary shares<br>HK\$700,000,000                        | 100.00%                                    | Banking business                |
| Chiyu Banking Corporation Limited                      | Hong Kong<br>24 April 1947                        | Ordinary shares<br>HK\$300,000,000                        | 70.49%                                     | Banking business                |
| BOC Credit Card (International) Limited                | Hong Kong<br>9 September 1980                     | Ordinary shares<br>HK\$480,000,000                        | 100.00%                                    | Credit card services            |
| Bank of China (Hong Kong) Nominees Limited*            | Hong Kong<br>1 October 1985                       | Ordinary shares<br>HK\$2                                  | 100.00%                                    | Nominee services                |
| Bank of China (Hong Kong) Trustees Limited*            | Hong Kong<br>6 November 1987                      | Ordinary shares<br>HK\$3,000,000                          | 100.00%                                    | Trustee and agency services     |
| BOC Group Trustee Company Limited*                     | Hong Kong<br>1 December 1997                      | Ordinary shares<br>HK\$200,000,000                        | 64.20%                                     | Trustee services                |
| BOC Travel Services Limited*                           | Hong Kong<br>24 August 1982                       | Ordinary shares<br>HK\$2,000,000                          | 100.00%                                    | Travel services                 |
| BOCHK Financial Products (Cayman) Limited              | Cayman Islands<br>10 November 2006                | Ordinary shares<br>US\$50,000                             | 100.00%                                    | Note issuing                    |
| BOCHK Information Technology (Shenzhen) Co., Ltd.*     | PRC<br>16 April 1990                              | Registered capital<br>HK\$70,000,000                      | 100.00%                                    | Property holding and investment |
| BOCHK Information Technology Services (Shenzhen) Ltd.* | PRC<br>26 May 1993                                | Registered capital<br>HK\$40,000,000                      | 100.00%                                    | Information technology services |
| BOCI-Prudential Trustee Limited*                       | Hong Kong<br>11 October 1999                      | Ordinary shares<br>HK\$300,000,000                        | 41.10%                                     | Trustee services                |

## Subsidiaries of the Company (continued)

| Name of company                                    | Country/place and date of incorporation/operation | Issued and fully paid up share capital/registered capital | Percentage of attributable equity interest | Principal activities                       |
|----------------------------------------------------|---------------------------------------------------|-----------------------------------------------------------|--------------------------------------------|--------------------------------------------|
| Che Hsing (Nominees) Limited*                      | Hong Kong<br>23 April 1980                        | Ordinary shares<br>HK\$10,000                             | 100.00%                                    | Nominee services                           |
| Chiyu Banking Corporation (Nominees) Limited*      | Hong Kong<br>3 November 1981                      | Ordinary shares<br>HK\$100,000                            | 70.49%                                     | Investment holding                         |
| Chung Chiat Company Limited                        | Hong Kong<br>9 April 1980                         | Ordinary shares<br>HK\$200                                | 100.00%                                    | Property holding and investment            |
| Dwell Bay Limited                                  | Hong Kong<br>19 December 1980                     | Ordinary shares<br>HK\$100,000                            | 100.00%                                    | Property holding and investment            |
| Glister Company Limited*                           | Hong Kong<br>26 March 2001                        | Ordinary shares<br>HK\$2                                  | 70.49%                                     | Investment holding                         |
| Glory Cardinal Limited*                            | Hong Kong<br>4 May 2001                           | Ordinary shares<br>HK\$2                                  | 70.49%                                     | Investment holding                         |
| Grace Charter Limited*                             | Hong Kong<br>4 May 2001                           | Ordinary shares<br>HK\$2                                  | 70.49%                                     | Investment holding                         |
| G.Z.Y. Microfilm Technology (Shenzhen) Co., Ltd.*  | PRC<br>24 September 1993                          | Registered capital<br>HK\$40,000,000                      | 100.00%                                    | Property holding and investment            |
| Kincheng Finance (H.K.) Limited                    | Hong Kong<br>30 March 1979                        | Ordinary shares<br>HK\$100                                | 100.00%                                    | Loan financing                             |
| Kincheng Investments & Developments (H.K.) Limited | Hong Kong<br>15 May 1981                          | Ordinary shares<br>HK\$6,000                              | 100.00%                                    | Property holding and investment            |
| Kincheng (Nominees) Limited*                       | Hong Kong<br>12 December 1980                     | Ordinary shares<br>HK\$100,000                            | 100.00%                                    | Nominee services                           |
| Kiu Nam Investment Corporation Limited             | Hong Kong<br>9 November 1963                      | Ordinary shares<br>HK\$2,000,000                          | 100.00%                                    | Property holding and investment            |
| Kwong Li Nam Investment Agency Limited*            | Hong Kong<br>25 May 1984                          | Ordinary shares<br>HK\$3,050,000                          | 100.00%                                    | Investment agency                          |
| Nan Song Company, Limited*                         | Hong Kong<br>13 April 1965                        | Ordinary shares<br>HK\$1,000,000                          | 100.00%                                    | Property investment and investment holding |

## Subsidiaries of the Company (continued)

| Name of company                                        | Country/place and date of incorporation/operation | Issued and fully paid up share capital/registered capital | Percentage of attributable equity interest | Principal activities                |
|--------------------------------------------------------|---------------------------------------------------|-----------------------------------------------------------|--------------------------------------------|-------------------------------------|
| Nanyang Commercial Bank (China), Limited               | PRC<br>14 December 2007                           | Registered capital<br>RMB4,100,000,000                    | 100.00%                                    | Banking business                    |
| Nanyang Commercial Bank (Nominees) Limited*            | Hong Kong<br>22 August 1980                       | Ordinary shares<br>HK\$50,000                             | 100.00%                                    | Nominee services                    |
| Nanyang Commercial Bank Trustee Limited*               | Hong Kong<br>22 October 1976                      | Ordinary shares<br>HK\$3,000,000                          | 100.00%                                    | Trustee services                    |
| Nanyang Finance Company Limited                        | Hong Kong<br>16 March 1979                        | Ordinary shares<br>HK\$50,000,000                         | 100.00%                                    | Financial services                  |
| Pacific Trend Profits Corporation*                     | British Virgin Islands<br>20 April 2001           | Registered shares<br>US\$1                                | 70.49%                                     | Investment holding                  |
| Patson (HK) Limited*                                   | Hong Kong<br>18 August 1970                       | Ordinary shares<br>HK\$1,000,000                          | 100.00%                                    | Property investment                 |
| Perento Limited                                        | Hong Kong<br>27 September 1983                    | Ordinary shares<br>HK\$10,000                             | 100.00%                                    | Property holding and investment     |
| Po Hay Enterprises Limited                             | Hong Kong<br>2 October 1979                       | Ordinary shares<br>HK\$100,000                            | 100.00%                                    | Property holding and investment     |
| Po Sang Financial Investment Services Company Limited* | Hong Kong<br>23 September 1980                    | Ordinary shares<br>HK\$25,000,000                         | 100.00%                                    | Gold trading and investment holding |
| Po Sang Futures Limited*                               | Hong Kong<br>19 October 1993                      | Ordinary shares<br>HK\$25,000,000                         | 100.00%                                    | Commodities brokerage               |
| Seng Sun Development Company, Limited*                 | Hong Kong<br>11 December 1961                     | Ordinary shares<br>HK\$2,800,000                          | 70.49%                                     | Investment holding                  |
| Shenstone Limited                                      | Hong Kong<br>4 September 1979                     | Ordinary shares<br>HK\$2                                  | 100.00%                                    | Property holding and investment     |
| Sin Chiao Enterprises Corporation, Limited*            | Hong Kong<br>13 September 1961                    | Ordinary shares<br>HK\$3,000,000                          | 100.00%                                    | Property holding and investment     |
| Sin Hua Trustee Limited*                               | Hong Kong<br>27 October 1978                      | Ordinary shares<br>HK\$3,000,000                          | 100.00%                                    | Trustee services                    |
| Sin Mei (Nominee) Limited*                             | Hong Kong<br>27 April 1982                        | Ordinary shares<br>HK\$100,000                            | 100.00%                                    | Nominee services                    |

**Subsidiaries of the Company (continued)**

| <b>Name of company</b>                           | <b>Country/place and date of incorporation/operation</b> | <b>Issued and fully paid up share capital/registered capital</b> | <b>Percentage of attributable equity interest</b> | <b>Principal activities</b>     |
|--------------------------------------------------|----------------------------------------------------------|------------------------------------------------------------------|---------------------------------------------------|---------------------------------|
| Sin Yeh Shing Company Limited                    | Hong Kong<br>28 November 1980                            | Ordinary shares<br>HK\$100,000                                   | 100.00%                                           | Property holding and investment |
| Sino Information Services Company Limited*       | Hong Kong<br>11 February 1993                            | Ordinary shares<br>HK\$7,000,000                                 | 100.00%                                           | Information services            |
| The China-South Sea (Nominees) Services Limited* | Hong Kong<br>13 February 1981                            | Ordinary shares<br>HK\$100,000                                   | 100.00%                                           | Nominee services                |
| Track Link Investment Limited                    | Hong Kong<br>8 February 1994                             | Ordinary shares<br>HK\$2                                         | 100.00%                                           | Property holding and investment |

Arene Trading Limited, Rams City (Nominees) Limited, Yien Yieh (Nominee) Limited and The China State Trustee Limited had been dissolved on 13 April 2010.

Sanicon Investment Limited, Hua Chiao Commercial (Nominees) Limited and The China State (Nominees) Limited had been dissolved on 14 June 2010.

Remarks:

Name of subsidiaries which are not included in the consolidation group for regulatory purposes in respect of capital adequacy is marked with \* in the above table. BOCHK and its subsidiaries specified by the HKMA form the basis of consolidation for its regulatory purposes in accordance with the Banking (Capital) Rules. For accounting purposes, subsidiaries are consolidated in accordance with the accounting standards issued by the HKICPA pursuant to section 18A of the Professional Accountants Ordinance.

## DEFINITIONS

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

| Terms                           | Meanings                                                                                                                                                                                                                                                                                             |
|---------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| "ABS"                           | Asset-backed securities                                                                                                                                                                                                                                                                              |
| "ADR"                           | American Depositary Receipt                                                                                                                                                                                                                                                                          |
| "ADS(s)"                        | American Depositary Share(s)                                                                                                                                                                                                                                                                         |
| "ALCO"                          | the Asset and Liability Management Committee                                                                                                                                                                                                                                                         |
| "ALMD"                          | the Asset and Liability Management Department                                                                                                                                                                                                                                                        |
| "ATM"                           | Automated Teller Machine                                                                                                                                                                                                                                                                             |
| "Board" or "Board of Directors" | the Board of Directors of the Company                                                                                                                                                                                                                                                                |
| "BOC"                           | Bank of China Limited, a joint stock commercial bank with limited liability established under the laws of the PRC, the H shares and A shares of which are listed on The Hong Kong Stock Exchange and the Shanghai Stock Exchange respectively                                                        |
| "BOC (BVI)"                     | BOC Hong Kong (BVI) Limited, a company incorporated under the laws of the British Virgin Islands and a wholly owned subsidiary of BOCHK                                                                                                                                                              |
| "BOC Insurance"                 | Bank of China Group Insurance Company Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOC                                                                                                                                                               |
| "BOC Life"                      | BOC Group Life Assurance Company Limited, a company incorporated under the laws of Hong Kong, in which the Group and BOC Insurance hold equity interests of 51% and 49% respectively                                                                                                                 |
| "BOC-CC"                        | BOC Credit Card (International) Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOCHK                                                                                                                                                                   |
| "BOCHK" or "the Bank"           | Bank of China (Hong Kong) Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of the Company                                                                                                                                                                   |
| "BOCHKG"                        | BOC Hong Kong (Group) Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOC                                                                                                                                                                               |
| "BOCI"                          | BOC International Holdings Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOC                                                                                                                                                                          |
| "BOCI-Prudential Manager"       | BOCI-Prudential Asset Management Limited, a company incorporated under the laws of Hong Kong, in which BOCI Asset Management Limited, a wholly owned subsidiary of BOC International Holdings Limited, and Prudential Corporation Holdings Limited hold equity interests of 64% and 36% respectively |
| "BOCI-Prudential Trustee"       | BOCI-Prudential Trustee Limited, a company incorporated under the laws of Hong Kong, in which BOC Group Trustee Company Limited and Prudential Corporation Holdings Limited hold equity interests of 64% and 36% respectively                                                                        |

| Terms                          | Meanings                                                                                                                                                                                                                       |
|--------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| "CAR"                          | Capital Adequacy Ratio, computed on the consolidated basis that comprises the positions of BOCHK and certain subsidiaries specified by the HKMA for its regulatory purposes and in accordance with the Banking (Capital) Rules |
| "CAS"                          | China Accounting Standards                                                                                                                                                                                                     |
| "CBRC"                         | China Banking Regulatory Commission                                                                                                                                                                                            |
| "CE"                           | Chief Executive                                                                                                                                                                                                                |
| "CIC"                          | China Investment Corporation                                                                                                                                                                                                   |
| "CRO"                          | Chief Risk Officer                                                                                                                                                                                                             |
| "Central Huijin"               | Central Huijin Investment Ltd. (formerly known as "Central SAFE Investments Limited")                                                                                                                                          |
| "Chiyu"                        | Chiyu Banking Corporation Limited, a company incorporated under the laws of Hong Kong, in which BOCHK holds an equity interest of 70.49%                                                                                       |
| "the Company"                  | BOC Hong Kong (Holdings) Limited, a company incorporated under the laws of Hong Kong                                                                                                                                           |
| "EURIBOR"                      | Euro Interbank Offered Rate                                                                                                                                                                                                    |
| "FIRB"                         | Foundation Internal ratings-based approach                                                                                                                                                                                     |
| "GDP"                          | Gross Domestic Product                                                                                                                                                                                                         |
| "the Group"                    | the Company and its subsidiaries collectively referred as the Group                                                                                                                                                            |
| "HIBOR"                        | Hong Kong Interbank Offered Rate                                                                                                                                                                                               |
| "HK GAAP"                      | Generally Accepted Accounting Principles in Hong Kong                                                                                                                                                                          |
| "HKAS(s)"                      | Hong Kong Accounting Standard(s)                                                                                                                                                                                               |
| "HKFRS(s)"                     | Hong Kong Financial Reporting Standard(s)                                                                                                                                                                                      |
| "HKICPA"                       | Hong Kong Institute of Certified Public Accountants                                                                                                                                                                            |
| "HKMA"                         | Hong Kong Monetary Authority                                                                                                                                                                                                   |
| "Hong Kong" or "Hong Kong SAR" | Hong Kong Special Administrative Region                                                                                                                                                                                        |
| "IFRS"                         | International Financial Reporting Standards                                                                                                                                                                                    |
| "IPO"                          | Initial Public Offering                                                                                                                                                                                                        |
| "IT"                           | Information Technology                                                                                                                                                                                                         |
| "LIBOR"                        | London Interbank Offered Rate                                                                                                                                                                                                  |
| "Listing Rules"                | the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited                                                                                                                                       |

| Terms                                             | Meanings                                                                                                                            |
|---------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------|
| "Mainland" or "Mainland China"                    | the mainland of the PRC                                                                                                             |
| "MBS"                                             | Mortgage-backed securities                                                                                                          |
| "MPF"                                             | Mandatory Provident Fund                                                                                                            |
| "MPF Schemes Ordinance"                           | the Mandatory Provident Fund Schemes Ordinance, Chapter 485 of the Laws of Hong Kong, as amended                                    |
| "MSCI Index"                                      | Morgan Stanley Capital International Index                                                                                          |
| "Moody's"                                         | Moody's Investors Service                                                                                                           |
| "Nanyang"                                         | Nanyang Commercial Bank, Limited, a company incorporated under the laws of Hong Kong and a wholly owned subsidiary of BOCHK         |
| "NCB (China)"                                     | Nanyang Commercial Bank (China), Limited, a company incorporated under the laws of the PRC and a wholly owned subsidiary of Nanyang |
| "OR&CD"                                           | the Operational Risk & Compliance Department                                                                                        |
| "ORSO schemes"                                    | the Occupational Retirement Schemes under Occupational Retirement Schemes Ordinance, Chapter 426 of the Laws of Hong Kong           |
| "PRC"                                             | the People's Republic of China                                                                                                      |
| "QDII(s)"                                         | Qualified Domestic Institutional Investor(s)                                                                                        |
| "RC"                                              | the Risk Committee                                                                                                                  |
| "RMB" or "Renminbi"                               | Renminbi, the lawful currency of the PRC                                                                                            |
| "RMBS"                                            | Residential mortgage-backed securities                                                                                              |
| "RMD"                                             | the Risk Management Department                                                                                                      |
| "SFO"                                             | the Securities and Futures Ordinance, Chapter 571 of the Laws of Hong Kong                                                          |
| "SME(s)"                                          | Small and medium-sized enterprise(s)                                                                                                |
| "Share Option Scheme"                             | the Share Option Scheme conditionally approved and adopted by the shareholders of the Company on 10 July 2002                       |
| "Sharesave Plan"                                  | the Sharesave Plan conditionally approved and adopted by the shareholders of the Company on 10 July 2002                            |
| "Standard & Poor's"                               | Standard & Poor's Ratings Services                                                                                                  |
| "Stock Exchange" or "Stock Exchange of Hong Kong" | The Stock Exchange of Hong Kong Limited                                                                                             |
| "US" or "USA"                                     | the United States of America                                                                                                        |
| "VAR"                                             | Value at Risk                                                                                                                       |

By Order of the Board  
**Jason C.W. Yeung**  
Company Secretary

Hong Kong, 26 August 2010

*As at the date of this announcement, the Board comprises Mr. XIAO Gang\* (Chairman), Mr. LI Lihui\* (Vice-chairman), Mr. HE Guangbei (Vice-chairman and Chief Executive), Mr. LI Zaohang\*, Mr. ZHOU Zaiqun\*, Mdm. ZHANG Yanling\*, Mr. GAO Yingxin, Dr. FUNG Victor Kwok King\*\*, Mr. KOH Beng Seng\*\*, Mr. SHAN Weijian\*\*, Mr. TUNG Chee Chen\*\* and Mr. TUNG Savio Wai-Hok\*\*.*

\* *Non-executive Directors*

\*\* *Independent Non-executive Directors*