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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)

2012 ANNUAL RESULTS ANNOUNCEMENT

The Board of Directors of the Company (the “Board”) is pleased to announce the audited results of the Company and its subsidiaries for the year ended 31 December 2012. This announcement, containing the full text of the 2012 Annual 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 annual results. Printed version of the Company’s 2012 Annual Report will be delivered to the Company’s shareholders who have chosen to receive printed version and will also be available for viewing on the websites of Hong Kong Exchanges and Clearing Limited at www.hkexnews.hk and of the Company at www.bochk.com in mid April 2013.

FINANCIAL HIGHLIGHTS

	2012	2011	Change
For the year	HK\$'m	HK\$'m	+/(-)%
Net operating income before impairment allowances	35,760	30,846	15.93
Operating profit	23,499	22,478	4.54
Profit before taxation	25,521	24,680	3.41
Profit for the year	21,547	20,813	3.53
Profit attributable to the equity holders of the Company	20,930	20,430	2.45
Per share	HK\$	HK\$	+/(-)%
Basic earnings per share	1.9796	1.9323	2.45
Dividend per share	1.2380	1.1880	4.21
At year-end	HK\$'m	HK\$'m	+/(-)%
Capital and reserves attributable to the equity holders of the Company	150,969	129,765	16.34
Issued and fully paid share capital	52,864	52,864	–
Total assets	1,830,763	1,738,510	5.31
Financial ratios	%	%	
Return on average total assets ¹	1.24	1.14	
Return on average shareholders' equity ²	14.91	16.68	
Cost to income ratio ³	31.88	25.49	
Loan to deposit ratio ⁴	63.32	61.00	
Average liquidity ratio ⁵	41.20	36.17	
Capital adequacy ratio ⁶	16.80	16.90	

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

2. Return on average shareholders' equity

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

3. In calculating cost to income ratio, cost includes the impact of Lehman Brothers minibonds.

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

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

6. Capital adequacy ratio is computed on the consolidated basis that comprises the positions of BOCHK and certain subsidiaries specified by the HKMA for its regulatory purposes and in accordance with the Banking (Capital) Rules. The bases of regulatory capital calculation for credit risk, market risk and operational risk are described in Note 4.5 to the Financial Statements in this Annual Report. As a result of the change in the bases used, the capital ratios shown above are not directly comparable.



FIVE-YEAR FINANCIAL SUMMARY



The financial information of the Group for the last five years commencing from 1 January 2008 is summarised below:

	2012	2011	2010	2009 ²	2008 ²
For the year	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m
Net operating income before impairment allowances	35,760	30,846	27,508	26,055	25,526
Operating profit	23,499	22,478	18,239	15,104	4,182
Profit before taxation	25,521	24,680	19,742	16,724	4,078
Profit for the year	21,547	20,813	16,690	14,251	2,977
Profit attributable to the equity holders of the Company	20,930	20,430	16,196	13,930	3,313
Per share	HK\$	HK\$	HK\$	HK\$	HK\$
Basic earnings per share	1.9796	1.9323	1.5319	1.3175	0.3134
At year-end	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m
Advances and other accounts	819,739	755,229	645,424	527,135	469,493
Total assets	1,830,763	1,738,510	1,661,040	1,212,794	1,147,245
Daily average balance of total assets	1,734,388	1,823,989	1,382,121	1,177,294	1,099,198
Deposits from customers ¹	1,229,131	1,146,590	1,027,267	844,453	811,516
Total liabilities	1,675,689	1,605,327	1,542,751	1,105,879	1,061,695
Issued and fully paid share capital	52,864	52,864	52,864	52,864	52,864
Capital and reserves attributable to the equity holders of the Company	150,969	129,765	115,181	104,179	83,734
Financial ratios	%	%	%	%	%
Return on average total assets	1.24	1.14	1.21	1.21	0.27
Cost to income ratio	31.88	25.49	34.84	46.60	34.36
Loan to deposit ratio	63.32	61.00	59.69	60.98	56.74

1. Deposits from customers include structured deposits reported as "Financial liabilities at fair value through profit or loss".

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





BRAND-NEW
CUSTOMER
EXPERIENCE



CHAIRMAN'S STATEMENT



The operating environment for Hong Kong's banking industry in 2012 was characterised by a sluggish global economy, stringent regulatory requirements and persistently low interest rates. Nevertheless, the Group succeeded in overcoming all these macro challenges and struck a balance between revenue and cost, and growth and capital management, which enabled us to achieve once again new highs in net operating income before impairment allowances and profit attributable to the equity holders since our listing. While driving our core business development, the Group stepped up efforts to support new business initiatives of strong growth potential and strived to maintain a proper mix of capital, liquidity, loan to deposit ratio and other key management indicators. Our pursuance of a sustainable balanced growth strategy has delivered solid results.

The Group's net operating income before impairment allowances, operating profit before impairment allowances and profit attributable to the equity holders maintained growth momentum in 2012. Excluding the impact of the Lehman Brothers-related products, operating profit before impairment allowances and profit attributable to the equity holders witnessed encouraging growth performance.

Solid financial capability and a pragmatic operating strategy are crucial to the foundation of our balanced growth. During the year, we remained well capitalised with consolidated capital adequacy ratio and average liquidity ratio staying at healthy levels. Our continuous efforts in maintaining financial strength have enabled us to withstand market uncertainties and capture opportunities pre-emptively whilst meeting regulatory requirements.

During the period, thanks to the adoption of a flexible deposit strategy coupled with the bundling of suitable auxiliary products, our customer deposit grew healthily. Against the backdrop of an unstable external environment, softened loan demand as well as stronger competition from peers and other capital markets, the Group captured timely opportunities in different credit categories and grew its loans in a balanced manner, achieving top business rankings in the Hong Kong new residential mortgage market and in the Hong Kong-Macau syndicated loan market. We also strictly stuck to the stringent lending policy and prudent management of loan portfolio risks, sustaining robust loan quality. Apart from that, facing a prolonged low interest rate environment, we improved the asset and liability mix and optimised funds deployment while proactively managing the cost of funding and loan pricing. These efforts, together with the eased dilution effect of the RMB clearing bank business, led to net interest margin improvement.

While continuously deploying resources in existing businesses, we never stopped making strategic investment in the new businesses with great potential. BOCHK launched its private banking service in November 2012 for top-tier customers extending our service scope. Taking advantage of trends in new information technology, we also enhanced the mobile banking platform, which has been well received by our customers. In asset management, a vast array of investment products, including a bond fund in cooperation with the World Bank, was launched to cater to diverse customer needs and won positive comments from the market. Despite enlarged investments in the key business areas, we adhered to our policy of assessing income and spend in accordance with the adoption of



stringent cost control measures, thereby sustaining a relatively low cost-to-income ratio.

In 2012, further regulatory relaxation fostered a favourable development in the Hong Kong offshore RMB market. Leveraging our brand advantage, the Group continued to steadily develop offshore RMB business and maintained our leading position. Firstly, we enriched our RMB product range in line with regulatory development and to meet customer needs. We also upgraded the comprehensive service capabilities of our RMB business, specifically in trade settlement, investment and financing, insurance and funds distribution to strengthen customer relationships and drive potential growth opportunities from other businesses with continuous service quality enhancement. During the year, we launched three new offshore RMB bond sub-indices, which not only garnered more market recognition for BOCHK but also strengthened our position in the offshore RMB market. With the extension of offshore RMB services to non-Hong Kong residents from August 2012, we swiftly geared up ourselves and were one of the first few banks providing the most comprehensive range of RMB products, earning us positive market feedback. Our customer base expanded further on the back of our distinguished services in the offshore RMB business. In addition to following through with a flexible strategy of RMB asset and liability management focusing on asset deployment optimisation, we also proactively managed RMB funding cost and promoted RMB lending business to achieve remarkable earnings growth. Our global clearing network was further strengthened and expanded with upgraded settlement facilities, so as to enhance our long-term and sustainable competitiveness. In line with the extension of the operating hours of the RMB Real Time Gross Settlement System in Hong Kong, BOCHK, as the RMB clearing bank, extended service hours of the clearing function since June 2012. This enabled participating banks in different time zones to conduct RMB clearing services more conveniently, increasing Hong Kong's competitive edge as an offshore RMB clearing hub. More importantly, by further deepening cooperation with our parent bank, BOC, we will enhance our financial service capabilities for global customers and jointly expand an even broader offshore RMB business market.

In 2012, BOCHK was named, for the second consecutive year, one of the world's strongest banks by Bloomberg Markets magazine. The significant jump in our ranking to No.2 from No.10 in 2011 is a recognition of our outstanding performance in terms of financial position, asset quality and operating efficiency. In 2013, we will stay attuned to market changes as the pace of global economic recovery remains uncertain and the low interest rate

environment may prevail in the near term. With the ongoing economic reforms in China, we believe that more new policies and measures will create business opportunities for the Group. By keeping up our acute market sense and prudent risk management principles while at the same time capitalising on our solid financial position and prescient operating strategy, we will continue to earnestly expand our business in the areas where our competitive advantages lie and capture new business opportunities to achieve a sustainable balance among growth, risks and return.

On behalf of the Board, I would like to welcome Mr. NING Gaoning who joined us as an Independent Non-executive Director of the Company and BOCHK on 24 August 2012. I believe that Mr. NING will bring new thinking to the Group with his abundant experience in China and Hong Kong markets.

Year 2012 marked the 100th anniversary of BOC and the 10th anniversary of BOCHK's listing. We not only take great pride in the sound development of BOC Group through the years, but also embrace more focus and greater collaboration on cross-border financial services for a brighter future. The Group's achievements in the past year are attributable to the long-standing trust and support of our customers and shareholders, wise counsel from our Board and the great efforts and devotion of our employees. The Board and the Group will firmly move forward towards the goal of a long-term sustainable development with a view to continuously creating greater value to our customers, shareholders and community.

XIAO Gang
Chairman

Hong Kong, 15 March 2013

CHIEF EXECUTIVE'S REPORT



I am pleased to report that the Group delivered another year of record results in 2012 with solid growth in income and profit. Despite a still challenging operating environment, this consistent performance was achieved on the back of our effective execution of the Group's balanced growth strategy. Our financial position remained strong while profitability of core businesses improved. We also made good progress in achieving our strategic objectives and enhancing our customer franchise. All these helped solidify our foundations to drive the Group's long-term sustainable development.

In 2012, the overall market conditions remained tough as characterised by the lack of obvious growth drivers in major economies and ongoing market uncertainties arising from the evolving European debt crisis. Growth of the Chinese economy softened for most part of the year but resumed momentum in the fourth quarter. In Hong Kong, GDP growth was modest with sluggish external trade and domestic consumption.

The operating environment for Hong Kong's banking industry was challenging as consistently low interest rates, reduced business activities and keen competition continued to affect banks' performance. On the positive side, we saw new business opportunities arising from the further development of offshore RMB market supported by a series of new government initiatives. These included the further relaxation of investment restrictions in relation to the RMB

Qualified Foreign Institutional Investors (RQFII) scheme, the expansion of personal RMB services to non-Hong Kong residents and the introduction of the Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone.

Key Initiatives and Achievements

During the period, the Group maintained its proactive yet prudent approach in managing its balance sheet and driving business development. Our consistent investments and efforts in our strategic focuses yielded rewarding results and market recognition, especially in the offshore RMB business and the enhancement of our product and service capabilities.

Strong Financial Position

- In view of the changing market environment and keen competition, we continued to pursue our proactive strategies in managing the Group's assets and liabilities to improve profitability and solidify financial strength.
- Our strong financial position earned us recognition as the world's second strongest bank and the top one among banks in Hong Kong by Bloomberg Markets in May 2012.
- The Group's balance sheet was strong with solid capital and liquidity position. Under the volatile economic environment, we continued to adopt stringent risk management and credit control to deliver quality



growth. Overall loan quality remained healthy with our classified or impaired loan ratio staying at a low level. Our investment book was prudently managed to optimise risk and return.

- Both loans and deposits recorded healthy growth with loan-to-deposit ratio staying at a decent level. Our conscious efforts to enhance the deployment of the offshore RMB funds, to improve loan pricing and to control deposit cost contributed to the net interest margin improvement.
- The Group remained focused on enhancing operational efficiency and maintaining disciplined cost control. We also continued to invest in new business platforms and Mainland operation to support long-term business growth. Investments were made judiciously with expenses well contained within our cost-to-income target.

Leading position and solid growth for offshore RMB business

- The offshore RMB market saw more favourable developments during the year. Capitalising on its core strengths, the Group acted swiftly to capture these rising opportunities. We maintained our leading positions in major RMB businesses and received a number of industry recognitions, including retail banking business, corporate banking business, insurance business and asset management business.
- We pioneered in launching new products and services to cater to the growing needs in RMB transactions around the world. We successfully arranged the first sizable 100% RMB syndicated loan in Hong Kong. Our competitiveness in the trade finance business was further strengthened with market-leading products launched. The “Multi-currency Shipping Finance (RMB and USD)” product that we offered has marked a number of milestones in the industry, including the first export shipping contract settled in RMB and issuance of the first cross-border RMB Refund Guarantee. This product also won the “Innovation Award – Business Innovation” in the Lloyd’s List Global Awards 2012.

- Taking advantage of the fast expanding Dim Sum bond market, we actively participated in the RMB bond underwriting business with a substantial increase in turnover year-on-year. Leveraging the opportunities arising from the RQFII programme, we became the largest RQFII funds distributor and custody service provider in Hong Kong.
- In August, RMB banking services were further extended to non-Hong Kong residents. The Group promptly offered an array of RMB services to global customers and took the lead by enabling RMB services for non-Hong Kong residents at all our branches.
- In line with the extension of the operating hours of the RMB RTGS system in Hong Kong, we upgraded our related services and extended our service hours. This service enhancement enables both personal and corporate customers in different time zones to enjoy the convenience of our settlement services.

Enhanced franchise for sustainable growth

- Investing in the Group’s franchise has always been a key management priority to bolster its long-term competitiveness. New business platforms set up over the past few years continued to deliver encouraging performance and received market recognition. Our custody business was named as the “Best Asian Bank for Cross-Border Custody” in the AsianInvestor Service Provider Awards 2012, in recognition of its outstanding cross-border custody services. The asset management team, set up in late 2010, has been granted five prestigious “2012 Best of the Best Awards” by Asia Asset Management. In November, we launched a new private banking platform to provide high-net-worth individuals and their families with unique and tailor-made wealth management services.
- In addition, we continued to build up our service capabilities and innovate products to cater to customer needs. For our securities brokerage business, we introduced a “Personalised Securities Services” to provide high-end customers with more flexible and



CHIEF EXECUTIVE'S REPORT

convenient trading services. Our mobile banking platform was further enhanced by being the first bank in the market to launch mobile functions for IPO share subscriptions and IPO financing. As a leader in the mortgage market, the Group pioneered the "1 Day Approval Mortgage Services" to facilitate more efficient loan applications for customers.

- The Group further optimised its distribution channels to meet the needs of both local and cross-border customers. A brand new concept branch was opened in Causeway Bay which offers a pleasant banking environment equipped with advanced banking service technologies and paperless counter services. Our automated channels were also enhanced in terms of network coverage and service functions. We upgraded our phone banking systems and services to meet the increasing demand for cross-border phone banking services. We launched the first chip-based ATM Card in Hong Kong, which not only offers greater security but also a number of new banking service functions. The Group's electronic platform and services were highly recognised in the industry with a number of awards received in 2012. The new corporate internet banking platform, BOCNET HK, was successfully launched which greatly enhanced the linkage of our e-banking and cash management platform with those of BOC and its overseas branches.
- For our Mainland operation, we further expanded our branch coverage to a total of 36 as at end of 2012. The enhancement of the Group's e-Banking platforms proved to be successful as the number of new accounts and transaction volume increased significantly.

Financial Performance

In 2012, the Group's profit attributable to the equity holders increased by 2.4% year-on-year to HK\$20,930 million, a record high since listing. Net operating income before impairment allowances was HK\$35,760 million, increased by 15.9% as compared to 2011. The growth was mainly driven by the increase in net interest income and net trading gain. Total operating expenses increased by

45.0% to HK\$11,402 million from a lower base in 2011 when a large net recovery from the underlying collateral of the Lehman Brothers Minibonds was recorded. Return on average total assets (ROA) and return on average shareholders' equity (ROE) was 1.24% and 14.91% respectively compared to 1.14% and 16.68% in 2011.

Excluding the impact of Lehman Brothers-related products, core operating expenses would have increased by 7.9% and cost-to-income ratio was at 32.15%. The increase reflected our investment in business expansion, annual salary adjustment and higher depreciation charges. The Group's profit attributable to the equity holders would have increased by 14.9%. ROA and ROE would have improved year-on-year by 0.23 percentage point to 1.24% and by 0.19 percentage point to 14.74% respectively.

For the period under review, net interest income rose by 12.4% year-on-year to HK\$24,708 million. The growth was driven by the widening of net interest margin which was 1.60%, up 28 basis points compared to 2011. The increase was mainly attributable to higher return on the offshore RMB business and eased diluting effect of the Group's RMB clearing bank business. Average interest-earning assets contracted by HK\$119.6 billion or 7.2%, mainly due to the drop in participating banks' RMB deposits with the clearing bank as a result of increased deployment of RMB funds in the market.

Net fee and commission income rose mildly by 0.9% year-on-year to HK\$7,906 million. Key growth drivers included fee and commission income from loans, credit cards and funds distribution. The increase, however, was mostly offset by the decline of commission income from securities brokerage, insurance and bills commissions, reflecting the subdued investors' sentiment and trade activities.

Net trading gain grew 83.0% year-on-year to HK\$3,129 million. The increase was mainly a result of higher net trading gain from interest rate instruments and items under fair value hedge, foreign exchange and foreign exchange products as well as equity instruments.



Total assets increased by 5.3% to HK\$1,830.8 billion as at 31 December 2012, mainly driven by increase in customer deposits. The Group pursued a proactive deposit strategy to support business growth while maintaining a cautious control of funding costs. Customer deposits expanded by 7.2% year-on-year to HK\$1,229.1 billion, driven by the increase in lower cost saving and demand deposits. Despite slower market demand, advances to customers grew healthily by 11.3% as compared with end-2011 to a total of HK\$778.3 billion with broad-based growth in both corporate and personal loans. Loan-to-deposit ratio increased to 63.32%, up 2.32 percentage points from the end of 2011. Overall loan quality remained sound with classified or impaired loan ratio at 0.26%.

Throughout the year, the Group continued to manage its capital and liquidity prudently. Consolidated CAR and core capital ratio as at 31 December 2012 were 16.80% and 12.31% respectively, compared to 16.90% and 12.51% at the end of 2011. Average liquidity ratio was at 41.2%, versus 36.17% a year ago.

The Board recommended the declaration of a final dividend of HK\$0.693 per share for 2012. Together with the interim dividend of HK\$0.545 per share, the total dividend of HK\$1.238 per share represents an increase of 4.2% year-on-year. The Group's total dividend payout as a percentage of profit attributable to the equity holders will be 62.5%.

Business Review

Personal Banking business delivered satisfactory performance in 2012 with solid growth in both loans and deposits. Net operating income before impairment allowances and profit before taxation reached HK\$11,643 million and HK\$5,513 million respectively.

We maintained our market leadership in new mortgage loans with 9.9% increase in residential mortgage loan balance. Our wealth management business posted solid performance with further increase in customer base. We enriched our products and services and provided more customised solutions to meet the different needs of our wealth management customers. Trading volume of the stock market in Hong Kong reduced substantially which dampened our brokerage business. Nevertheless, our other investment services performed strongly. Commission from

funds distribution rose substantially by 60.2%, benefiting from the Group's strong performance in the distribution of RQFII funds and product diversification. Credit card business sustained its growth momentum in 2012. Fee income from the credit card business grew by 14.5%, driven by the increase of 10.9% in cardholder spending and 14.6% in merchant acquiring volume. Credit card advances rose by 19.5%. In the Bancassurance business, the Group strengthened its position as a prominent life insurance provider and maintained its lead in the RMB insurance market.

Corporate banking business continued to make good progress and delivered broad-based income growth. Net operating income before impairment allowances increased by 14.3% to HK\$13,654 million while profit before taxation surged by 12.6% to HK\$9,725 million.

Despite slower loan demand in the market, the corporate loan book grew 11.6% with encouraging growth in offshore RMB loans. The pricing of our corporate loan book improved on the back of our consistent strategy to balance growth and profitability. It strived to provide "Total Solutions" with a full range of financial services, including innovative trade-related products and "Integrated Branches for Commercial Business", to better serve the needs of major corporate and SME customers.

We also maintained our position as the top mandated arranger in Hong Kong-Macau syndicated loan market. In recognition of its long-standing support for SMEs in Hong Kong, the Group received for the fifth consecutive year the "SME's Best Partner Award" presented by the Hong Kong General Chamber of Small and Medium Business Limited.

The Group made solid progress in developing its cash management business. The linkage of the Group's e-banking platform with those of BOC and its overseas branches has been completed. This has greatly stepped up the Group's cross-border cash management capabilities. Our custody business successfully secured mandates from a number of RQFII fund products. It also continued to expand its institutional client base and secured mandates to provide global custody services to various Qualified Domestic Institutional Investors.



CHIEF EXECUTIVE'S REPORT

Treasury segment recorded outstanding financial results in 2012. Net operating income before impairment allowances increased by 30.5% year-on-year to HK\$9,625 million while profit before taxation increased by 28.7% to HK\$8,382 million.

We continued to focus on prudently managing our banking book investments in view of the market complications and changes. Portfolio mix was further optimised. We increased our investments in government-related bonds, high quality bonds issued by Asia-Pacific financial institutions and corporations as well as RMB-denominated bonds.

On the product development front, we introduced various innovative products to help customers better manage their exchange rate risk and financing costs, which were well-received by customers. We also made good progress in expanding our offshore RMB business. As part of its ongoing efforts to facilitate the development of the offshore RMB bond market, the Group launched three new offshore RMB bond sub-indices and remained an active participant in the underwriting of offshore RMB-denominated bonds. Capitalising on our strong RMB franchise and close collaboration with BOC, we expanded our business relationships with banks and financial institutions in different geographical regions.

Our **Mainland** business delivered encouraging performance in a challenging banking environment. We recorded satisfactory growth in both deposits and loans which increased by 12.8% and 21.2% respectively. Net operating income increased by 17.9%.

The business platform of our NCB (China) was further strengthened in terms of product offering and distribution channels. A new series of products that were linked to interest rates, exchange rates, gold and commodity prices was introduced to cater to the increasing demand for wealth management services. Leveraging the "Channel Sharing" model, which allows NCB (China)'s debit card holders to access services through BOC's branches and ATMs, it helped boost deposit growth and generate more retail banking business. During the year, eight new NCB (China) sub-branches were added.

Insurance business recorded robust profit growth and maintained its strong position in the RMB insurance market. Net operating income before impairment allowances increased by 106.1% year-on-year to HK\$843 million. Profit before taxation grew substantially to HK\$609 million from a low base of HK\$33 million last year. The growth in profit was mainly attributable to the better investment performance as compared to an investment loss in 2011 amid the credit volatility in the financial market.

During the year, BOC Life was granted the approval to invest directly in the Mainland's interbank bond market, thus facilitating the expansion of RMB assets and the further development of its RMB insurance products. BOC Life received the honour of the "Hong Kong Offshore RMB Centre – 1st RMB Business Outstanding Awards – The Outstanding Insurance Business" organised by some local media.

Outlook

Looking into 2013, the overall operating environment looks mixed. We started the year with improved sentiment in global markets which brings along optimism to the outlook. However, some key fundamental issues in major economies are still unresolved which may continue to affect the stability of global markets. We, therefore, need to stay alert. Mainland China's economic performance, the US's fiscal cliff and the European debt crisis will remain the three major factors affecting the macroeconomic and market environment. There are still uncertainties over the pace of recovery for major economies and the growth could be fragile. Against this backdrop, the growth outlook for Hong Kong's economy would be modest.

For the local banking industry, banks may continue to face challenges coming from a fragile macro environment, persistently low interest rates and increasingly fierce competition. In addition, starting from 1 January 2013, the first phase of Basel III implementation has come into operation in Hong Kong. The new regulatory environment will require banks to operate on a higher capital base and efficiency. To adapt to the new capital requirement, banks may need to adjust their business strategies accordingly.



Despite the still challenging environment, the Group remains focused on driving its business development and capturing new opportunities, especially in the offshore RMB business. In January, leveraging the opportunities from the "Cross-boundary RMB Loan Trial Scheme in Qianhai", the Group swiftly launched its cross-border RMB loan business and signed agreements with five enterprises registered in Qianhai to provide them with cross-border RMB direct loans. BOCHK has also been designated as a market maker for the USD/CNH (offshore RMB) futures by the Chicago Mercantile Exchange Group, being the sole bank among the first group of market makers. Our asset management arm continues to expand its business through strategic partnerships with overseas financial institutions to develop RMB-related investment products. Capitalising on our strong RMB franchise, we will continue to create new growth drivers by expanding our business scope, customer base and geographical coverage. We will also continue to work closely with BOC, our parent bank, to promote the global RMB service capabilities of BOC Group.

In view of the evolving market trends, the Group will continue to broaden and strengthen its business capabilities to better serve the diverse needs of customers. The investments we made over the past years proved to be very effective in supporting the development of our major business segments. Capitalising on our enhanced platforms, we successfully deepened customer relationships and attracted new customers. Our strategy will remain customer-centric. Through product and service innovation as well as channel optimisation, we aim to substantially enhance the overall customer experience. We will continue to focus on our customer segmentation strategy to provide more customised services to targeted customers.

Maintaining a strong financial position will continue to be one of the management's key priorities, especially amid current market conditions. As shown in our 2012 results, all our key financial ratios were at solid levels with strong capital and liquidity profile. With Basel III implementation to be effective this year, the Group is well prepared to meet the new capital standards while continuing our growth plans. We will continue to adopt our proactive approach in managing our assets and liabilities. While striving for income and profit growth, we will exercise rigorous risk

management to safeguard our asset quality. We will also remain focused on disciplined cost control and attaining greater efficiency when growing our business.

2012 was the tenth anniversary of the Company's public listing in Hong Kong. I am pleased to see the healthy development and continuous reinforcement of our franchise over the past 10 years. For the success we achieved, I would like to express my deep appreciation to our customers and shareholders for their unwavering support and trust which enables us to realise our potential. I am also grateful to our Board of Directors for their wisdom and council. Of equal importance is the contribution of all my colleagues through their hard work and devotion.

Due to the need of the state financial work, Mr. XIAO Gang has resigned as Chairman and Non-executive Director of the Company and the Bank with effect from 17 March 2013. On behalf of the Group, I would like to take this opportunity to express our sincere gratitude and highest respect to him for his strong leadership and outstanding contributions during his tenure. We wish him every success in his new endeavour.

To support the Group's long-term development, we fully understand the importance of promoting sustainable development of the economy, society and environment where we operate. As a leading banking group in Hong Kong, we are committed to making positive contribution to the community's development and promoting CSR in every facet of our business. Going forward, I am confident that the Group will remain strongly positioned to capture quality growth opportunities and to create greater value for its stakeholders by building on its distinct competitive edges and financial strength.

HE Guangbei
Vice Chairman & Chief Executive

Hong Kong, 26 March 2013



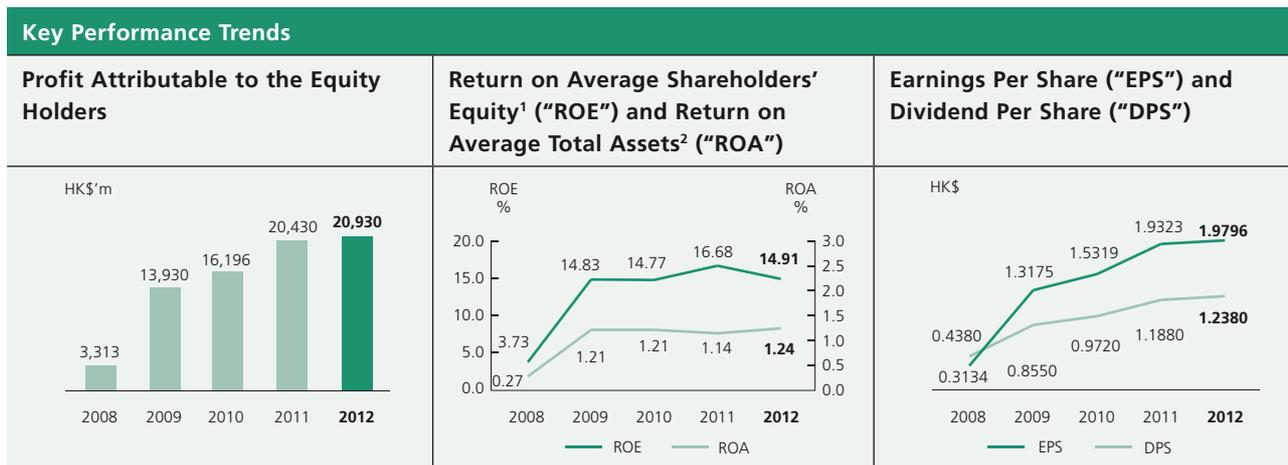
INNOVATIVE RMB SERVICE



MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL PERFORMANCE AND CONDITION AT A GLANCE

The Group achieved another set of encouraging financial results in 2012 with profit attributable to the equity holders reaching a new high. The financial position remains solid with key financial ratios at healthy levels.



Profit attributable to the equity holders reaching new high

- Profit attributable to the equity holders increased by 2.4% year-on-year to HK\$20,930 million, a record high since listing. Excluding the impact of Lehman Brothers-related products³, it would have increased by 14.9%.

Solid return with sustainable growth

- ROE was 14.91%. Excluding the impact of Lehman Brothers-related products, ROE would have been 14.74%, up 0.19 percentage point year-on-year.
- ROA was 1.24%. Excluding the impact of Lehman Brothers-related products, ROA would have remained at 1.24%, up 0.23 percentage point year-on-year.

Consistent return to shareholders

- EPS rose to HK\$1.9796. DPS was HK\$1.238, increasing by 4.2% year-on-year.

MANAGEMENT'S DISCUSSION AND ANALYSIS



Financial Position

Loan-to-Deposit Ratio ⁴	Capital Adequacy Ratio ⁵	Average Liquidity Ratio ⁶
<p>%</p> <p>2008 2009 2010 2011 2012</p> <p>* as at 31 December</p>	<p>%</p> <p>2008 2009 2010 2011 2012</p> <p>■ Core Capital Ratio ■ Capital Adequacy Ratio</p> <p>* as at 31 December</p>	<p>%</p> <p>2008 2009 2010 2011 2012</p>

Satisfactory loan and deposit growth

- Advances to customers increased by 11.3% while deposits from customers rose by 7.2%. Loan-to-deposit ratio was 63.32%.

Solid capital position to support business growth

- CAR was 16.80%, while core capital ratio stood at 12.31%.

Sound liquidity position

- Average liquidity ratio improved to 41.20%.

Key Operating Ratios

Net Interest Margin ("NIM")	Cost-to-Income Ratio	Classified or Impaired Loan Ratio ⁷
<p>%</p> <p>2008 2009 2010 2011 2012</p>	<p>%</p> <p>2008 2009 2010 2011 2012</p>	<p>%</p> <p>2008 2009 2010 2011 2012</p> <p>* as at 31 December</p>

Significant improvement in NIM

- NIM was 1.60%, up 28 basis points year-on-year with improved loan pricing and return on offshore RMB business as well as an eased diluting effect by the RMB clearing bank⁸ business.

Effective cost control

- Cost-to-income ratio was 31.88%, among the lowest in the industry. Excluding the impact of Lehman Brothers-related products, it would have fallen by 2.41 percentage points year-on-year.

Classified or impaired loan ratio at a low level

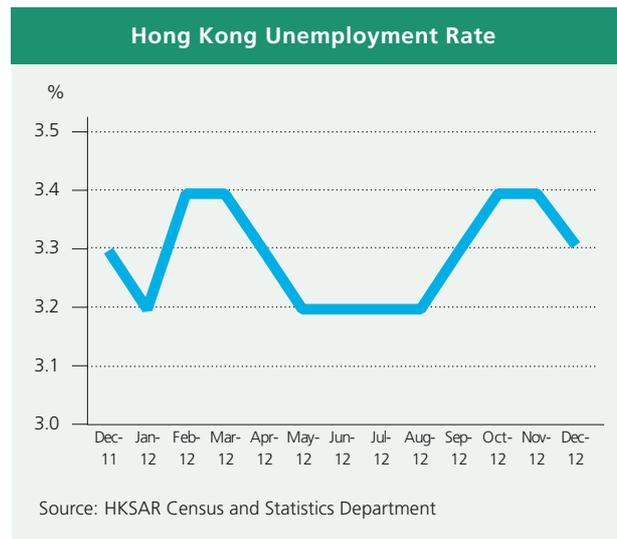
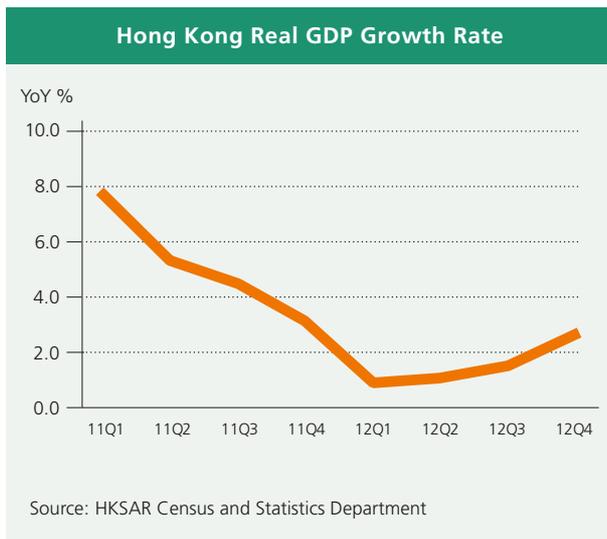
- Classified or impaired loan ratio stood at a sound level of 0.26%, below the market average.

- Return on Average Shareholders' Equity as defined in "Financial Highlights".
- Return on Average Total Assets as defined in "Financial Highlights".
- The net amount of HK\$97 million recovered by the Group in 2012 from the underlying collateral of the Lehman Brothers Minibonds was credited to operating expenses (2011: HK\$2,854 million). The net recovery together with the expenses of Lehman Brothers-related products is referred to as "impact of Lehman Brothers-related products" in the Management's Discussion and Analysis.
- The deposit base also includes structured deposits reported as "Financial liabilities at fair value through profit or loss".
- Capital adequacy ratio is computed on the consolidated basis that comprises the positions of BOCHK and certain subsidiaries specified by the HKMA for its regulatory purposes and in accordance with the Banking (Capital) Rules. The bases of regulatory capital calculation for credit risk, market risk and operational risk are described in Note 4.5 to the Financial Statements in this Annual Report.
- The average liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio of BOCHK for the year.
- Classified or impaired loans follow the definitions set out in the Banking (Disclosure) Rules under the Banking Ordinance 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.
- Since December 2003, the Bank has been appointed as the clearing bank to provide RMB clearing services in Hong Kong.

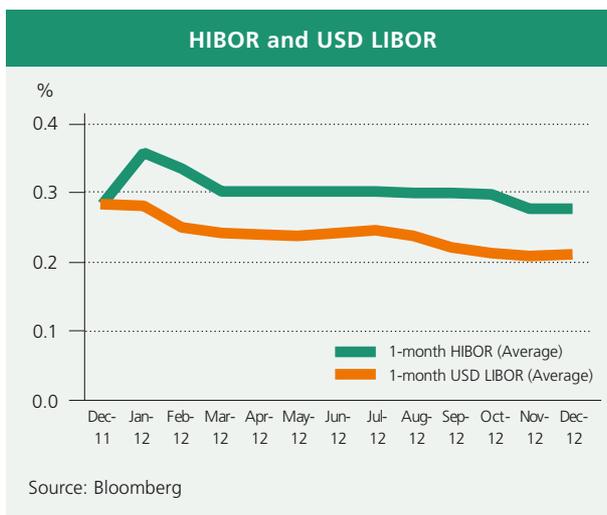
MANAGEMENT'S DISCUSSION AND ANALYSIS

ECONOMIC BACKGROUND AND OPERATING ENVIRONMENT

In 2012, the operating environment for Hong Kong's banking industry remained tough. The European debt crisis and the slow recovery of the US economy continued to weigh on the global economy. Economic fundamentals of the Eurozone further deteriorated, although the debt crisis stabilised as the European Central Bank pledged to save the Euro currency. Weak household balance sheets and growing fiscal uncertainties continued to hinder the growth in the US. In view of sluggish demand and high unemployment, the Federal Reserve extended its Operation Twist programme in June and announced an open-ended quantitative easing in September. Market interest rates remained at an extremely low level. On a positive note, the Mainland economy saw cyclical recovery from the marked slowdown earlier in the year with respective growth recorded in industrial production, investment and consumption.



Notwithstanding subdued external demand, the Hong Kong economy continued to grow at a modest pace. The GDP growth in 2012 was 1.4%. The unemployment rate remained at a low level. Inflationary pressure moderated, with the Composite CPI rising by 4.1% year-on-year in 2012.



The low interest rate environment in Hong Kong continued amid the ongoing accommodative monetary policy in the US. Average 1-month HIBOR and USD LIBOR fell slightly from 0.29% and 0.28% in December 2011 to 0.28% and 0.21% respectively in December 2012.

Investment sentiment in the Hong Kong stock market weakened in the first half in view of the deteriorating external environment. Nevertheless, with additional easing measures adopted by the US and the likely pick-up of economic growth in the Mainland, market sentiment improved in the fourth quarter. The Hang Seng Index reached the lowest point of the year at 18,186 in June and closed at 22,657 at the end of 2012, up 22.9% on a yearly basis.

MANAGEMENT'S DISCUSSION AND ANALYSIS



The local residential property market was buoyant since March 2012. The up-tick in the property market prompted the government to implement stabilising measures, including further tightening of mortgage criteria, raising Special Stamp Duty rates and extension of the restriction period. As a result, the level of transaction activity moderated towards the end of the year with the number of agreements for sale and purchase for residential building units in 2012 registering a decline over 2011. Meanwhile, the average price of private domestic properties showed a further increase from 2011.

During the year, the offshore RMB business in Hong Kong continued to expand. A series of initiatives were announced to support the development of the business. These included the further relaxation of investment restrictions in relation to the RMB Qualified Foreign Institutional Investors ("RQFII") scheme, the expansion of RMB services to non-Hong Kong residents and the introduction of the Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone ("Qianhai Cooperation Zone"), a new financial and commercial hub between the Mainland and Hong Kong. From a regulatory perspective, the HKMA revised regulations to enhance the liquidity of the offshore RMB market in Hong Kong. These changes provided banks with more business opportunities and allowed them additional flexibility and liquidity to facilitate offshore RMB transactions.

In summary, the operating environment for the banking industry was highly challenging in 2012. Local economic growth was weak and market competition intensified. Improvement of banks' net interest margin was also restrained by the low interest rate environment. Nevertheless, the further expansion of the offshore RMB business continued to present business opportunities to the banking sector.

Outlook for 2013

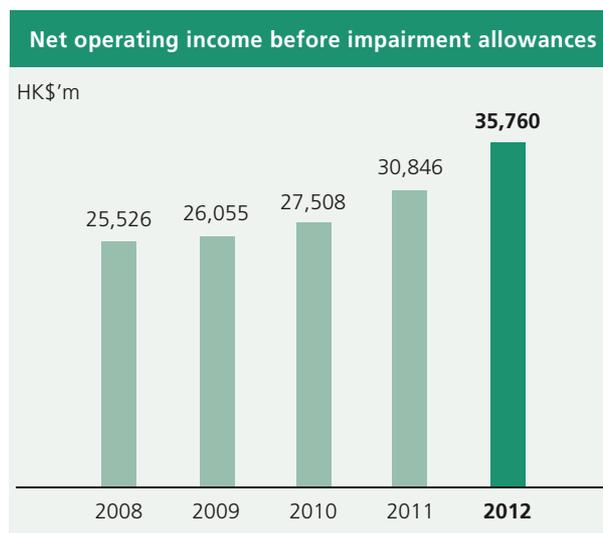
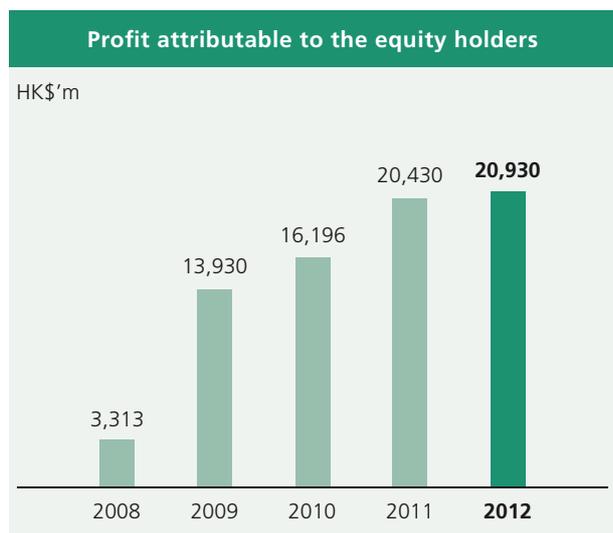
The outlook for the Hong Kong economy in 2013 remains challenging. It is expected that the local economy will continue to benefit from gradual economic recovery in the US and a pick-up in the Mainland, but uncertainties and challenges still exist, particularly in the external environment. The fiscal uncertainty in the US and the further evolution of the European debt crisis could pose major threats to the global economy and hence external demand for Hong Kong. Domestically, abundant liquidity leading to overheating of the property market and further asset rallies could bring huge volatility in the financial market. At the same time, persistently low interest rates continue to exert pressure on banks' profit. Additional regulatory requirements, including the implementation of Basel III, may increase banks' operating costs.

However, the continuing development of offshore RMB business in Hong Kong will provide new opportunities. New initiatives for the Qianhai Cooperation Zone and RQFII are expected to bring new customers and business opportunities to the banking sector in 2013.

MANAGEMENT'S DISCUSSION AND ANALYSIS

CONSOLIDATED FINANCIAL REVIEW

Financial Highlights



HK\$'m	2012	2011
Net operating income before impairment allowances	35,760	30,846
Operating expenses	(11,402)	(7,862)
Operating profit before impairment allowances	24,358	22,984
Operating profit after impairment allowances	23,499	22,478
Profit before taxation	25,521	24,680
Profit attributable to the equity holders of the Company	20,930	20,430

Despite external uncertainties and sluggish demand, the Group achieved encouraging financial results in 2012. By capitalising on its core competencies and proactively managing its assets and liabilities, the Group responded swiftly to market changes and was able to capture new business opportunities. As a result, the Group recorded solid growth in core businesses and saw increased contribution from the offshore RMB businesses. At the same time, it maintained stringent risk management in the challenging environment. The financial position of the Group remains solid with key financial ratios at healthy levels.

The Group's net operating income before impairment allowances increased by HK\$4,914 million or 15.9% to HK\$35,760 million. Net interest income was the major driver, with growth attributable to loan growth with improved yield and better deployment of RMB funds. Net fee and commission income rose slightly. Other income increased, mainly driven by the mark-to-market gain and growth in income from the Group's insurance segment. Operating expenses rose by 45.0%, primarily due to the net recovery from the underlying collateral of the Lehman Brothers Minibonds in 2011. Operating profit before impairment allowances grew by 6.0%. Excluding the impact of the Lehman Brothers related products, it would have increased by 20.2%. Net charge of loan impairment allowances increased while the net gain on investment property revaluation fell year-on-year. As a result, profit attributable to the equity holders of the Company rose by 2.4% compared to 2011. Excluding the impact of Lehman Brothers-related products, profit attributable to the equity holders would have increased by 14.9%.

As compared to the first half of 2012, the Group's net operating income before impairment allowances declined by 3.1% in the second half. The decrease was mainly due to the lower net interest income and the decline in net fee and commission income. It was partially offset by growth in other income. The Group recorded a higher net charge of loan impairment allowances and a lower net gain on investment property revaluation in the second half of the year. Profit attributable to the equity holders decreased by HK\$1,556 million or 13.8% on a half-on-half basis.

MANAGEMENT'S DISCUSSION AND ANALYSIS



Factors Affecting the Group's Performance in 2012

The key positive factors that contributed to the Group's 2012 financial performance are outlined below:

- The Group's proactive asset and liability management achieved a **healthy growth in both loans and deposits** with **effective control of deposit costs and improved loan pricing**.
- Fee and commission income on **traditional banking businesses** and **funds distribution** performed strongly with double-digit growth.
- The Group successfully captured business opportunities in the **offshore RMB business**. The better deployment of RMB funds is one of the key factors contributing the rise in profit.
- The Group further improved its service capabilities and focused on **operational efficiency**.

The Group's financial performance in 2012 was also subject to the following key negative factors:

- The exceptionally low market interest rates constrained enhancement of the Group's **asset yield**. Intense market competition for deposits also led to higher **funding costs**.
- The uncertain economic prospects resulting in **sluggish demand and lower trade activities** adversely affected the related fee income.

INCOME STATEMENT ANALYSIS

Net Interest Income and Margin

HK\$m, except percentages	2012	2011
Interest income	35,413	31,931
Interest expense	(10,705)	(9,952)
Net interest income	24,708	21,979
Average interest-earning assets	1,542,565	1,662,201
Net interest spread	1.49%	1.24%
Net interest margin [#]	1.60%	1.32%

[#] Net interest margin is calculated by dividing net interest income by average interest-earning assets.

The Group's net interest income increased by HK\$2,729 million or 12.4% year-on-year, driven by widening net interest margin. Average interest-earning assets contracted by HK\$119,636 million or 7.2%, mainly due to the drop in participating banks' RMB deposits with the clearing bank. Net interest margin was 1.60%, up 28 basis points compared to 2011, with net interest spread increasing by 25 basis points and contribution from net free funds rising by 3 basis points.

The growth in net interest margin was mainly attributable to improved return from the offshore RMB business and eased dilution by the Group's RMB clearing bank business. The return from the offshore RMB business improved with the increased deployment of RMB funds in loans and advances and bonds. In previous periods, the Group's RMB clearing bank business had a lower average spread than other businesses and dragged on overall net interest margin. In line with new developments in the offshore RMB market, participating banks reduced their RMB deposits with the clearing bank. As a result, the diluting effect of the Group's RMB clearing bank business on net interest margin was insignificant in 2012. Meanwhile, the pricing of corporate and residential mortgage loans improved, but the positive impact was partially offset by rising deposit costs amid keen market competition and increase in lower yielding investments in short-term debt securities.

MANAGEMENT'S DISCUSSION AND ANALYSIS

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

	Year ended 31 December 2012		Year ended 31 December 2011	
	Average balance HK\$'m	Average yield %	Average balance HK\$'m	Average yield %
ASSETS				
Balances and placements with banks and other financial institutions	335,842	2.43%	571,705	1.48%
Debt securities investments	471,662	2.07%	420,154	2.35%
Loans and advances to customers	720,488	2.38%	654,802	2.04%
Other interest-earning assets	14,573	1.71%	15,540	1.50%
Total interest-earning assets	1,542,565	2.29%	1,662,201	1.92%
Non interest-earning assets	191,823	–	161,788	–
Total assets	1,734,388	2.04%	1,823,989	1.75%

	Average balance HK\$'m	Average rate %	Average balance HK\$'m	Average rate %
	LIABILITIES			
Deposits and balances from banks and other financial institutions	143,219	0.68%	378,841	0.77%
Current, savings and fixed deposits	1,112,820	0.81%	1,023,278	0.61%
Subordinated liabilities	28,678	1.09%	27,800	2.02%
Other interest-bearing liabilities	44,012	0.92%	39,403	0.50%
Total interest-bearing liabilities	1,328,729	0.80%	1,469,322	0.68%
Non interest-bearing deposits	83,588	–	69,877	–
Shareholders' funds* and non interest-bearing liabilities	322,071	–	284,790	–
Total liabilities	1,734,388	0.62%	1,823,989	0.55%

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

Second Half Performance

Compared to the first half of the year, net interest income decreased by HK\$530 million, or 4.2%, to HK\$12,089 million. Average interest-earning assets dropped slightly by 0.3%. Net interest margin was 1.56%, down 8 basis points half-on-half. Average asset yields of debt securities and interbank placements were lower with the decline in market interest rates. Rising RMB customer deposit costs amid keen market competition, coupled with increase in lower yielding investments in short-term debt securities also put pressure on net interest margin. Meanwhile, RMB bonds and loans continued to increase while the pricing of corporate and residential mortgage loans also improved in the second half.

MANAGEMENT'S DISCUSSION AND ANALYSIS



Net Fee and Commission Income

HK\$'m	2012	2011
Credit cards business	3,307	2,887
Securities brokerage	2,114	2,782
Loan commissions	1,628	1,160
Insurance	965	1,097
Bills commissions	736	854
Payment services	667	637
Funds distribution	540	337
Trust and custody services	360	379
Safe deposit box	228	211
Currency exchange	156	156
Others	409	358
Fee and commission income	11,110	10,858
Fee and commission expenses	(3,204)	(3,025)
Net fee and commission income	7,906	7,833

Net fee and commission income increased by HK\$73 million, or 0.9%, to HK\$7,906 million. Fee and commission income from loans, credit cards and funds distribution grew strongly. The increase, however, was mostly offset by the decline of commission income from securities brokerage, insurance and bills, reflecting the subdued investors' sentiment and trade activities. Loan commissions surged by 40.3%, driven by higher commissions from corporate loans. Fee income from the credit card business grew by 14.5%, driven by the increase of 10.9% and 14.6% respectively in cardholder spending and merchant acquiring volume. Commission from funds distribution rose substantially by 60.2% with the Group's strong performance in the distribution of RQFII funds and its continuous efforts in developing products to meet customers' needs. Meanwhile, fee income from payment services also registered growth.

Second Half Performance

Compared to the first half of 2012, net fee and commission income decreased by HK\$298 million or 7.3% in the second half. Fee and commission income from the credit card business and funds distribution saw continued growth momentum from the first half. However, loan commissions dropped from a high level in the first half and insurance commission income decreased.

Net Trading Gain

HK\$'m	2012	2011
Foreign exchange and foreign exchange products	1,988	1,430
Interest rate instruments and items under fair value hedge	900	12
Equity instruments	120	82
Commodities	121	186
Net trading gain	3,129	1,710

Net trading gain was HK\$3,129 million, up HK\$1,419 million or 83.0% year-on-year. Reduction in foreign exchange loss on foreign exchange swap contracts* was the major driver for the increase in net trading gain from foreign exchange and foreign exchange products. This was partly offset by the lower gain from currency exchange activities. The growth in net trading gain from interest rate instruments and items under fair value hedge was mainly attributable to the mark-to-market changes on certain interest rate instruments, caused by market interest rate movements. The growth in net trading gain from equity instruments was mainly attributable to the gain from equity-linked products that were well received by customers. The decrease in trading gain from commodities was due to the decline in bullion transactions.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Second Half Performance

Compared to the first half of 2012, net trading gain increased by HK\$313 million or 22.2%. This was mainly due to the mark-to-market changes of foreign exchange swap contracts and certain interest rate instruments.

* 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 gain/(loss)"), 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 (FVTPL)

HK\$'m	2012	2011
Banking business of the Group	42	(1)
BOC Life	705	(339)
Net gain/(loss) on financial instruments designated at fair value through profit or loss	747	(340)

The Group recorded a net gain of HK\$747 million on financial instruments designated at FVTPL this year, compared to a net loss recorded in the previous year. The net gain in 2012 was mainly attributable to the mark-to-market changes of debt securities and the gain from equity investments of BOC Life, compared to the net loss in 2011 amid the weak financial market. The changes in market value of its securities portfolio were substantially offset by the corresponding changes in policy reserves, as reflected in the changes in net insurance benefits and claims which were attributable to the movement of market interest rates.

Second Half Performance

Net gain on financial instruments designated at FVTPL in the second half of the year was HK\$561 million, up HK\$375 million half-on-half. The gain recorded in the second half of the year was mainly attributable to the improved performance of BOC Life's investment portfolio amid the recovering financial market.

Operating Expenses

HK\$'m	2012	2011
Staff costs	6,406	6,038
Premises and equipment expenses (excluding depreciation)	1,456	1,390
Depreciation on owned fixed assets	1,493	1,277
Other operating expenses	2,143	1,954
Core operating expenses	11,498	10,659
Impact of Lehman Brothers-related products*	(96)	(2,797)
Total operating expenses	11,402	7,862

	At 31 December 2012	At 31 December 2011
Staff headcount measured in full-time equivalents	14,638	14,475

* Refer Note 12 to the Financial Statements for details.

MANAGEMENT'S DISCUSSION AND ANALYSIS



Total operating expenses increased by HK\$3,540 million, or 45.0%, to HK\$11,402 million, as there was a larger net recovery from the underlying collateral of the Lehman Brothers Minibonds in 2011. Core operating expenses rose by HK\$839 million, or 7.9%. The Group focused on operational efficiency and maintained disciplined cost control while continuing to invest in new business platforms and Mainland operations to support long-term business growth.

Staff costs increased by 6.1%, reflecting higher salaries as a result of annual salary increment and increase in headcount in the Mainland business.

Premises and equipment expenses rose by 4.7% with higher rental for branches in Hong Kong and the Mainland.

Depreciation on owned fixed assets rose by 16.9% due to larger depreciation charge on premises following upward property revaluation in Hong Kong and on IT equipment as the Group continued to invest in its IT infrastructure.

Other operating expenses were up 9.7% mainly due to higher expenses to support business growth, such as marketing expenses, and business taxes of NCB (China).

Compared to the end of 2011, headcount measured in full-time equivalents rose by 163, mostly in the Mainland business as a result of the expansion of NCB (China).

Second Half Performance

Compared to the first half of 2012, operating expenses rose by HK\$620 million. The increase was due to higher staff costs, marketing, rental and depreciation expenses, as well as business taxes of the Mainland business in the second half of the year.

Net Charge of Loan Impairment Allowances

HK\$'m	2012	2011
Net charge of allowances before recoveries		
– individual assessment	(512)	(12)
– collective assessment	(606)	(720)
Recoveries	264	353
Net charge of loan impairment allowances	(854)	(379)

The Group maintained stringent risk management in a volatile economic environment. Overall loan quality remained sound. The net charge of loan impairment allowances amounted to HK\$854 million, up HK\$475 million from previous year, owing to the increase in the net charge of individually assessed impairment allowances.

Net charge of individually assessed impairment allowances increased to HK\$512 million, mainly caused by the downgrade of a few corporate loans.

Net charge of collectively assessed impairment allowances decreased year-on-year. The higher net charge in 2011 was largely due to the stronger loan growth.

Recoveries amounted to HK\$264 million, down HK\$89 million or 25.2% from 2011.

Second Half Performance

A net charge of loan impairment allowances of HK\$767 million was recorded in the second half of 2012, up from a net charge of HK\$87 million in the first half. The increase was mainly due to a higher net charge of individual assessed impairment allowances.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Total loan impairment allowances as a percentage of gross advances to customers

	At 31 December 2012	At 31 December 2011
Loan impairment allowances		
– individual assessment	0.10%	0.03%
– collective assessment	0.38%	0.37%
Total loan impairment allowances	0.48%	0.40%

BALANCE SHEET ANALYSIS

Asset Deployment

HK\$m, except percentages	At 31 December 2012		At 31 December 2011	
	Amount	% of total	Amount	% of total
Cash and balances with banks and other financial institutions	198,748	10.9%	278,795	16.0%
Placements with banks and other financial institutions maturing between one and twelve months	66,025	3.6%	107,910	6.2%
Hong Kong SAR Government certificates of indebtedness	82,930	4.5%	65,890	3.8%
Securities investments ¹	531,696	29.0%	425,600	24.5%
Advances and other accounts	819,739	44.8%	755,229	43.5%
Fixed assets and investment properties	63,107	3.4%	52,091	3.0%
Other assets ²	68,518	3.8%	52,995	3.0%
Total assets	1,830,763	100.0%	1,738,510	100.0%

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

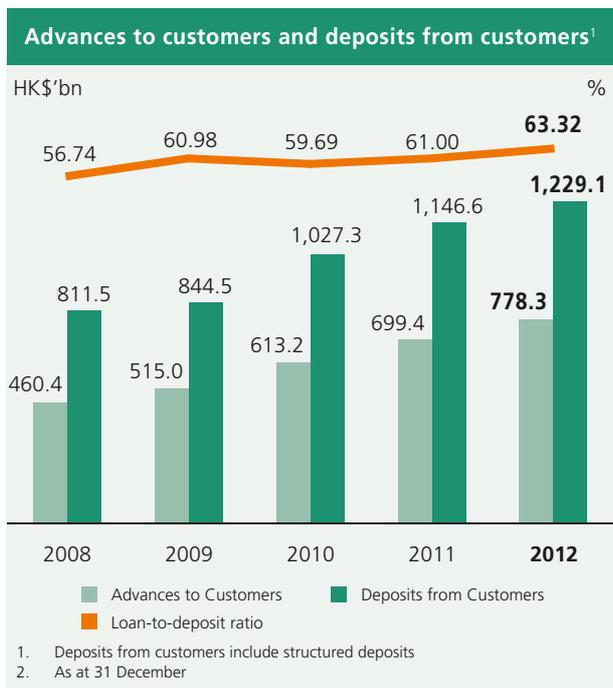
2. Interests in associates, deferred tax assets and derivative financial instruments are included in other assets.

As at 31 December 2012, the Group's total assets amounted to HK\$1,830,763 million, increasing by HK\$92,253 million or 5.3% from the end of 2011. In 2012, the Group continued to strengthen its asset and liability management with the aim to improve profitability and enhance its risk profile. It maintained a balanced strategy in business growth. Conscious efforts were made to enhance loan pricing, control funding costs and optimise asset allocation.

Key changes in the Group's total assets include:

- Cash and balances with banks and other financial institutions decreased by 28.7%, mainly due to the decrease in RMB funds placed with the People's Bank of China ("PBOC") by BOCHK's clearing business as participating banks' RMB deposits with the clearing bank continued to decline.
- Placements with banks and other financial institutions maturing between one and twelve months dropped by 38.8% as the Group redeployed its funds for advances to customers and securities investments.
- Securities investments increased by 24.9% with increase mainly in government-related bonds, high-quality financial institutions and corporate bonds.
- Advances and other accounts rose by 8.5%, which was mainly attributable to the growth in advances to customers by 11.3%.
- Other assets grew strongly by 29.3%, which was mainly led by the increase in reinsurance assets, derivative financial instruments as well as accounts receivable and prepayments.

MANAGEMENT'S DISCUSSION AND ANALYSIS



Advances to Customers

HK\$'m, except percentages	At 31 December 2012		At 31 December 2011	
	Amount	% of total	Amount	% of total
Loans for use in Hong Kong	480,753	61.8%	444,540	63.6%
Industrial, commercial and financial	252,877	32.5%	237,557	34.0%
Individuals	227,876	29.3%	206,983	29.6%
Trade finance	67,137	8.6%	59,508	8.5%
Loans for use outside Hong Kong	230,374	29.6%	195,331	27.9%
Total advances to customers	778,264	100.0%	699,379	100.0%

Despite the global economic slowdown, the Group continued to capitalise on its strong customer base and financial position to capture loan growth opportunities. At the same time, it adhered to stringent risk control and customer selection to achieve quality and sustainable growth. Advances to customers grew by HK\$78,885 million or 11.3% to HK\$778,264 million in 2012.

Loans for use in Hong Kong grew by HK\$36,213 million or 8.1%.

- Lending to the industrial, commercial and financial sectors increased by HK\$15,320 million, or 6.4%, to HK\$252,877 million, covering a wide range of industries. Lending to the information technology, manufacturing and property investment sectors grew by 33.1%, 25.4% and 5.6% respectively.
- Lending to individuals increased by HK\$20,893 million, or 10.1%. Residential mortgage loans (excluding those under the Government-sponsored Home Ownership Scheme) grew by 9.9% as the Group captured the growth opportunities arising from the revival of the local residential property market. Credit card advances increased by 19.5%. Other loans to individuals rose by 20.1%.

Trade finance rose by HK\$7,629 million, or 12.8%. Meanwhile, loans for use outside Hong Kong grew by HK\$35,043 million or 17.9%.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Second Half Performance

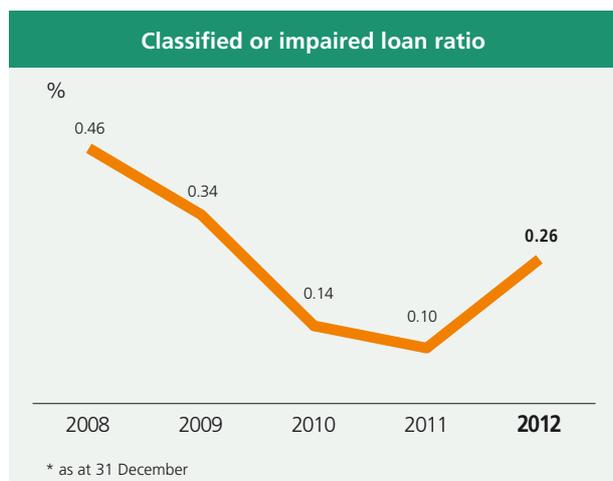
Loan growth slowed down in the second half of the year against the backdrop of slowing economic growth. The Group's advances to customers increased by HK\$31,512 million or 4.2%, mainly driven by the growth in lending to individuals and loans for use outside Hong Kong.

Loan Quality

HK\$m, except percentages	At 31 December 2012	At 31 December 2011
Advances to customers	778,264	699,379
Classified or impaired loan ratio	0.26%	0.10%
Impairment allowances	3,705	2,830
Regulatory reserve for general banking risks	7,754	6,967
Total allowances and regulatory reserve	11,459	9,797
Total allowances as a percentage of advances to customers	0.48%	0.40%
Impairment allowances ¹ on classified or impaired loan ratio	37.44%	39.86%
Residential mortgage loans ² – delinquency and rescheduled loan ratio ³	0.02%	0.01%
Card advances – delinquency ratio ³	0.17%	0.16%

	2012	2011
Card advances – charge-off ratio ⁴	1.24%	1.07%

- 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.
- Residential mortgage loans exclude those under the Home Ownership Scheme and other government-sponsored home purchasing schemes.
- Delinquency ratio is measured by a ratio of total amount of overdue loans (more than three months) to total outstanding loans.
- Charge-off ratio is measured by a ratio of total write-offs made during the year to average card receivables during the year.



The Group's overall loan quality remained sound. The classified or impaired loan ratio was at 0.26%. Classified or impaired loans rose by HK\$1,344 million to HK\$2,054 million, mainly due to the downgrade of a few corporate loans. Formation of new classified loans in 2012 represented approximately 0.26% of total loans outstanding.

Total impairment allowances, including both individual assessment and collective assessment, amounted to HK\$3,705 million. Total impairment allowances on classified or impaired loans as a percentage of total classified or impaired loans was at 37.44%.

The credit quality of the Group's residential mortgage loans remained sound with the combined delinquency and rescheduled loan ratio standing at 0.02% at the end of 2012. As compared to 2011, the charge-off ratio of card advances increased by 0.17 percentage point to 1.24%, better than the market average.

MANAGEMENT'S DISCUSSION AND ANALYSIS



Deposits from Customers*

HK\$m, except percentages	At 31 December 2012		At 31 December 2011	
	Amount	% of total	Amount	% of total
Demand deposits and current accounts	97,295	7.9%	77,440	6.7%
Savings deposits	603,565	49.1%	504,868	44.0%
Time, call and notice deposits	525,430	42.8%	563,643	49.2%
	1,226,290	99.8%	1,145,951	99.9%
Structured deposits	2,841	0.2%	639	0.1%
Deposits from customers	1,229,131	100.0%	1,146,590	100.0%

* Including structured deposits.

The Group maintained a proactive deposit strategy to support business growth with cautious control of funding costs. In spite of intense competition, the Group enlarged its deposit base by HK\$82,541 million, or 7.2% to HK\$1,229,131 million. Demand deposits and current accounts grew by 25.6% while savings deposits increased by 19.5%. Time, call and notice deposits fell by 6.8%. The Group's loan-to-deposit ratio was 63.32% at the end of 2012, up 2.32 percentage points from the end of last year.

Second Half Performance

Total deposits from customers increased by HK\$43,850 million or 3.7% in the second half of 2012. Demand deposits and current accounts increased strongly by 31.5% while savings deposits went up by 15.0%. Time, call and notice deposits declined by 10.1%.

Capital and Reserves Attributable to the Equity Holders of the Company

HK\$m	At 31 December 2012	At 31 December 2011
Share capital	52,864	52,864
Premises revaluation reserve	31,259	23,150
Reserve for fair value changes of available-for-sale securities	5,510	1,787
Regulatory reserve	7,754	6,967
Translation reserve	771	674
Retained earnings	52,811	44,323
Reserves	98,105	76,901
Capital and reserves attributable to the Equity Holders of the Company	150,969	129,765

Capital and reserves attributable to the equity holders increased by HK\$21,204 million, or 16.3% to HK\$150,969 million at 31 December 2012. Retained earnings increased by 19.2%, reflecting the 2012 profit after the appropriation of dividends. Premises revaluation reserve increased by 35.0%, which was attributable to the increase in property prices in 2012. Regulatory reserve rose by 11.3% due to loan growth. Reserve for fair value changes of available-for-sale securities increased by 208.3%, mainly due to the changes in market interest rates.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Capital and Liquidity Ratio

HK\$m, except percentages	At 31 December 2012	At 31 December 2011
Core capital after deductions	89,096	84,600
Supplementary capital after deductions	32,452	29,654
Total capital base after deductions	121,548	114,254
Total risk-weighted assets	723,699	676,024
Capital adequacy ratios (consolidated basis)		
Core capital ratio	12.31%	12.51%
Capital adequacy ratio	16.80%	16.90%

	2012	2011
Average liquidity ratio	41.20%	36.17%

Consolidated capital adequacy at 31 December 2012 was 16.80%, down 0.10 percentage point from that at the end of 2011. Total capital base expanded by 6.4% to HK\$121,548 million, mainly due to the increase in retained earnings. Total risk-weighted assets increased by 7.1% to HK\$723,699 million. The increase was mainly due to the growth of credit risk-weighted assets in light of the growth in loans and debt securities investments in 2012. The increase was counterbalanced by the effect of no additional risk-weighted amount required for the capital floor adjustment as the Group's capital charges for the year exceeded the required capital floor amount*.

For information on the components of total capital base and type of capital instruments used, please refer to Note 4.5 and 41 to the Financial Statements in this Annual Report.

The average liquidity ratio in 2012 remained strong at 41.20%.

* The HKMA requires that all reporting institutions using the IRB approach (whether foundation or advanced) for capital adequacy purposes are subject to a capital floor for the first three years of the adoption of the IRB approach. The use of the capital floor is to prevent a sudden fall in capital charges solely as a result of the changes in how the risk-weighted amount for credit risk is measured. The capital floor is derived by applying an adjustment factor to the capital charge calculated under the STC approach where the adjustment factors are 90%/80%/70% for the respective 1st/2nd/3rd year of the implementation of IRB approach. As at 31 December 2012 and in its second year of the implementation of IRB approach, the Group's capital charges exceeded the capital floor amount as required by the HKMA and therefore no additional risk-weighted amount was required for the year.



BUSINESS REVIEW

2012 Business Highlights

Personal Banking

- Maintained leading position in residential mortgages with a larger market share
- Commission income from funds distribution surged by 60.2% through widened and customer-oriented product offerings and enhanced sales model
- Introduced three new funds through BOCHK Asset Management Limited
- Consolidated Wealth Management platform and launched Private Banking service to high-net-worth customers
- Achieved strong growth in credit card business with credit card advances rising by 19.5%
- Continued to invest in servicing capabilities via branches, electronic means and cross-border connection to elevate customer experience
- Received "Best Internet Banking" and "Best Mobile Telephone Banking" awards under the Capital Weekly Service Awards 2012

Corporate Banking

- Remained the top mandated arranger in the Hong Kong-Macau syndicated loan market
- Recorded a healthy growth of 11.6% in corporate loans with improvement in pricing
- Received "SME's Best Partner Award" for the fifth consecutive year
- Further expanded the range of cash management services and launched the new corporate internet banking platform, BOCNET HK
- Expanded the client base for custody services with BOCHK being named the "Best Asian Bank for Cross-Border Custody" in the AsianInvestor Service Provider Awards 2012

Treasury

- Proactively adjusted portfolio mix to enhance return while staying attuned to risk. Increased investments in government-related bonds, high-quality financial institutions and corporate bonds as well as RMB-denominated bonds
- Extended the overseas RMB banknotes business and established business relationships with banks, financial institutions and non-bank institutions in different countries and regions

Insurance

- Maintained leading position in RMB insurance market in Hong Kong
- Improved product features and varieties to meet changing customer needs
- Granted approval to invest directly in the Mainland's interbank bond market

Mainland Business

- Focused on asset and liability management to improve asset yields and deposit mix
- Expanded branch network to a total of 36 at end-2012 with the addition of nine new sub-branches
- "Channel Sharing" with BOC garnered satisfactory business growth and became a vital service channel
- SME business platform achieved success with strong business momentum

RMB Business in Hong Kong

- Maintained leading position in offshore RMB banking businesses, including deposit taking, trade settlement, bond underwriting, credit card and insurance
- Arranged the first 100% RMB-denominated syndicated loan
- Launched RMB services to non-Hong Kong residents from August 2012
- Remained the largest service provider for RQFII authorised funds in the market
- Launched three new offshore RMB bond sub-indices
- Extended operating hours of the RMB RTGS system

Others

- BOCHK Asset Management Limited established exclusive partnerships for the provision of investment services with the World Bank in Hong Kong, a prestigious private bank in Germany and a reputable asset management company in Taiwan
- BOCHK Asset Management Limited was granted five prestigious "2012 Best of the Best Awards" by Asia Asset Management

MANAGEMENT'S DISCUSSION AND ANALYSIS

Business Segment Performance

Profit before Taxation by Business Segments

HK\$m, except percentages	2012		2011	
	Amount	% of total	Amount	% of total
Personal Banking	5,513	21.6%	4,896	19.8%
Corporate Banking	9,725	38.1%	8,636	35.0%
Treasury	8,382	32.8%	6,515	26.4%
Insurance	609	2.4%	33	0.1%
Others ¹	1,292	5.1%	4,600	18.7%
Total profit before taxation	25,521	100.0%	24,680	100.0%

1. Profit before taxation of Others in 2012 and 2011 included the net recovery from the underlying collateral of the Lehman Brothers Minibonds.
2. For additional segmental information, see Note 49 to the Financial Statements.

PERSONAL BANKING

Financial Results

Personal Banking recorded an increase of HK\$617 million, or 12.6%, in profit before taxation.

Net interest income increased notably by 15.5%. This was made possible by the improvement in deposit spread coupled with the growth in average loans and deposits. Personal loans and customer deposits grew by 10.7% and 10.9% respectively from last year end.

Net fee and commission income decreased by 2.4%, mainly due to the lower commission income from securities brokerage as investors' sentiment weakened. Nevertheless, there was strong growth in fee income from funds distribution and credit cards. Net trading gain dropped by 4.1%, due to lower foreign exchange related income.

Business operation

The Group's Personal Banking business continued to flourish in 2012. Growth was satisfactory in both the deposit and lending businesses. It remained the market leader in new mortgage loans and gained a larger market share in its loan outstanding. The funds and bond distribution businesses performed strongly. In addition to the Group investing in service enhancement and consolidating its wealth management business, the new Private Banking service was launched to provide unique and tailor-made services targeted at high-net-worth customers. Distribution channels were further optimised to enhance customer experience.

Residential mortgages – gaining a larger market share

With the widest range of products and dedicated services across all channels, the Group was the bank of choice and the market leader in new mortgage loans during the year. The "1 Day Approval Mortgage Services" was the first-of-its-kind in the market, allowing eligible home buyers to obtain formal approval of their mortgage loan applications within one business day. RMB mortgage services to non-Hong Kong residents was also the first in the market. At the end of 2012, the balance of the Group's mortgage book grew by 9.9% compared with the end of last year.

Investment and insurance businesses – robust growth in the sales of funds and bonds

In 2012, sentiment in the local stock market was adversely affected by the external environment. Nevertheless, the Group continued to expand its stock brokerage services to reinforce its strong position in the personal securities business. In addition to maintaining stable trading environments through various channels, including internet, mobile and phone banking as well as at branches, new services continued to be rolled out during the year to strengthen the Group's service range. IPO share subscriptions and IPO financing through mobile banking were launched to give convenience to customers. The "Personalised Securities Services" was introduced to provide high-end customers with more flexible and convenient trading services. The Group also launched the new "Securities Club" which provides services suited to the needs of customers of various segments.

MANAGEMENT'S DISCUSSION AND ANALYSIS



With regards to the funds distribution business, the Group rolled out new products to both high-end and mass retail customers. A private fund, the “BOCHK Asian Dynamic Income Fund”, and two retail funds, the “BOCHK-World Bank Emerging Markets Bond Fund” and the “BOCHK All Weather Global Opportunities Fund”, were launched. During the year, the Group distributed 14 RQFII funds, making it the largest distributor of RQFII funds in Hong Kong. As a result, commission income from funds distribution surged by 60.2% year-on-year. The Group also actively engaged in the bond distribution business. It underwrote a significant number of RMB bond issuances in the market with a substantial increase in turnover compared with 2011. At the same time, considerable effort was put into diversifying the business by engaging in USD and HKD bond issuance, which was well received by customers. The Group's private placement services for bonds in the secondary market were launched in January 2012. Meanwhile, the Group led the iBond market in terms of over-the-counter turnover. As a result, the Group achieved considerable improvement in commission from bond distribution.

In the Bancassurance business, the Group strengthened its position as a prominent life insurance provider and maintained its lead in the RMB insurance market. It continued to roll out different new products to meet customers' demand at different life stages and aimed to be the life partner of all customers. The “IncomeGrowth Annuity Insurance Plan” was introduced to offer life protection with guaranteed annuity payments. Professional training programmes were conducted throughout the year to develop the financial planning team's sales capabilities.

Credit card business – double-digit volume growth

The Group's credit card business sustained its growth momentum in 2012. It maintained its leadership in the China UnionPay merchant acquiring business and card issuing business. Dual currency credit cards were offered to Hong Kong and non-Hong Kong residents. The Group continued to exploit its competitive edge by launching appealing merchant offer programmes to customers through its comprehensive merchant network in Hong Kong, Macau and the Mainland. Credit card advances rose by 19.5%. Cardholder spending and merchant acquiring volumes grew by 10.9% and 14.6% respectively.

Wealth Management service – one-stop wealth management solutions

In 2012, the Group consolidated its Wealth Management service platform to strengthen its brand awareness and position in the market. It strived to foster long-term relationships with Wealth Management customers by offering more diverse services and customised solutions to meet their different needs. In addition, the Group launched Private Banking services to cater to the more sophisticated needs of high-net-worth customers and fulfil increasing demand for premium services in the Mainland and the rest of Asia. The Group also strengthened cooperation with BOC branches to provide banking services with extra convenience to customers of the two banks. The linkage of BOCHK's customer service hotline with that of BOC was completed, providing cross-border enquiry services between the two banks. The Group also launched “Time Housekeeper” service, allowing Wealth Management customers of BOCHK and BOC's branches in Guangdong province to perform designated services in selected branches in either region by advanced appointment. At the end of 2012, the total number of Wealth Management customers and the value of their assets under management increased by 6.7% and 18.0%, respectively, from end-2011.

Distribution channels – a new concept branch was grandly opened

The Group continued to optimise its distribution channels to meet the needs of both local and cross-border customers. During the year, a brand new concept branch, in a unique and contemporary design, was opened in Causeway Bay, to enhance customer service experience. At the end of 2012, the Group's service network in Hong Kong comprised 269 branches, including 140 wealth management centres.

The Group further invested in automated banking channels. In April, it launched Hong Kong's first chip-based ATM card with enhanced security and new banking service functions. The features of the Group's e-Banking platform were expanded, including the use of a new security device for two-factor authentication.

In recognition of its well-received electronic platform and outstanding services, the Group was honoured with the “Best Internet Banking” award for the fourth consecutive year and the “Best Mobile Telephone Banking” award for the second consecutive year under the Capital Weekly Service Awards 2012. The Group also received the “2012 APCCAL Recognition Award – HKCCA Awards Best Contact Centre in Sustainability” by Asia Pacific Contact Centre Association Leaders (“APCCAL”) and 11 other awards by the Hong Kong Call Centre Association (“HKCCA”).



MANAGEMENT'S DISCUSSION AND ANALYSIS

CORPORATE BANKING

Financial Results

Corporate Banking recorded a growth of HK\$1,089 million, or 12.6%, in profit before taxation. This was mainly attributable to the increase in net interest income as well as net fee and commission income.

Net interest income rose by 14.0%, mainly driven by the growth of loans and deposits. Corporate loans and customer deposits grew by 11.6% and 3.3% respectively.

Net fee and commission income increased by 13.4%, largely led by the growth in loan commissions and trust services, which was partly set off by the decline of bills commissions. Net trading gain rose by 22.1%, mainly attributable to higher income from foreign exchange services.

Business operation

Despite sluggish demand from corporates, the Group's Corporate Banking business maintained its growth momentum in 2012. It strived to provide "Total Solutions", with a full range of financial services, including innovative trade-related products and "Integrated Branches for Commercial Business", to better serve customers' needs. As a result, corporate loans grew satisfactorily with improvement in loan pricing. The Group also made good progress in its custody and cash management businesses. It was the largest custody service provider for RQFII authorised funds in the market. The service range of the cash management business was significantly expanded and the new corporate internet banking platform, BOCNET HK, was successfully launched.

Corporate lending business – 11.6% growth of corporate loans

The Group continued to focus on providing "Total Solutions" for core customers, and tailor-made services to large corporates and public sector entities. The Group also worked closely with BOC through the "Global Relationship Manager Programme" to provide comprehensive cross-border services to its customers. It strengthened customer relationships by enhancing expertise in industry management with better customer segmentation. At the end of 2012, the Group's balance of corporate loans grew by 11.6% from the end of 2011 with improvement in loan pricing. In 2012, the Group successfully arranged the first 100% RMB-denominated syndicated loan in Hong Kong and it remained the top mandated arranger in the Hong Kong-Macau syndicated loan market.

SME business – "SME's Best Partner Award" for the fifth consecutive year

The Group enhanced its services for SME customers by offering total solutions and participating actively in the new "SME Financing Guarantee Scheme" supported by the HKSAR government. It optimised the business model of "Integrated Branches for Commercial Business" by establishing exclusive counters in selected branches and launching the "Business Integrated Account" to provide one-stop financial solutions to SME companies and their proprietors, partners and shareholders. In recognition of its long-standing support for SMEs in Hong Kong, the Group received for the fifth consecutive year the "SME's Best Partner Award" presented by the Hong Kong General Chamber of Small and Medium Business Limited.

Trade finance – launched innovative products

The Group further enhanced its competitiveness in the trade finance business and led the market in product innovation. New products and services launched this year included "RMB Offshore Export Finance" and "Supply-chain Finance". In recognition of its contribution to the shipping industry by offering the innovative "Multi-currency Shipping Finance (RMB and USD)", the Group was granted the "Innovation Award – Business Innovation" by Lloyd's List Global Awards 2012. The Lloyd's List is a leading daily newspaper in the global maritime industry. The provision of this finance product has marked a number of milestones for the Group in the industry, including the first export shipping contract settled in RMB and issuance of the first cross-border RMB Refund Guarantee. At the end of 2012, the Group's balance of trade finance grew by 12.8% from the end of 2011.

MANAGEMENT'S DISCUSSION AND ANALYSIS



Cash Management service – expanded service range

The Group made solid progress in developing its cash management business. BOCNET HK, a new corporate internet banking platform targeting medium to large corporates, was launched to meet cash management needs as well as provide comprehensive e-banking services. “Business Integrated Account” was introduced during the year to provide better banking services to its corporate customers. The intra-day cash pooling service was launched to facilitate the development of internal cash pools by corporate customers for better internal cash flow management. In addition, the Group introduced “SWIFT for Corporate Service” to allow corporate customers to give instructions and communicate with the bank via the SWIFT network.

Custody service – further expansion of client base

The Group's custody business continued to flourish in 2012. It successfully secured mandates from a number of RQFII fund products during the year and was the largest service provider for RQFII authorised funds in the market. It continued to expand its institutional client base and secured mandates to provide global custody services to various Qualified Domestic Institutional Investors. In recognition of its outstanding cross-border custody capabilities and services, BOCHK won the “Best Asian Bank for Cross-Border Custody” in the AsianInvestor Service Provider Awards 2012. At the end of 2012, excluding the RMB fiduciary account for participating banks, total assets under the Group's custody were valued at HK\$619 billion.

Risk management – proactive measures to safeguard asset quality

The Group continued to carry out rigorous risk management and credit control to safeguard asset quality in a volatile economic environment. Through frequent and comprehensive market and industry analysis, the Group has put in place prudent credit standards for corporate lending under the principle of “Know Your Customers”. Furthermore, rigorous post-lending monitoring measures are taken to track early signs of loan deterioration and formulate timely and effective precautionary courses of action.

MAINLAND BUSINESS

Financial performance – encouraging growth

In 2012, the Group's Mainland business maintained encouraging growth in a challenging banking environment. Customer deposits and loans registered satisfactory growth of 12.8% and 21.2% respectively from the end of last year. Loan quality remained sound. During the year, the PBOC cut benchmark deposit and loan interest rates and adjusted the interest rate floating range. Both of these posed pressure on interest margin of the Mainland business. Nevertheless, the Group swiftly adjusted its asset and liability structure to improve asset yields. As a result, net operating income increased by 17.9%.

Product and service offerings – enhanced product and service capability

In response to the increasing demand for wealth management services, the Group successfully introduced a new series of “Yi Da” wealth management products. The return of these products is linked to interest rates, exchanges rates, gold and commodity prices. The first series of off-balance sheet wealth management products, “Yixiang”, was also launched in the second half of the year. All wealth management products can be accessed through the e-Banking platform. NCB (China) has been granted regulatory approval for the issuance of credit cards in the Mainland. The SME business platform was instrumental to the completion of the “SME Business Win” product series, leading to strong growth in both loans to and deposits from SMEs.

Distribution channels – expanded branch network and channel sharing with BOC

The Group continued to deepen business collaboration with BOC. The “Channel Sharing” model, which allows NCB (China)'s debit card holders to access services through BOC's branches and ATMs, has been effective in serving its purpose. The model not only boosted deposit growth but also generated more retail banking business, becoming one of the most vital service channels for card holders. Meanwhile, the enhancement of the Group's e-Banking platforms proved to be successful as the number of new accounts and transaction volume increased significantly. During the year, there was an addition of nine new sub-branches, including eight NCB (China) sub-branches and one sub-Branch of Chiyu Banking Corporation Limited. The Group's total number of branches and sub-branches in the Mainland increased to 36 by the end of 2012.



MANAGEMENT'S DISCUSSION AND ANALYSIS

TREASURY

Financial Results

Treasury recorded a strong year-on-year increase of 28.7% in profit before taxation.

Net interest income increased by 15.4%. This was mainly driven by an increase in the balance of debt securities investments coupled with the improved yield on interbank placements.

Net trading gain was up 158.7%. The increase was mainly caused by the lower foreign exchange loss on foreign exchange swap contracts and the improved mark-to-market changes of certain interest rate instruments.

Business Operation

Proactive investment strategy – enhanced portfolio return while staying attuned to risk

The Group continued to take a proactive approach in managing its banking book investments. It closely monitored market changes and acted swiftly to adjust its investment portfolio to enhance return while remaining vigilant of risks. In 2012, the Group selectively increased its investments in government-related bonds, high-quality financial institutions and corporate bonds. Meanwhile, the Group also increased its holdings in RMB-denominated bonds.

Product innovation – responsive to customers' needs

The Group remained customer-centric and continued to develop innovative products to meet customers' needs. Various innovative products were introduced during the year and were well-received by customers. New product offerings bundled offshore RMB exchange rate-related and interest rate-related products with deposits, loans and trade finance, thus lowering customers' exchange rate risk and financing costs.

As part of its ongoing efforts to facilitate the development of the offshore RMB bond market, the Group launched three new offshore RMB bond sub-indices. The BOCHK Offshore RMB Chinese Sovereign Bond Index, the BOCHK Offshore RMB Investment Grade Bond Index and the BOCHK Offshore RMB 1 to 3 Years Central Government Bond Index serve as performance benchmarks for the offshore RMB bond market. Meanwhile, the Group remained an active participant in the offshore RMB bond underwriting business, which saw a significant increase in market turnover over 2011.

RMB-clearing bank service – service hours extended to offshore markets

The Group continued to provide strong support in clearing services. The operating hours of the RMB RTGS were extended to cover the working hours in other major financial centres, including those in Europe and the US. Meanwhile, the use of the RMB RTGS system has been extended to a number of overseas participating banks, including BOC's overseas branches across Europe and Asia. These moves not only facilitated the increasing use of RMB for cross-border settlement and payment, but also enhanced the RMB clearing efficiency and service capability of BOCHK.

Banknotes business – global network expansion

The Group continued to cooperate with BOC in extending its overseas RMB banknotes business. The Group has also successfully established banknotes business relationships with other banks, financial institutions as well as non-bank institutions in different countries and regions.

MANAGEMENT'S DISCUSSION AND ANALYSIS



INSURANCE

Financial Results

The Group's Insurance segment registered a profit before taxation of HK\$609 million in 2012 versus HK\$33 million in 2011. The growth was mainly attributable to the improved mark-to-market changes of debt securities and gain from equity investments, compared to an investment loss recorded in 2011 amid the credit volatility in the financial market.

Net insurance premium income grew by 13.5%.

Net charge of impairment allowances on securities investments decreased significantly year-on-year due to the relatively stable environment of credit market in 2012.

Business Operation

Driving growth through product and service enhancement

The Group continued to widen the insurance product range and enhance product features. "IncomeGrowth Annuity Insurance Plan", a major new product providing life protection with guaranteed annuity payments, was launched and well received by customers. A series of training programmes were conducted to improve the sales team's integrated capabilities. BOC Life also carried out several promotional campaigns to promote its product offerings. The sales of unit-linked products registered a satisfactory growth.

Core system migration to improve long-term competitiveness

During the year, BOC Life successfully revamped a life insurance administration system which enhances the speed of service and sales support and hence the overall service quality. This platform is more compatible to the long-term business development of BOC Life.

RMB insurance products – a prominent provider

The Group's leading position in the RMB insurance market was further enhanced through optimisation of and innovation in RMB products. Popular RMB insurance products such as the "Target 5 Years Insurance Plan Series", "Multi-Plus Savings Insurance Plan" and "RMB Universal Life Insurance Plan" continued to attract substantial new business. To cater to customers' needs, the Group launched the RMB denominated "IncomeGrowth Annuity Insurance Plan". During the year, BOC Life was granted the approval to invest directly in the Mainland's interbank bond market, thus facilitating the expansion of RMB assets and the further development of its RMB insurance products. In recognition of its significant contribution to the RMB market, BOC Life has been granted the honour of the "Hong Kong Offshore RMB Centre – 1st RMB Business Outstanding Awards – The Outstanding Insurance Business" organised by Metro Finance and Metro Finance Digital, with Hong Kong Wen Wei Po as the co-organiser.

OTHERS

Asset management service – making solid progress

Following the successful launch of two private RMB bond funds in 2011, the Group introduced three new funds to both high-end and mass retail customers in 2012 through BOCHK Asset Management Limited ("BOCHK AM"), a wholly owned subsidiary of BOC Hong Kong (Holdings) Limited. These included a private fund and two retail funds which were well received by customers. During the year, BOCHK AM established exclusive partnerships for the provision of investment services with the World Bank in Hong Kong, a prestigious private bank in Germany and a reputable asset management company in Taiwan.

In recognition of its outstanding performance since its establishment in December 2010, BOCHK AM has been granted five prestigious "2012 Best of the Best Awards" by Asia Asset Management. The five awards include three Hong Kong and two regional honours. In addition, the RMB bond fund introduced in 2011, the "BOCHK RMB High Yield Bond Fund", was ranked by Bloomberg in 2012 as the best performing offshore RMB bond fund launched globally.



MANAGEMENT'S DISCUSSION AND ANALYSIS

2013 Business Focuses

The year 2013 will bring both challenges and opportunities to the banking sector. The Group will stay highly aware and respond swiftly to market changes while maintaining stringent risk management and control.

To reinforce its strong franchise in the local market, the Group will focus on further enhancing customer experience to meet the needs of existing customers, while at the same time aim to increase penetration of targeted customers. Products and services of new business platforms will be further developed in conjunction with traditional core businesses to enhance the Group's service capabilities and competitive edge.

Leveraging opportunities from the further expansion of the offshore RMB business, the Group will continue to strengthen its core competencies and focus on its comparative advantages in the international arena. At the same time, it will work closely with BOC in cross-border services to enhance the overall service capabilities of the BOC Group.

In the Mainland, the Group will continue to build upon its business infrastructure by encouraging product customisation and innovation, and expanding service capabilities and product offerings to SMEs and personal customers. It will also leverage the competitive advantages of BOC to further extend its business network and increase cooperation.

REGULATORY DEVELOPMENT

Implementation of Basel III

Following the negative vetting of the Banking (Capital) (Amendment) Rules 2012 completed by the Legislative Council, the first phase of Basel III requirements came into operation on 1 January 2013. The rules detail revised capital requirements for all locally-incorporated authorised institutions in Hong Kong with amendments mainly relating to:

1. revisions to both the minimum capital ratio requirement (in terms of expanding the existing capital adequacy ratio into three ratios, namely, a Common Equity Tier 1 capital ratio, a Tier 1 capital ratio, and a Total capital ratio) and the definition of regulatory capital;
2. enhancements to the counterparty credit risk framework, including a revised capital framework for exposures to central counterparties; and
3. amendments on the capital treatment for certain trade financing activities and securities financing transactions.

The implementation of the Basel III Accord will enhance the resilience of the banking system in Hong Kong. The Group has assessed the relevant impact and is well prepared for the implementation of the new capital standards.

Implementation of LM-2 "Sound Systems and Controls for Liquidity Risk Management"

The Supervisory Policy Manual LM-2 "Sound Systems and Controls for Liquidity Risk Management" was issued by the HKMA in 2011. This module provides a detailed description of the system and control standards for the governance, risk management and disclosure of liquidity risk that authorised institutions are expected to have in place. In accordance with the requirements set forth in the module, the Group has embarked to refine the behaviour model and assumptions of existing cash flow analysis and stress test to enhance the Group's cash flow analysis under both normal and stressed conditions. In addition, the Group has a policy in place to manage liquidity even under stressed scenarios. A contingency plan is being established, detailing action plans and relevant procedures and responsibility of relevant departments. For details of the Group's actions taken in response to LM-2, please refer to Note 4.3 to the Financial Statements in this Annual Report.

MANAGEMENT'S DISCUSSION AND ANALYSIS



TECHNOLOGY AND OPERATIONS

In 2012, the Group continued to strengthen its information technology and business operation infrastructure to support business growth and enhance operational efficiency. The Corporate Online Banking system has been revamped to provide a number of functionalities to improve customer experience. The linkage to BOC's global cash management platform was completed to facilitate local and cross-border fund pooling services to multinational enterprises, giving support to establish BOC Group's leading position in global cash management. The Centralised Limit Control and Customer Group Limit Management platform was established to support a more comprehensive review on credit monitoring, risk analysis and reporting. The core system of BOC Life was revamped to make use of additional parameters and simplifies the development of new life insurance products, resulting in development time reduction and time-to-market improvement.

CREDIT RATINGS

As at 31 December 2012	Long-term	Short-term
Standard & Poor's	A+	A-1
Moody's	Aa3	P-1
Fitch	A	F1

On 25 October 2012, Standard & Poor's affirmed the 'A+' long-term and 'A-1' short-term issuer credit ratings on BOCHK. The outlook is stable.

On 2 August 2012, Moody's affirmed 'Aa3' long-term and 'P-1' short-term local and foreign currency bank deposit ratings on BOCHK. The outlook is stable. The Bank Financial Strength Rating is 'C+'.

On 31 October 2012, Fitch Ratings affirmed 'A' long-term and 'F1' short-term foreign currency issuer default ratings on BOCHK. The outlook is stable.

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 risks inherent in the Group's businesses are credit risk, interest rate risk, market risk, liquidity risk, operational risk, reputation risk, legal and compliance risk, and strategic risk. The Group's risk management objective is to enhance shareholder value by maintaining risk exposures within acceptable limits. The Group has a defined risk appetite statement approved by the Board, which is an expression of the types and level of risk that the Group is willing to take in order to achieve its business goals and to meet the expectations of its stakeholders under a controllable risk level. For details of the Group's risk management governance structure, please refer to Note 4 to the Financial Statements in this Annual Report.

Credit Risk Management

Credit risk is the risk of loss arising from that a customer or counterparty will be unable to or unwilling to meet its contractual obligations. Credit risk exists in the trading book and banking book, on- and off-balance sheet exposures of a bank. It arises principally from the lending, trade finance and treasury businesses, and covers inter-bank transactions, foreign exchange and derivative transactions as well as investments in bonds and securities. For details of the Group's Credit Risk Management, please refer to Note 4.1 to the Financial Statements in this Annual Report.

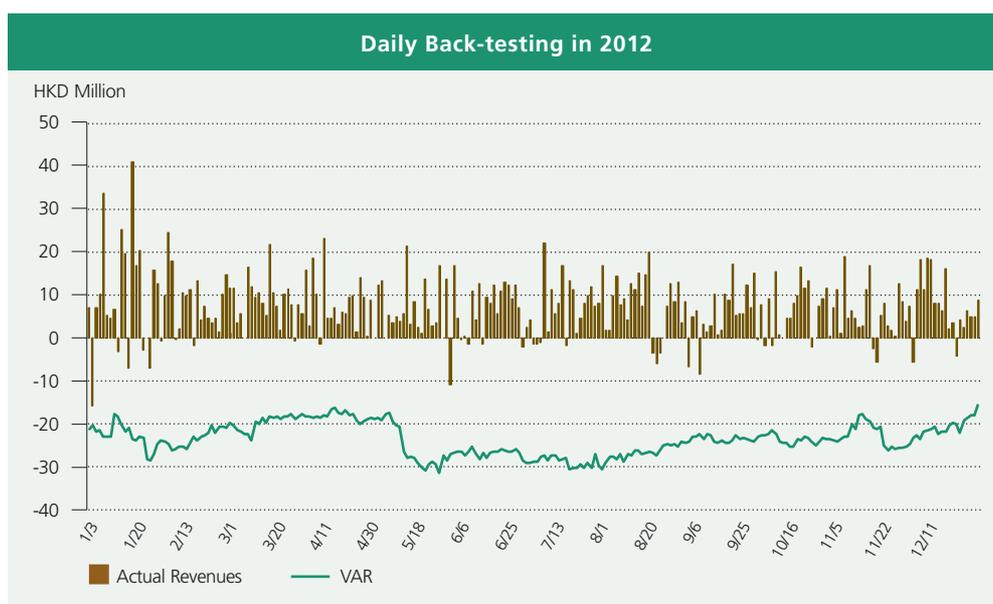
MANAGEMENT'S DISCUSSION AND ANALYSIS

Market Risk Management

Market risk refers to the risk of losses arising from adverse movements in the value of foreign exchange, commodity, interest rate and equity positions held by the Group due to the volatility of financial market price (debt security price/interest rate, foreign exchange rate, equity price, commodity price). The Group adopts a robust market risk appetite to achieve a balance between risk and return. For details of the Group's market risk management, please refer to Note 4.2 to the Financial Statements in this Annual Report.

The Group uses the VAR to measure and report general market risks to the Risk Committee ("RC") and senior management on a periodic basis. The Group adopts a uniformed VAR calculation model, using historical simulation approach and 2-year historical data, to calculate VAR of the Group and subsidiaries over a 1-day holding period with 99% confidence level, and to set up the VAR limit of the Group and subsidiaries.

The predictive power of the VAR measure is monitored by back-testing, which compares the calculated VAR figure of market risk exposures of each business day with the actual and hypothetical revenues arising on those exposures on the next business day. Generally speaking, the number of back-testing exceptions in a rolling 12-month period will not exceed four times, given a 99% confidence level. The graph below shows the back-testing result of the VAR against actual revenues of the Group.



There were no actual losses exceeding the VAR estimates for the Group in 2012 as shown in the back-testing results.

Interest Rate Risk Management

Interest rate risk means the risks to a bank's earnings and economic value arising from adverse movements in interest rate and term structures of the bank's asset and liability positions. The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are repricing risk, basis risk, yield curve risk and option risk. For details of the Group's Interest Rate Risk Management, please refer to Note 4.2 to the Financial Statements in this Annual Report.

Liquidity Risk Management

Liquidity risk is the risk that banks fail to provide sufficient funds to grow assets or pay due obligations, and need to bear an unacceptable loss. The Group follows the sound liquidity risk appetite to provide stable, reliable and adequate sources of cash to meet liquidity needs under normal circumstances or stressed scenarios; and survive with net positive cumulative cash flow in extreme scenarios, without requesting HKMA to act as the lender of last resort. For details about Liquidity Risk Management, please refer to Note 4.3 to the Financial Statements in this Annual Report.

MANAGEMENT'S DISCUSSION AND ANALYSIS



Operational Risk Management

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

The Group has implemented the “Three Lines of Defence” for its operational risk management. All departments or functional units as the first line of defence are the first parties responsible for operational risk management, and carry out the duties and functions of self risk control in the process of business operation through self assessment, self checking, self correction and self development. The Operational Risk and Compliance Department (“OR&CD”) together with certain specialist functional units in relation to operational risk management within the Group, including the Human Resources Department, Information Technology Department, Corporate Services Department, Financial Management Department and General Accounting & Accounting Policy Department (collectively known as “Specialist functional units”), are the second line of defence. They are responsible for assessing and monitoring the operational risk conditions in the first line of defence, and providing them with guidance. The OR&CD, being independent from the business units, is responsible for assisting the Management in managing the Group’s operational risk, including the establishment and review of the operational risk management policy and framework, designing the operational risk management tools and reporting mechanism, and assessing and reporting the overall operational risk position to the Management and RC. Specialist functional units are required to carry out their managerial duties of the second line defence with respect to some specific aspects of operational risk and its related issues. Besides taking charge of operational risk management in their own units, these units are also required to provide other units with professional advice/training in respect of certain operational risk categories and to lead the Group-wide operational risk management. Group Audit is the third line of defence which provides independent assessment to the robustness and adequacy of the operational risk management framework and is required to conduct periodic audit of the operational risk management activities of various departments or functional units within the Group regarding their compliance and effectiveness and to put forward recommendations for remedial actions.

The Group has put in place an effective internal control process which requires the establishment of policies and control procedures for all the key activities. The Group adheres to the fundamental principle of proper segregation of duties and authorisation. The Group adopts various operational risk management tools or methodologies such as key risk indicators, self-assessment, operational risk events reporting and review to identify, assess, monitor and control the risks inherent in business activities and products, as well as purchase of insurance to mitigate unforeseeable operational risks. Business continuity plans are established 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 about 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 decrease. Reputation risk is inherent in other types of risk and every aspect of business operation and covers a wide spectrum of issues.

In order to mitigate reputation risk, the Group has formulated and duly followed its Reputation Risk Management Policy. The policy aims to prevent and manage reputation risk proactively at an early stage when an incident occurs. Since reputation risk is often caused by various types of operational and strategic issues that negatively impact the trust and perception of the Group, all operational and key risks identified are assessed through the established Key Control Self-Assessment framework, including risk assessment tools, to evaluate the severity of their impact on the Group, including the damage to reputation.

In addition, the Group has put in place a comprehensive framework to continuously monitor reputation risk incidents in the financial industry. This continuous monitoring enables the Group to effectively manage, control and mitigate any potential adverse impact from an incident. The Group also adopts robust disclosure practices to keep our stakeholders informed at all times, which helps build confidence in the Group and establish a strong public image.



MANAGEMENT'S DISCUSSION AND ANALYSIS

Legal and Compliance Risk Management

Legal risk is the risk that unenforceable contracts, lawsuits or adverse judgements may disrupt or otherwise negatively affect the operations or financial conditions of the Group. Compliance risk is the risk of legal or regulatory sanctions, financial losses or losses in reputation the Group 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, which reports directly to the Chief Risk Officer ("CRO"). All legal matters are handled by the Legal Services Centre ("LSC"), which reports to the Chief Operating Officer. The OR&CD is responsible for legal risk management of the Group with support rendered by the LSC. As part of the Group's corporate governance framework, the policy for the management of legal and compliance risk is approved by the RC as delegated by the Board.

Strategic Risk Management

Strategic risk generally refers to the risks that may induce some current or future negative impacts on the earnings, or capital or reputation or market position of the Group because of poor business decisions, improper implementation of decisional strategies and lack of response to the market. The Board reviews and approves the strategic risk management policy. Key strategic issues have to be fully evaluated and properly endorsed by the senior management and the Board.

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

Capital Management

The major objective of the Group's capital management is to maximise total shareholders' return while maintaining a capital adequacy position in relation to the Group's overall risk profile. The Asset and Liability Management Committee ("ALCO") periodically reviews the Group's capital structure and adjusts the capital mix where appropriate to maintain an optimal balance among risk, return and capital adequacy.

To comply with the HKMA's requirements as stated in the Supervisory Policy Manual "Supervisory Review Process", the Group adopts the internal capital adequacy assessment process ("ICAAP") and reviews it annually. Based on the HKMA's guidelines on Pillar II, ICAAP has been initiated to assess the extra capital needed to cover the material risks not captured under Pillar I, and therefore minimum common equity CAR, minimum core CAR and the minimum CAR are determined. Meanwhile, an operating CAR Range has also been established which enables the flexibility for future business growth and efficiency of capital utilisation.

The Group has assessed the relevant impact and been well prepared for the implementation of Basel III capital standards which came into operation on 1 January 2013.

Stress Testing

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

BOC Life

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

Insurance Risk Management

BOC Life is in the business of insuring against the risk of mortality, morbidity, disability, critical illness, accidents and related risks. These risks are managed through the application of underwriting policies and reinsurance arrangements.

MANAGEMENT'S DISCUSSION AND ANALYSIS



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

The reinsurance arrangement helps to transfer the insurance risk associated with the insurance contracts to the third party. It does not, however, discharge BOC Life's liability as the primary insurer. If a reinsurer fails to pay a claim for any reasons, BOC Life remains liable for the payment to the policyholder. The creditworthiness of reinsurers is considered by reviewing the reinsurers' financial strength prior to finalisation of any contract. BOC Life directs its reinsurance placement policy and assesses the creditworthiness of all reinsurers and intermediaries by reviewing credit grades provided by rating agencies and other publicly available financial information. BOC Life also monitors the recoverability of its reinsurance assets on an ongoing basis. It maintains records of the payment history for significant contract holders with whom it conducts regular business.

For details of the Group's Insurance Risk Management, please refer to Note 4.4 to the Financial Statements in this Annual Report.

Interest Rate Risk Management

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

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 and inforce policies 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 they have 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 its credit risk management, BOC Life has strengthened its communication with the Investment Management of the Group while closely monitoring and updating the established Bonds Issuers Disposal and Watch Lists to ensure consistency with the Group's credit risk management and investment strategy.



PREMIER **WEALTH** MANAGEMENT SERVICE





CORPORATE INFORMATION

BOARD OF DIRECTORS

Chairman

XIAO Gang[#] (resignation effective from
17 March 2013)

Vice Chairmen

LI Lihui[#]

HE Guangbei

Directors

LI Zaohang[#]

ZHOU Zaiqun[#]

CHEN Siqing[#]

GAO Yingxin

FUNG Victor Kwok King^{*}

KOH Beng Seng^{*}

NING Gaoning^{*} (appointment effective from
24 August 2012)

SHAN Weijian^{*}

TUNG Chee Chen^{*}

TUNG Savio Wai-Hok^{*}

[#] Non-executive Directors

^{*} Independent Non-executive Directors

COMPANY SECRETARY

CHAN Chun Ying

REGISTERED OFFICE

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

AUDITOR

PricewaterhouseCoopers

SENIOR MANAGEMENT

Chief Executive

HE Guangbei

Deputy Chief Executive

GAO Yingxin

Chief Financial Officer

ZHUO Chengwen

Deputy Chief Executives

WONG David See Hong

YEUNG Jason Chi Wai

Chief Risk Officer

LI Jiuzhong

Chief Operating Officer

LEE Alex Wing Kwai

Assistant Chief Executive

ZHU Yanlai

SHARE REGISTRAR

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

ADR DEPOSITARY BANK

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14th Floor
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United States of America

WEBSITE

www.bochk.com

BOARD OF DIRECTORS AND SENIOR MANAGEMENT



Mr. XIAO Gang



Mr. LI Lihui



Mr. HE Guangbei



Mr. LI Zaohang



Mr. ZHOU Zaiqun

Directors

Mr. XIAO Gang

Chairman (resignation effective from 17 March 2013)

Aged 54, is the Chairman of the Board of Directors of the Company and BOCHK. He is also a Director of BOC (BVI) and BOCHKG. Mr. XIAO was Chairman and President of BOC from March 2003 to August 2004 and has been Chairman of BOC since its restructuring in August 2004. Prior to joining BOC, Mr. XIAO joined People's Bank of China ("PBOC") in 1981 and has served various positions in PBOC, including Director of the Research Bureau, Head of the China Foreign Exchange Trading Center, Director of the Planning and Treasury Department, Assistant Governor and Director of the Monetary Policy Department, Assistant Governor and President of Guangdong Branch of PBOC and Director of the Guangdong Branch of the State Administration of Foreign Exchange. Mr. XIAO served as Deputy Governor of PBOC from 1998 to 2003. He was also Chairman of China Association of Banks from June 2003 to December 2004. Mr. XIAO graduated from Renmin University of China with a Master's Degree in Law.

Mr. LI Lihui

Vice Chairman

Born in 1952, is the Vice Chairman of the Board of Directors and a member of the Nomination and Remuneration Committee of the Company and BOCHK. He is currently the Vice Chairman and the President of BOC and a Director of BOC (BVI) and BOCHKG. Prior to joining BOC in August 2004, Mr. LI served as the Deputy Governor of Hainan Province from September 2002 to August 2004. Mr. LI was an Executive Vice President of Industrial and Commercial Bank of China ("ICBC") from July 1994 to September 2002 and served in a number of positions at ICBC from January 1989 to July 1994, including the Deputy General Manager of the Fujian Branch, the Chief Representative

of the Singapore Representative Office and the General Manager of the International Business Department. Mr. LI graduated from the Economics Department of Xiamen University in 1977 and obtained a Doctorate in Economics from the Guanghai School of Management of Peking University in 1999.

Mr. HE Guangbei

Vice Chairman and Chief Executive

Aged 58, is the Vice Chairman and the Chief Executive with overall responsibility for the business and operations of BOCHK and a member of the Strategy and Budget Committee of the Company and BOCHK. Mr. HE is also Chairman of NCB (China), Chiyu, BOC Life and BOCHK Charitable Foundation. He is currently the Chairman and Director of each of Hong Kong Interbank Clearing Limited and HKICL Services Limited, a Director of Hong Kong Note Printing Limited. He is the designated representative of BOCHK to the Hong Kong Association of Banks where he served as the presiding Chairman in 2011. He holds various public positions which include member of 12th National Committee of the Chinese People's Political Consultative Conference, non-official member of Economic Development Commission, member of the HKMA Exchange Fund Advisory Committee, member of the Banking Advisory Committee, member of General Committee of Hong Kong General Chamber of Commerce, member of Risk Management Committee of Stock Exchange, member of Hong Kong/Japan Business Co-operation Committee, member of Hong Kong-United States Business Council, member of Advisory Committee of Qianhai Shenzhen-Hong Kong Modern Service Industry Corporation Zone and Honorary President of the Hong Kong Chinese Enterprises Association. Mr. HE joined BOC in 1980 and since then, he has assumed various positions at BOC and was posted to its New York Branch and Paris Branch. He was Managing Director of BOC from 1999 to 2004 and Executive

Vice President from 2000 to 2003. Mr. HE graduated from the Beijing Second Foreign Languages Institute in 1979 with a Bachelor's Degree and obtained a Master's Degree in International Management Studies from the University of Texas at Dallas in 1985.

Mr. LI Zaohang

Non-executive Director

Aged 57, is a Non-executive Director and a member of the Risk Committee and the Nomination and Remuneration Committee of the Company and BOCHK. He joined China Construction Bank ("CCB") in 1980 and had held various positions including Manager, Branch Manager, General Managers of various departments at CCB's Head Office and Executive Vice President. In 2000, Mr. LI joined BOC as Executive Vice President and has served as Managing Director and Executive Director successively. Mr. LI graduated from Nanjing University of Information Science and Technology.

Mr. ZHOU Zaiqun

Non-executive Director

Aged 60, is a Non-executive Director, Chairman of the Strategy and Budget Committee and a member of the Audit Committee of the Company and BOCHK. He is also Chairman of Nanyang and a Vice Chairman of NCB (China). Mr. ZHOU was the Executive Director of BOC during the period from February 2008 to May 2011 and the Executive Vice President of BOC during the period from November 2000 to May 2011. He was the Managing Director of BOC from 2000 to 2004. During the period from January 1997 to November 2000, Mr. ZHOU held various positions in ICBC, namely General Manager of Beijing Branch, General Manager of Accounting Department and General Manager of Financial Planning Department. Mr. ZHOU has over 20 years' experience in the banking industry. Mr. ZHOU obtained a Master's Degree from Dongbei University of Finance and Economics in 1997.

BOARD OF DIRECTORS AND SENIOR MANAGEMENT



Mr. CHEN Siqing



Mr. GAO Yingxin



Dr. FUNG Victor Kwok King



Mr. KOH Beng Seng

Directors

Mr. CHEN Siqing

Non-executive Director

Aged 52, is a Non-executive Director and a member of the Risk Committee and the Strategy and Budget Committee of the Company and BOCHK. He is currently the Executive Vice President of BOC. Mr. CHEN joined BOC in 1990 and worked in the Hunan Branch before he was seconded to the Hong Kong Branch of China and South Sea Bank Ltd. as Assistant General Manager. Mr. CHEN held various positions in BOC from June 2000 to May 2008, including Assistant General Manager, Vice General Manager of the Fujian Branch, General Manager of the Risk Management Department of BOC and General Manager of the Guangdong Branch. Mr. CHEN was appointed the Chairman of BOC Aviation Pte. Ltd. since December 2011. He is also a member of Trade Finance Committee, Factoring Committee and Syndicated Loan and Deal Committee of China Banking Association. Mr. CHEN graduated from Hubei College of Finance and Economics in 1982 and obtained a MBA from Murdoch University, Australia in 1999.

Mr. GAO Yingxin

Executive Director and Deputy Chief Executive

Aged 50, is an Executive Director of the Company and BOCHK as well as the Deputy Chief Executive in charge of Corporate Banking and Financial Institutions. He is also Vice Chairman of NCB (China) and Director of Nanyang and BOCG Insurance. Before joining BOCHK, he was President and Chief Operating Officer of BOCI. Mr. GAO joined the BOC Group in 1986 where he began working on financing projects for various industries at BOC's Head Office in Beijing. In 1999, he became General Manager of Corporate Banking at BOC Head Office where he was responsible for managing and building BOC Group's customer relationships with and global financing for multinational corporations and premium domestic clients in the Mainland China. He was also in charge of BOC's major financing projects. From 1995 to 1996, he worked for the Finance Department of Northern Telecom (Nortel)

Head Office in Canada. Mr. GAO graduated from the East China University of Science and Technology in Shanghai with a Master's Degree in Engineering in 1986.

Dr. FUNG Victor Kwok King

Independent Non-executive Director

Aged 67, is an Independent Non-executive Director and a member of the Audit Committee and the Strategy and Budget Committee of the Company and BOCHK. Dr. FUNG holds Bachelor's and Master's Degrees in Electrical Engineering from the Massachusetts Institute of Technology and a Doctorate in Business Economics from Harvard University. He is Group Chairman of the Fung Group (formerly known as Li & Fung Group), a Hong Kong-based multinational which comprises major subsidiaries in trading, logistics, distribution and retailing. They include publicly-listed Li & Fung Limited, Convenience Retail Asia Limited and Trinity Limited. He is also an Independent Non-executive Director of Chow Tai Fook Jewellery Group Limited (Hong Kong), China Petrochemical Corporation (PRC) and Koc Holding A.S. (Turkey). He served on the Board of Baosteel Group Corporation (PRC) from 2005 until the expiry of the term end of January 2013. Dr. FUNG is the Founding Chairman of the Fung Global Institute, an independent and non-profit think-tank based in Hong Kong. He is also Honorary Chairman of the International Chamber of Commerce and a member of the WTO Panel on Defining the Future of Trade (since April 2012). In public service, Dr. FUNG is a member of the Chinese People's Political Consultative Conference and a vice chairman of China Centre for International Economic Exchanges. He has also been appointed as a member of the Economic Development Commission of the Hong Kong Government recently. Dr. FUNG was Chairman of the Hong Kong Trade Development Council (1991-2000), the Hong Kong representative on the APEC Business Advisory Council (1996-2003). He was also Chairman of the Hong Kong Airport Authority (1999-2008), Chairman of the Council of The University of Hong Kong (2001-2009), Chairman of the International Chamber of Commerce (2008-2010), Chairman of the Hong Kong-Japan Business

Co-operation Committee (2004-2010), Chairman of the Greater Pearl River Delta Business Council (2004-February 2013) and a member of the Commission on Strategic Development of the Hong Kong Government (2005-June 2012). The Hong Kong Government awarded Dr. FUNG the Gold Bauhinia Star and Grand Bauhinia Medal in 2003 and 2010 respectively for his distinguished services to the community.

Mr. KOH Beng Seng

Independent Non-executive Director

Aged 62, is an Independent Non-executive Director, Chairman of the Risk Committee and a member of the Audit Committee of the Company and BOCHK. Mr. KOH is currently the Chief Executive Officer of Octagon Advisors Pte Ltd, a business and management consulting company based in Singapore. He is also an Independent Non-executive Director of two Singaporean listed companies, namely, Singapore Technologies Engineering Ltd and Great Eastern Holdings Limited. He was formerly an Independent Non-executive Director of Fraser and Neave Limited, a company listed in Singapore. He is also a Director of Sing Han International Financial Services Limited. Mr. KOH was Deputy President of United Overseas Bank ("UOB") and a member of UOB's Executive Committee from 2000 to 2004. During this period, he was in charge of UOB's operations, delivery channels, information technology, corporate services, risk management and compliance functions and played a key role in driving the successful integration of Overseas Union Bank and UOB in 2001. Prior to that, Mr. KOH has spent over 24 years at the Monetary Authority of Singapore where he made significant contributions to the development and supervision of the Singapore financial sector in his capacity as Deputy Managing Director, Banking & Financial Institutions Group. He has also served as a Director of Chartered Semiconductor Manufacturing and as a part-time adviser to the International Monetary Fund. Mr. KOH holds a Bachelor's Degree in Commerce from Nanyang University in Singapore and a Master's Degree in Business Administration from Columbia University in the United States.

BOARD OF DIRECTORS AND SENIOR MANAGEMENT



Mr. NING Gaoning



Mr. SHAN Weijian



Mr. TUNG Chee Chen



Mr. TUNG Savio Wai-Hok

Directors

Mr. NING Gaoning

Independent Non-executive Director

Aged 54, is an Independent Non-executive Director and a member of the Strategy and Budget Committee of the Company and BOCHK. Mr. NING is currently the Chairman of COFCO Corporation and COFCO (Hong Kong) Limited. Mr. NING is also an Executive Director of China Foods Limited, a Non-executive Director of China Agri-Industries Holdings Limited, a Non-executive Director of CPMC Holdings Limited, Chairman and Non-executive Director of China Mengniu Dairy Company Limited, all of which are companies listed in Hong Kong. In addition, Mr. NING is an Independent Director of Huayuan Property Co., Ltd. (a company listed in Shanghai) and a Director of BOCI. Mr. NING was a Director of Smithfield Foods, Inc. (a company listed in New York) until March 2011. Before joining COFCO Corporation, Mr. NING held various positions including Vice Chairman, Director and General Manager of China Resources (Holdings) Company Limited and certain of its subsidiaries. Mr. NING has over 20 years of experience in corporate management, investment and corporate finance, business restructurings and governmental relations. Mr. NING obtained a Bachelor's degree in Economics from Shandong University, China in 1983 and obtained a Master degree in Business Administration from University of Pittsburgh, United States in 1985.

Mr. SHAN Weijian

Independent Non-executive Director

Aged 59, is an Independent Non-executive Director, Chairman of the Audit Committee and a member of the Nomination and Remuneration Committee of the Company and BOCHK. Mr. SHAN is the Chairman

and Chief Executive Officer of PAG, an investment firm. He is also a director of TCC International Holdings Limited, a company listed on the Stock Exchange. Mr. SHAN is also a Governor of China Venture Capital and Private Equity Association Limited. Mr. SHAN resigned as a Director of Taishin Financial Holding Co., Ltd. and Taiwan Cement Corporation, both are companies listed in Taiwan, in May 2012 and June 2012 respectively. He was Senior Partner of TPG, Co-Managing Partner of Newbridge Capital, Managing Director of JP Morgan, an assistant professor at the Wharton School of the University of Pennsylvania and an Investment Officer at the World Bank in Washington DC. Mr. SHAN graduated from the Beijing Institute of Foreign Trade with a major in English in 1979. He obtained a Master's Degree in Business Administration from the University of San Francisco in 1981, and received a Master of Arts Degree in Economics and a PhD Degree in Business Administration from the University of California at Berkeley in 1984 and 1987 respectively.

Mr. TUNG Chee Chen

Independent Non-executive Director

Aged 70, is an Independent Non-executive Director, Chairman of the Nomination and Remuneration Committee and a member of the Audit Committee of the Company and BOCHK. Mr. TUNG is also the Chairman and Chief Executive Officer of Orient Overseas (International) Limited. He is an Independent Non-executive Director of a number of listed companies, including Wing Hang Bank Limited, U-Ming Marine Transport Corp., Sing Tao News Corporation Limited and Cathay Pacific Airways Limited. He was formerly an Independent Non-executive Director of PetroChina Company Limited and Zhejiang Expressway

Company Limited, both are listed in Hong Kong. Mr. TUNG was educated at the University of Liverpool, United Kingdom, where he obtained a Bachelor's Degree in Science in 1964. He later obtained a Master's Degree in Mechanical Engineering from the Massachusetts Institute of Technology in 1966.

Mr. TUNG Savio Wai-Hok

Independent Non-executive Director

Aged 61, is an Independent Non-executive Director and a member of the Audit Committee, the Nomination and Remuneration Committee, the Risk Committee and the Strategy and Budget Committee of the Company and BOCHK. Mr. TUNG is currently the Chief Executive, North America, of Investcorp and he is one of the founding partners of Investcorp. Mr. TUNG was appointed a Director and a member of the Audit Committee of Tech Data Corporation, a company listed on NASDAQ, in June 2010. Before joining Investcorp in 1984, he worked for Chase Manhattan Bank for about 11 years, holding various positions in its front, middle and back offices and served in its offices in New York, Bahrain, Abu Dhabi and London. Mr. TUNG has served on the boards of many of Investcorp portfolio companies, including Club Car, Circle K, Saks Fifth Avenue, Simmons Mattresses, Star Market, and Stratus Computer. He is also a board member and treasurer of the Aaron Diamond AIDS Research Center, an affiliate of Rockefeller University and a board member of the Committee of 100, a Chinese-American organisation in the U.S. He ceased to be the Chairman of Wireless Telecom Group in May 2010. Mr. TUNG holds a BSc in Chemical Engineering from Columbia University of New York, where he is also a trustee emeritus and a member of the Columbia University Medical Center Board of Visitors.

BOARD OF DIRECTORS AND SENIOR MANAGEMENT



Mr. ZHUO Chengwen



Mr. WONG David See Hong



Mr. YEUNG Jason Chi Wai

Senior Management

Mr. ZHUO Chengwen

Chief Financial Officer

Aged 42, is the Chief Financial Officer of the Group. He is also a Director of Nanyang and BOCHK Asset Management Limited. Prior to joining the Group, Mr. ZHUO was a Deputy General Manager in the Financial Management Department of BOC responsible for various financial management functions of BOC Group including financial planning, accounting policy, financial compliance, management reporting and financial disclosure. Mr. ZHUO has assumed a financial management role for over 15 years in the banking industry and has extensive knowledge and experience in financial management. Mr. ZHUO graduated from the Peking University with a Bachelor's Degree in Economics in 1992 and a Master's Degree in Economics in 1995 and was awarded a MBA Degree by the City University of New York in 2005. Mr. ZHUO has been a member of the Chinese Institute of Certified Public Accountants, the American Institute of Certified Public Accountants and the Hong Kong Institute of Certified Public Accountants since 1995, 2005 and 2009 respectively.

Mr. WONG David See Hong

Deputy Chief Executive

Aged 59, is the Deputy Chief Executive of the Group with overall responsibility for the financial market businesses which include Global Markets, Global Transaction Banking, Investment Management, Insurance, Asset Management and other capital market-related businesses. He is also a Director of BOC Life. Prior to joining the Group, Mr. WONG was the Corporate Executive Vice President and Country Executive of ABN AMRO Bank ("ABN") and was responsible for ABN's operations in South East Asia. He joined ABN in 1995 and has held various senior positions within ABN, including Regional Head of Financial Markets, Country Executive in Singapore, and Managing Director of the Hong Kong Branch. Mr. WONG has spent over 25 years in the banking sector and has extensive knowledge and experience in treasury and financial products. Mr. WONG served as a board member of Energy Market Authority till March 2009. He is currently a board member of Civil Service College in Singapore, Customer Advisory Board Member of Thomson Reuters and Finance Management Committee Member of the HK Management Association in Hong Kong. Mr. WONG graduated from the University of Singapore with a Bachelor's Degree in Business Administration and was awarded a Master's Degree in Science in Investment Management by the Hong Kong University of Science and Technology. He was awarded the Financial Industry Certified Professional from the Institute of Banking and Finance, Singapore. He has also received the Distinguished Award for his contribution to the financial industry in Singapore.

Mr. YEUNG Jason Chi Wai

Deputy Chief Executive

Aged 58, is the Deputy Chief Executive of the Group in charge of the Personal Banking business. He is currently a member of the Management Committee of the Group which provides overall leadership and guidance on the business development, strategic planning and operation of the Group. He is the Vice Chairman of BOC-CC and a Director of BOC Life. Mr. YEUNG joined the Group as the Board Secretary and Company Secretary of the Company and its principal operating subsidiary, BOCHK, in 2001. He also acted as the Board and Company Secretary of BOC from November 2005 to April 2008. Prior to joining the Group, Mr. YEUNG was General Counsel and director of China Everbright Limited, a company listed on the main board of the Stock Exchange, and before that, a partner of Woo, Kwan, Lee & Lo with over 10 years' experience practising corporate and commercial law. He had also served at the Securities and Futures Commission in Hong Kong. Mr. YEUNG was educated at the University of Hong Kong where he obtained a Bachelor's Degree in social sciences. Mr. YEUNG later graduated from The College of Law, United Kingdom and further obtained a Bachelor's Degree in law from the University of Western Ontario, Canada and a Master's Degree in business administration from the Richard Ivey School of Business of the University of Western Ontario, Canada.

BOARD OF DIRECTORS AND SENIOR MANAGEMENT



Mr. LI Jiuzhong



Mr. LEE Alex Wing Kwai



Mdm. ZHU Yanlai

Senior Management

Mr. LI Jiuzhong

Chief Risk Officer

Aged 50, is the Chief Risk Officer of the Group in charge of the Group's overall risk management function, overseeing BOCHK's Risk Management Department and Operational Risk and Compliance Department. He is also a Director of Nanyang, NCB (China), BOC-CC and BOC Life. Mr. LI has over 29 years' experience in the banking industry. Mr. LI joined BOC in 1983 and, since then, he has assumed various positions at BOC Head Office and overseas branch. He served as Assistant General Manager and became Deputy General Manager of BOC London Branch from 1996 to 2002, Deputy General Manager of Corporate Banking Department of BOC Head Office from 2002 to 2004, and also General Manager of Corporate Banking Department, Risk Management Department, and Global Markets Department of BOC Head Office from 2004 to 2009. Mr. LI graduated from Daqing Petroleum Institute in 1983 with a Bachelor's Degree in Science in Oilfield Development and Management and obtained a Master's Degree in Science in International Banking and Financial Studies from Heriot-Watt University (UK) in 1993.

Mr. LEE Alex Wing Kwai

Chief Operating Officer

Aged 54, is the Chief Operating Officer of the Group. He is also a Director of BOC-CC. Prior to joining the Group, Mr. LEE was the Managing Director responsible for the operations and technology of the entire business of Citigroup in Hong Kong. Mr. LEE held various leadership roles within Citigroup. He has strong experience in operation and technology with major financial institutions for over 27 years. Mr. LEE graduated from the Arizona State University with a Bachelor's Degree in General Business Administration in 1981 and a MBA Degree specialised in Accounting in 1983. Mr. LEE passed the uniform examination of the American Institute of Certified Public Accountants in 1984. He has been an Associate Member of the Institute of Internal Auditor and a Chartered Bank Auditor of the Bank Administration Institute of the United States of America since 1986.

Mdm. ZHU Yanlai

Assistant Chief Executive

Aged 58, is the Assistant Chief Executive of the Group in charge of overall leadership for the planning and implementation of the Group's strategy, business direction, market positioning and sustainable development. Mdm. ZHU has been the General Manager of Economics and Strategic Planning Department of BOCHK since the merger of the Group in October 2001. She is currently a Director of Nanyang. Mdm. ZHU joined BOC in 1997 and was the Head of Business Development of BOC (Canada), and Assistant General Manager of Hong Kong and Macau Regional Office of BOC. Prior to joining BOC, Mdm. ZHU worked for Royal Bank of Canada and Nesbitt Burns, Bank of Montreal Group. She was previously the visiting scholar of York University in Canada and the lecturer in Renmin University of China. Mdm. ZHU obtained a Master's Degree in Sociology from the University of Regina, Sask, Canada, and graduated from Renmin University of China with Bachelor's and Master's Degrees in Philosophy.



REPORT OF THE DIRECTORS

The Directors are pleased to present their report together with the audited consolidated financial statements of the Company and its subsidiaries for the year ended 31 December 2012.

Principal Activities

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

Results and Appropriations

The results of the Group for the year are set out in the consolidated income statement on page 102.

The Board has recommended a final dividend of HK\$0.693 per share, amounting to approximately HK\$7,327 million, subject to the approval of shareholders at the forthcoming annual general meeting to be held on Tuesday, 28 May 2013. If approved, the final dividend will be paid on Friday, 14 June 2013 to shareholders whose names appear on the Register of Members of the Company on Thursday, 6 June 2013. Together with the interim dividend of HK\$0.545 per share declared in August 2012, the total dividend payout for 2012 would be HK\$1.238 per share.

Closure of Register of Members for Entitlement to Attend and Vote at Annual General Meeting

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to attend and vote at

the Annual General Meeting of the Company, from Thursday, 23 May 2013 to Tuesday, 28 May 2013 (both days inclusive), during which period no transfer of shares will be registered. In order to attend and vote at the Annual General Meeting of the Company, 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 Wednesday, 22 May 2013. The Annual General Meeting of the Company will be held at 2:00 p.m. on Tuesday, 28 May 2013.

Closure of Register of Members for Entitlement to Final Dividend

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to the proposed final dividend, from Monday, 3 June 2013 to Thursday, 6 June 2013 (both days inclusive), during which period no transfer of shares will be registered. In order to qualify for the proposed final 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, 31 May 2013. Shares of the Company will be traded ex-dividend as from Thursday, 30 May 2013.

Reserves

Details of movements in the reserves of the Group are set out in the consolidated statement of changes in equity on page 107.

Donations

Charitable and other donations made by the Group during the year amounted to approximately HK\$10 million.

Note: These donations do not include the donations and sponsorships made by BOCHK Charitable Foundation ("the Foundation". For details, please refer to the "Corporate Social Responsibility" section of this Annual Report). The Foundation is a separate legal entity established in Hong Kong and is a charitable institution exempt from tax under the Inland Revenue Ordinance.

Properties, Plant and Equipment

Details of movements in properties, plant and equipment of the Group are set out in Note 31 to the Financial Statements.

Share Capital

Details of the share capital of the Company are set out in Note 42 to the Financial Statements.

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

Distributable Reserves

Distributable reserves of the Company as at 31 December 2012, calculated under section 79B of the Hong Kong Companies Ordinance, amounted to approximately HK\$10,628 million.



Five-year Financial Summary

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

Directors

The list of Directors of the Company is set out on page 46. The biographical details of the Directors and senior management are set out on pages 47 to 51 of this Annual Report. The term of office for each Non-executive Director is approximately three years.

Mr. XIAO Gang resigned as Chairman and Non-executive Director with effect from 17 March 2013. The Board would like to express its sincere gratitude and the highest respect to Mr. XIAO for his excellent contributions in all aspects during his tenure of office. Mr. NING Gaoning was appointed as an Independent Non-executive Director with effect from 24 August 2012. The Board welcomes Mr. NING to join the Board.

In accordance with Article 98 of the Articles of Association and pursuant to Code A.4.2 of the Corporate Governance Code, Mr. LI Lihui, Mr. GAO Yingxin, Mr. SHAN Weijian and Mr. TUNG Chee Chen will retire by rotation at the forthcoming annual general meeting. Mr. TUNG Chee Chen has notified the Company that he has decided not to stand for re-election at the forthcoming annual general meeting. The other three retiring Directors, being eligible, will offer themselves for re-election. Further, pursuant to the Articles of Association, any Director appointed by the Board during the year shall hold office only until the next following annual

general meeting of the Company, and shall then be eligible for re-election at such meeting. Accordingly, Mr. NING Gaoning, being a Director appointed on 24 August 2012, shall retire at the forthcoming annual general meeting and, being eligible, offer himself for re-election.

Directors' Service Contracts

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

Directors' Interests in Contracts of Significance

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

Directors' Interests in Competing Business

Prior to Mr. XIAO Gang's resignation on 17 March 2013, he was the Chairman and an Executive Director of BOC. Mr. LI Lihui and Mr. LI Zaohang are Executive Directors of BOC. Mr. CHEN Siqing is an Executive Vice President of BOC.

BOC is a joint stock limited liability commercial bank in the Mainland of China providing a full range of commercial banking and other

financial services through its associates throughout the world. Certain of the Group's operations overlap with and/or are complementary to those of BOC and its associates. To the extent that BOC or its associates compete with the Group, the Directors believe that the Group's interests are adequately protected by good corporate governance practices and the involvement of the Independent Non-executive Directors.

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

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

Directors' Rights to Acquire Shares

On 5 July 2002, the following Directors were granted options by BOC (BVI), the immediate holding company of the Company, pursuant to a Pre-Listing Share Option Scheme to purchase from BOC (BVI) the 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.

REPORT OF THE DIRECTORS

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

Name of Director	Date of grant	Exercise price per share (HK\$)	Exercisable period	Number of share options					
				Granted on 5 July 2002	Balances as at 1 January 2012	Exercised during the year	Surrendered during the year	Lapsed during the year	Balances as at 31 December 2012
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	-
Total				2,892,000	2,530,500	-	-	2,530,500	-

Note: According to the rules of the Pre-Listing Share Option Scheme, all outstanding options granted pursuant to the said Scheme had been lapsed on 5 July 2012.

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

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

As at 31 December 2012, 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					Total	% of the issued share capital
	Personal interests	Family interests	Corporate interests	Other interests			
HE Guangbei	100,000	-	-	-	-	100,000	0.0009%
NING Gaoning	-	25,000	Note	-	-	25,000	0.0002%
Total	100,000	25,000	-	-	-	125,000	0.0011%

Note: Such shares are held by the spouse of Mr. NING Gaoning.

Save as disclosed above, as at 31 December 2012, none of the Directors or the Chief Executive of the Company or their respective associates had any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.



Substantial Interests in Share Capital

The register maintained by the Company pursuant to section 336 of the SFO recorded that, as at 31 December 2012, the following parties had the following interests (as defined in the SFO) in the Company set opposite their respective names:

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

Notes:

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

All the interests stated above represented long positions. Save as disclosed above, as at 31 December 2012, 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 31 December 2012.

Management Contracts

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

REPORT OF THE DIRECTORS

Share Options

Pursuant to written resolutions of all the Company's shareholders passed on 10 July 2002, the Company has approved and adopted two share option schemes, namely, the Share Option Scheme and the Sharesave Plan, both of which expired in July 2012. No options have been granted by the Company pursuant to the Share Option Scheme or the Sharesave Plan during the year.

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

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

REPORT OF THE DIRECTORS



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

REPORT OF THE DIRECTORS

	Share Option Scheme	Sharesave Plan
(a) Amount payable on acceptance of the option	(a) HK\$1.00	(a) HK\$1.00
(b) Period within which payments or calls must or may be made	(b) Payment or an undertaking to make payment on demand of the Company must be received by the Company within the period open for acceptance as set out in the letter of offer which shall not be less than 7 days after the offer date.	(b) Payment or an undertaking to make payment on demand of the Company must be received by the Company not later than the date specified in the letter of invitation as the directors may determine.
(c) The period within which loans for such purposes must be repaid	(c) Not applicable.	(c) Not applicable.
Basis of determining the exercise price	<p>The exercise price is determined on the date of grant by the Board and shall not be less than the highest of:</p> <p>(a) the nominal value of the Company's shares;</p> <p>(b) the closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheet on the date of grant, which must be a business day; and</p> <p>(c) the average closing price of the Company's shares as stated in the Stock Exchange's daily quotations sheets for the five business days immediately preceding the date of grant.</p>	Same as Share Option Scheme.
Remaining life	The Share Option Scheme shall remain in force for a period of ten years commencing on the first day of dealings in the Company's shares on the Stock Exchange which was 25 July 2002. Accordingly, the expiry of the Share Option Scheme took effect from 25 July 2012.	The Sharesave Plan shall remain in force for a period of ten years after the date of approval and adoption of the Sharesave Plan by the Company's shareholders which was 10 July 2002. Accordingly, the expiry of the Sharesave Plan took effect from 10 July 2012.

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



Purchase, Sale or Redemption of the Company's Shares

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

Major Customers

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

Connected Transactions

The Independent Non-executive Directors have reviewed the transactions which the Company disclosed in a public announcement on 30 December 2010 and confirmed that these transactions were:

- (i) entered into in the ordinary and usual course of business of the Group;
- (ii) conducted either on normal commercial terms or, if there were not sufficient comparable transactions to judge whether they were on normal commercial terms, on terms no less favourable to the Group than terms available to or from (as appropriate) independent third parties;
- (iii) entered into in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole; and
- (iv) in each case where an annual cap had been set, that such cap was not exceeded.

In accordance with paragraph 14A.38 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, the Board of Directors engaged the auditor of the Company to report on the Group's continuing connected transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. The auditor has issued its unqualified letter containing its findings and conclusions in respect of the above continuing connected transactions. A copy of the auditor's letter has been provided by the Company to The Stock Exchange of Hong Kong Limited.

Budgetary Discipline and Reporting

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

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

This annual report complies with the applicable requirements set out in the Banking (Disclosure) Rules under the Banking Ordinance and the applicable disclosure provisions of the Listing Rules.

Auditor

The financial statements for the year 2012 have been audited by PricewaterhouseCoopers ("PwC").

PwC will retire as auditor of the Company upon expiration of its current term of office at the close of the forthcoming annual general meeting of the Company to be held on Tuesday, 28 May 2013 (the "2013 AGM").

On 25 March 2013, the Board resolved to propose the appointment of Messrs. Ernst & Young as the new auditor of the Company to fill the vacancy immediately following the retirement of PwC and to hold office until the conclusion of the next forthcoming annual general meeting of the Company, subject to the approval of the shareholders of the Company at the 2013 AGM.

On behalf of the Board

LI Lihui
Vice Chairman

Hong Kong, 26 March 2013



CORPORATE GOVERNANCE

The Company is committed to maintaining and upholding high standards of corporate governance

in order to safeguard the interests of shareholders, customers and employees. The Company abides strictly by the laws and regulations in Hong Kong, and observes the rules and guidelines issued by regulatory authorities including HKMA, Hong Kong Securities and Futures Commission and the Stock Exchange of Hong Kong. The Company from time to time reviews the corporate governance practices as adopted and strives to comply with the relevant requirements of international and local corporate governance best practices.

The Stock Exchange of Hong Kong merged the "Corporate Governance Report" contained in Appendix 23 to the Listing Rules with the "Code on Corporate Governance Practices" contained in Appendix 14 (the "Former CG Code") to form the "Corporate Governance Code and Corporate Governance Report" as set out in the amended Appendix 14 (the "Corporate Governance Code"). Such Corporate Governance Code took effect on 1 April 2012. The Company is committed to embracing and enhancing good corporate governance principles and practices. **During the period under review, the Company has been in full compliance with all code provisions as set out in the Former CG Code as well as the Corporate Governance Code. The Company has also complied with nearly all the recommended best practices set out in the Corporate Governance Code throughout the period.** In particular, the Company publishes quarterly financial and business reviews so that shareholders can be better updated of the performance, financial positions

and prospects of the Company on a timely basis.

BOCHK, the Company's wholly-owned and principal operating subsidiary, is in full compliance with the guidelines as set out in the Supervisory Policy Manual module CG-1 entitled "Corporate Governance of Locally Incorporated Authorized Institutions" ("SPM CG-1") issued by HKMA. Meanwhile, BOCHK has also complied with almost all guidelines as set out in the latest SPM CG-1 revised by HKMA in August 2012 with further enhancement to be made prior to August 2013 so as to bring its corporate governance practices in line with the guidance stipulated in the revised module.

In 2012, the Company was awarded Category 1 (Hang Seng Index Constituent Companies) of The Hong Kong Corporate Governance Excellence Awards which was co-organised by the Chamber of Hong Kong Listed Companies and the Centre for Corporate Governance and Financial Policy of Hong Kong Baptist University with an aim to encourage improvements in corporate governance of listed companies in Hong Kong. This was the second consecutive year for the Company to be granted such recognised awards. The Company will continue to maintain sound corporate governance standards and procedures to ensure the completeness, transparency and quality of our information disclosure.

Corporate Governance Policy

Policy Statement

The Company recognises the importance of high standards of corporate governance and maintains

an effective corporate governance framework which delivers long-term success of the Group. The Company is also strongly committed to embracing and enhancing sound corporate governance principles and practices. The established and well-structured corporate governance framework directs and regulates the business ethical conduct of the Company, thereby protects and upholds the value of shareholders and stakeholders as a whole in a sustainable manner.

Essential Principles

(1) Eminent Board

Authority

The Board is responsible for supervising the Management of the business and affairs of the Group with due regard to maximising shareholder value and enhancing corporate governance standard of the Group. The Board is obliged to act honestly and in good faith and to make decisions objectively in the best interests of the Group and its shareholders as a whole.

Structure

The Company is led by a high caliber Board with strong representation of Independent Non-executive Directors. The Board has a well-balanced composition of Executive Directors, Non-executive Directors and Independent Non-executive Directors. Both the number and percentage of the Independent Non-executive Directors are well above the requirements set by relevant rules and regulations. All Directors are eminent individuals from diverse disciplines with extensive professional experience and are able to make objective judgement.



Roles of Chairman and Chief Executive

In order to promote balance of power, the roles of Chairman and Chief Executive are segregated. The Company may benefit from the segregation as the Chairman can focus on leading the Board and monitoring corporate governance and shareholder issues, while the Chief Executive leading the Management to perform the day-to-day operations and affairs of the Company.

Board Committees

The Board has established four standing Board Committees which are delegated with different responsibilities to assist the Board in performing its duties. They are Audit Committee, Nomination and Remuneration Committee, Risk Committee, and Strategy and Budget Committee. Most of them are composed of a majority of Independent Non-executive Directors. Each of the Board Committees has a well-defined mandate with the roles and responsibilities delineated therein. The performance and effectiveness of these standing Board Committees are evaluated periodically with a view to making further enhancement. Other Board Committees like Independent Board Committee and Search Committee will be formed as and when required under the appropriate circumstances.

(2) Prudent Risk Management

The Board recognises the need for risk control and management being a vital component of the business of the Group. The Board formulates and oversees the risk management strategies, and the related framework and policies with the assistance of the Risk Committee and other

relevant Board Committee(s). The Management performs the daily risk management responsibilities of the Group under the guidance of the Risk Committee.

(3) Fair Remuneration System

The Company ensures that Directors' remuneration should be appropriate and reflect their duty and responsibility to fulfil the expectations of the shareholders and meet regulatory requirements. Directors' fees are subject to the approval of the shareholders. The Board, based on the recommendations of the Nomination and Remuneration Committee which is mainly responsible for ensuring the fairness and reasonableness of the overall human resources and remuneration strategies, approves the remuneration policies of the Group. No Director shall be involved in deciding his or her own remuneration.

(4) Effective Disclosure Mechanism

The Board reviews and monitors from time to time the effectiveness of the Group's disclosure process for reports, announcements, price sensitive and inside information. It encourages and takes necessary steps to disclose information in a timely manner and to ensure the information concerning the Group is expressed and communicated in a clear and objective manner that enables the shareholders and the public to appraise the position of the Group to make informed investment decisions.

(5) Upholding Shareholders' Rights

The Board respects the rights of shareholders as mandated by the memorandum and articles of association of the Company (the "Articles of Association")

and relevant applicable laws and regulatory requirements. The Board places utmost importance on maintaining effective communications with shareholders and also makes its best efforts to keep the shareholders informed of the business and affairs of the Company by maintaining various channels of communications and having direct dialogue with shareholders. In addition, the shareholders also have the rights to obtain all available information of the Company, make proposals at general meetings, nominate a person for election as a director, and make enquiries about the Company.

(6) Safeguarded Stakeholders' Interests

The Board has a fiduciary duty to protect and serve, with due care and consideration of, the interest of all stakeholders of the Company including but not limited to employees, customers, business partners, suppliers, regulators and the community. All the interests of stakeholders of the Company are further safeguarded by strictly complying with applicable laws and regulations as well as governance policies.

(7) Sustainable Corporate Social Responsibility

The Company attaches great importance to corporate social responsibility. The Board is committed to undertaking corporate social responsibility by strengthening relationship with its stakeholders with a view to contributing to the sustainable development of the economy, society and environment. The Company consistently supports and participates in activities that are beneficial to the community.



CORPORATE GOVERNANCE

(8) Pursuit of “Good to Great”

The Board encourages the pursuit of “Good to Great”. With the assistance of the Nomination and Remuneration Committee, the Board ensures that each Board Committee shall conduct regular self-assessment of its effectiveness, and based on the evaluation results, the Board gives such feedback, directions and guidance as may be necessary to enhance its efficiency and effectiveness.

Policy Goal

The Board and the senior management of the Company are responsible for adhering to the corporate governance principles and executing this policy. The Company seeks to manage its business in accordance with the well-defined corporate governance principles which therefore provide a solid governance framework for excellent performance and sustainable growth.

Corporate Governance Framework

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

- formulating the Group’s mid and long-term strategy and monitoring the implementation thereof;
- reviewing and approving the annual business plans and financial budgets;
- approving the annual, interim and quarterly results;

- reviewing and monitoring the Group’s risk management and internal control;
- ensuring good corporate governance and effective compliance; and
- monitoring the performance of the Management.

The Board authorises the Management to implement the strategies as approved by the Board. The Management is responsible for the day-to-day operations of the Group and reports to the Board. **For this purpose, the Board has formulated clear written guidelines which stipulate the circumstances whereas the Management should report to and obtain prior approval from the Board before making decisions or entering into any commitments on behalf of the Group.** The Board will conduct regular review on these authorisation and guidelines.

To avoid concentration of power in any single individual, the **positions of the Chairman and the Chief Executive should be held by two different individuals. Their roles are distinct, clearly established and stipulated in the Board’s Mandate.** In short, the Chairman is responsible for ensuring that the Board properly discharges its responsibilities and conforms to good corporate governance practices and procedures. In addition, as the Chairman of the Board, he is also responsible for ensuring that all Directors are properly briefed on all issues currently on hand, and that all Directors receive adequate, accurate and reliable information in a timely manner. The Chief Executive is responsible for providing leadership for the whole Management and implementing important policies and

development strategies as adopted by the Board.

Taking into consideration market practices and international best practices in corporate governance, **the Board has established four standing Board Committees** to assist in performing its responsibilities. They are the Audit Committee, the Nomination and Remuneration Committee, the Risk Committee, and the Strategy and Budget Committee. In addition, the Board will authorise an independent board committee comprising all Independent Non-executive Directors as and when required to review, approve and monitor connected transactions (including the continuing connected transactions) in accordance with the relevant rules and regulations that should be approved by the Board.

Each of the Board Committees has a well-defined Mandate and makes recommendations to the Board on relevant matters within its scope of responsibilities or makes decisions under appropriate circumstances in accordance with the power delegated by the Board. **All Board Committees are assigned a professional secretarial department which ensures that the Board Committees have adequate resources to perform their duties effectively and properly.** The Board and Board Committees will participate in the annual performance appraisal of those professional secretarial departments to ensure and enhance the services provided and ensure that adequate and efficient supports are provided to the Board and Board Committees. In addition, according to their respective Mandates, **the Board and each of the Board Committees will evaluate and review their work process and effectiveness annually, with a view to identifying areas for further improvements.**



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



Details including the Company's corporate governance principles and framework adopted by the Board, the composition of the Board and each of the Board Committees and their respective Mandates, Corporate Governance Policy, Shareholder Communication Policy, Information Disclosure Policy and Fair Disclosure Policy are available under the subsection "Corporate Governance" of the section headed "About Us" on the Company's website at www.bochk.com.

Board of Directors

The Board of the Company is composed of majority of Non-executive Directors and Independent Non-executive Directors that ensures the independence and objectivity of the decisions of the Board, as well as comprehensive and impartial control of the Management. The Board acts honestly and in good faith so that decisions are made objectively with a view to delivering long-term and maximum shareholder value and fulfilling its corporate responsibility to other stakeholders of the Group.

The Board currently has twelve members, comprising six Independent Non-executive Directors, four Non-executive Directors and two Executive Directors. Mr. XIAO Gang resigned as Chairman and Non-executive Director of the Company on 17 March 2013; and Mr. NING Gaoning was appointed as an Independent Non-executive Director of the Company on 24 August 2012. Save as disclosed above, there were no other changes to the composition of the Board in 2012 and up to the date of this Annual Report.

Under the current board membership, all Directors possess extensive experience in banking and management. In addition, over one-third of them are Independent Non-executive Directors, of whom some of them are experts in financial and/or risk management. The Board has adopted the "Policy on Independence of Directors" (the "Independence Policy") which stipulates the criteria on independence of Independent Non-executive Directors. The Company has received from each of the Independent Non-executive Directors an annual confirmation of his independence by reference to the Independence Policy. Based on the information available to the Company,

it considers that all of the Independent Non-executive Directors are independent. Biographical details of the Directors are set out in the section headed "Board of Directors and Senior Management" of this Annual Report and are available under the subsection "Organisation" of the section headed "About Us" on the Company's website at www.bochk.com.

All the existing **Non-executive Directors and Independent Non-executive Directors** of the Company have been **appointed for a fixed term of approximately 3 years, with formal letters of appointment** setting out the key terms and conditions of their appointment. In accordance with Article 98 of the Articles of Association and pursuant to Code A.4.2 of the Corporate Governance Code, Mr. LI Lihui, Mr. GAO Yingxin, Mr. SHAN Weijian and Mr. TUNG Chee Chen will retire by rotation at the forthcoming annual general meeting. Mr. TUNG Chee Chen has notified the Company that he has decided not to stand for re-election at the forthcoming annual general meeting. The other three retiring Directors, being eligible, will offer themselves for re-election. Further, pursuant to the Articles of Association,



CORPORATE GOVERNANCE

any Director appointed by the Board during the year shall hold office only until the next following annual general meeting of the Company, and shall then be eligible for re-election at such meeting. Accordingly, Mr. NING Gaoning, being a Director appointed on 24 August 2012, shall retire at the forthcoming annual general meeting and, being eligible, offer himself for re-election. Further details regarding the proposed re-election of Directors are set out in the section headed "Report of the Directors" of this Annual Report. In addition, the Nomination and Remuneration Committee has also established a **written and formal process for the appointment of Independent Non-executive Directors to ensure that the appointment procedures are standardised, thorough and transparent.**

Prior to Mr. XIAO Gang's resignation on 17 March 2013, he was the Chairman and an Executive Director of BOC. Mr. LI Lihui and Mr. LI Zaohang are Executive Directors of BOC. Mr. ZHOU Zaiqun was a former Executive Director and Executive Vice President of BOC (he ceased to be an Executive Director and Executive Vice President of BOC with effect from 28 May 2011). Mr. CHEN Siqing is an Executive Vice President of BOC. **Save as disclosed above, there are no other relationships between the Board members, including financial, business, family or other material/relevant relationships.**

In addition, it is expressly provided in the Board's Mandate that, unless the applicable laws or regulations allow otherwise, if a substantial shareholder or Director has a conflict of interest in the matter to be considered by the Board, a Board meeting must be convened and attended by Independent Non-executive Directors who have no material interest, and give professional advice to the subject matter for further consideration and approval.

During the year, the Company has arranged for **appropriate cover on Directors' Liability Insurance Policy to indemnify the Directors for liabilities arising from the corporate activities.** The coverage and the amount insured under such policy are reviewed annually by the Company.

To ensure the newly appointed Directors to have adequate understanding of the Company's business operations and to enable all Directors to update their knowledge regularly so as to provide informed recommendation and advice and make contribution to the Company, **the Board establishes a set of written policy specifying guidelines on Directors' induction and training upon appointment.**

The Company also provides regular updates to Board members on material changes to regulatory requirements applicable to the Directors and the Company on a timely basis; and arranges regular

meetings with the Management to facilitate the understanding of the latest business development of the Company. In addition, Board members are encouraged to participate actively in continuous training programmes. The Company also arranges relevant professional training programmes for Board members at Company's expense. In 2012, the Company invited Mr. CAO Yuanzheng, Chief Economist of BOC, to deliver a seminar to the Directors and senior management with regard to the trend and outlook of macro-economic in Mainland China, and the reform of international monetary system and RMB Internationalisation.

During the year, all Directors have participated in continuous professional development to develop and refresh their knowledge and skills in accordance with Code A.6.5 contained in Appendix 14 to the Listing Rules. Each of the Directors received a series of training locally or overseas as he thought fit, relevant trainings and briefings included, among others:

- development of national and global economy;
- national policy outlook;
- corporate governance;
- regulatory updates; and
- banking industry development trend, etc.



All of them have also provided to the Company their records of training received for the year, the information of which has been entered in the register of directors' training records maintained and updated by the Company from time to time. The following summarises the compliance status of all Directors of the Company in respect of Code A.6.5 during the year:

Directors	In compliance with Code A.6.5
<i>Non-executive Directors</i>	
Mr. XIAO Gang (<i>Chairman</i>) (<i>Note 1</i>)	✓
Mr. LI Lihui (<i>Vice Chairman</i>)	✓
Mr. LI Zaohang	✓
Mr. ZHOU Zaiqun	✓
Mr. CHEN Siqing	✓
<i>Independent Non-executive Directors</i>	
Dr. FUNG Victor Kwok King	✓
Mr. KOH Beng Seng	✓
Mr. NING Gaoning (<i>Note 2</i>)	✓
Mr. SHAN Weijian	✓
Mr. TUNG Chee Chen	✓
Mr. TUNG Savio Wai-Hok	✓
<i>Executive Directors</i>	
Mr. HE Guangbei (<i>Vice Chairman and Chief Executive</i>)	✓
Mr. GAO Yingxin	✓

Note 1: Mr. XIAO Gang resigned as Chairman and Non-executive Director of the Company with effect from 17 March 2013.

Note 2: Mr. NING Gaoning was appointed as an Independent Non-executive Director of the Company with effect from 24 August 2012.

Seven Board meetings were held during 2012 with an average attendance rate of 93%. The meeting schedule for the year was prepared and approved by the Board in the preceding year. In general, Board agenda and meeting materials are despatched to all Board members for review at least seven

days prior to the scheduled meetings. Board agenda is approved by the Chairman following consultation with other Board members and the senior management. In addition, in order to facilitate open discussion with all Non-executive Directors, the Chairman meets with all Non-executive Directors

(including Independent Non-executive Directors), in the absence of Executive Directors and the senior management, during the discussion session before each Board meeting. Relevant practice has been incorporated in the Working Rules of the Board.

CORPORATE GOVERNANCE

In 2012, details of respective Directors' attendance at the Board meetings are set out as follows:

Directors	Number of Board meetings attended	Attendance rate
<i>Non-executive Directors</i>		
Mr. XIAO Gang (<i>Chairman</i>) (<i>Note 1</i>)	6 out of 7	86%
Mr. LI Lihui (<i>Vice Chairman</i>)	7 out of 7	100%
Mr. LI Zaohang	7 out of 7	100%
Mr. ZHOU Zaiqun	7 out of 7	100%
Mr. CHEN Siqing	6 out of 7	86%
<i>Independent Non-executive Directors</i>		
Dr. FUNG Victor Kwok King	5 out of 7	71%
Mr. KOH Beng Seng	7 out of 7	100%
Mr. NING Gaoning (<i>Note 2</i>)	0 out of 2	0%
Mr. SHAN Weijian	7 out of 7	100%
Mr. TUNG Chee Chen	7 out of 7	100%
Mr. TUNG Savio Wai-Hok	7 out of 7	100%
<i>Executive Directors</i>		
Mr. HE Guangbei (<i>Vice Chairman and Chief Executive</i>)	7 out of 7	100%
Mr. GAO Yingxin	7 out of 7	100%

Note 1: Mr. XIAO Gang resigned as Chairman and Non-executive Director of the Company with effect from 17 March 2013.

Note 2: Mr. NING Gaoning was appointed as an Independent Non-executive Director of the Company with effect from 24 August 2012.

Apart from formal Board meetings and annual general meetings, the Company arranges, on a regular basis, other casual events for the Board members and the senior management to facilitate their communication and interactions. For example, **the Company organises breakfast meetings from time to time, Board members and senior management have been invited to join and share insights on the Company's business and strategic issues. Further, a board retreat has also been held during the year to enhance communication between the Board and the senior management.**

Audit Committee

The Audit Committee currently comprises six members, including

five Independent Non-executive Directors, namely Mr. SHAN Weijian, Dr. FUNG Victor Kwok King, Mr. KOH Beng Seng, Mr. TUNG Chee Chen and Mr. TUNG Savio Wai-Hok, and one Non-executive Director, Mr. ZHOU Zaiqun. Independent Non-executive Directors make up 83% of the Committee members. The Audit Committee is chaired by Mr. SHAN Weijian, an Independent Non-executive Director.

The Audit Committee assists the Board in performing the duties in respect of the Company and its subsidiaries in, among others, the following areas:

- integrity of financial statements and financial reporting process;
- internal control systems;

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



The work performed by the Audit Committee during 2012 included the review and, where applicable, approval of:

- the Company's Directors' Report and financial statements for the year ended 31 December 2011 and the annual results announcement that were recommended to the Board for approval;
- the Company's interim financial statements for the six months ended 30 June 2012 and the interim results announcement that were recommended to the Board for approval;
- the Company's announcements on quarterly financial and business review for the period ended 31 March 2012 and 30 September 2012 that were recommended to the Board for approval;

- the audit reports and report on internal control recommendations submitted by external auditor, and the on-site examination reports issued by regulators;
- the appointment of external auditor, the fees payable to external auditor for the annual audit, interim review and other non-audit services;
- the Company's audit plan for 2012 and key issues identified;
- the deployment of human resources and pay level of the Internal Audit and its budget for 2012; and
- the 2011 performance appraisal of and 2012 key performance indicators for the Head of Group Audit and the Group Audit.

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

Pursuant to paragraph C.2 of the Corporate Governance Code, the Audit Committee conducted an annual review of the effectiveness of the internal control systems of the Group in 2012. The review covers all the material internal controls and measures, including financial, operational and compliance controls as well as risk management functions. The review also considers the adequacy of resources, staff qualifications and experience and training of the Group's accounting and financial reporting functions. Details of the relevant review will be elaborated in the sub-section headed "Internal Control".

Seven Audit Committee meetings were held during 2012 with an average attendance rate of 90%. Individual attendance records of the relevant Directors are set out as follows:

Directors	Number of committee meetings attended	Attendance rate
Mr. SHAN Weijian (<i>Chairman</i>)	6 out of 7	86%
Mr. ZHOU Zaiqun	7 out of 7	100%
Dr. FUNG Victor Kwok King	5 out of 7	71%
Mr. KOH Beng Seng	7 out of 7	100%
Mr. TUNG Chee Chen	6 out of 7	86%
Mr. TUNG Savio Wai-Hok	7 out of 7	100%

Nomination and Remuneration Committee

The Nomination and Remuneration Committee comprises five members, including two Non-executive Directors, namely Mr. LI Lihui and Mr. LI Zaohang, and three Independent Non-executive Directors, namely Mr. TUNG Chee Chen, Mr. SHAN Weijian and Mr. TUNG Savio Wai-Hok. It was chaired by Mr. TUNG Chee Chen, an Independent Non-executive Director of the Board. With effect from 9 January 2012, Mr. LI Lihui resigned as the Chairman of Nomination and Remuneration Committee, but remained as a member; Mr. TUNG Chee Chen was appointed as the Chairman; Dr. FUNG Victor Kwok King resigned as a member and Mr. TUNG Savio Wai-Hok was appointed as a member in place of Dr. FUNG Victor Kwok King. Prior and subsequent to such changes, the Independent Non-executive Directors represent 60% of the Committee members.

The Nomination and Remuneration Committee assists the Board in performing the duties in respect of the Company and its subsidiaries in, among others, the following areas:

- human resources, remuneration strategy and incentive framework of the Group;
- selection and nomination of Directors, Board Committee members and certain senior executives as designated by the Board from time to time (defined as “Senior Management”);

- structure, size and composition (including skills, experience and knowledge) of the Board and Board Committees;
- remuneration of Directors, Board Committee members, Senior Management and Key Personnel;
- effectiveness of the Board and Board Committees;
- training and continuous professional development of Directors and Senior Management; and
- code of conduct applicable to employees.

Key tasks performed by the Nomination and Remuneration Committee during 2012 included the approval, review and proposal to the Board on the following according to the responsibilities and authorities:

- formulation, review and amendment on the major human resources and remuneration policies, including adjustment and optimisation of the derivation method of the Group Bonus Funding based on the Board’s approved business objectives and positioning of NCB (China) to facilitate a successful strategic transformation by strengthening incentive mechanic and; to enhance indicators used in the Risk Adjustment Method based on the Bank’s latest risk management profile, by introducing more quantitative measures, to make the Risk Adjustment Method more scientific and objective; to

review the identification criteria of “Senior Management”, “Key Personnel”, “Key Employee Group” and “Risk Control Personnel” as delineated in the “Guideline on a Sound Remuneration System” published by HKMA, as well as the review of specified jobs for “Senior Management” and “Key Personnel” in accordance with the changes in organisational structure and risk management requirements;

- performance appraisal results of the Executive Directors and Senior Management for year 2011;
- proposal on staff bonus for year 2011 and salary adjustment for year 2012 for the Group, including the Senior Management;
- key performance indicators of the Group and the Senior Management for year 2012;
- proposal on human resources budget of the Group for year 2012 and 2013;
- monitoring the implementation progress of the Group’s medium-term human resources strategies and other major human resources policies;
- analysis and report of self-evaluation results of the Board and Board Committees, put forward recommendations to the Board to further enhance the functions and effectiveness of the Board and Board Committees;



- recruitment of an Independent Non-executive Director of the Company, include considering the candidates from the open and global recruitment conducted by the Search Committee in the sense of their professional knowledge and abilities, and recommending to the Board on the proposed candidate; and
- consideration of the matters relating to the adjustment and appointment of directors in major subsidiaries of the Group.

Pursuant to the “**Policy on Directors’ Remuneration**” adopted by the Company, when recommending the remuneration of Directors, the Committee

should benchmark against companies of comparable business type or scale, and job nature and workload at both the Board and Board Committee levels (including frequency of meetings and nature of agenda items) in order to compensate Directors fairly. **No individual Director is allowed to participate in the procedures**

for deciding his/her individual remuneration package. Information relating to the remuneration of each Director for 2012 is set out in Note 21 to the financial statements of this Annual Report. The present scale of Director’s fees, including additional fees for membership of Board Committees, is given below:

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

Note: For the year ended 31 December 2012, all Non-executive Directors waived their Directors’ fee as mentioned above.

The Nomination and Remuneration Committee also has the delegated responsibility to **determine the remuneration packages of the Executive Directors and Senior Management, including long-term incentive, share option, benefits in kind, pension rights**

and compensation payments (including any compensation payable for loss or termination of their office or appointment, early payout of deferred remuneration), as well as the performance-based remuneration. Moreover, it will recommend to the Board on their

remuneration package upon joining, sign-on bonus and contract guaranteed bonus, etc.

Six Nomination and Remuneration Committee meetings were held during 2012 with an average attendance rate of 83%. Attendance records of relevant Directors are set out as follows:

Directors	Number of committee meetings attended	Attendance rate
Mr. TUNG Chee Chen (<i>Chairman</i>) (<i>Note</i>)	6 out of 6	100%
Mr. LI Lihui	5 out of 6	83%
Mr. LI Zaohang	6 out of 6	100%
Dr. FUNG Victor Kwok King (<i>Note</i>)	0 out of 1	0%
Mr. SHAN Weijian	4 out of 6	67%
Mr. TUNG Savio Wai-Hok (<i>Note</i>)	4 out of 5	80%

Note: With effect from 9 January 2012, Mr. LI Lihui resigned as the Chairman of Nomination and Remuneration Committee, but remained as a member of the Committee; Mr. TUNG Chee Chen was appointed as the Chairman of Nomination and Remuneration Committee; in addition, Dr. FUNG Victor Kwok King resigned as a member of the Nomination and Remuneration Committee and Mr. TUNG Savio Wai-Hok was appointed as a member in place of Dr. FUNG Victor Kwok King.

CORPORATE GOVERNANCE

Risk Committee

The Risk Committee comprises four members, including two Non-executive Directors, namely Mr. LI Zaohang and Mr. CHEN Siqing, and two Independent Non-executive Directors, namely Mr. KOH Beng Seng and Mr. TUNG Savio Wai-Hok. The Risk Committee is chaired by Mr. KOH Beng Seng.

The Risk Committee assists the Board in performing the duties in respect of the Company and its subsidiaries in, among others, the following areas:

- formulation of the risk appetite and risk management strategy of the Group and determination of the Group's risk profile;
- identification, assessment and management of material risks faced by various business units of the Group;
- review and assessment of the adequacy and effectiveness of the Group's risk management policies, system and internal control;
- review and monitoring of the Group's capital management;
- review and approval of the Group's target balance sheet;

- review and monitoring of the Group's compliance with the risk management policies, system and internal control, including the Group's compliance with prudential, legal and regulatory requirements governing the businesses of the Group;
- review and approval of high-level risk-related policies of the Group;
- review and approval of significant or high risk exposures or transactions; and
- review of key reports, including risk exposure reports, model development and validation reports, and credit risk model performance reports.

The work performed by the Risk Committee during 2012 included the following:

- review/approval of policies, including the "BOCHK Group Operating Principles", the "Risk Management Policy Statement of BOCHK Group", the "Capital Management Policy", the "Staff Code of Conduct", the "Policy for Validating Internal Rating Systems", the "Connected Transactions Management Policy", and a range

of risk management policies covering strategic risk, credit risk, market risk, liquidity risk, interest rate risk, operational risk, legal, compliance and reputation risk and stress testing, etc;

- review/approval of the risk adjustment method for group bonus funding mechanics;
- review/approval of the Group's operating plans, including the Group's target balance sheets, the BOCHK's banking book investment plans and portfolio key risk indicators, results of Internal Capital Adequacy Assessment Process (ICAAP), as well as risk management limits;
- review and monitoring of Basel II implementation, including approval of IRB models, review of model validation reports, receiving the implementation progress reports of IRB, as well as the status reports of the allocation of risk-weighted assets;
- review of various risk management reports; and
- review/approval of significant high risk exposures or transactions.

Six Risk Committee meetings were held during 2012 with an average attendance rate of 87%. Attendance records of relevant Directors are set out as follows:

Directors	Number of committee meetings attended	Attendance rate
Mr. KOH Beng Seng (<i>Chairman</i>)	6 out of 6	100%
Mr. LI Zaohang	6 out of 6	100%
Mr. CHEN Siqing	4 out of 6	67%
Mr. TUNG Savio Wai-Hok	5 out of 6	83%



Strategy and Budget Committee

The Strategy and Budget Committee comprises six members, including two Non-executive Directors, namely Mr. ZHOU Zaiqun and Mr. CHEN Siqing, and three Independent Non-executive Directors, namely Dr. FUNG Victor Kwok King, Mr. NING Gaoning and Mr. TUNG Savio Wai-Hok and Mr. HE Guangbei, the Chief Executive as well as the Executive Director of the Company. Mr. NING Gaoning was appointed as a member of the Strategy and Budget Committee with effect from 24 August 2012. The Strategy and Budget Committee is chaired by Mr. ZHOU Zaiqun, a Non-executive Director.

The Strategy and Budget Committee assists the Board in performing the duties in respect of the Company and its subsidiaries in, among others, the following areas:

- drafting, review of, making motion, and monitoring the Group's medium to long-term strategies;

- drafting and review of the process of formulating the Group's medium to long-term strategies to ensure that they are sufficiently robust to take into account a range of alternatives;
- monitoring the implementation of the Group's medium to long-term strategies through pre-determined metrics and providing guidance to the Management;
- review of and monitoring the Group's regular/periodic (including annual) business plans and financial budgets; and
- making recommendations to the Board on major capital expenditures, merger & acquisition and strategic commitments of the Group and monitoring the implementation thereof.

During the year, the Strategy and Budget Committee played a prominent role in providing guidance and monitoring the implementation

of the Group's short-term business strategies and driving the formulation and implementation of the Group's key business strategies, such as the development of China business, RMB business, private banking business, etc. In response to the new operating environment which posed new opportunities and challenges to the implementation of bank strategies, the Strategy and Budget Committee discussed the overseas development of Chinese peer banks from the Mainland and BOCHK's strategies. In addition, it also reviewed and monitored the implementation of the Group's financial budgets and business plans for 2012. The Strategy and Budget Committee also reviewed and endorsed the Group's financial budgets and business plans for the year 2013 and recommended the same to the Board for approval.

Six Strategy and Budget Committee meetings were held during 2012 with an average attendance rate of 78%. Attendance records of relevant Directors are set out as follows:

Directors	Number of committee meetings attended	Attendance rate
Mr. ZHOU Zaiqun (<i>Chairman</i>)	6 out of 6	100%
Mr. HE Guangbei	6 out of 6	100%
Mr. CHEN Siqing	4 out of 6	67%
Dr. FUNG Victor Kwok King	4 out of 6	67%
Mr. NING Gaoning (<i>Note</i>)	0 out of 2	0%
Mr. TUNG Savio Wai-Hok	5 out of 6	83%

Note: Mr. NING Gaoning was appointed as a member of the Strategy and Budget Committee with effect from 24 August 2012.

Ad Hoc Committee

The Board established an ad hoc Search Committee during the year with details as follows:

Search Committee

The Search Committee was established in January 2012 to conduct an open recruitment to search for a suitably qualified candidate as an Independent Non-executive Director of the Company. The Committee was chaired by Dr. FUNG Victor Kwok King, an Independent Non-executive Director. Its members included Mr. HE Guangbei, an Executive Director, Mr. LI Lihui, a Non-executive Director and Mr. KOH Beng Seng, Mr. SHAN Weijian, Mr. TUNG Chee Chen and Mr. TUNG Savio Wai-Hok, four Independent Non-executive Directors. After several rounds of selection and with the recommendation of the Nomination and Remuneration Committee, the Board resolved to appoint Mr. NING Gaoning as an Independent Non-executive Director of the Company with effect from 24 August 2012.

Directors' Securities Transactions

The Company has established and implemented the "Code for Securities Transactions by Directors" (the "Company's Code") to govern securities transactions by Directors. 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" as contained in Appendix 10 of the Listing Rules. Apart from the securities of the Company, the Company's Code also applies to the Director's dealings in the securities of BOC which has been listed on the Stock Exchange of Hong Kong since June 2006. Upon inquiry by the Company, all Directors confirmed that they had strictly complied with the provisions as set

out in both the Company's Code and the said Model Code throughout the year 2012.

Remuneration and Incentive Mechanism

The Remuneration and Incentive Mechanism of the Group is based on the principles of "effective motivation" and "sound remuneration management". It links remuneration with performance and risk factors closely. It serves to encourage staff to enhance their performance, and at the same time, to strengthen their awareness of risk so as to achieve sound remuneration management.

The Remuneration and Incentive Policy of the Group is applicable to the Company and all of its subsidiaries (including the branches and institutions in and out of Hong Kong).

- **"Senior Management" and "Key Personnel"**

The following groups of employees have been identified as the "Senior Management" and "Key Personnel" as defined in the HKMA's "Guideline on a Sound Remuneration System":

- "Senior Management": The senior executives designated by the Board who are responsible for oversight of the firm-wide strategy or material business lines, including Chief Executive, Deputy Chief Executives, Chief Financial Officer, Chief Risk Officer, Chief Operating Officer, Assistant Chief Executive, Board Secretary and Head of Group Audit.
- "Key Personnel": The employees whose individual business activities involve the assumption of material risk which may have significant impact on risk exposure, or whose individual responsibilities are directly and

materially linked to the risk management, or those who have direct influence to the profit, including heads of material business lines, heads of major subsidiaries, Head of Trading and Chief Dealer, as well as heads of risk control functions.

- **Determination of the Remuneration Policy**

To fulfil the above-mentioned principles and to facilitate effective risk management within the framework of the Remuneration Policy of the Group, the Remuneration Policy of the Group is initiated by Human Resources Department with consultation of the risk control units including risk management, financial management and compliance in order to balance the needs for staff motivations, sound remuneration and prudent risk management. After the proposed Remuneration Policy is cleared by the Management Committee, it will be submitted to the Nomination and Remuneration Committee for review and thereafter to the Board for approval. The Nomination and Remuneration Committee and the Board will seek opinions from other Board Committees (e.g. Risk Committee, Audit Committee, etc.) where they consider necessary under the circumstances.

- **Key Features of the Remuneration and Incentive Mechanism**

1. *Performance Management Mechanism*

To reflect the "performance-driven" corporate culture, the Group has put in place a performance management mechanism to formalise the performance management at the levels of the Group, units and individuals. The annual targets of the Group will be cascaded down



under the framework of balanced scorecard whereby the performance of the “Senior Management” and different units (including business units, risk control units and other units) would be assessed from the perspectives of financial, customer, building blocks/key tasks, human capital, risk management and compliance. For individual staff at different levels, annual targets of the Group will be tied to their job requirements through the performance management mechanism. Performance of individuals will be appraised on their achievement against targets, their contribution towards performance of their units and fulfilment of risk management duties and compliance. Not only is target accomplishment taken into account, but the risk exposure involved during the course of work could also be evaluated and managed, ensuring security and normal operation of the Group. Core values are also assessed to facilitate the attainment of them.

2. *Risk Adjustment of Remuneration*
To put the principle of aligning performance and remuneration with risk into practice, based on “The Risk Adjustment Method for Group Bonus Funding Mechanics”, the key risk modifiers of the Bank have been incorporated into the performance management mechanism of the Group. The size of the Variable Remuneration Pool of the Group is calculated according to the risk adjusted performance results approved by the Board and is subject to the Board’s discretion. This method ensures the Group to fix the Group’s Variable Remuneration Pool after considering risk exposures and changes and to maintain effective risk management through the remuneration mechanism.

“The Risk Adjustment Method for Group Bonus Funding Mechanics” was reviewed this year. With professional advices sought from the Risk Committee, the enhancement was approved by the Board after review carried out by the Nomination and Remuneration Committee. The framework of using credit risk, market risk, interest rate risk, liquidity risk, operational risk, legal risk, compliance risk and reputation risk was maintained. To be more scientific and objective, more quantitative measures were introduced based on the Bank’s latest risk management profile.

3. *Performance-based and Risk-adjusted Remuneration Management*

The remuneration of staff is composed of “fixed remuneration” and “variable remuneration”. The proportion of one to the other for individual staff members depends on job grades, roles, responsibilities and functions of the staff with the prerequisite that balance has to be struck between the fixed and variable portion. Generally speaking, the higher the job grades and/or the greater the responsibilities, the higher will be the proportion of variable remuneration so as to encourage the staff to follow the philosophy of prudent risk management and sound long-term financial stability.

Every year, the Group will conduct periodic review on the fixed remuneration of the staff with reference to various factors like remuneration strategy, market pay trend and staff salary level, and will determine the remuneration based on the affordability of the Group as well as the performance of the Group, units and individuals. As mentioned above, performance assessment criteria include

quantitative and qualitative factors, as well as financial and non-financial indicators.

According to the Group Bonus Funding Mechanics, the size of the Variable Remuneration Pool of the Group is determined by the Board on the basis of the financial performance of the Group and the achievement of non-financial strategic business targets under the long-term development of the Group. Thorough consideration is also made to the risk factors in the determination process. The size of the Pool is reached based on pre-defined formulaic calculations but the Board can make discretionary adjustment to it if deemed appropriate under prevailing circumstances. When the Group’s performance is relatively weak (e.g. failed to meet the threshold performance level), no variable remuneration will be paid out that year in principle, however, the Board reserves the rights to exercise its discretion.

As far as individual units and individual staff are concerned, allocation of the variable remuneration is closely linked to the performance of the units, and that of each individual staff as well as the unit he/she is attaching to, and the assessment of which should include risk modifiers. The performance and remuneration arrangement of risk control personnel are determined by the achievement of their core job responsibilities, independent from the business they oversee; for front-line risk controllers, a matrix reporting and performance management system is applied to ensure the suitability of performance-based remuneration. Within the acceptable risk level of the Group, the better the performance of the unit and the

individual staff, the higher will be the variable remuneration for the individual staff.

4. *Linking the payout of the variable remuneration with the time horizon of the risk to reflect the long-term value creation of the Group*

To work out the principle of aligning remuneration with the time horizon of risk and to ensure that sufficient time is allowed to ascertain the associated risk and its impact before the actual payout, payout of the variable remuneration of staff is required to be deferred in cash if such amount reaches certain prescribed threshold. The Group adopts a progressive approach towards deferral. The longer the time horizon of risk in the activities conducted by the staff, the higher the job grade or the higher amount of the variable remuneration, the higher will be the proportion of deferral. Deferral period lasts for 3 years.

The vesting of the deferred variable remuneration is linked with the long term value creation of the Group. The vesting conditions are linked to the yearly performance (financial and non-financial) of the Group in the next 3 years to the effect that the variable remuneration could only be vested to such extent as set for the relevant year in that 3-year period subject to the condition that the Group's performance has met the threshold requirement in the corresponding year. In case of material revision of the original estimates of the performance of the Group or individual units, or if a staff is found to commit fraud, or found to be of malfeasance or in violation of internal control policies, the unvested portion of the deferred variable remuneration of the relevant staff will be clawed back.

- **External Remuneration Consultant**

To ensure the suitability and competitiveness of the remuneration and incentive mechanism, the Group appointed Towers Watson Pennsylvania Inc. and McLagan for independent consultation in areas of pay management mechanism of Senior Management and market remuneration data.

External Auditor

With the recommendation of the Audit Committee, the Board has proposed Ernst & Young to be appointed as the new auditor of the Company at the Company's 2013 annual general meeting to hold office until the conclusion of the next forthcoming annual general meeting of the Company. Subject to shareholders' authorisation, the Board will authorise the Audit Committee to determine the remuneration of Ernst & Young. Pursuant to the "Policy on External Auditor Management" adopted by the Board, the Audit Committee reviewed and monitored and was satisfied with the independence and professionalism of Ernst & Young, based on the principles and standards set out in the said Policy that were in line with international best practices. PricewaterhouseCoopers, the existing auditor of the Company, will retire upon expiration of its current term of office at the Company's 2013 annual general meeting.

For 2012, the fee paid by the Group to PricewaterhouseCoopers was HK\$37 million, of which HK\$33 million was for audit services and HK\$4 million related to other services. For 2011, the fee charged by PricewaterhouseCoopers was HK\$38 million, of which HK\$32 million was for audit services and HK\$6 million related to other services.

Internal Control

The Board has the responsibility to ensure that the Group maintains sound and effective internal controls

to safeguard the Group's assets. According to the Board's scope of delegation, the Management is responsible for the day-to-day operations and risk management.

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

The Group conducts an annual review of the effectiveness of its internal control systems covering all material controls, including financial, operational and compliance controls as well as risk management. The review is conducted by reference to the guidelines and definitions given by the regulatory and professional bodies for the purpose of assessing five different internal control elements, namely, the control environment, risk assessment, control activities, information and communication, and monitoring. The assessment covers all the major internal controls and measures, including financial, operational and compliance controls as well as risk management functions. The review also considers the adequacy of resources, staff qualifications and experience and training of the Group's accounting and financial reporting functions. The review is coordinated by the Group's internal audit which, after the Management and various business departments have performed their self-assessment, then carries out an independent examination and other post-assessment work on the review process and results. The results of the 2012 review have been reported to the Audit Committee and the Board.



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

- a rational organisational structure with appropriate personnel is developed and whose responsibility, authority, and accountability are clearly delineated. The Group has formulated policies and procedures to ensure reasonable checks and balances for all the operating units, reasonable safeguard for the Group's assets, the implementation of internal controls and adherence to relevant laws and regulations and risk management in its operations;
- the Management draws up and continuously monitors the implementation of the Group's strategies, business plans and financial budgets. The accounting and management systems that are in place provide the basis for evaluating financial and operational performance;
- the Group has various risk management and human resources policies. There are specific units and personnel that are responsible for identifying, assessing and managing all the major risks. These include reputation, strategic, legal, compliance, credit, market, operational, liquidity and interest rate risks (The Group's risk management is given on page 39 to page 43 in this Annual Report);
- the Group has established an information technology governance structure that produces a range of reports on information systems and management, including information on the monitoring of various business units, financial information and operating performance. Such information facilitates the

Management, business units and the regulatory bodies in assessing and monitoring the Group's operation and performance. Proper communication channels and reporting mechanisms are in place at various business units and levels to facilitate exchange of information;

- pursuant to a risk-based approach and in accordance with the internal audit plan approved by the Audit Committee, the Group's internal audit conducts independent reviews on such aspects as financial activities, various business areas, various kinds of risks, operations and activities. Reports are submitted directly to the Audit Committee. The Group's internal audit closely follows up on the items that require attention in a systematic way and reports to the Management and the Audit Committee in a timely manner; and
- the Audit Committee reviews the reports submitted by external auditor to the Group's Management in connection with the annual audit as well as the recommendations made by regulatory bodies on internal control. The Group's internal audit follows up on the same to ensure timely implementation of the recommendations, and also periodically reports the status of the implementation to the Management and the Audit Committee.

The Group is committed to upholding good corporate governance practices and the internal control system of all subsidiaries are reviewed regularly. During the year of 2012, continuous improvements on the organisation structure and segregation of duty,

the risk management policy and procedure, and the enhancement of disclosure transparency have been undertaken by the Group. In response to internal and external changes in global economic condition, operating environment, regulatory requirement and business development, the Group has implemented a series of measures and undertaken an on-going review on the effectiveness of the internal control mechanism. In 2012, areas for improvement have been identified and appropriate measures have been implemented.

Communication with Shareholders

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

Mr. XIAO Gang, the former Chairman of the Board who resigned on 17 March 2013, Mr. TUNG Chee Chen, the Chairman of the Nomination and Remuneration Committee, Mr. KOH Beng Seng, the Chairman of the Risk Committee, Mr. ZHOU Zaiqun, the Chairman of the Strategy and Budget Committee, four members of the Audit Committee on behalf of the Chairman of the Audit Committee, and representatives of PricewaterhouseCoopers were present at the Company's 2012 annual general meeting held on 29 May 2012 at Four Seasons Grand Ballroom, Level 2, Four Seasons Hotel Hong Kong, 8 Finance Street, Central, Hong Kong to respond to enquiries raised by shareholders. Mr. SHAN Weijian and Mr. TUNG Savio Wai-Hok, the Chairman and a member of the Audit Committee respectively were unable to attend the meeting due to other business engagements. Save as disclosed above, all other Directors including Mr. LI Lihui, Mr. HE



CORPORATE GOVERNANCE

Guangbei, Mr. LI Zaohang, Mr. CHEN Siqing, Mr. GAO Yingxin and Dr. FUNG Victor Kwok King were also present at the meeting. Resolutions passed at the Company's 2012 annual general meeting included: adoption of the Company's 2011 financial statements, declaration of 2011 final dividend, re-election of Directors, re-appointment of auditor and the grant of general mandates to the Board to issue and repurchase shares of the Company.

As disclosed in the 2011 Annual Report of the Company, in view of the investors' concern regarding the potential dilution of the shareholders' value arising from the exercise of power pursuant to the grant of a general mandate to issue shares to the Board, the Board has voluntarily reduced the general mandate to issue shares of up to 5% of the issued share capital as compared to the 20% limit permitted under the Listing Rules in the event that the issue of shares is for cash and not related to any acquisition of assets for approval by the shareholders at the 2012 annual general meeting. The Board would also recommend the said 5% threshold at the forthcoming 2013 annual general meeting for approval by shareholders. Further, given its commitment to high standards of corporate governance, the Board also adopted certain **internal policies for the exercise of the powers granted to the Board under the general mandates to issue shares solely for cash and repurchase shares**. The relevant policies are summarised as follows:

- the Board will not exercise the mandate at a discount that will result in significant dilution of shareholders' value. In the exercise of such power to issue shares for cash, the Board will have regard to factors such as the Group's capital

adequacy ratio, and in particular, its Tier 1 capital, cost and benefit of raising Tier 2 capital, need for cash for the Group's business development, the principle that shareholders should be treated equally and the alternative of conducting a rights issue; and

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

All the resolutions proposed at the Company's 2013 annual general meeting will be voted on by poll.

Accordingly, the Company will engage Computershare Hong Kong Investor Services Limited, the Company's Share Registrar, to act as the scrutineer for such purpose. The results of the poll voting will be posted on the Company's website and the Stock Exchange's website as soon as practicable following conclusion of the vote-counting for shareholders' information.

Besides, in order that shareholders can have a better understanding of the agenda items to be discussed at the 2013 annual general meeting and to encourage their active participation so that exchange of views and communication can be further enhanced, **the Company has provided detailed information on the 2013 annual general meeting in a circular to shareholders** which includes introduction to the proposed resolutions to be approved at the annual general meeting, information on the retiring Directors who are eligible for re-election and information on voting and other issues relating to the 2013 annual general meeting in the form of "Frequently Asked Questions".

Shareholders' Rights

Shareholders are entitled to convene an extraordinary general meeting, make any proposals at shareholders' meetings and propose a person for election as a Director. Please see the detailed procedures as follows:

- **the way in which shareholders can convene an extraordinary general meeting:**
Any shareholder(s) holding not less than 5% of the issued capital of the Company may request the Board to convene an extraordinary general meeting. The requisition, duly signed by the shareholder(s) concerned, must clearly state the objects of the meeting and must be deposited at the registered office of the Company, 52nd Floor, Bank of China Tower, 1 Garden Road, Central, Hong Kong. The Company would take appropriate actions and make necessary arrangements in accordance with the requirements under Section 113 of the Companies Ordinance once a valid requisition is received.



- **the procedures for making proposals at shareholders' meetings:**

The following shareholders are entitled to put forward a proposal (which may properly be put to the meeting) for consideration at a general meeting of the Company:

- (a) any number of members representing not less than 2.5% of the total voting rights of the Company on the date of the requisition; or
- (b) not less than 50 members holding shares in the Company on which there has been paid up an average sum, per member, of not less than HK\$2,000.

The requisition specifying the proposal, duly signed by the shareholders concerned, together with a statement of not more than 1,000 words with respect to the matter referred to in the proposal must be deposited at the registered office of the Company, (52nd Floor, Bank of China Tower, 1 Garden Road, Central, Hong Kong), not less than six weeks before the general meeting. The Company would take appropriate actions and make necessary arrangements, and the shareholders concerned would be responsible for the expenses incurred in giving effect thereto in accordance with the requirements under Section 115A of the Companies Ordinance once valid documents are received.

- **the procedure for Director's nomination and election by shareholders:**

If a shareholder wishes to propose a person other than a retiring

Director for election as a Director at a general meeting, the shareholder should lodge at the registered office of the Company (52nd Floor, Bank of China Tower, 1 Garden Road, Central, Hong Kong), (a) a notice signed by such shareholder (other than the proposed person) duly qualified to attend and vote at the meeting of his/her intention to propose such person for election; and (b) a notice signed by the proposed person indicating his/her willingness to be elected.

The period during which the aforesaid notices may be given will be at least seven days. Such period will commence on the day after the despatch of the notice of the general meeting for which such notices are given and end no later than seven days prior to the date of such general meeting. The Company would take appropriate actions and make necessary arrangements, and the shareholder concerned would be responsible for the expenses incurred in giving effect thereto in accordance with the requirements under Article 99 of the Articles of Association of the Company once valid notices are received.

Further shareholder information is set out in the section headed "Investor Relations" of this Annual Report. Shareholders are welcome to send in any written enquiries to the Board for the attention of the Company Secretary either by post to the registered office of the Company at 52nd Floor, Bank of China Tower, 1 Garden Road, Central, Hong Kong or by way of email to investor_relations@bochk.com. The Company Secretary would direct the enquiries received to appropriate Board Member(s) or the Chairman of the Board Committee(s) who is in charge of the areas of concern

referred therein for further handling. The Board, assisted by the Company Secretary, would make its best efforts to ensure that all such enquiries are addressed in a timely manner.

Directors' Responsibility Statement in relation to Financial Statements

The following statement should be read in conjunction with the auditor's statement of their responsibilities as set out in the auditor's report contained in this Annual Report. The statement aims to distinguish the responsibilities of the Directors and the auditor in relation to the financial statements.

The Directors are required by the Hong Kong Companies Ordinance to prepare financial statements, which give a true and fair view of the state of affairs of the Company. The financial statements should be prepared on a going concern basis unless it considers inappropriate. The Directors are responsible for ensuring that the accounting records kept by the Company at any time reasonably and accurately reflect the financial position of the Company, and also ensure that the financial statements comply with the requirements of the Hong Kong Companies Ordinance. The Directors also have duties to take reasonable and practicable steps to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

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

INVESTOR RELATIONS

Investor Relations Policy and Guidelines

The Company recognises the fundamental importance of maintaining effective communication with its existing and potential investors. We strive to provide clear and timely information that is reasonably required to make a fair investment decision with regard to the Company's equity and debt securities. We also highly value investor feedback and comments which are important for the formulation of the Company's growth strategies to ensure its sustainable development and to enhance shareholder values.

Investor Relations Programmes

The objective of the Company's investor relations programmes aims to

promote, through various channels, timely and effective communication with the investment community to enhance their knowledge and understanding of the Company's development and strategies. The investment community refers to existing and potential investors of the Company's securities, analysts and securities market professionals. The Company's securities include both equity securities and debt securities.

The Company's investor relations strategies and programmes are formulated and overseen by the Investor Relations Committee, which is chaired by the Company's Chief Executive and consists of other senior management. The Investor Relations Division of the Board Secretariat, which reports directly to the Board, is responsible for the implementation

of these strategies and acts as an intermediary between the Company and the investment community. Both the Board and the Committee evaluate the effectiveness of the investor relations programmes on a regular basis.

The Company's senior management is highly supportive and actively involved in investor relations activities. We will actively meet with the investment community in meetings, conferences and road-shows. During these meetings, we will discuss general public information, including disclosed financial information and historical data, markets and products strategies, business strengths and weaknesses, growth opportunities and threats etc. Such contents will be discussed so long as it is not considered to be material non-public information.

Multi-communication channels

- Annual General Meeting
- Results briefings
- Investor/Analyst feedback

- Corporate website
- Investor emails or inquiries
- Email alert service

- Global road-shows
- Investor conferences
- Company visits
- Investor/Analyst workshops

Information Disclosure Policy

Relevant laws in respect of information disclosure of listing companies has become effective since 1 January 2013. The Company attaches high importance to the principles of information disclosure on timeliness, fairness and transparency, and in addition proactively discloses the information that may have impact on making investment decisions. In accordance with relevant legislations and statutory requirements, the Company formulates Information Disclosure Policy, which is available on the Company's website for public reference. Such policy contains clear guidelines to ensure:

1. disclosure information is in compliance with the Listing Rules and other regulatory requirements;
2. all communications with the public, including the investment community and the media, follow the principles of timeliness, fairness, truthfulness, accuracy and compliance;
3. effective monitoring of procedures for information disclosure.

Access to Corporate Information

The Investor Relations section of the Company's website (www.bochk.com/ir) provides shareholders and investors with access to the Company's latest development according to the principles of Information Disclosure Policy. These include information in relation to the Company's key developments, interim and annual results as well as quarterly financial and business review updates. Public can also access such important

announcements through the Stock Exchange of Hong Kong.

The Investor Relations section also includes information on credit ratings, share and dividend, as well as a corporate calendar which provides dates of important events.

Shareholders and investors are encouraged to view the Company's corporate materials online to support environmental conservation. The Investor Relations website also includes an e-mail alert service to provide corporate updates on the Company's financial performance and latest development. Shareholders and other interested parties may register if they are interested to receive such updates by email.



Overview of Investor Relations Activities in 2012

In 2012, the Company continued its efforts to provide effective channels for proactive communication with the investment community.

Annual General Meeting

At the Annual General Meeting held in May 2012, the former Chairman of the Board, who resigned on 17 March 2013, the Chairmen of the Nomination and Remuneration Committee, the Risk Committee and the Strategy and Budget Committee respectively, members of the Audit Committee, the Company's senior management as well as external auditor were present to respond to questions and comments from shareholders. A total of 973 registered shareholders, 260 authorised corporate representatives and 428 authorised proxies holding an aggregate of 10,353,615,678 shares, representing 97.93% of the total issued share capital of the Company were present at the 2012 AGM. Minutes of the AGM were available to shareholders on the Company's website.

Results Announcement

At the Company's 2011 annual results announcement and 2012 interim results announcement, the senior management led by the Chief Executive conducted briefings with analysts and the press to apprise them of the Company's operating and financial results, business strategies and outlook. The presentation materials, announcements and webcasts were available to the public on the Company's website.

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

Communication with the investment community

In 2012, the Company held over 170 meetings with investors and analysts across the world with total attendances of approximately 450. These meetings were conducted during global road-shows, investor conferences, company visits and conference calls in order to enable investors better understand the Company's strategies and new business initiatives. The Company is widely covered by more than 20 securities research institutions.

Through emails, direct dialogue with investors and investor feedback, the Company continued to promote two-way communication. The responses received from investors enabled the Company to better understand the market focus which helped formulate its investor relations plan and continually improved the investor relations practices.

Investor Relations Awards

During 2012, BOC Hong Kong (Holdings) was ranked top 4 in Best Investor Relations in "a Hong Kong Company" and in "Banks & Financial Services" by IR Magazine. Over 400 portfolio managers and analysts across Greater China and South East Asia

participated in the survey and were asked to nominate and rank up to 4 companies which they believed to be the best investor relations in such categories. This recognition from the investment community demonstrated the Company's efforts in investor relations practices.

Going Forward

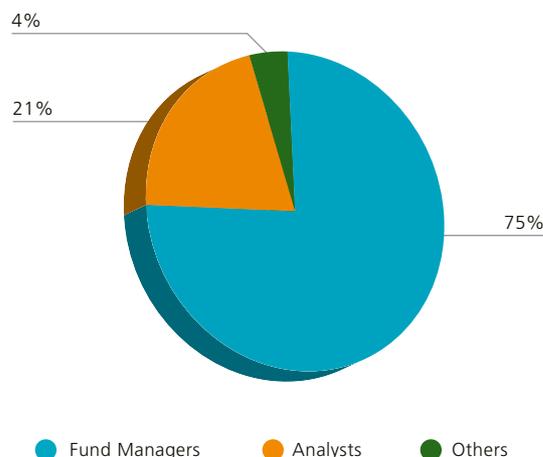
Under the principles of timeliness, fairness and transparency, the Company will continue to pursue proactive investor relations practices. Effective investor relations programmes will be formulated to keep the investment community adequately informed of the Company's present and future development. The Company will also benchmark its programmes against best practices for continuous improvement and more efficient communication with the investment community.

Investor Relations Contact

Enquiries can be directed to:

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

Investor Meetings by Category



INVESTOR RELATIONS

Shareholder Information

Financial Calendar 2013

Major Events	Dates
Announcement of 2012 annual results	26 March (Tuesday)
Latest time for lodging transfers for entitlement to attend and vote at the 2013 Annual General Meeting	22 May (Wednesday) 4:30 p.m.
Book closure period (both days inclusive)	23 May (Thursday) to 28 May (Tuesday)
Latest time for lodging proxy forms for the 2013 Annual General Meeting	26 May (Sunday) 2:00 p.m.
2013 Annual General Meeting	28 May (Tuesday) 2:00 p.m.
Last day in Hong Kong for dealing in the Company's shares with entitlement to final dividend	29 May (Wednesday)
Ex-dividend date	30 May (Thursday)
Latest time for lodging transfers for entitlement to final dividend	31 May (Friday) 4:30 p.m.
Book closure period (both days inclusive)	3 June (Monday) to 6 June (Thursday)
Record date for final dividend	6 June (Thursday)
Final dividend payment date	14 June (Friday)
Announcement of 2013 interim results	Mid to late August

Annual General Meeting

The 2013 Annual General Meeting will be held at 2:00 p.m. on Tuesday, 28 May 2013 at Four Seasons Grand Ballroom, Level 2, Four Seasons Hotel Hong Kong, 8 Finance Street, Central, Hong Kong.

Share Information

Listing and Stock Codes

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

Market Capitalisation and Index Recognition

As at 31 December 2012, the Company's market capitalisation was HK\$254.8 billion, among the top 20 leading stocks on the Main Board of Hong Kong Stock Exchange in terms of market capitalisation. Given the Company's market capitalisation and liquidity, its shares are a constituent of Hang Seng Index, MSCI Index and FTSE Index series. In addition, the Company is a constituent of Hang Seng Corporate Sustainability Index Series which recognises its performance in relation to corporate sustainability issues. During the year, the Company has been included as a constituent of the newly launched Hang Seng High Dividend Yield Index, demonstrating the provision of persistent stable return by the Company to investors.



Debt Securities

Issuer	: Bank of China (Hong Kong) Limited, a wholly-owned and principal subsidiary of the Company		
Listing	: The Notes are listed and traded on The Stock Exchange of Hong Kong Limited (HKEX)		
Subordinated Notes			
Description	: Bank of China (Hong Kong) Limited 5.55% Subordinated Notes 2020		
Issue size	: US\$2,500 million		
Stock codes	: HKEX	4316	
	: ISIN	USY1391CAJ00	
	: Bloomberg	E1388897	
Senior Notes			
Description	: Bank of China (Hong Kong) Limited 3.75% Senior Notes due 2016 issued under the Medium Term Note Programme of US\$15 billion		
Issue size	: US\$750 million		
Stock codes	: HKEX	4528	
	: ISIN	USY1391CDU28	
	: Bloomberg	E18623411	

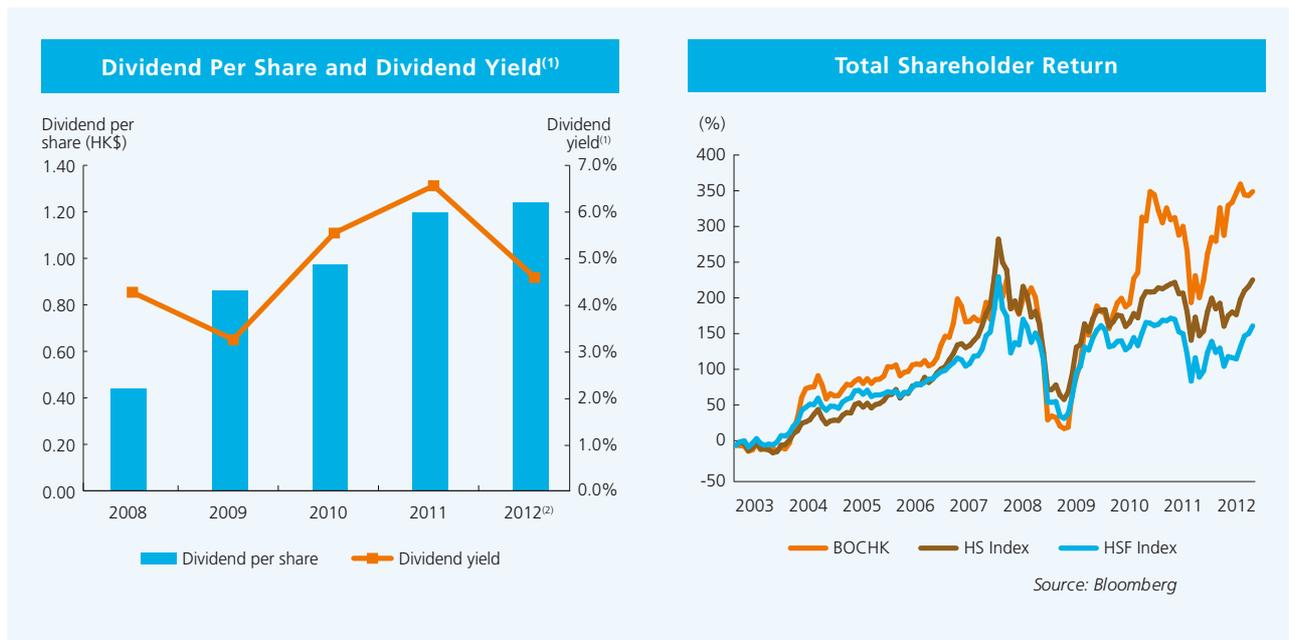
Share Price and Trading Information

Share price (HK\$)	2012	2011	2010
Closing price at year end	24.10	18.40	26.45
Highest trading price during the year	25.00	28.35	29.40
Lowest trading price during the year	18.18	14.24	15.92
Average daily trading volume (m shares)	11.77	18.97	17.20
Number of ordinary shares issued (shares)	10,572,780,266		
Public float	Approximately 34%		
Nominal value per share	HK\$5.00		

INVESTOR RELATIONS

Dividends

The Directors has recommended a final dividend of HK\$0.693 per share, which is subject to the approval of shareholders at the 2013 Annual General Meeting. With the interim dividend per share of HK\$0.545 paid during 2012, the total dividend per share will be amounted to HK\$1.238 for the whole year.



- (1) Annual dividend yield is calculated based on actual dividends paid to shareholder during that year (final dividend of previous year and interim dividend of the year) and closing share price of previous year-end.
- (2) 2012 final dividend will be subject to shareholders' approval at the Company's forthcoming Annual General Meeting.

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

Credit Ratings (long-term)

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

Shareholding Structure and Shareholder Base

As at 31 December 2012, the Company had 10,572,780,266 shares in issue of which approximately 34% was held by the public and 0.24% was held in the form of ADSs. The Company's 85,968 registered shareholders were distributed in various parts of the world, including Asia, Europe, North America and Australia. Apart from BOC, the Company is not aware of any major shareholders with a shareholding of more than 5% which has to be reported under the SFO of Hong Kong.



During the year, the shareholder structure of the Company remained stable. The following table shows the distribution of ownership according to the register of members which includes registered shareholders and shareholders recorded in the participant shareholding report generated from the Central Clearing and Settlement System as at 31 December 2012:

Category	Number of registered shareholders	% of shareholders	Number of shares held by registered shareholders	% of total issued share capital
Individuals	85,836	99.85	228,216,842	2.16
Institutions, corporates and nominees ^(Note)	131	0.15	3,403,485,668	32.19
Bank of China Group ^(Note)	1	0.00	6,941,077,756	65.65
Total	85,968	100.00	10,572,780,266	100.00

Note:

As recorded in the register maintained by the Company pursuant to section 336 of the SFO, the total number of shares held by Bank of China Group was 6,984,274,213 shares, representing 66.06% of the total issued share capital of the Company as at 31 December 2012. This figure included certain numbers of shares held for Bank of China Group in the securities account opened with BOCI Securities Limited, a participant of Central Clearing and Settlement System. Accordingly, these shares are included under the category of 'Institutions, corporates and nominees'.

Shareholder Enquiries

For any enquiries or requests relating to shareholder's shareholding, e.g. change of personal details, transfer of shares, loss of share certificates and dividend warrants, etc., please send in writing to:

Hong Kong	Computershare Hong Kong Investor Services Limited 17M Floor, Hopewell Centre 183 Queen's Road East, Wan Chai, Hong Kong Telephone: (852) 2862 8555 Facsimile: (852) 2865 0990 E-mail: hkinfo@computershare.com.hk
USA	Citibank Shareholder Services 250 Royall Street Canton, MA 02021, USA Telephone: 1-877-248-4237 (toll free) 1-781-575-4555 (outside USA) E-mail: Citibank@shareholders-online.com

Other Information

This Annual Report is available in both English and Chinese. A copy prepared in the language different from that in which you have received is available by writing to the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong or email to bochk.ecom@computershare.com.hk. This Annual Report is also available (in both English and Chinese) on the Company's website at www.bochk.com and the Stock Exchange's website at www.hkexnews.hk. You are encouraged to access the corporate communications of the Company through these websites in lieu of receiving printed copies to help protect the environment. We believe that it is also the most efficient and convenient method of communication with our shareholders.

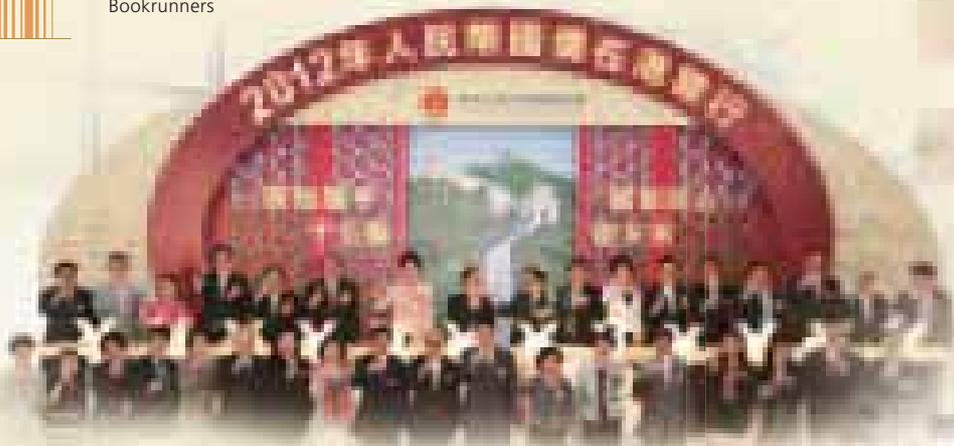
If you have any queries about how to obtain copies of this Annual Report or how to access the corporate communications on the Company's website, please call the Company's hotline at (852) 2846 2700.



COMPREHENSIVE
CROSS-BORDER
FINANCIAL SERVICE



In the fourth issue of RMB sovereign bonds in Hong Kong, BOCHK was appointed as one of the Joint Coordinators, Lead Managers and Bookrunners



CORPORATE SOCIAL RESPONSIBILITY

We actively participated in different RMB seminars and conferences locally and globally to promote Hong Kong as an offshore RMB business centre

At the Group, sustainability is at the core of how we manage our business and plan for our development. We incorporate Corporate Social Responsibility (“CSR”) in our business operation and strategy to achieve our vision of becoming the premier choice for customers, employees, shareholders and investors.

The Group has made significant progress in CSR measurement and reporting. Our first standalone CSR Report which followed the Global Reporting Initiative G3.1 Guidelines was published in 2012. Covering a wide range of areas in CSR and sustainability through more systematic data collection, the report enhances the disclosure and transparency of our accomplishments in CSR.

The Group’s outstanding performance with regard to sustainability has earned us broad recognition. For three years in a row, BOC Hong Kong (Holdings) Limited has

been included as a constituent of the *Hang Seng Corporate Sustainability Index Series*. The Company’s ranking has moved up from 18th in 2011 to 12th in 2012, with the rating upgraded from “A” (satisfactory) to “AA-” (stable). In addition, BOCHK has been named as a *Caring Company* by the Hong Kong Council of Social Service (“HKCSS”) since 2002. We recognise the importance of high standards of corporate governance and thus maintain an effective corporate governance framework. In compliance with the relevant requirements of international and local corporate governance best practices, BOC Hong Kong (Holdings) Limited was presented the *Award for Corporate Governance Excellence* under the Category for Hang Seng Index Companies by the Chamber of Hong Kong Listed Companies for two successive years. All these recognitions demonstrated, once again, our prominent advancement in environmental, social and corporate governance initiatives.

At the Grand Inauguration of our premier Private Banking Service, we launched our unique “1+1+1” service model to help high-net-worth customers meet their personal, family and business needs



Customer-centric through Innovation and Service

In the ever-changing market environment, we strive to embrace customer service values by enhancing our products and service platform. We are also committed to promoting the development of Hong Kong as a major financial hub and offshore RMB centre.

Ongoing innovation to meet diverse customer needs

The Group fully supports the development of offshore RMB business in Hong Kong. We strive to provide comprehensive and convenient services to our customers. Following the regulatory extension of RMB services to non-Hong Kong residents in August 2012, we promptly offered diversified RMB services in all branches.

To better serve the increasing needs from RMB trade settlement, we continued to enrich our products. We launched the multi-currency shipping finance product in RMB which was designed to help minimise risks associated with the movement of RMB exchange rates for both shipowners and shipyards. This product was a breakthrough in the traditionally USD-dominated shipping market and earned us the *Innovation Award – Business Innovation* from the Lloyd's List. Through the close collaboration with our parent, BOC, we enhanced our capabilities in serving cross-border enterprises by launching a number of cross-border trade finance products. These included the acceptance L/C discounting, RMB offshore import/export finance, RMB outward documentary bills supplemented by deliverable forward solutions, as well as CNH swaps for Hong Kong subsidiaries of the Mainland enterprises to hedge FX risks.

For our RMB settlement services, we have extended our service hours to 9:30 pm (Hong Kong time) from Monday to Friday since June 2012 for the setting up of RMB telegraphic transfer and express transfer (CHATS) instructions through Internet and Mobile Banking. This service enables customers in different time zones to enjoy same-day settlement of their remittances.

In view of the growing demand for RMB insurance products, our insurance arm, BOC Life has broadened its product range by launching the IncomeGrowth Annuity Insurance Plan offering immediate annuity income to customers. RMB riders, the first of its kind in Hong Kong, were also introduced to provide customers with greater flexibility and wider protection. Our ongoing efforts in offering quality and innovative RMB services won us four honours in the *Hong Kong Offshore RMB Centre – 1st RMB Business Outstanding Awards* organised by Metro Finance in 2012.

During the year, we enhanced our investment product suite by helping investors to grasp RMB market opportunities. BOCHK participated in the underwriting of 14 offshore RMB bonds, including the fourth issuance of RMB sovereign bonds. The ground-breaking issuance of China Development Bank's 20-year offshore RMB bonds extended the yield curve of offshore RMB bonds in Hong Kong. We are also a leading distributor by offering customers a wide choice of 13 RMB Qualified Foreign Institutional Investor funds

in Hong Kong. Our asset management arm, joined hands with the World Bank to launch the "BOCHK – World Bank Emerging Markets Bond Fund", the first global emerging market currency bond fund in Hong Kong with a China theme. During the year, our Asset Management was also granted five prestigious *2012 Best of the Best Awards* by Asia Asset Management.

For our mortgage business, we pioneered the 1-Day Approval Mortgage Service. This enables eligible home buyers to obtain formal approval results of their mortgage loan applications more expediently.

BOCHK's Global Custody business has established an extensive sub-custodian network to cover multiple markets around the world. Our outstanding cross-border custody service received the award as the *Best Asian Bank for Cross-Border Custody* from the AsianInvestor.

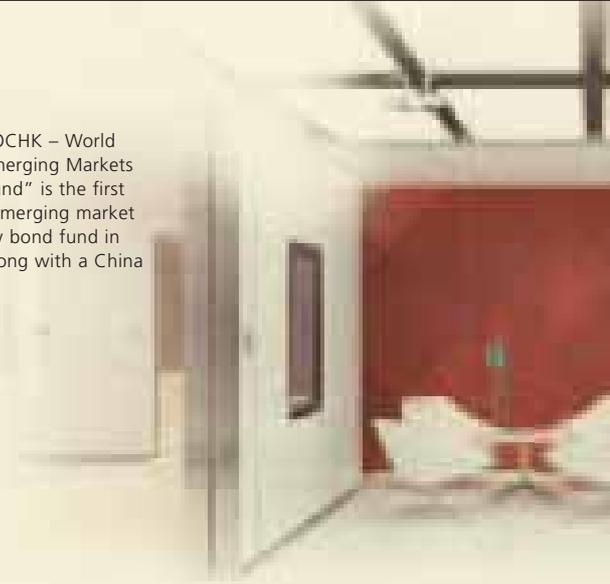


We introduced the first-ever RMB cash deposit machine in Hong Kong





The "BOCHK – World Bank Emerging Markets Bond Fund" is the first global emerging market currency bond fund in Hong Kong with a China theme



Supporting Local Enterprises

Local enterprises are an important pillar of growth of the Hong Kong economy. To meet the financing and liquidity needs of commercial customers, BOCHK offered a privileged guarantee fee subsidy in 2012 to support the Special Concessionary Measures of the SME Financing Guarantee Scheme of the Hong Kong Mortgage Corporation. We also supported the new Microfinance Scheme to provide assistance to those who wish to start their own businesses, become self-employed, upgrade their skills or obtain professional qualifications.

To recognise the outstanding achievements of local industrialists and manufacturers, we continued to sponsor the *Young Industrialist Awards of Hong Kong* and the *Hong Kong Awards for Industries*.

Enhancing Service Platforms

The Group is committed to meeting the banking needs of local customers from all walks of life. We provide the most extensive branch network among Hong Kong banks with 269 branches and over 1,000 automated banking machines in Hong Kong, including the first RMB cash deposit machines.

With an aim to provide more convenient banking services, we further upgraded our electronic channels. We are the first banking group in Hong Kong to launch the Mobile Banking functions for IPO shares subscription and IPO financing application. A dedicated hotline and free connection from BOC's hotline to ours have been set up for customers in the Mainland to obtain investment information with ease. The pioneering chip-based BOC Card was launched with enhanced ATM security. At the same time, the CUP QuickPass and Unionpay Online Payment introduced by BOC-CC provide new and flexible electronic payment solutions and online platform for merchants. By connecting customers' accounts maintained separately in Hong Kong and the Mainland, the new "NCB Wealth Express Card Service" launched by NCB jointly with NCB (China) offers greater flexibility in cross-border financial management and features the hassle-free auto-sweeping function.

Caring Banking Services

Special procedures for the handling of design and planning of the branches and ATMs are continuously reviewed for customers with specific needs. All newly renovated branches have already incorporated barrier-free facilities, such as sloping platforms, to facilitate disabled customers to enter the branches. For ATM services, the Group launched the first-ever Voice Navigation ATM in Hong Kong to assist the visually impaired in using ATMs. All of our ATMs feature protruding symbols which further improve those customers' access to ATM services. In addition, all newly installed or replaced ATMs are designed with the height of both keypads and screens suitable for wheelchair access, and around 93% of ATMs have soft keypads. We have also designed our Internet Banking with functions for visually impaired customers, including the support of screen readers and provision for font resizing.

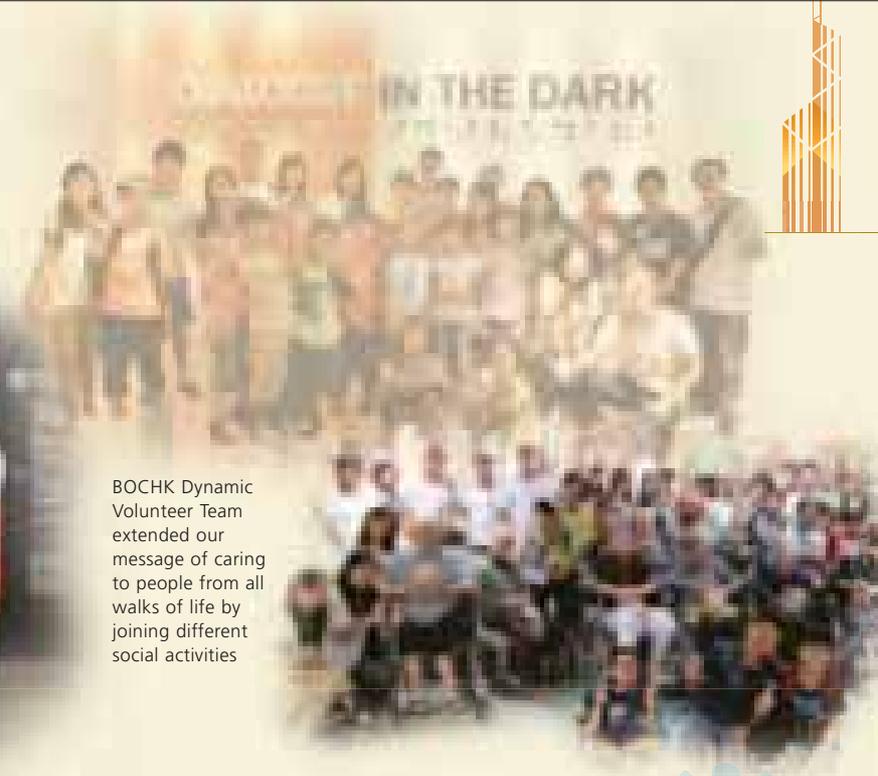
The Group also offers monthly fee waivers on deposit accounts to senior citizens aged 65 or above, account holders aged below 18, and recipients of Government Disability Allowances/Comprehensive Social Security Assistance. Other special banking privileges are offered to senior citizens aged 65 or above. BOCHK strives to provide elderly customers with a flexible financial solution and becomes a leading bank offering the "Reverse Mortgage Programme" from 2011. In 2011/2012, we assisted eligible Hong Kong citizens in registering for "Scheme HK\$6,000" of the Hong Kong Special Administrative Region ("HKSAR") Government via our branches or Internet Banking and enabling payments to be received through bank transfer.

Contributing to the Community We Serve

With our roots in Hong Kong, BOCHK attaches great importance to our community and considers the fulfilment of social responsibility as crucial for creating and maintaining our long-term core competences. Over the years, through the BOCHK Charitable Foundation ("the Foundation"), we actively participate in a diverse range of charitable activities, covering education and culture, sports and arts, environmental protection, and social welfare and assistance to the needy in Hong Kong and the Mainland of China.



The opening of our innovative Causeway Bay Branch brings new banking experience to our customers



BOCHK Dynamic Volunteer Team extended our message of caring to people from all walks of life by joining different social activities

Building a Harmonious Community

The Group encourages employee participation in various community and charity activities. As at 2012, over 1,300 staff members registered as members of our Dynamic Volunteer Team. All our staff receives one-day annual leave for volunteer activities. During the year, we joined 55 service activities, including the “Green Concert – Power Generating Challenge”, the “Hong Kong Geopark Charity Green Walk” and other volunteer events organised jointly with a number of charity organisations. By supporting various fund-raising activities in 2012, BOCHK helped raise a total donation of over HK\$13.2 million for social welfare agencies.



In 2009, we set up the “BOCHK’s Caring Hong Kong – A Heart Warming Campaign” with the net proceeds from the sale of the Olympic Commemorative Banknote. The objectives of the campaign are to assist disadvantaged groups and to build a harmonious community. As at the end of 2012, an aggregate of HK\$87 million was approved under the campaign to support 78 large-scale projects of the member social welfare agencies of the Community Chest of Hong Kong and HKCSS. Over 900,000 service attendees have benefitted from these donations.

Recognising the importance of corporate citizenship, BOCHK has been the lead sponsor of the “Hong Kong Corporate Citizenship Programme” organised by the Hong Kong Productivity Council (“HKPC”) for three consecutive years. The aim of the programme is to encourage enterprises to adopt social responsibility principles in their business strategies and management philosophies. The programme also develops a number of initiatives to enhance young people’s awareness of social responsibility.



Our staff joined the “Long March for Education Walkathon” of Sowers Action to help improve rural education

Spreading the Message of Caring

Caring has no boundaries. The Group has extended its support to Yunnan in the Mainland of China through participating in the "Long March for Education Walkathon" of Sowers Action. In 2012, we formed a team of 30 existing and retired staff members to take part in the 10-day Walkathon to Shangri-la in Yunnan. Over HK\$800,000 was raised to help improve rural education. We also donated some basic necessities to children in the mountain areas. We have supported the Walkathon for the fourth consecutive year since 2009. With a commitment to undertake CSR in the Mainland communities it serves, NCB (China) continued to support a local school called Yangping School with donations.

Through our credit card company, BOC-CC, we continuously support various social welfare organisations to collect donations. Charities can enjoy waivers of the transaction processing fees for the donations made with BOC credit cards by cardholders.

We fully supported the "Bank of China Hong Kong Sports Stars Awards" to recognise the excellent performance of athletes and promote their sportsmanship



Nurturing Future Talent

We spare no effort in nurturing our younger generation to build a better society. The Foundation has awarded HK\$15.4 million scholarships and bursaries to nine universities in Hong Kong since 1990, benefitting a total of 1,661 students. The Group also organised the "Summer Internship Programme" offering university and tertiary institution students valuable internship opportunities.

To reinforce our commitment to support tertiary education, BOCHK established the Financial Services Learning Centre in cooperation with the Hong Kong Institute of Vocational Education ("IVE") to provide a simulated branch environment for formal financial training. Under the programme, students can acquire practical banking knowledge and customer service skills effectively through role playing. To give students opportunities to apply what they have learnt, BOCHK provided over 200 vacancies of the position of Customer Service Officer to IVE graduates by the end of 2012.

To promote the importance of CSR among enterprises and the youth, we sponsored the "Hong Kong Corporate Citizenship Programme"



The Group also continued to support youth development. Our insurance arm, BOC Life, has sponsored the "Meet Challenge in Wudang" for two consecutive years, a martial art training programme organised by the Hong Kong Federation of Youth Groups. The programme aims to help the participants to build up their physical and mental strength during their stay at the Wudang Monastery in Hubei Province, China. In 2012, a total of 40 youths from local tertiary institutions participated.

Fostering a Culture of Sport for All

Participation in sports not only promotes good health, but also the development of a positive attitude towards life. We advocate the "Sport for All" message in the community through sponsorship of the "Bank of China Hong Kong Sports Stars Awards" and "Festival of Sport" for seven years in a row. In the online public voting of the "Hong Kong Sports Stars Awards 2012" held in 2013, we recorded a total of over 145,000 votes, representing an increase of 1.3 times from 63,000 votes in 2011.

Badminton is a key sports initiative of the Foundation. A total of more than HK\$13 million was allocated for the development of the badminton over the past 14 years, with more than 1 million participants. Over HK\$4 million has been donated to the "Badminton Development and Training Scheme 2011-2014" for organising a diverse range of competitions, family fun days, training courses, reward programmes and demonstration sessions, recording over 125,000 participants in 2012.

For 10 consecutive years, the Foundation has sponsored the "Hong Kong Island & Kowloon Regional Inter-school Sports Competition", the largest school sports competition of its kind in Hong Kong. The competition's top honours, *BOCHK Bauhinia Bowls Award* and *BOCHK Rising Star Award*, have

"BOCHK Banknote Exhibition" displayed to the general public over 200 pieces of our precious collection of banknotes





been set up to foster the talents of young athletes. In 2012, we recorded over 80,000 athlete enrolments from 269 schools, which participated in more than 8,000 matches of this competition.

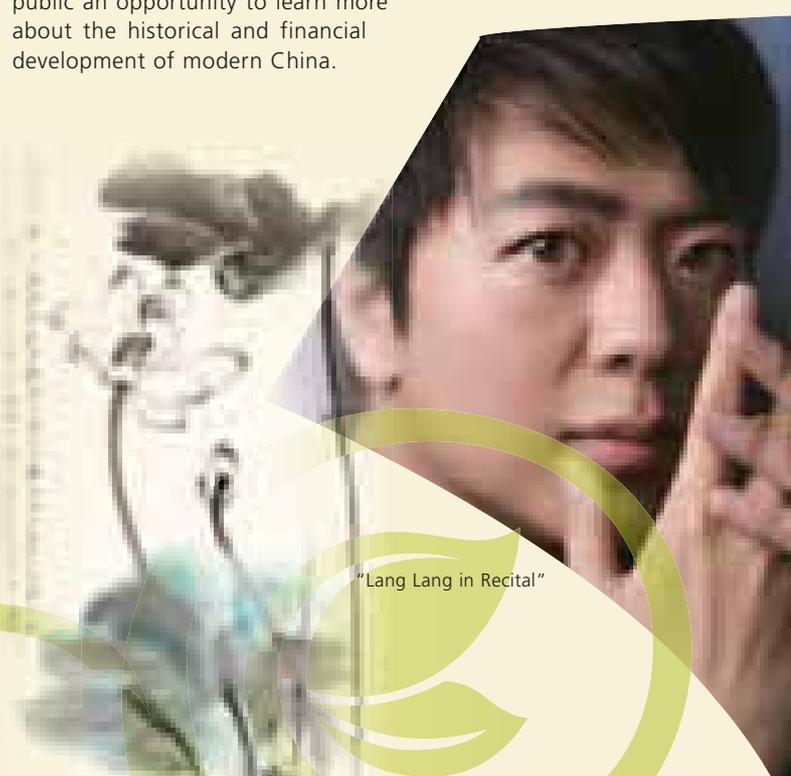
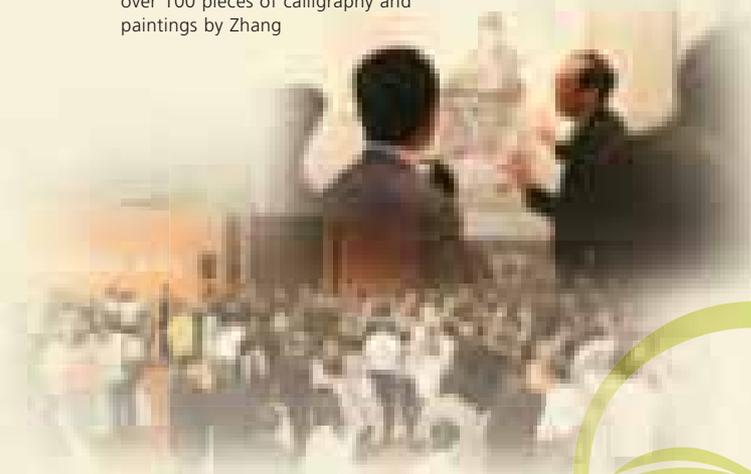
Promoting Culture

Music and art provide us not only with cultural appreciation but also inspiration for personal development. In celebration of the Centenary of BOC and the 15th anniversary of the establishment of HKSAR, we solely sponsored the "International Military Tattoo" presented by the Home Affairs Bureau and organised by the Leisure and Cultural Services Department. The military tattoo featured stunning marching and military music performances by over 1,000 representatives from 12 world famous military bands. We offered 1,870 free tickets to the underprivileged groups so as to share this spectacular show with them. The entire event, including two free open-air performances and a series of "meet-the-band" sessions, attracted an audience of more than 43,800.

BOCHK endeavours to promote cultural development by supporting a variety of programmes and exhibitions. We exclusively sponsored "A Testament of Friendship – Zhang Daqian Paintings and Calligraphy from the Collection of You Yi Tang" organised by Sotheby's Hong Kong in 2012. The exhibition showcased a magnificent ensemble of over 100 pieces of calligraphy and paintings collection by Zhang.

To mark the 100th anniversary of BOC in 2012, we issued the "Commemorative Banknote in Celebration of the Centenary of BOC" which was well received by the general public. We also held the "BOCHK's Banknote Exhibition" at the Bank of China Tower ("BOC Tower"), sharing a precious collection of about 200 pieces of banknote over the century from the late Qing Dynasty. This exhibition provided the public an opportunity to learn more about the historical and financial development of modern China.

We sponsored "A Testament of Friendship – Zhang Daqian Paintings and Calligraphy" to showcase a magnificent ensemble of over 100 pieces of calligraphy and paintings by Zhang



"Lang Lang in Recital"

During the year, the Foundation sponsored the "Majestic Drums XVI" organised by the Hong Kong Chinese Orchestra. It was an exciting "East meets West" percussion performance presented by Li Biao, the phenomenal percussionist, and the Philharmonic Percussion Group in Berlin. At the end of 2012, BOCHK specially presented "Lang Lang in Recital", with the world-class young talent performed an array of enchanting piano classics.

The "International Military Tattoo" featuring stunning military marching was well received by the public



Conservation of Resources for Environmental Protection

The Group is committed to conserving the environment. Through implementation of our Environmental Policy, we endeavour to minimise our environmental impact by reducing our carbon footprint, using resources more efficiently and effectively as well as promoting environmentally responsible business practices.

Building a Green Bank

We continued to implement energy efficiency and water saving measures in the Group's four main buildings including BOC Tower, Bank of China Building ("BOC Building"), Bank of China Centre ("BOC Centre") and the IT Centre in Fo Tan, Shatin. In addition, the Group supports resources recycling with an in-house recycling system for waste paper, aluminium cans and plastic bottles. We continue to carry out recycling projects with regard to batteries, compact fluorescent lamps, fluorescent tubes, toner cartridges and used computers on our premises. A food waste recycling scheme has been implemented in our staff canteen at the BOC Tower to promote food recycling. Our environmental practices have earned us recognition and environmental accreditations from a number of professional organisations for many years. In 2012, the BOC Tower has been included in the category of energy efficient buildings following the completion of an energy audit in accordance with the Buildings Energy Efficiency Ordinance.

To help reduce paper use, the Group continues to promote the use of e-Statement to customers. We encourage customers, shareholders and investors to view information at the Group's website. We also provide customers with sophisticated Internet Banking and Mobile Banking services. As at the end of 2012, the number of customers using our Internet and Mobile Banking increased significantly. In addition, those choosing to receive consolidated statements and investment statements in electronic form rose 53% and 26% respectively. The paper used for statements was substantially reduced by 47%.

In our new Causeway Bay Branch, we incorporated environmental elements in the design including the use of eco-friendly lighting and promotion of paperless transactions. We will adopt this design concept when renovating branches to enhance customer experience while minimising our environmental impact.

BOCHK has continuously consolidated and upgraded computer equipment to achieve further reduction in energy consumption. In recognition of our efforts, we received the Hong Kong ICT Awards: *Best Green ICT Grand Award* and *Best Green ICT (Adoption – Large-scale Enterprises) Gold Award* in 2012 from the Green ICT Consortium.

To demonstrate our efforts to promote low-carbon living, we participated in the "Eco Expo Asia" for the second consecutive year to exchange information with environmental experts and companies on air quality control and energy management.

The Group has put into practice its Sustainable Procurement Policy and Supply Chain Code of Conduct since 2011. During the year, a Self-Assessment Questionnaire was sent to 73 companies supplying goods and services to the Group.

To promote low-carbon living, we supported the "Eco Expo Asia" with active participation by the public



The assessed suppliers were in compliance with the Code of Conduct and ensured that the content and packaging of their products could be recycled and environmental certification was obtained. Corporate and marketing literature, as well as Lunar New Year cards and posters are printed on paper with environmental certification by the Forest Stewardship Council. Company motor vehicles are economy models.

Since 2009, we have participated in the global environmental initiative "Earth Hour" organised by WWF to raise public awareness of the global climate change. Shark's fin, endangered reef species and black mosses have not been served at corporate banquets since 2009. To pledge our support for the conservation of sharks, the Group has signed the "No Shark's Fin Pledge" initiated by WWF Hong Kong since 2011, discontinuing the supply or serving of shark's fin and promotions related to shark's fin.

Promoting Green Credit Services

Recognising the importance of environmental protection to conducting ethical business, we have incorporated environmental, social and governance factors into our lending and credit policies, to ensure more sustainable business growth for both the Group and the community.

In 2012, we continued to offer the "Green Equipment Financing Scheme" through our collaboration with the HKPC to encourage corporate customers to purchase environment-friendly equipment. We also provided the "Energy Efficiency Loan Scheme" launched jointly with the two electricity companies in Hong Kong to extend loans to commercial and industrial customers for the implementation of energy saving initiatives.

In Support of Bio-environmentalism

Environmental education is another key focus of our CSR work. In 2011-2012, the Foundation sponsored the "1,000 Environment-Friendly Youth Ambassadors Action" organised by the eight national authorities of the PRC. Under the programme, an Energy and Water Conservation Contest was held for the primary and secondary students in Hong Kong and the Mainland.



Around 1,200 contestants have been selected in the Contest and appointed as Youth Ambassadors to play an active role in arousing public awareness about energy saving and carbon reduction in their communities.

BOCHK spearheaded the "Hong Kong Geopark Charity Green Walk", which brought together the important elements of environmental protection and charity. Over 100 eco-tours were organised for 9,500 customers, citizens, staff members and their companions to better understand Hong Kong's geo-conservation. In addition, the "Itinerary Planner Contest" was launched in 2012 and more than 300 new immigrants and members from the underprivileged groups were invited to take part in the eco-tours free of charge to explore the geological wonders.

Since 2011, we have also jointly organised the "Global Geopark E-Classroom" with the Agriculture, Fisheries and Conservation Department and the Association for Geo-conservation, Hong Kong ("AGHK"). The first-ever E-Classroom provides local and overseas students with an online platform to learn more about geo-conservation from world class experts. About 10 online sessions were held as at September 2012.

To further promote the significance of environmental protection, we cooperated with the AGHK in launching other eco-friendly initiatives, including the "Floating Geopark Kiosk" and the first-ever "Hong Kong Global Geopark of China – Prehistoric Story Room" which features life on earth at the BOC Tower. Designed to showcase the geological spectacles of the Hong Kong Geopark to the world in an interactive way, these initiatives have

We pioneered the "Master of Ceremony Talent Training and Competition" which received overwhelming response from staff



To encourage innovation among staff, we organise a variety of team work building activities



The Group recruits talents from universities every year and provides multi-facet training programmes for their career advancement

received overwhelming responses. Since the opening of the Prehistoric Story Room in October 2011, it has welcomed more than 94,000 visitors and over 680 visiting organisations as at the end of 2012.

People-oriented with Team Spirit

People are important asset for the Group and CSR helps increase the sense of belonging among our staff and has a positive impact on staff morale. We have laid a solid foundation for future business development with a well-established and comprehensive talent management and training system.

Staff Training and Development

The Group has a staff team of over 14,000, including talented professionals from different backgrounds with diverse experience and expertise. We recruit highly qualified management and business professionals, as well as graduates of tertiary institutions and universities.

We have in place a systematic talent development mechanism underpinned by a "four-in-one" approach involving senior executives, departmental heads, human resources personnel and individual staff. By formulating talent management strategy, planning for career advancements, rotating jobs, and encouraging staff to pursue further education, our talent management is closely aligned with the Group's long-term strategy. The Group offers diverse and multi-facet training programmes such as in-house training, cross-posting, secondment and mentorship schemes to prepare our staff for career advancement. We continue to nurture our future talent through our Management Trainee, Officer Trainee and Summer Internship Programmes.



To enhance the leadership and strategic thinking capabilities of our management staff, we offer various programmes of renowned universities such as Richard Ivey School of Business and Cambridge University. Capitalising on the flexibility of the e-learning platform, we cultivate a continuous learning atmosphere by allowing staff to fulfil their learning objectives online. In 2012, we were granted the honourable award of *ERB Manpower Developer 1st* by the Employees Retraining Board for two successive years.

In addition, staff is encouraged to improve themselves by attaining professional qualifications. BOCHK received the *Qualifications Framework Partnerships Commendation* issued by the Education Bureau in 2012, for designing a training curriculum with reference to Specifications of Competency Standards and promoting the qualifications framework in our manpower development.

We continue to strengthen our culture of compliance. By organising workshops and making compliance training courses mandatory for every staff, we strive to uphold the Group's compliance management approach and to comply with relevant regulatory requirements.

We identify and reward outstanding staff and distinguished teams in our annual award presentation

Employee Benefits

The Group is committed to providing its staff with competitive remuneration packages. In addition, we believe the provision of a congenial workplace is as crucial to achieving good performance. The Group has been providing free and regular body check-ups, competitive medical schemes and counselling services to our staff. Moreover, to adopt family-friendly employment practices, we offer our staff early leave from duty on their birthdays and on the days of special festivals. We also offer paid paternity leave to our staff.

Employee Engagement

The Group conducts "online staff engagement survey" to collect staff opinions for continuous enhancement of our working environment, management policies and measures. Appreciation and recognition are important to motivate staff. We, therefore, identify and reward outstanding staff and distinguished teams in our annual award presentation.

Work-life Balance

We proactively encourage staff to maintain a good work-life balance. Different recreational activities are organised for our staff and their family members. Our staff fun day at the Hong Kong Ocean Park in September 2012 recorded a phenomenal turnout, with over 20,000 staff members and their families participated.



"Staff Fun Day at Hong Kong Ocean Park"



A diverse range of staff recreational activities are organised to advocate work-life balance and strengthen the bonding among all levels of staff

Serving Our Shareholders with a Solid Foundation

The Group is committed to safeguarding shareholders' interests by enhancing corporate governance and ensuring a higher degree of transparency. For details, please refer to "Corporate Governance", "Investor Relations" and "Management's Discussion and Analysis" in the Annual Report.

We believe CSR creates long-term value for the Group, which will remain its priority going forward. We will continue to uphold our CSR and strengthen the communication with our stakeholders, to contribute our part in the sustainable development of our economy, environment and society.



AWARDS AND RECOGNITION

Financial Strength and Corporate Governance

- The world's second strongest bank and the top among banks in Hong Kong (**Bloomberg Markets**)
- Award for Corporate Governance Excellence (Hang Seng Index Companies) for two consecutive years (**The Chamber of Hong Kong Listed Companies**)
- Corporate Governance Asia Recognition Awards (**Corporate Governance Asia Magazine**)



RMB Business

- In the capacity of the Sole Global Coordinator of China Development Bank's issuance of its 20-year offshore RMB bonds:
 - Triple A Regional Awards: Best Local Currency Bond and Best Dim Sum Bond (**Asset**)
 - Triple A Country Awards: Best Deal (China) (**Asset**)
- Innovation Award – Business Innovation in the Lloyd's List Global Awards (**Lloyd's List**)
- Excellent Brands of RMB Banking Service and Mortgage Service of the Hong Kong Leaders' Choice Brand Awards (**Metro Finance**)
- Hong Kong Offshore RMB Centre – 1st RMB Business Outstanding Awards presented by **Metro Finance**, **Metro Finance Digital** and **Wen Wei Po**:
 - Outstanding Retail Banking Business – Traditional Retailing
 - Outstanding Retail Banking Business – Diversified Businesses

Outstanding Corporate/Commercial Banking Business – International Trade

Outstanding Insurance Business

- Best of the Best Awards presented to BOCHK Asset Management by **Asia Asset Management**:
 - Best RMB Bonds, Offshore (One Year)
 - Most Innovative Product
 - Best Newcomer
 - Best RMB Offshore Manager in Asia
 - CEO of the Year (Hong Kong)
- Campaign in the issuance of RMB Sovereign Bonds in Hong Kong: Silver Prize for Financial Public Relations (**10th China International Public Relations Association Awards**)
- RMB Business Advertisements: Bronze Award for Campaigns – Multi-Media (**International Astrid Awards**)





Service Excellence

- Best Asian Bank for Cross-Border Custody in the AsianInvestor Service Provider Awards (**AsianInvestor**)
- Best SME's Partner Award for five consecutive years (**The Hong Kong General Chamber of Small and Medium Business**)
- Quality Recognition Award (US Dollar Clearing) for 14 consecutive years (**JPMorgan Chase**)
- Quality Management System of ISO 9001: 2008 Certification presented to the Loans Division of the Bank-wide Operation Department (**SGS Hong Kong**)
- China's Most Reliable Bank presented to NCB (China) by **CFO World**:
Best Offshore Business Award
Best Cross-border Trade Settlement Award
Best Corporate E-Banking Award
- My Favourite "The Most Convenient" MTR Shops – Excellence Award (**Mass Transit Railway Corporation**)

- 44th Distinguished Salesperson Awards (**Hong Kong Management Association** and **Sales and Marketing Executives International**)
- Financial Management Planners – Certificates of Merit in the 7th HKIB Outstanding Financial Management Planner Awards (**The Hong Kong Institute of Bankers**)
- Awards presented by the **Hong Kong Call Centre Association**:
APCCAL Recognition Award – Best Contact Centre in Sustainability
Mystery Caller Assessment Award – Gold
Outbound Contact Centre Team Leader of the Year – Gold
Contact Centre Technical Support Professional of the Year – Gold
- Silver Award in the Customer Service Excellence Award – Individual Award (Internal Support Service) (**Hong Kong Association for Customer Service Excellence**)
- Sing Tao Excellent Services Brand Award – Mortgage Service (**Sing Tao Daily**)
- BOC Express Cash: Elite Brand Awards – Bank Credit Service (**The Sun**)



AWARDS AND RECOGNITION

2013年銀行卡同業年會



- Awards presented to BOC-CC by various organisations:
Customer Complaint Management of ISO 10002 Certification
(Hong Kong Quality Assurance Agency)

China UnionPay:

Largest Card Number (Credit Card) – Gold Award – Hong Kong
Highest Card Volume (Credit Card) – Gold Award – Hong Kong
Highest Acquiring Volume – Gold Award – Hong Kong
Highest Acquiring Volume Growth – Gold Award – Hong Kong
Bank of the Year Award – Hong Kong and Macau

Visa International:

Global Service Quality Performance Award – Commercial Issuer
Largest Card Growth – Hong Kong
Platinum Card Best Performance – Macau
Highest Payment Volume and Largest Payment Volume Growth –
Macau
Commercial Card Largest Payment Volume Growth – Macau
Highest Merchant Sales Volume – Macau
Cross-border Largest Outbound Volume Growth – Macau

MasterCard Worldwide:

Best New Youth Segment MasterCard Card Programme in
Hong Kong: BOC i-card
Highest Market Share: Number of Open Cards and Merchant
Purchase Volume in Macau – Champion
Highest Market Share: Cardholder Spending and e-Commerce
Cardholder Spending Volume in Macau – Champion



Social Responsibility

- BOC Hong Kong (Holdings) Limited 2010/2011
Corporate Social Responsibility Report:
Silver Award for Annual Reports – Specialised:
Sustainability Report **(International Astrid
Awards)**
Honours for Annual Reports – Sustainability
Report **(International Galaxy Awards)**
- Silver Prize for Corporate Social Responsibility
**(10th China International Public Relations
Association Awards)**

i) Caring for the needy

- Caring Company for 10 consecutive years
(The Hong Kong Council of Social Service)
- Jade Award of Web Care Award **(Internet
Professional Association)**

NCB, BOC-CC and BOC Life:

- Caring Company **(The Hong Kong Council of
Social Service)**

NCB:

- Heart to Heart Company **(The Hong Kong
Federation of Youth Groups)**

BOC-CC:

- Gold Award for Volunteer Service **(Social
Welfare Department)**

Professional Training

- ERB Manpower Developer 1st
(Employees Retraining Board)
- Qualifications Framework
Partnerships Commendation
(Education Bureau)
- Outstanding New Trainer Award
in the Awards for Excellence
in Training and Development
**(Hong Kong Management
Association)**
- Strategic Partner Award
(Vocational Training Council)



AWARDS AND RECOGNITION



ii) Environmental Protection

- Best Green ICT Grand Award and Best Green ICT (Adoption – Large-scale Enterprises) Gold Award in the Hong Kong ICT Awards (**Green ICT Consortium**)
- **International Astrid Awards**
Hong Kong Geopark Charity Green Walk: Silver Award for Campaigns – Climate/Environmental Awareness
Hong Kong Global Geopark of China – Prehistoric Story Room: Bronze Award for Green Marketing – Earth Science
- The Beauty of GEO ROCKS – BOCHK Hong Kong Geopark Photo Competition Album: Bronze Award for Special Projects – Book (**International Astrid Awards**) and Honours for Design – Photography (**International Galaxy Awards**)



BOC Tower, BOC Building, BOC Centre and Bank of China Wanchai Commercial Centre:

- ISO 14001 Certification (**UKAS**)
- Certificate of Quality Water Recognition Scheme for Building (**Water Supplies Department**)

BOC Tower and BOC Centre:

- Indoor Air Quality Certificate – Excellent Class (**Environmental Protection Department**)
- Energy Management System of ISO 50001:2011 Certification (**SGS Hong Kong**)
- Hygiene Control Management Systems Certificate (**SGS Hong Kong**)

BOC Tower:

- In the category of energy efficient buildings

BOC Building:

- Indoor Air Quality Certificate – Good Class (**Environmental Protection Department**)

BOC Group Life Assurance Tower:

- Indoor Air Quality Certificate – Good Class (**Environmental Protection Department**)
- Certificate of Quality Water Recognition Scheme for Building (**Water Supplies Department**)

Innovation and Creativity

- Outstanding Corporate Image Award (**TVB Weekly**)
- Metro Creative Awards – The Best Green Ad: Hong Kong Geopark Charity Green Walk (**Metro Daily**)
- BOC Life's Love Weight: Honour (Finance and Investment Category) of TVB Most Popular TV Commercial Awards (**Televisions Broadcasts Limited**)
- **International ARC Awards**
Annual Report 2011 of BOC Hong Kong (Holdings) Limited: Silver for Interior Design: Banks: Regional and Bronze for Written Text: Banks: Regional

- **International Astrid Awards**
Desk Top Calendar: Gold Award for Calendars: Corporate
Seasons Greetings e-Cards: Silver Award for Websites – e-Card
Christmas and Chinese New Year Decorations of BOC Tower: Bronze Award for Self-Promotion: Christmas and Chinese New Year Decorations

- **International Galaxy Awards**
Christmas and Chinese New Year Decorations of BOC Tower: Gold Award for Design – Christmas and Chinese New Year Decorations



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INDEPENDENT AUDITOR'S REPORT

To the shareholders of BOC Hong Kong (Holdings) Limited

(incorporated in Hong Kong with limited liability)

We have audited the consolidated financial statements of BOC Hong Kong (Holdings) Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 102 to 231, which comprise the consolidated and company balance sheets as at 31 December 2012, and the consolidated income statement, the consolidated and company statements of comprehensive income, the consolidated and company statements of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Consolidated Financial Statements

The directors of the Company are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, and the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

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

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

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2012, and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.



PricewaterhouseCoopers

Certified Public Accountants

Hong Kong, 26 March 2013

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December	Notes	2012 HK\$'m	2011 HK\$'m
Interest income		35,413	31,931
Interest expense		(10,705)	(9,952)
Net interest income	5	24,708	21,979
Fee and commission income		11,110	10,858
Fee and commission expense		(3,204)	(3,025)
Net fee and commission income	6	7,906	7,833
Gross earned premiums		11,881	12,927
Gross earned premiums ceded to reinsurers		(5,430)	(7,244)
Net insurance premium income		6,451	5,683
Net trading gain	7	3,129	1,710
Net gain/(loss) on financial instruments designated at fair value through profit or loss		747	(340)
Net gain on other financial assets	8	750	308
Other operating income	9	589	525
Total operating income		44,280	37,698
Gross insurance benefits and claims	10	(14,147)	(13,844)
Reinsurers' share of benefits and claims		5,627	6,992
Net insurance benefits and claims		(8,520)	(6,852)
Net operating income before impairment allowances		35,760	30,846
Net charge of impairment allowances	11	(859)	(506)
Net operating income		34,901	30,340
Operating expenses	12	(11,402)	(7,862)
Operating profit		23,499	22,478
Net gain from disposal of/fair value adjustments on investment properties	13	1,889	2,213
Net gain/(loss) from disposal/revaluation of properties, plant and equipment	14	106	(34)
Share of profits less losses after tax of associates	29	27	23
Profit before taxation		25,521	24,680
Taxation	15	(3,974)	(3,867)
Profit for the year		21,547	20,813
Profit attributable to:			
Equity holders of the Company		20,930	20,430
Non-controlling interests		617	383
		21,547	20,813
Dividends	17	13,089	12,560
		HK\$	HK\$
Earnings per share for profit attributable to the equity holders of the Company			
Basic and diluted	18	1.9796	1.9323

The notes on pages 110 to 231 are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December	Notes	2012 HK\$'m	2011 HK\$'m
Profit for the year		21,547	20,813
Premises:			
Revaluation of premises		9,796	8,989
Deferred tax	39	(1,601)	(1,422)
		8,195	7,567
Available-for-sale securities:			
Change in fair value of available-for-sale securities		5,398	(548)
Release upon disposal of available-for-sale securities		(644)	(469)
Net reversal of impairment allowances on available-for-sale securities transferred to income statement	11	(2)	(7)
Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities		(12)	(29)
Deferred tax	39	(730)	156
		4,010	(897)
Change in fair value of hedging instruments under net investment hedges		(7)	(117)
Currency translation difference		115	345
Other comprehensive income for the year, net of tax		12,313	6,898
Total comprehensive income for the year		33,860	27,711
Total comprehensive income attributable to:			
Equity holders of the Company		32,865	27,293
Non-controlling interests		995	418
		33,860	27,711

The notes on pages 110 to 231 are an integral part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December	Notes	2012 HK\$'m	2011 HK\$'m
Profit for the year	16	12,820	12,823
Available-for-sale securities:			
Change in fair value of available-for-sale securities		22	(269)
Other comprehensive income for the year, net of tax		22	(269)
Total comprehensive income for the year		12,842	12,554

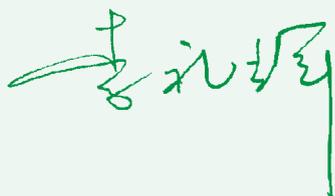
The notes on pages 110 to 231 are an integral part of these financial statements.

CONSOLIDATED BALANCE SHEET

As at 31 December	Notes	2012 HK\$'m	2011 HK\$'m
ASSETS			
Cash and balances with banks and other financial institutions	22	198,748	278,795
Placements with banks and other financial institutions maturing between one and twelve months		66,025	107,910
Financial assets at fair value through profit or loss	23	49,332	48,602
Derivative financial instruments	24	31,339	26,787
Hong Kong SAR Government certificates of indebtedness		82,930	65,890
Advances and other accounts	25	819,739	755,229
Investment in securities	27	482,364	376,998
Interests in associates	29	259	234
Investment properties	30	14,364	12,441
Properties, plant and equipment	31	48,743	39,650
Deferred tax assets	39	89	210
Other assets	32	36,831	25,764
Total assets		1,830,763	1,738,510
LIABILITIES			
Hong Kong SAR currency notes in circulation	33	82,930	65,890
Deposits and balances from banks and other financial institutions		179,206	236,694
Financial liabilities at fair value through profit or loss	34	20,172	3,237
Derivative financial instruments	24	21,214	22,281
Deposits from customers	35	1,226,290	1,145,951
Debt securities in issue at amortised cost	36	5,923	5,985
Other accounts and provisions	37	47,983	41,811
Current tax liabilities		1,873	2,237
Deferred tax liabilities	39	7,406	5,365
Insurance contract liabilities	40	53,937	47,220
Subordinated liabilities	41	28,755	28,656
Total liabilities		1,675,689	1,605,327
EQUITY			
Share capital	42	52,864	52,864
Reserves	43	98,105	76,901
Capital and reserves attributable to the equity holders of the Company		150,969	129,765
Non-controlling interests		4,105	3,418
Total equity		155,074	133,183
Total liabilities and equity		1,830,763	1,738,510

The notes on pages 110 to 231 are an integral part of these financial statements.

Approved by the Board of Directors on 26 March 2013 and signed on behalf of the Board by:



LI Lihui
Director



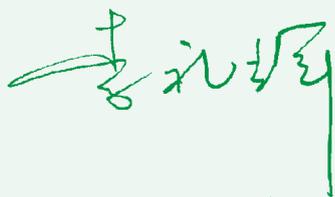
HE Guangbei
Director

BALANCE SHEET

As at 31 December	Notes	2012 HK\$'m	2011 HK\$'m
ASSETS			
Bank balances with a subsidiary		86	281
Investment in securities	27	2,528	2,506
Investment in subsidiaries	28	54,834	54,814
Amounts due from a subsidiary		7,318	5,983
Other assets		1	1
Total assets		64,767	63,585
LIABILITIES			
Amounts due to a subsidiary		2	1
Other accounts and provisions		1	1
Total liabilities		3	2
EQUITY			
Share capital	42	52,864	52,864
Reserves	43	11,900	10,719
Total equity		64,764	63,583
Total liabilities and equity		64,767	63,585

The notes on pages 110 to 231 are an integral part of these financial statements.

Approved by the Board of Directors on 26 March 2013 and signed on behalf of the Board by:



LI Lihui
Director



HE Guangbei
Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Attributable to the equity holders of the Company								
	Share capital HK\$'m	Premises revaluation reserve HK\$'m	Reserve for fair value changes of available- for-sale securities HK\$'m	Regulatory reserve* HK\$'m	Translation reserve HK\$'m	Retained earnings HK\$'m	Total HK\$'m	Non- controlling interests HK\$'m	Total equity HK\$'m
At 1 January 2011	52,864	15,750	2,629	5,076	453	38,409	115,181	3,108	118,289
Profit for the year	-	-	-	-	-	20,430	20,430	383	20,813
Other comprehensive income:									
Premises	-	7,508	-	-	-	-	7,508	59	7,567
Available-for-sale securities	-	-	(838)	-	-	(28)	(866)	(31)	(897)
Change in fair value of hedging instruments under net investment hedges	-	-	-	-	(110)	-	(110)	(7)	(117)
Currency translation difference	-	4	(4)	-	331	-	331	14	345
Total comprehensive income	-	7,512	(842)	-	221	20,402	27,293	418	27,711
Release upon disposal of premises	-	(112)	-	-	-	112	-	-	-
Transfer from retained earnings	-	-	-	1,891	-	(1,891)	-	-	-
Dividends	-	-	-	-	-	(12,709)	(12,709)	(108)	(12,817)
At 31 December 2011	52,864	23,150	1,787	6,967	674	44,323	129,765	3,418	133,183
Company and subsidiaries	52,864	23,150	1,787	6,967	674	44,251	129,693		
Associates	-	-	-	-	-	72	72		
	52,864	23,150	1,787	6,967	674	44,323	129,765		
At 1 January 2012	52,864	23,150	1,787	6,967	674	44,323	129,765	3,418	133,183
Profit for the year	-	-	-	-	-	20,930	20,930	617	21,547
Other comprehensive income:									
Premises	-	8,126	-	-	-	-	8,126	69	8,195
Available-for-sale securities	-	-	3,715	-	-	(12)	3,703	307	4,010
Change in fair value of hedging instruments under net investment hedges	-	-	-	-	(6)	-	(6)	(1)	(7)
Currency translation difference	-	1	8	-	103	-	112	3	115
Total comprehensive income	-	8,127	3,723	-	97	20,918	32,865	995	33,860
Release upon disposal of premises	-	(18)	-	-	-	18	-	-	-
Transfer from retained earnings	-	-	-	787	-	(787)	-	-	-
Dividends	-	-	-	-	-	(11,661)	(11,661)	(308)	(11,969)
At 31 December 2012	52,864	31,259	5,510	7,754	771	52,811	150,969	4,105	155,074
Company and subsidiaries	52,864	31,259	5,510	7,754	771	52,714	150,872		
Associates	-	-	-	-	-	97	97		
	52,864	31,259	5,510	7,754	771	52,811	150,969		
Representing:									
2012 final dividend proposed (Note 17)						7,327			
Others						45,484			
Retained earnings as at 31 December 2012						52,811			

* 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 110 to 231 are an integral part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

	Share capital HK\$'m	Reserve for fair value changes of available-for-sale securities HK\$'m	Retained earnings HK\$'m	Total equity HK\$'m
At 1 January 2011	52,864	1,519	9,355	63,738
Profit for the year	–	–	12,823	12,823
Other comprehensive income: Available-for-sale securities	–	(269)	–	(269)
Total comprehensive income	–	(269)	12,823	12,554
Dividends	–	–	(12,709)	(12,709)
At 31 December 2011	52,864	1,250	9,469	63,583
At 1 January 2012	52,864	1,250	9,469	63,583
Profit for the year	–	–	12,820	12,820
Other comprehensive income: Available-for-sale securities	–	22	–	22
Total comprehensive income	–	22	12,820	12,842
Dividends	–	–	(11,661)	(11,661)
At 31 December 2012	52,864	1,272	10,628	64,764

The notes on pages 110 to 231 are an integral part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December	Notes	2012 HK\$'m	2011 HK\$'m
Cash flows from operating activities			
Operating cash outflow before taxation	44(a)	(75,946)	(102,729)
Hong Kong profits tax paid		(4,243)	(3,267)
Overseas profits tax paid		(264)	(248)
Net cash outflow from operating activities		(80,453)	(106,244)
Cash flows from investing activities			
Purchase of properties, plant and equipment	31	(1,045)	(910)
Purchase of investment properties	30	(2)	(14)
Proceeds from disposal of properties, plant and equipment		266	94
Proceeds from disposal of investment properties		66	38
Dividend received from associates	29	2	1
Net cash outflow from investing activities		(713)	(791)
Cash flows from financing activities			
Dividend paid to the equity holders of the Company		(11,661)	(12,709)
Dividend paid to non-controlling interests		(308)	(108)
Interest paid for subordinated liabilities		(604)	(630)
Net cash outflow from financing activities		(12,573)	(13,447)
Decrease in cash and cash equivalents		(93,739)	(120,482)
Cash and cash equivalents at 1 January		340,446	446,679
Effect of exchange rate changes on cash and cash equivalents		(3,752)	14,249
Cash and cash equivalents at 31 December	44(b)	242,955	340,446

The notes on pages 110 to 231 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. Principal activities

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

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

2. Summary of significant accounting policies

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

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

2.1 Basis of preparation

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

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

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

(a) Standards and amendments already mandatorily effective for accounting periods beginning on 1 January 2012

Standard	Content	Applicable for financial years beginning on/after	Currently relevant to the Group
HKAS 12 (Amendment)	Income Taxes	1 January 2012	Yes
HKFRS 1 (Amendment)	First-time Adoption of Hong Kong Financial Reporting Standards: Hyperinflation and Fixed Dates	1 July 2011	No
HKFRS 7 (Amendment)	Financial Instruments: Disclosures – Transfer of Financial Assets	1 July 2011	Yes

- HKAS 12 (Amendment), 'Income Taxes'. The standard which was revised in December 2010 is mandatorily effective for reporting periods beginning on or after 1 January 2012. Earlier application is permitted. The Group has considered that the required treatment under the revised standard better reflects the tax position of the investment properties of the Group, and has early adopted the amended standard retrospectively since the year ended 31 December 2010.
- HKFRS 7 (Amendment), 'Financial Instruments: Disclosures – Transfer of Financial Assets'. The amendment introduces new quantitative disclosure requirements for transfers of financial assets that are either fully derecognised or derecognised not in their entirety. The Group will disclose relevant information in the financial statements when the Group undertakes transfers of financial assets that fall within its scope.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2012

The following standards, amendments and interpretations have been issued and are mandatory for accounting periods beginning on or after 1 July 2012:

Standard/ Interpretation	Content	Applicable for financial years beginning on/after	Currently relevant to the Group
HKAS 1 (Revised)	Presentation of Financial Statements	1 July 2012	Yes
HKAS 19 (2011)	Employee Benefits	1 January 2013	Yes
HKAS 27 (2011)	Separate Financial Statements	1 January 2013	Yes
HKAS 28 (2011)	Investments in Associates and Joint Ventures	1 January 2013	Yes
HKAS 32 (Amendment)	Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities	1 January 2014	Yes
HKFRS 1 (Amendment)	First Time Adoption of Hong Kong Financial Reporting Standards – Government Loans	1 January 2013	No
HKFRS 7 (Amendment)	Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities	1 January 2013	Yes
HKFRS 7 (Amendment)	Financial Instruments: Disclosures – Transition to HKFRS 9	1 January 2015	Yes
HKFRS 9	Financial Instruments	1 January 2015	Yes
HKFRS 10	Consolidated Financial Statements	1 January 2013	Yes
HKFRS 11	Joint Arrangements	1 January 2013	Yes
HKFRS 12	Disclosure of Interests in Other Entities	1 January 2013	Yes
HKFRS 10, 11 and 12 (Amendment)	Transition Guidance	1 January 2013	Yes
HKFRS 10, 12 and HKAS 27 (Amendments)	Investment Entities	1 January 2014	No
HKFRS 13	Fair Value Measurement	1 January 2013	Yes
HK(IFRIC) – Int 20	Stripping Costs in the Production Phase of a Surface Mine	1 January 2013	No

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2012 (continued)

- HKAS 1 (Revised), 'Presentation of Financial Statements'. The amendments to HKAS 1 (Revised) require companies preparing financial statements in accordance with HKFRSs to group together items within other comprehensive income (OCI) that may be reclassified to the profit or loss section of the income statement. The amendments also reaffirm existing requirements that items in OCI and profit or loss should be presented as either a single statement or two consecutive statements. The adoption of this revised standard will affect the presentation of the Group's statement of comprehensive income.
- HKAS 19 (2011), 'Employee Benefits'. The revised standard mainly amends the part related to accounting for changes in defined benefit obligations and plan assets, and related presentation and disclosure. The amendments do not have impact on the Group's financial statements.
- HKAS 27 (2011), 'Separate Financial Statements'. Please refer to the below on HKFRS 10, 'Consolidated Financial Statements'.
- HKAS 28 (2011), 'Investments in Associates and Joint Ventures'. Please refer to the below on HKFRS 11, 'Joint Arrangements'.
- HKAS 32 (Amendment), 'Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities'. The amendment addresses inconsistencies in current practice when applying the offsetting criteria and clarifies the meaning of 'currently has a legally enforceable right of set-off'; and the application of offsetting criteria to some gross settlement systems (such as central clearing house systems) that may be considered equivalent to net settlement. The Group is considering the financial impact of the amendment.
- HKFRS 7 (Amendment), 'Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities'. The amendments require new disclosures to include information that will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements, including rights of set-off associated with the entity's recognised financial assets and recognised financial liabilities, on the entity's financial position. The adoption of this amended standard will affect the disclosure of the Group's financial statements.
- HKFRS 7 (Amendment), 'Financial Instruments: Disclosures – Transition to HKFRS 9'. The amendments provide relief from the requirement to restate comparative financial statements which was originally available only to entities that chose to apply HKFRS 9 prior to 2012. Instead, additional transition disclosures will be required to help users to better understand the effect of initial application of the standard.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2012 (continued)

- HKFRS 9, 'Financial Instruments'. The first part of HKFRS 9 was issued in November 2009 and will replace those parts of HKAS 39 relating to the classification and measurement of financial assets. In November 2010, a further pronouncement was published to address financial liabilities and derecognition. Key features are as follows:

(i) Classification and Measurement

Financial assets are required to be classified into one of the following measurement categories: (1) those to be measured subsequently at fair value or (2) those to be measured subsequently at amortised cost. Classification is to be made on transition, and subsequently on initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.

A financial instrument is subsequently measured at amortised cost only if it is a debt instrument, and the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and the asset's contractual cash flows represent only unleveraged payments of principal and interest. All other debt instruments are to be measured at fair value through profit or loss.

All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than income statement. Once elected to be recognised through other comprehensive income, there will be no reclassification of fair value gains and losses to income statement. Dividends are to be presented in income statement as long as they represent a return on investment.

(ii) Financial Liabilities and Derecognition

Except for the two substantial changes described below, the classification and measurement requirements of financial liabilities have been basically carried forward with minimal amendments from HKAS 39. For the derecognition principles, they are consistent with that of HKAS 39.

The requirements related to the fair value option for financial liabilities were changed to address own credit risk. It requires the amount of change in fair value attributable to changes in the credit risk of the financial liabilities be presented in other comprehensive income. The remaining amount of the total gain or loss is included in income statement. If this requirement creates or enlarges an accounting mismatch in profit or loss, then the whole fair value change is presented in income statement. The determination of whether there will be a mismatch will need to be made at initial recognition of individual liabilities and will not be re-assessed. Amounts presented in other comprehensive income are not subsequently reclassified to income statement but may be transferred within equity.

The standard eliminates the exception from fair value measurement contained in HKAS 39 for derivative liabilities that are linked to and must be settled by delivery of an unquoted equity instrument.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2012 (continued)

The mandatory effective date of HKFRS 9 is 1 January 2015 with earlier adoption permitted. New transitional disclosures are required instead of comparative restatement. The Group is considering the financial impact of the standard and the timing of its application.

- HKFRS 10, 'Consolidated Financial Statements'. HKFRS 10 builds on existing principles by identifying the concept of control as the determining factor when considering whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. It also replaces all of the guidance on control and consolidation stipulated in HKAS 27 (Revised), 'Consolidated and Separate Financial Statements' and HK(SIC)-Int 12, 'Consolidation – Special Purpose Entities'. The remainder of HKAS 27 (Revised) is renamed HKAS 27 (2011), 'Separate Financial Statements' as a standard dealing solely with separate financial statements without changing the existing guidance for separate financial statements.
- HKFRS 11, 'Joint Arrangements'. Changes in the definitions stipulated in HKFRS 11 have reduced the types of joint arrangements to two: joint operations and joint ventures. A joint operation is a joint arrangement that gives parties to the arrangement direct rights to the assets and obligations for the liabilities. The 'jointly controlled assets' classification in HKAS 31, 'Interests in Joint Ventures', has been merged into joint operations, as both types of arrangements generally result in the same accounting outcome. A joint venture, in contrast, gives the parties rights to the net assets or outcome of the arrangement. Joint ventures are accounted for using the equity method in accordance with HKAS 28, 'Investments in Associates' which is renamed as HKAS 28 (2011), 'Investments in Associates and Joint Ventures'. The standard is amended to include the requirements of joint ventures accounting and to merge with the requirements of HK(SIC)-Int 13, 'Jointly Controlled Entities – Non-Monetary Contributions by Venturers'. After the application of HKAS 28 (2011), entities can no longer account for an interest in a joint venture using the proportionate consolidation method.
- HKFRS 12, 'Disclosure of Interests in Other Entities'. The standard sets out the required disclosures for entities reporting under the two new standards, HKFRS 10 and HKFRS 11, and the revised standard HKAS 28 (2011). The existing guidance and disclosure requirements for separate financial statements stipulated in HKAS 27 (Revised) are unchanged. HKFRS 12 requires entities to disclose information that helps financial statements readers to evaluate the nature, risks and financial effects associated with the entity's interests in subsidiaries, associates, joint arrangements and unconsolidated structured entities.

The above HKFRS 10, HKFRS 11, HKFRS 12, HKAS 27 (2011) and HKAS 28 (2011) issued in June 2011 are a group of five new standards that address the scope of reporting entity and will supersede HKAS 27 (Revised), HKAS 28, HKAS 31, HK(SIC)-Int 12 and HK(SIC)-Int 13. Earlier application of these standards are permitted but only when they are applied at the same time. The adoption of these standards does not have a material impact on the Group's financial statements.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2012 (continued)

- HKFRS 10, 11 and 12 (Amendment), on transition guidance. The amendments provide additional transition relief to HKFRS 10, 11 and 12, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. The adoption of this amendment will not materially affect the disclosure of the Group's financial statements.
- HKFRS 13, 'Fair Value Measurement'. The new standard which was issued in June 2011 replaces the fair value measurement guidance contained in individual HKFRSs by providing a revised definition of fair value and a single source of fair value measurement and disclosure requirements for use across HKFRSs. The requirements do not extend the use of fair value accounting, but provide guidance on how it should be applied when its use is already required or permitted by other standards within HKFRSs. The Group will apply HKFRS 13 prospectively from 1 January 2013.

(c) Improvements to HKFRSs

'Improvements to HKFRSs' contains numerous amendments to HKFRSs which the HKICPA considers not 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 HKFRSs. The amendments are effective for annual periods beginning on or after 1 January 2013. No material changes to accounting policies are expected as a result of these amendments.

2.2 Consolidation

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

(1) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group controls the composition of the Board of Directors, controls more than half of the voting power, holds more than half of the issued capital or by any other means that entitle the Group to govern the financial and operating policies of the entities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

(i) Business combinations not under common control

Acquisitions of businesses not under common control are accounted for using the acquisition method. The consideration transferred in a business combination is the fair values at the acquisition date of the assets transferred, the liabilities incurred (including contingent consideration arrangement) and the equity interests issued by the Group in exchange for control of the acquiree. Acquisition-related costs are expensed in the income statement as incurred.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.2 Consolidation (continued)

(1) Subsidiaries (continued)

(i) *Business combinations not under common control (continued)*

Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the Group's previously held equity interest in the acquiree (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. If after assessment, the fair value of the acquiree's identifiable net assets exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the Group's previously held interest in the acquiree (if any), the excess is recognised immediately in income statement as a bargain purchase gain. Subsequently, goodwill is subject to impairment testing.

Where the consideration transferred by the Group in a business combination includes assets or liabilities resulting from a contingent consideration arrangement, the contingent consideration is measured at fair value at the acquisition date and considered as part of the consideration transferred in a business combination. Changes in the fair value of the contingent consideration that qualify as measurement period adjustments are adjusted retrospectively, with the corresponding adjustments being made against goodwill or gain on bargain purchase. Measurement period adjustments are adjustments that arise from additional information obtained during the measurement period about facts and circumstances that existed as of the acquisition date. Measurement period does not exceed one year from the acquisition date.

On an acquisition-by-acquisition basis, the Group recognises any non-controlling interests in the acquiree either at fair value or at the non-controlling interests' proportionate share of the fair value of the acquiree's identifiable net assets.

(ii) *Business combinations under common control*

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

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the transaction provides evidence of impairment of the assets transferred. Where necessary, accounting policies of subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet, the investments in subsidiaries are stated at cost less allowance for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable. Dividend income from subsidiaries is recognised in the income statement when the right to receive payment is established.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.2 Consolidation (continued)

(2) Transactions with non-controlling interests

The Group treats transactions with non-controlling interests without change of control as transactions with equity owners of the Group. For purchases from non-controlling interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recognised in equity. Gains or losses on disposals to non-controlling interests are also recognised in equity.

When the Group ceases to have control or significant influence, any retained interest in the entity is re-measured to its fair value, with the change in carrying amount recognised in income statement. The fair value is the initial carrying amount for the purposes of subsequent accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. Amounts previously recognised in other comprehensive income are reclassified to income statement.

(3) Associates

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

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

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

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income are reclassified to income statement where appropriate.

2.3 Segmental reporting

The operating result of segments are reported in a manner consistent with the internal reporting provided to the Management Committee, which is the chief operating decision maker of the Group, that allocates resources and assesses the performance of operating segments. Income and expenses directly associated with each segment are included in determining operating segment performance.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.4 Foreign currency translation

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Hong Kong dollars, which is the Company's functional and presentation currency.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or exchange rates at the end of the reporting period for items that are re-measured. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions using the exchange rates prevailing at the dates of the transactions and monetary assets and liabilities denominated in foreign currencies translated at the exchange rate at the end of the reporting period are recognised directly in the income statement, except when deferred in other comprehensive income as qualifying cash flow hedges and qualifying net investment hedges.

Translation differences on monetary securities held at fair value through profit or loss are reported as part of the fair value gain or loss. Changes in the fair value of monetary securities denominated in foreign currency classified as available-for-sale are analysed between translation differences resulting from changes in the amortised cost of the securities and other changes in the carrying amount of the securities. Translation differences related to changes in the amortised cost are recognised in the income statement, and other changes in the carrying amount are recognised in other comprehensive income.

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

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

- assets and liabilities are translated at the closing rate at the end of the reporting period;
- income and expenses are translated at average exchange rates; and
- all resulting exchange differences are recognised in the currency translation reserve in equity through other comprehensive income.

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

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.5 *Derivative financial instruments and hedge accounting*

Derivatives are initially recognised at fair value on the date the derivative contract is entered into and are subsequently re-measured at fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and through the use of valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e., the fair value of the consideration given or received).

Certain derivatives embedded in other financial instruments are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement.

Derivatives are categorised as held for trading and changes in their fair value are recognised immediately in the income statement unless they are designated as hedges and are effective hedging instruments, then they are subject to measurement under the hedge accounting requirements.

For derivative instruments designated as hedging instrument and are effectively hedged, the method of recognising the resulting fair value gain or loss depends on the nature of the item being hedged. The Group designates certain derivatives as either:

- (a) hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge); or
- (b) hedges of a particular risk associated with a highly probable future cash flows attributable to a recognised asset or liability, or a highly probable forecasted transaction (cash flow hedge).

Hedge accounting is used for derivatives designated in this way.

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

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.5 *Derivative financial instruments and hedge accounting (continued)*

(a) **Fair value hedge**

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

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 no longer meets the criteria for hedge accounting or is terminated for reasons other than 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) to the hedged item is amortised to the income statement over the remaining life of the hedged item by the effective interest method. If the hedged item is derecognised, the unamortised carrying value adjustment is recognised immediately in the income statement.

(b) **Cash flow hedge**

The effective portion of changes in the fair value of derivatives that are designated and qualified as cash flow hedges are recognised in other comprehensive income and accumulated in equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement. Amounts accumulated in equity are reclassified to the income statement in the periods when the hedged item affects profit or loss.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any accumulated gain or loss existing in equity at that time remains in equity and is recognised in the income statement when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the accumulated gain or loss that was reported in equity is immediately reclassified to the income statement.

(c) **Net investment hedge**

Hedges of net investments in foreign operations are accounted for in a similar way to cash flow hedges. A gain or loss on the effective portion of the hedging instrument is recognised in other comprehensive income and accumulated in equity; a gain or loss on the ineffective portion is recognised immediately in the income statement. Accumulated gains and losses previously recognised in other comprehensive income are reclassified to income statement upon disposal of the foreign operation as part of the gain or loss on disposal.

2.6 *Offsetting financial instruments*

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

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.7 *Interest income and expense and fee and commission income and expense*

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

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates future cash flows considering all contractual terms of the financial instrument (e.g. prepayment options or incentives relating to residential mortgage loans) but does not consider future credit losses. The calculation includes fees, premiums or discounts and basis points paid or received between parties to the contract, and directly attributable origination fees and costs which represent an integral part of the effective yield.

For all hedge transactions where interest rate is the hedged risk, interest income or interest expense from hedged instruments such as fixed rate debt securities or fixed rate subordinated notes are disclosed on a net basis together with net interest income/expense arising from the hedging instrument such as interest rate swap.

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

Fee and commission income and expenses that are not an integral part of the effective yield are recognised on an accrual basis ratably over the period when the related service is provided, such as administrative fee, asset management fee and custody services fee. Loan syndication fees are recognised as revenue when the related syndication arrangement has been completed and the Group has retained no part of the loan package for itself or has retained a part at the same effective interest rate as that of other participants.

2.8 *Financial assets*

The Group classifies its financial assets into the following four categories: financial assets at fair value through profit or loss, loans and receivables, held-to-maturity securities and available-for-sale financial assets. The Management determines the classification of investments at initial recognition. The classification depends on the purpose for which the financial assets are held. All financial assets are recognised initially at fair value. Except for financial assets carried at fair value through profit or loss, all transaction costs of financial assets are included in their amortised costs.

(1) **Financial assets at fair value through profit or loss**

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception.

A financial asset which has been acquired or incurred principally for the purpose of selling in the short term or is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking is classified as held-for-trading. Derivatives are also classified as held for trading unless they are designated as effective hedges.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.8 Financial assets (continued)

(1) Financial assets at fair value through profit or loss (continued)

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

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

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

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

(2) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, including placements with and advances to banks and other financial institutions, investment debt securities without an active market and loans and advances to customers. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method less allowances for impairment losses.

(3) Held-to-maturity

Financial assets classified as held-to-maturity are those traded in active markets, with fixed or determinable payments and fixed maturities that the Group's Management has both the positive intention and the ability to hold to maturity. Where the Group sold held-to-maturity assets (i) other than due to an isolated event beyond the Group's control, non-recurring and could not have been reasonably anticipated by the Group, such as a significant deterioration in the issuer's creditworthiness, significant change in statutory or regulatory requirement or (ii) other than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available-for-sale. They are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method less allowances for impairment losses.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.8 Financial assets (continued)

(4) Available-for-sale

Financial assets classified as available-for-sale are those that are either designated as such or are not classified in any of the other categories. They are intended to be held for an indefinite period of time but may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Available-for-sale financial assets are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at fair value. Unrealised gains and losses arising from changes in the fair value of investments are recognised directly in other comprehensive income, until the financial asset is derecognised or impaired at which time the accumulated gain or loss previously recognised in equity should be transferred to the income statement. However, interest income which includes the amortisation of premium and discount is calculated using the effective interest method and is recognised in the income statement. Dividends on equity instruments classified as available-for-sale are recognised in other operating income when the Group's right to receive payment is established.

The treatment of translation differences on available-for-sale securities is dealt with in Note 2.4.

2.9 Financial liabilities

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

(1) Trading liabilities

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

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.9 Financial liabilities (continued)

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

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

2.10 Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a contract between the holder and the debtor.

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

2.11 Recognition and derecognition of financial instruments

Purchases and sales of financial assets at fair value through profit or loss, available-for-sale and held-to-maturity securities are recognised on the trade date, the date on which the Group purchases or sells the assets. Loans and receivables (except investment securities without an active market) are recognised when cash is advanced to the borrowers. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership. When the Group neither transfers nor retains substantially all the risks and rewards of ownership of the financial asset, the Group either continues to recognise the transferred financial asset to the extent of its continuing involvement if control remains or derecognise it if there is no retained control.

Trading liabilities, financial liabilities designated at fair value through profit or loss and debt securities in issue are recognised on the trade date. Deposits that are not trading liabilities are recognised when money is received from customers, other liabilities are recognised when such obligations arise. Financial liabilities are derecognised from the balance sheet when and only when the obligation specified in the contract is discharged, cancelled or expired. If the Group purchases its own debt, it is removed from the balance sheet, and the difference between the carrying amount of a liability and the consideration paid is included in net trading gain/loss.

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

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

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.12 Determination of fair value of financial instruments

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

2.13 Precious metals

Precious metals comprise gold, silver and other precious metals. Precious metals are initially recognised at fair value and subsequently re-measured at their respective market prices as at the end of the reporting period. Mark-to-market gains or losses on precious metals are included in net trading gain/loss.

2.14 Impairment of financial assets

The Group assesses as at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Objective evidence that a financial asset or group of financial assets may be impaired includes observable data that comes to the attention of the Group about the following probable loss events:

- (i) significant financial difficulty of the issuer or obligor;
- (ii) a breach of contract, such as a default or delinquency in interest or principal payment;
- (iii) the Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;
- (iv) it becoming probable that the borrower will enter into bankruptcy or other financial reorganisation;
- (v) the disappearance of an active market or downgrading below investment grade level for that financial asset because of financial difficulties; or
- (vi) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:
 - adverse changes in the payment status of borrowers in the group; or
 - national or local economic conditions that correlate with defaults on the assets in the group.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.14 Impairment of financial assets (continued)

(1) Assets carried at amortised cost

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

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity securities has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred), discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral.

For the purposes of a collective assessment of impairment, financial assets are grouped on the basis of similar and relevant credit risk characteristics. Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

When a loan is uncollectible, it is written off against the related allowance for impairment losses. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses in the income statement.

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

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

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.14 Impairment of financial assets (continued)

(2) Assets classified as available-for-sale

If evidence of impairment exists for available-for-sale financial assets, the accumulated losses, measured as the difference between the acquisition cost or amortised cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement, is removed from equity and recognised in the income statement. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss to the extent of its decrease is reversed through the income statement. With respect to equity instruments, further fair value changes are recognised in the reserve for fair value change of available-for-sale securities through other comprehensive income, impairment losses are not reversed through the income statement.

2.15 Impairment of investment in subsidiaries, associates and non-financial assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Potential indications of impairment may include significant adverse changes in the technological, market, economic or legal environment in which the assets operate or whether there has been a significant or prolonged decline in value below their cost.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

In the Company's financial statements, impairment testing of the investment in a subsidiary or associate is also required upon receiving dividend from that entity if the dividend exceeds the total comprehensive income of that entity concerned in the period the dividend is declared or if the carrying amount of that entity in the Company's balance sheet exceeds the carrying amount of that entity's net assets including goodwill in its consolidated balance sheet.

2.16 Investment properties

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

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

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.16 *Investment properties (continued)*

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The item is stated at cost less impairment and is included in the carrying amount of investment properties. Once the item begins to generate economic benefits, it is then measured at fair value. All other repairs and maintenance costs are expensed in the income statement during the financial period in which they are incurred.

Any changes in fair value are recognised directly in the income statement.

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

2.17 *Properties, plant and equipment*

Properties are mainly branches and office premises. Premises are shown at fair value based on periodic, at least annual, valuations by external independent valuers less subsequent accumulated depreciation and subsequent accumulated impairment losses. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. In the intervening periods, the directors review the carrying amount of premises, by reference to the open market value of similar properties, and adjustments are made when there has been a material change.

All plant and equipment are stated at historical cost less accumulated depreciation and impairment. Historical cost includes expenditures that are directly attributable to the acquisition and installation of the items.

Subsequent costs are included in an asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The item is stated at cost less impairment until it begins to generate economic benefits, then the item is subsequently measured according to the measurement basis of its respective assets class. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

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

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.17 Properties, plant and equipment (continued)

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

- Properties Over the life of government land leases
- Plant and equipment 3-15 years

The useful lives of assets are reviewed, and adjusted if appropriate, as at the end of each reporting period.

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

Gains and losses on disposals are determined by comparing proceeds with carrying amount, relevant taxes and expenses. These are recognised in the income statement.

2.18 Leases

(1) Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. The total payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place. Rental income from operating leases is recognised on a straight-line basis over the lease term.

(2) Finance leases

Leases of assets where lessee have obtained substantially all the risks and rewards of ownership are classified as finance leases. Government land leases in Hong Kong are classified as finance leases as the present value of the minimum lease payments (i.e. transaction price) of the land amounted to substantially all of the fair value of the land as if it were freehold.

Finance leases are capitalised at the lease's commencement at the lower of the fair value of the leased asset and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in other liabilities. Investment properties acquired under finance leases are carried at their fair value.

When assets are leased out under a finance lease, the present value of the lease payments is recognised as a receivable. Lease income is recognised over the term of the lease using net investment method, which reflects a constant periodic rate of return.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.19 Insurance contracts

(1) Insurance contracts classification, recognition and measurement

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

The Group issues insurance contracts, which are contracts that transfer significant insurance risk. As a general guideline, the Group defines significant insurance risk as the possibility of having to pay benefits on the occurrence of an insured event that are at least 10% more than the benefit payable if the insured event did not occur. The Group issues long term business insurance contracts, which insure events covered by life policies (for example death, survival, or total permanent disability) over a long duration. A liability for contractual benefits that are expected to be incurred in the future is recorded when premiums are recognised.

For linked long term insurance contracts with embedded derivatives (which are closely related to the host insurance contracts) linking payments on the contract to units of the investment funds which the Group has invested with the consideration received from the contract holders, the liability is adjusted for all changes in the fair value of the underlying assets, and includes a liability for contractual benefits that are expected to be incurred in the future which is recorded when the premiums are recognised.

Retirement scheme management category III insurance contracts, as defined in the Insurance Companies Ordinance, insure events associated with the cessation of employment due to death. A liability for contractual benefits that are expected to be incurred in the future is recorded when premiums are recognised. The portion of the premium received on in-force contracts that relates to unexpired risks at the end of the reporting period is reported as the unearned premium liability, which is included in insurance liabilities.

Premiums are recognised as revenue when they become payable by the contract holders before the deduction of commissions. Benefits and claims are recorded as an expense when they are incurred.

The Group does not separately measure embedded derivatives that meet the definition of an insurance contract or options to surrender insurance contracts for a fixed amount (or an amount based on a fixed amount and an interest rate).

Contracts entered into by the Group with reinsurers under which the Group is compensated for losses on one or more contracts issued by the Group and that meet the classification requirement for insurance contracts as noted above are classified as reinsurance contracts held.

The benefits to which the Group is entitled under its reinsurance contracts held are recognised as reinsurance assets. These reinsurance assets consist of short-term amounts due from reinsurers as well as longer term receivables that are dependent on the expected claims and benefits arising from the related reinsured insurance contracts. Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the underlying insurance contracts and in accordance with the terms of each reinsurance contract. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised as an expense when due.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.19 Insurance contracts (continued)

(2) Liability adequacy test

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

2.20 Cash and cash equivalents

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

2.21 Provisions

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

2.22 Employee benefits

(1) Retirement benefit costs

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

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

(2) Leave entitlements

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

Compensated absences other than sick leave and special approved annual leaves are non-accumulating; they lapse if the current period's entitlement is not used in full. Except for unexpired annual leaves, they do not entitle employees to a cash payment for unused entitlement on leaving the Group.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.22 *Employee benefits (continued)*

(3) Bonus plans

The expected cost of bonus payments are recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made. Liabilities for bonus plans that are expected to be settled longer than twelve months will be recognised using discounted cash flow method if the amounts are significant.

2.23 *Current and deferred income taxes*

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

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

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from asset impairment provisions, depreciation of premises and equipment, revaluation of certain assets including available-for-sale securities and premises, and tax losses carried forward. However, the deferred income tax is not recognised if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Deferred income tax liabilities are provided in full on all taxable temporary differences and deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

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

Deferred tax liability or deferred tax asset arising from investment property is determined based on the presumption that the revaluation amount of such investment property will be recovered through sale with the relevant tax rate applied.

2.24 *Reposessed assets*

Reposessed assets are initially recognised at the lower of their fair value less costs to sell and the amortised cost of the related outstanding loans on the date of repossession, and the related loans and advances together with the related impairment allowances are derecognised from the balance sheet. Subsequently, reposessed assets are measured at the lower of their cost and fair values less costs to sell and are reported as 'non-current assets held for sale' included in 'Other assets'.

NOTES TO THE FINANCIAL STATEMENTS

2. Summary of significant accounting policies (continued)

2.25 *Fiduciary activities*

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

2.26 *Contingent liabilities and contingent assets*

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

A contingent liability is not recognised as a provision but is disclosed in the notes to the financial statements. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

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

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

2.27 *Related parties*

For the purposes of these financial statements, a party is considered to be related to the Group if that party controls, jointly controls or has significant influence over the Group; is a member of the same financial reporting group, such as parents, subsidiaries and fellow subsidiaries; is an associate or a joint venture of the Group or parent reporting group; is a key management personnel of the Group or parents, or where the Group and the party are subject to common control. Related parties may be individuals or entities.

3. Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the carrying amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Areas susceptible to changes in essential estimates and judgements, which affect the carrying amount of assets and liabilities, are set out below. The effect of changes to either the key assumptions or other estimation uncertainties will be presented below if it is practicable to determine. It is possible that actual results may require material adjustments to the estimates referred to below.

NOTES TO THE FINANCIAL STATEMENTS

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

3.1 *Impairment allowances on loans and advances*

The Group reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and advances before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group (e.g. payment delinquency or default), or economic conditions that correlate with defaults on assets in the group. The Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when estimating expected future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly.

Carrying amounts of loans and advances as at 31 December 2012 are shown in Note 25 to the Financial Statements.

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

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

Carrying amounts of investment in securities as at 31 December 2012 are shown in Note 27 to the Financial Statements.

3.3 *Fair values of derivative financial instruments*

The fair values of derivative financial instruments that are not quoted in active markets are determined by using valuation techniques. Valuation techniques used include discounted cash flows analysis and models with built-in functions available in externally acquired financial analysis or risk management systems widely used by the industry such as option pricing models. To the extent practical, the models only use observable data.

Carrying amounts of derivative financial instruments as at 31 December 2012 are shown in Note 24 to the Financial Statements.

3.4 *Held-to-maturity securities*

The Group follows the guidance of HKAS 39 in classifying certain non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity securities. This classification requires significant management judgement to evaluate the Group's intention and ability to hold such investments to maturity. If the Group fails to hold these investments to maturity other than for specific circumstances defined in HKAS 39, such as selling an insignificant amount, selling close to maturity or due to significant credit deterioration of such investments, it will be required to reclassify the entire portfolio of financial assets as available-for-sale securities. The investments would then be measured at fair value and not amortised cost.

Carrying amounts of held-to-maturity securities as at 31 December 2012 are shown in Note 27 to the Financial Statements.

NOTES TO THE FINANCIAL STATEMENTS

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

3.5 *Estimate of future benefit payments and premiums arising from long term insurance contracts*

In determining the Group's long term business fund liabilities (a component of insurance contract liabilities), the Group follows the Insurance Companies (Determination of Long Term Liabilities) Regulation under the Insurance Companies Ordinance and makes prudent assumptions which include appropriate margins for adverse deviation of the relevant factors. Estimates are made as to the expected number of deaths for each of the years in which the Group is exposed to risk. The Group bases these estimates on Hong Kong Assured Lives Mortality Table HKA01 that reflect recent historical mortality experience, adjusted where appropriate to reflect the Group's own experience. For contracts that insure the risk of longevity, appropriate prudent allowances are made for expected mortality improvements. The estimated number of deaths determines the value of the benefit payments and the value of the valuation premiums. The main source of uncertainty is that epidemics such as AIDS, SARS, avian flu and wide-ranging lifestyle changes, such as in eating, smoking and exercise habits, could result in future mortality being significantly worse than in the past for the age groups in which the Group has significant exposure to mortality risk. However, continuing improvements in medical care and social conditions could result in improvements in longevity in excess of those allowed for in the estimates used to determine the liability for contracts where the Group is exposed to longevity risk.

Were the number of deaths in future years to differ by 10% from the Management's estimate, the long term business fund liability would increase by approximately HK\$103 million (2011: approximately HK\$91 million), which accounts for 0.2% (2011: 0.2%) of the liability. In this case, it is assumed there is no relief arising from reinsurance contracts held.

For linked long term insurance contracts with a life cover component, it is assumed that the Group will be able to increase mortality risk charges in future years in line with emerging mortality experience.

Estimates are also made as to future investment income arising from the assets backing long term insurance contracts. These estimates are based on current market returns as well as expectations about future economic and financial developments. Were the average future investment returns to decrease by 50 basis points from the Management's estimates, the long term business fund liability would increase by approximately HK\$1,410 million (2011: approximately HK\$993 million). In this case, it is assumed there is no relief arising from reinsurance contracts held.

The Group has also assessed whether a provision for expense is necessary in accordance with the Insurance Companies Ordinance. A provision for expense is the amount required to meet the total net cost that would likely be incurred in fulfilling contracts if the Group were to cease to transact new business 12 months after the valuation date.

A resilience reserve was set up and included in long term business fund liabilities in accordance with the Insurance Companies (Determination of Long Term Liabilities) Regulation to provide a prudent provision against the effects of possible future changes to the value of the assets to meet the liabilities. The resilience reserve was set up based on the appointed actuary's advice of a 16 basis points (2011: 20 basis points) change in market yield of the underlying assets and valuation interest rates. The amount of resilience reserve set up depends on the degree of change in interest rate assumed.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management

The Group is exposed to financial risks as a result of engaging in a variety of business activities. The principal financial risks are credit risk, market risk (including currency risk and interest rate risk) and liquidity risk. This note summarises the Group's exposures to these risks, as well as its objectives, risk management governance structure, policies and processes for managing and the methods used to measure these risks.

Financial risk management framework

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 formulating risk management strategies and ensuring that the Group has an effective risk management system to implement these strategies.

The Risk Committee ("RC"), a standing committee established by the Board of Directors, is responsible for overseeing the Group's various types of risks, reviewing and approving high-level risk-related policies and overseeing their implementation, reviewing significant or high risk exposures or transactions and exercising its power of veto if it considers that any transaction should not proceed. The Audit Committee 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. Moreover, the Group's non-banking subsidiaries, such as BOC Life, are subject to the Group's risk management requirements. These subsidiaries are required to formulate their respective risk management policies based on the characteristics of their own industries, perform daily risk management responsibilities and report to BOCHK on a regular basis. Risk management units of BOCHK monitor the risk management status of these subsidiaries respectively.

The Group has put in place appropriate internal control systems, including establishment of an organisation structure that sets clear lines of authority and responsibility for monitoring compliance with policies, procedures and limits. Proper reporting lines also provide sufficient independence of the control functions from the business areas, as well as adequate segregation of duties throughout the organisation which helps to promote an appropriate internal control environment.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

Product development

To ensure effective risk assessment and monitoring, the Group has developed a comprehensive product development and management framework which clearly defines the roles and responsibilities of all related units, and the proper risk assessment procedures for the product development process.

In accordance with the strategic objectives set by the Board and the Management, the respective product management units are responsible for formulating business and product development plans, and the department of strategic development shall ensure the plans are aligned with the Group's overall strategies. Departments that are responsible for risk management, legal, compliance and finance etc. are accountable for risk assessment and review.

Apart from product development, the respective product management units shall work closely with relevant risk evaluating departments to identify and assess all the related risks. Risk evaluating departments shall conduct independent review on risk management procedures and assessment results. Products can only be launched after the risk management procedures are fulfilled and endorsed by all risk evaluating departments.

In order to be prudent in offering treasury products to our clients, all treasury products, regardless brand new or modified, require approval from a special committee before launching.

4.1 Credit Risk

Credit risk is the risk of loss arising from that a customer or counterparty will be unable to or unwilling to meet its contractual obligations. Credit risk exists in the trading book and banking book, on- and off-balance sheet exposures of a bank. It arises principally from the lending, trade finance and treasury businesses, and covers inter-bank transactions, foreign exchange and derivative transactions as well as investments in bonds and securities.

Credit risk management framework

The Group has formulated a comprehensive set of credit risk management policies and procedures, and appropriate credit risk limits to manage and control credit risk that may arise. These policies, procedures and credit risk limits are regularly reviewed to cope with changes in market conditions and business strategies.

The Group's organisation structure establishes a clear set of authority and responsibility for monitoring compliance with policies, procedures and limits.

The Chief Credit Officer, who reports directly to the CRO, takes charge of credit risk management and is also responsible for the control of credit risk exposure of subsidiaries in line with the credit risk management principles and requirements set by the Group. The Chief Analytics Officer, who also reports directly to the CRO, is responsible for the development and maintenance of internal rating models and establishing the rating criteria. Various units of the Group have their respective credit risk management responsibilities. Business units act as the first line of defence. The Risk Management Department ("RMD"), which is independent from the business units, is responsible for the day-to-day management of credit risks and has the primary responsibility for providing an independent due diligence through identifying, measuring, monitoring and controlling credit risk to ensure an effective checks and balances, as well as drafting, reviewing and updating credit risk management policies and procedures. It is also responsible for the design of the Group's internal rating system and ensuring the system complies with the relevant regulatory requirements.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Credit risk management framework (continued)

In accordance with Group's operating principle, the Group's principal banking subsidiaries, Nanyang, NCB (China) and Chiyu, have also formulated their own credit risk policies that are consistent with those of the Group. These subsidiaries execute their risk management strategies independently and report to the Group's management on a regular basis.

The Board of Directors delegates credit approval authority to the CE. The CE can further delegate to the subordinates within his limit authorised by the Board of Directors. The Group sets the limits of credit approval authority according to the business nature, rating, the level of transaction risk, and the extent of the credit exposure.

Credit risk measurement and control

In view of the rapidly changing market conditions, the Group has been continuously revisiting its credit strategies and conducting rigorous reviews on the concerned portfolios.

Loans and advances

Different credit approval and control procedures are adopted according to the level of risk associated with the customer, counterparty or transaction. The Credit Risk Assessment Committee comprising experts from credit and other functions is responsible for making an independent assessment of all credit facilities which require the approval of Deputy Chief Executives ("DCE") or above. Credit applications for non-retail exposure are independently reviewed and objectively assessed by risk management units. Obligor ratings (in terms of PD) and facility ratings (in terms of LGD) are assigned to these portfolios to support credit approval. Retail internal rating systems are deployed in risk assessment of retail credit transactions, including small business retail exposures, residential mortgage loans, personal loans and credit cards. Loan grades, obligor and facility ratings as well as loss estimates (if applicable) are used to support credit approval.

The Group uses loan grades, obligor ratings and loss estimates (if applicable) to support credit monitoring, analysis and reporting. For non-retail exposures, more frequent rating review and closer monitoring are required for higher-risk customers. For retail exposures, monthly updated internal ratings and loss estimates are used for credit monitoring on a portfolio basis. More comprehensive review is required for obligors being identified under high-risk pools.

The Group has established credit master scale for internal rating purpose, which is in compliance with the Banking (Capital) Rules under the Hong Kong Banking Ordinance on internal rating structure, and can be mapped to Standard & Poor's external ratings.

RMD provides regular credit management information reports and ad hoc reports to MC, RC and Board of Directors to facilitate their continuous monitoring of credit risk.

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

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Credit risk measurement and control (continued)

Loans and advances (continued)

As of 31 December 2012, the Group continues to adopt loan grading criteria which divide credit assets into 5 categories with reference to HKMA's guidelines, as below:

"Pass" represents loans where the borrower is current in meeting its repayment obligations and full repayment of interest and principal is not in doubt.

"Special Mention" represents loans where the borrower is experiencing difficulties which may threaten the Group's position. Ultimate loss is not expected at this stage but could occur if adverse conditions persist.

"Substandard" represents loans where the borrower displays a definable weakness that is likely to jeopardise repayment.

"Doubtful" represents loans where collection in full is improbable and the Group expects to sustain a loss of principal and/or interest, taking into account the net realisable value of the collateral.

"Loss" represents loans which are considered uncollectible after all collection options (such as the realisation of collateral or the institution of legal proceedings) have been exhausted.

Debt securities and derivatives

For investments in debt securities and securitisation assets, the obligor ratings or external credit ratings, assessment of the underlying assets and credit limits setting on customer/security issuer basis are used for managing credit risk associated with the investment. For derivatives, the Group sets customer limits to manage the credit risk involved and follows the same approval and control processes as applied for loans and advances. On-going monitoring and stop-loss procedures are established.

The methodology and assumptions used for impairment assessments are reviewed regularly. In evaluating impairment of asset backed securities ("ABS") and mortgage backed securities ("MBS"), the Group continued to use a significant decline in market price and credit deterioration of the underlying assets to be the key indicators of impairment. The Group also considered other objective evidence of impairment, taking into account the impact of liquidity on market prices and the movement in loss coverage ratios of individual ABS and MBS held by the Group.

Settlement risk arises mainly from foreign exchange transactions with counterparties and also from derivatives in any situation where a payment in cash, securities or equities is made in the expectation of a corresponding receipt in cash, securities or equities. Daily settlement limits are established for each counterparty or customer to cover all settlement risk arising from the Group's market transactions on any single day.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

Collateral held as security and other credit enhancements

The valuation and management of collateral have been documented in the credit risk management policies and procedures which cover acceptance criteria, validity of collateral, loan-to-value ratio, haircut ratio, valuation and insurance, etc. The collateral is revalued on a regular basis, though the frequency and the method used varies with the type of collateral involved and the nature and the risk of the underlying credit. The Group has established a mechanism to update the value of its main type of collateral, real estate properties, with the use of public indices on a portfolio basis. Collateral is insured with the Group as the beneficiary. In the personal sector, the main types of collateral are real estate properties, cash deposits and securities. In the commercial and industrial sector, the main types of collateral are real estate properties, securities, receivables, cash deposits and machinery.

For loans guaranteed by a third party, the Group will assess the guarantor's financial condition, credit history and ability to meet obligations.

As at 31 December 2012 and 2011, the Group did not hold any collateral that it was permitted to sell or re-pledge in the absence of default by the borrower.

(A) Credit exposures

The maximum exposure is a worst case scenario of credit risk exposure to the Group without taking into account any collateral held or other credit enhancements. For on-balance sheet assets, the maximum exposure to credit risk equals their carrying amount. For letters of guarantee issued, the maximum exposure to credit risk is the maximum amount that the Group could be required to pay if the guarantees are called upon. For loan commitment and other credit related liabilities, the maximum exposure to credit risk is the full amount of the committed facilities.

The nature of the collateral held and other credit enhancements and their financial effect to the different classes of the Group's financial assets are as follows.

Balances and placements with banks and other financial institutions

These exposures are generally considered to be low risk due to the nature of the counterparties. Collateral is generally not sought on these assets.

Financial assets at fair value through profit or loss and investment in securities

Collateral is generally not sought on debt securities.

Derivative financial instruments

The International Swaps and Derivatives Association Master Agreement is the preferred agreement for documenting derivatives activities of the Group. It provides the contractual framework within which dealing activities of OTC products are conducted, and contractually bind both parties to apply close-out netting on outstanding transactions covered by an agreement if either party defaults or another pre-agreed termination event occurs.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(A) Credit exposures (continued)

Advances and other accounts, contingent liabilities and commitments

The general types of collateral are disclosed on page 140. Advances and other accounts, contingent liabilities and commitments are collateralised to the extent considered appropriate by the Group taking account of the risk assessment of individual exposures. The collateral coverage of advances to customers is analysed on pages 148 to 149. The components and nature of contingent liabilities and commitments are disclosed in Note 45. Regarding the commitments that are unconditionally cancellable without prior notice, the Group would assess the necessity to withdraw the credit line in case where the credit quality of a borrower deteriorates. For contingent liabilities and commitments, 11.4% (2011: 12.9%) is covered by collateral as at 31 December 2012.

(B) Gross advances and other accounts

Gross advances and other accounts before loan impairment allowances are summarised by product type as follows:

	2012 HK\$'m	2011 HK\$'m
Advances to customers		
Personal		
– Mortgages	202,386	185,259
– Credit cards	11,534	9,655
– Others	24,782	20,801
Corporate		
– Commercial loans	472,425	424,156
– Trade finance	67,137	59,508
	778,264	699,379
Trade bills	45,180	56,506
Advances to banks and other financial institutions	–	2,174
Total	823,444	758,059

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.

Advances are 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 advances that can be reliably estimated.

If there is objective evidence that an impairment loss on advances 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 advances. Objective evidence that advances are impaired includes observable data that comes to the attention of the Group about the loss events.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include:

- Significant financial difficulty incurred by the borrower;
- A breach of contract, such as a default or delinquency in interest or principal payment;
- For economic or legal reasons related to the borrower's financial difficulty, the Group has granted to the borrower a concession that it would not otherwise consider;
- Probable that the borrower will become bankrupt or undergo other financial reorganisation; or
- Other observable data indicating that there is a measurable decrease in the estimated future cash flows from such advances.

(a) Advances neither overdue nor impaired

Advances that were neither overdue nor impaired are analysed by internal credit grades as follows:

	2012			
	Pass HK\$'m	Special mention HK\$'m	Substandard or below HK\$'m	Total HK\$'m
Advances to customers				
Personal				
– Mortgages	199,838	242	37	200,117
– Credit cards	11,103	–	–	11,103
– Others	24,193	121	9	24,323
Corporate				
– Commercial loans	465,123	4,693	65	469,881
– Trade finance	66,563	369	–	66,932
	766,820	5,425	111	772,356
Trade bills	45,172	–	–	45,172
Total	811,992	5,425	111	817,528

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(a) Advances neither overdue nor impaired (continued)

	2011			
	Pass HK\$'m	Special mention HK\$'m	Substandard or below HK\$'m	Total HK\$'m
Advances to customers				
Personal				
– Mortgages	183,192	165	53	183,410
– Credit cards	9,395	–	–	9,395
– Others	20,447	117	9	20,573
Corporate				
– Commercial loans	418,412	4,369	98	422,879
– Trade finance	59,127	181	5	59,313
	690,573	4,832	165	695,570
Trade bills	56,103	398	5	56,506
Advances to banks and other financial institutions	2,174	–	–	2,174
Total	748,850	5,230	170	754,250

The occurrence of loss event(s) may not necessarily result in impairment loss where the advances are fully collateralised. While such advances are of “substandard” or lower grades, they are regarded as not being impaired and have been included in the above tables.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(b) Advances overdue but not impaired

The gross amount of advances overdue but not impaired is analysed as follows:

	2012				
	Overdue for three months or less HK\$'m	Overdue for six months or less but over three months HK\$'m	Overdue for one year or less but over six months HK\$'m	Overdue for over one year HK\$'m	Total HK\$'m
Advances to customers					
Personal					
– Mortgages	2,209	13	7	22	2,251
– Credit cards	403	–	–	–	403
– Others	417	2	–	9	428
Corporate					
– Commercial loans	960	6	15	19	1,000
– Trade finance	19	–	–	–	19
	4,008	21	22	50	4,101
Trade bills	8	–	–	–	8
Total	4,016	21	22	50	4,109

	2011				
	Overdue for three months or less HK\$'m	Overdue for six months or less but over three months HK\$'m	Overdue for one year or less but over six months HK\$'m	Overdue for over one year HK\$'m	Total HK\$'m
Advances to customers					
Personal					
– Mortgages	1,825	11	1	3	1,840
– Credit cards	239	–	–	–	239
– Others	181	2	1	10	194
Corporate					
– Commercial loans	1,017	3	1	37	1,058
– Trade finance	36	–	–	3	39
	3,298	16	3	53	3,370
Total	3,298	16	3	53	3,370

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(c) Impaired advances

Advances individually identified to be impaired are analysed by product type as follows:

	2012		2011	
	Gross advances HK\$'m	Market value of collateral HK\$'m	Gross advances HK\$'m	Market value of collateral HK\$'m
Advances to customers				
Personal				
– Mortgages	18	19	9	5
– Credit cards	28	–	21	–
– Others	31	6	34	5
Corporate				
– Commercial loans	1,544	1,315	219	52
– Trade finance	186	86	156	97
Total	1,807	1,426	439	159
Loan impairment allowances made in respect of such advances	768		281	

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

As at 31 December 2012 and 2011, there were no impaired trade bills and advances to banks and other financial institutions.

	2012 HK\$'m	2011 HK\$'m
Current market value of collateral held against the covered portion of such advances to customers	1,426	159
Covered portion of such advances to customers	1,177	108
Uncovered portion of such advances to customers	630	331

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(c) Impaired advances (continued)

Classified or impaired advances to customers are analysed as follows:

	2012 HK\$'m	2011 HK\$'m
Gross classified or impaired advances to customers	2,054	710
Gross classified or impaired advances to customers as a percentage of gross advances to customers	0.26%	0.10%
Individually assessed loan impairment allowances made in respect of such advances	736	259

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

(d) Advances overdue for more than three months

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

	2012		2011	
	Amount HK\$'m	% of gross advances to customers	Amount HK\$'m	% of gross advances to customers
Gross advances to customers which have been overdue for:				
– six months or less but over three months	153	0.02%	78	0.01%
– one year or less but over six months	129	0.02%	83	0.01%
– over one year	323	0.04%	227	0.04%
Advances overdue for over three months	605	0.08%	388	0.06%
Individually assessed loan impairment allowances made in respect of such advances	303		219	

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(d) Advances overdue for more than three months (continued)

	2012 HK\$'m	2011 HK\$'m
Current market value of collateral held against the covered portion of such advances to customers	1,115	468
Covered portion of such advances to customers	253	116
Uncovered portion of such advances to customers	352	272

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

As at 31 December 2012 and 2011, there were no trade bills and advances to banks and other financial institutions overdue for more than three months.

(e) Rescheduled advances

	2012		2011	
	Amount HK\$'m	% of gross advances to customers	Amount HK\$'m	% of gross advances to customers
Rescheduled advances to customers net of amounts included in "Advances overdue for more than three months"	1,119	0.14%	90	0.01%

As at 31 December 2012 and 2011, there were no rescheduled advances to banks and other financial institutions.

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

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers

(i) Sectoral analysis of gross advances to customers

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

	2012					
	Gross advances to customers HK\$'m	% Covered by collateral or other security	Classified or impaired HK\$'m	Overdue* HK\$'m	Individually assessed impairment allowances HK\$'m	Collectively assessed impairment allowances HK\$'m
Loans for use in Hong Kong						
Industrial, commercial and financial						
– Property development	31,408	38.05%	1	2	–	115
– Property investment	76,975	83.98%	49	424	4	458
– Financial concerns	5,984	27.09%	–	3	–	52
– Stockbrokers	1,146	45.39%	–	–	–	11
– Wholesale and retail trade	30,031	57.89%	70	175	33	173
– Manufacturing	21,758	32.25%	53	158	24	125
– Transport and transport equipment	27,241	41.75%	1,104	4	313	166
– Recreational activities	614	21.77%	6	–	6	6
– Information technology	21,369	0.62%	2	2	1	74
– Others	36,351	34.12%	60	264	25	151
Individuals						
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	9,847	99.97%	34	304	–	8
– Loans for purchase of other residential properties	186,601	99.98%	68	1,835	–	110
– Credit card advances	11,534	–	28	431	–	79
– Others	19,894	62.98%	31	290	11	29
Total loans for use in Hong Kong	480,753	69.92%	1,506	3,892	417	1,557
Trade finance	67,137	14.94%	186	202	151	294
Loans for use outside Hong Kong	230,374	26.45%	362	720	168	1,118
Gross advances to customers	778,264	52.31%	2,054	4,814	736	2,969

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

	2011					
	Gross advances to customers HK\$m	% Covered by collateral or other security	Classified or impaired HK\$m	Overdue* HK\$m	Individually assessed impairment allowances HK\$m	Collectively assessed impairment allowances HK\$m
Loans for use in Hong Kong						
Industrial, commercial and financial						
– Property development	30,788	46.81%	3	3	–	112
– Property investment	72,910	85.78%	59	747	6	433
– Financial concerns	10,562	22.52%	–	4	–	58
– Stockbrokers	931	78.93%	–	–	–	3
– Wholesale and retail trade	32,755	69.51%	31	152	13	184
– Manufacturing	17,352	41.95%	67	132	36	115
– Transport and transport equipment	26,525	43.36%	61	4	1	108
– Recreational activities	605	15.87%	–	–	–	3
– Information technology	16,050	0.74%	2	2	1	58
– Others	29,079	41.17%	54	195	24	128
Individuals						
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	10,987	99.96%	48	324	–	9
– Loans for purchase of other residential properties	169,780	99.98%	44	1,443	–	99
– Credit card advances	9,655	–	21	260	–	71
– Others	16,561	62.65%	30	153	13	22
Total loans for use in Hong Kong	444,540	73.09%	420	3,419	94	1,403
Trade finance	59,508	15.85%	166	189	85	281
Loans for use outside Hong Kong	195,331	25.11%	124	184	80	887
Gross advances to customers	699,379	54.82%	710	3,792	259	2,571

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

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

The amount of new impairment allowances charged to the income statement, and classified or impaired loans written off during the year are shown below:

	2012		2011	
	New impairment allowances HK\$'m	Classified or impaired loans written off HK\$'m	New impairment allowances HK\$'m	Classified or impaired loans written off HK\$'m
Loans for use in Hong Kong				
Industrial, commercial and financial				
– Property development	3	–	28	–
– Property investment	34	1	75	1
– Financial concerns	11	–	14	–
– Stockbrokers	8	–	1	–
– Wholesale and retail trade	29	6	62	6
– Manufacturing	22	5	48	6
– Transport and transport equipment	365	–	30	–
– Recreational activities	9	–	1	–
– Information technology	16	–	16	–
– Others	31	6	59	15
Individuals				
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	–	–	1	–
– Loans for purchase of other residential properties	11	–	15	–
– Credit card advances	149	141	103	103
– Others	79	72	43	39
Total loans for use in Hong Kong	767	231	496	170
Trade finance	94	3	135	26
Loans for use outside Hong Kong	311	4	235	25
Gross advances to customers	1,172	238	866	221

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers

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

Gross advances to customers

	2012 HK\$'m	2011 HK\$'m
Hong Kong	607,965	540,862
Mainland China	138,345	121,207
Others	31,954	37,310
	778,264	699,379
Collectively assessed loan impairment allowances in respect of the gross advances to customers		
Hong Kong	2,074	1,855
Mainland China	729	550
Others	166	166
	2,969	2,571

Overdue advances

	2012 HK\$'m	2011 HK\$'m
Hong Kong	3,937	3,506
Mainland China	639	182
Others	238	104
	4,814	3,792
Individually assessed loan impairment allowances in respect of the overdue advances		
Hong Kong	198	187
Mainland China	175	28
Others	33	36
	406	251
Collectively assessed loan impairment allowances in respect of the overdue advances		
Hong Kong	76	57
Mainland China	6	5
Others	3	2
	85	64

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

Classified or impaired advances

	2012 HK\$'m	2011 HK\$'m
Hong Kong	1,631	574
Mainland China	385	79
Others	38	57
	2,054	710
Individually assessed loan impairment allowances in respect of the classified or impaired advances		
Hong Kong	526	193
Mainland China	177	28
Others	33	38
	736	259
Collectively assessed loan impairment allowances in respect of the classified or impaired advances		
Hong Kong	29	21
Mainland China	3	2
Others	1	1
	33	24

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(C) Repossessed assets

During the year, the Group obtained assets by taking possession of collateral held as security. The nature and carrying value of such assets held as at 31 December are summarised as follows:

	2012 HK\$'m	2011 HK\$'m
Commercial properties	–	1
Industrial properties	5	–
Residential properties	12	10
	17	11

The estimated market value of repossessed assets held by the Group as at 31 December 2012 amounted to HK\$27 million (2011: HK\$19 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 proprietors concerned) for release in full or in part of the obligations of the borrowers.

When the repossessed assets are not readily convertible into cash, the Group may consider the following alternatives:

- adjusting the selling prices
- selling the loans together with the assets
- arranging loan restructuring

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(D) Balances and placements with banks and other financial institutions

The following tables present an analysis of balances and placements with banks and other financial institutions that are neither overdue nor impaired as at 31 December by rating agency designation.

	2012			
	Aaa to A3 HK\$m	Lower than A3 HK\$m	Unrated HK\$m	Total HK\$m
Central banks	84,387	–	–	84,387
Banks and other financial institutions	125,082	31,918	16,698	173,698
	209,469	31,918	16,698	258,085

	2011			
	Aaa to A3 HK\$m	Lower than A3 HK\$m	Unrated HK\$m	Total HK\$m
Central banks	158,950	–	–	158,950
Banks and other financial institutions	161,436	15,731	44,163	221,330
	320,386	15,731	44,163	380,280

As at 31 December 2012 and 2011, there were no overdue or impaired balances and placements with banks and other financial institutions.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(E) Debt securities

The following tables present an analysis of the carrying value of debt securities by issue rating. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	2012					
	Aaa HK\$'m	Aa1 to Aa3 HK\$'m	A1 to A3 HK\$'m	Lower than A3 HK\$'m	Unrated HK\$'m	Total HK\$'m
Available-for-sale securities	97,987	142,536	168,142	22,606	19,826	451,097
Held-to-maturity securities	4,828	6,173	5,569	1,319	509	18,398
Loans and receivables	-	-	8,277	-	957	9,234
Financial assets at fair value through profit or loss	16,977	13,842	11,420	1,669	3,351	47,259
Total	119,792	162,551	193,408	25,594	24,643	525,988

	2011					
	Aaa HK\$'m	Aa1 to Aa3 HK\$'m	A1 to A3 HK\$'m	Lower than A3 HK\$'m	Unrated HK\$'m	Total HK\$'m
Available-for-sale securities	90,540	148,444	47,446	11,277	14,192	311,899
Held-to-maturity securities	15,637	26,991	8,973	1,815	511	53,927
Loans and receivables	-	4,797	1,876	-	-	6,673
Financial assets at fair value through profit or loss	3,306	22,730	15,706	1,498	3,263	46,503
Total	109,483	202,962	74,001	14,590	17,966	419,002

As at 31 December 2012, the Group's exposure to MBS/ABS amounted to HK\$12,016 million (2011: HK\$11,614 million), representing 2.3% (2011: 2.8%) of the total debt securities of the Group.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(E) Debt securities (continued)

The following tables present an analysis of debt securities neither overdue nor impaired as at 31 December by issue rating. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	2012					
	Aaa HK\$'m	Aa1 to Aa3 HK\$'m	A1 to A3 HK\$'m	Lower than A3 HK\$'m	Unrated HK\$'m	Total HK\$'m
Available-for-sale securities	97,987	142,536	168,133	22,606	19,826	451,088
Held-to-maturity securities	4,758	6,142	5,568	1,319	509	18,296
Loans and receivables	-	-	8,277	-	957	9,234
Financial assets at fair value through profit or loss	16,977	13,842	11,420	1,669	3,351	47,259
Total	119,722	162,520	193,398	25,594	24,643	525,877

	2011					
	Aaa HK\$'m	Aa1 to Aa3 HK\$'m	A1 to A3 HK\$'m	Lower than A3 HK\$'m	Unrated HK\$'m	Total HK\$'m
Available-for-sale securities	90,521	148,444	47,435	11,265	14,192	311,857
Held-to-maturity securities	15,508	26,957	8,885	1,815	511	53,676
Loans and receivables	-	4,797	1,876	-	-	6,673
Financial assets at fair value through profit or loss	3,306	22,730	15,706	1,498	3,263	46,503
Total	109,335	202,928	73,902	14,578	17,966	418,709

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.1 Credit Risk (continued)

(E) Debt securities (continued)

The following tables present an analysis of impaired debt securities by issue rating. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	2012						
	Carrying values						Of which accumulated impairment allowances HK\$'m
	Aaa HK\$'m	Aa1 to Aa3 HK\$'m	A1 to A3 HK\$'m	Lower than A3 HK\$'m	Unrated HK\$'m	Total HK\$'m	
Available-for-sale securities	–	–	9	–	–	9	1
Held-to-maturity securities	70	31	1	–	–	102	9
Total	70	31	10	–	–	111	10
Of which accumulated impairment allowances	6	3	1	–	–	10	

	2011						
	Carrying values						Of which accumulated impairment allowances HK\$'m
	Aaa HK\$'m	Aa1 to Aa3 HK\$'m	A1 to A3 HK\$'m	Lower than A3 HK\$'m	Unrated HK\$'m	Total HK\$'m	
Available-for-sale securities	19	–	11	12	–	42	2
Held-to-maturity securities	129	34	88	–	–	251	25
Total	148	34	99	12	–	293	27
Of which accumulated impairment allowances	15	4	7	1	–	27	

As at 31 December 2012 and 2011, there were no overdue debt securities.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.2 Market Risk

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

In accordance with the Group's corporate governance principles in respect of risk management, the Board and RC, senior management and functional departments/units perform their duties and responsibilities to manage the Group's market risk. The Market Risk Management Division of the RMD is mainly responsible for managing market risk, assisting senior management to perform their day-to-day duties, independently monitoring the market risk profile and compliance of management policies and limits of the Group and BOCHK, ensuring that the aggregate and individual market risks are within acceptable level.

The Group's market risk management covers BOCHK and its subsidiaries. The Group establishes consistent market risk management policies to regulate BOCHK's and subsidiaries' market risk management; meanwhile, the Group sets up the Group VAR and stress test limits, which are allocated and monitored across the Group, according to subsidiaries' business requirements and risk tolerance levels. In line with the requirements set in the Group policy, the subsidiaries may, subject to prior consent by BOCHK, formulate the detailed policies and procedures and are responsible for managing their daily market risk. The subsidiaries set up independent risk monitoring teams to monitor daily market risk and limit compliance, and submit management information and reports to BOCHK on a regular basis.

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

(A) VAR

The Group uses the VAR to measure and report general market risks to the RC and senior management on a periodic basis. The Group adopts a uniformed VAR calculation model, using historical simulation approach and 2-year historical data, to calculate the VAR of the Group and subsidiaries over 1-day holding period with 99% confidence level, and sets up the VAR limit of the Group and subsidiaries.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.2 Market Risk (continued)

(A) VAR (continued)

The following table sets out the VAR for all general market risk exposure¹ of the Group.

	Year	At 31 December HK\$m	Minimum for the year HK\$m	Maximum for the year HK\$m	Average for the year HK\$m
VAR for all market risk	2012	14.6	14.6	35.1	25.4
	2011	15.5	6.8	20.7	12.2
VAR for foreign exchange risk	2012	9.2	9.2	25.7	16.7
	2011	11.2	2.1	19.1	9.7
VAR for interest rate risk	2012	9.9	8.9	29.5	17.7
	2011	10.4	4.9	10.9	7.8
VAR for equity risk	2012	0.0	0.0	2.3	0.4
	2011	1.0	0.0	1.3	0.1
VAR for commodity risk	2012	0.0	0.0	1.7	0.2
	2011	0.2	0.0	0.7	0.1

In 2012, the average daily revenue² of the Group earned from market risk-related trading activities was HK\$7.2 million (2011: HK\$8.3 million).

Notes:

1 Structural FX positions have been excluded. In 2012, all general market risk exposure are presented on the Group basis, comparative amounts are presented on the same basis accordingly.

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

Although a valuable guide to market 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% 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 formulating stress test indicators and limits to assess and manage the market risk uncovered by VAR. The stress testing programme of the market risk includes sensitivity testing on changes in risk factors with various degrees of severity, as well as scenario analysis on historical events including the 1987 Equity Market Crash, 1994 Bond Market Crash, 1997 Asian Financial Crisis, 2001 9-11 event and 2008 Financial Tsunami, etc.

(B) Currency risk

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

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.2 Market Risk (continued)

(B) Currency risk (continued)

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

	2012							
	Renminbi HK\$'m	US Dollars HK\$'m	HK Dollars HK\$'m	Euro HK\$'m	Japanese Yen HK\$'m	Pound Sterling HK\$'m	Others HK\$'m	Total HK\$'m
Assets								
Cash and balances with banks and other financial institutions	156,693	24,087	12,051	1,796	376	889	2,856	198,748
Placements with banks and other financial institutions maturing between one and twelve months	28,365	31,872	4,525	419	-	201	643	66,025
Financial assets at fair value through profit or loss	5,178	11,273	32,801	-	-	-	80	49,332
Derivative financial instruments	367	5,074	25,871	-	-	-	27	31,339
Hong Kong SAR Government certificates of indebtedness	-	-	82,930	-	-	-	-	82,930
Advances and other accounts	97,641	191,418	517,998	6,125	758	148	5,651	819,739
Investment in securities								
– Available-for-sale securities	61,840	193,050	89,735	8,080	77,766	353	23,908	454,732
– Held-to-maturity securities	948	10,672	2,042	-	1,912	-	2,824	18,398
– Loans and receivables	1,157	5,846	-	-	-	2,231	-	9,234
Interests in associates	-	-	259	-	-	-	-	259
Investment properties	112	-	14,252	-	-	-	-	14,364
Properties, plant and equipment	855	4	47,884	-	-	-	-	48,743
Other assets (including deferred tax assets)	14,982	1,998	18,794	548	226	51	321	36,920
Total assets	368,138	475,294	849,142	16,968	81,038	3,873	36,310	1,830,763
Liabilities								
Hong Kong SAR currency notes in circulation	-	-	82,930	-	-	-	-	82,930
Deposits and balances from banks and other financial institutions	82,762	48,667	45,710	102	50	26	1,889	179,206
Financial liabilities at fair value through profit or loss	776	48	18,525	7	-	6	810	20,172
Derivative financial instruments	382	3,682	16,621	337	-	-	192	21,214
Deposits from customers	234,719	246,065	683,270	11,156	3,393	12,127	35,560	1,226,290
Debt securities in issue at amortised cost	-	5,919	4	-	-	-	-	5,923
Other accounts and provisions (including current and deferred tax liabilities)	9,995	16,162	28,536	645	298	685	941	57,262
Insurance contract liabilities	17,550	6,400	29,987	-	-	-	-	53,937
Subordinated liabilities	-	22,006	-	6,749	-	-	-	28,755
Total liabilities	346,184	348,949	905,583	18,996	3,741	12,844	39,392	1,675,689
Net on-balance sheet position	21,954	126,345	(56,441)	(2,028)	77,297	(8,971)	(3,082)	155,074
Off-balance sheet net notional position*	(12,217)	(105,886)	190,779	1,917	(77,231)	8,714	3,305	9,381
Contingent liabilities and commitments	47,614	90,233	315,496	3,756	538	1,074	5,058	463,769

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.2 Market Risk (continued)

(B) Currency risk (continued)

	2011							
	Renminbi HK\$'m	US Dollars HK\$'m	HK Dollars HK\$'m	Euro HK\$'m	Japanese Yen HK\$'m	Pound Sterling HK\$'m	Others HK\$'m	Total HK\$'m
Assets								
Cash and balances with banks and other financial institutions	222,388	30,932	17,138	1,991	2,390	543	3,413	278,795
Placements with banks and other financial institutions maturing between one and twelve months	93,278	10,689	3,443	-	25	-	475	107,910
Financial assets at fair value through profit or loss	4,547	11,833	32,146	-	-	-	76	48,602
Derivative financial instruments	843	4,586	21,330	4	-	-	24	26,787
Hong Kong SAR Government certificates of indebtedness	-	-	65,890	-	-	-	-	65,890
Advances and other accounts	54,189	214,930	472,415	3,105	1,835	84	8,671	755,229
Investment in securities								
– Available-for-sale securities	27,671	149,143	58,883	9,467	44,335	251	26,648	316,398
– Held-to-maturity securities	17,015	20,522	8,262	1,089	2,125	-	4,914	53,927
– Loans and receivables	-	-	-	1,876	-	4,640	157	6,673
Interests in associates	-	-	234	-	-	-	-	234
Investment properties	106	-	12,335	-	-	-	-	12,441
Properties, plant and equipment	554	1	39,095	-	-	-	-	39,650
Other assets (including deferred tax assets)	9,381	412	15,007	423	381	72	298	25,974
Total assets	429,972	443,048	746,178	17,955	51,091	5,590	44,676	1,738,510
Liabilities								
Hong Kong SAR currency notes in circulation	-	-	65,890	-	-	-	-	65,890
Deposits and balances from banks and other financial institutions	155,582	40,110	38,668	40	181	5	2,108	236,694
Financial liabilities at fair value through profit or loss	203	51	2,665	-	-	-	318	3,237
Derivative financial instruments	886	4,025	16,752	393	1	1	223	22,281
Deposits from customers	245,375	231,136	596,308	13,634	1,756	14,434	43,308	1,145,951
Debt securities in issue at amortised cost	-	5,868	117	-	-	-	-	5,985
Other accounts and provisions (including current and deferred tax liabilities)	5,607	14,309	26,225	670	806	778	1,018	49,413
Insurance contract liabilities	10,728	6,501	29,991	-	-	-	-	47,220
Subordinated liabilities	-	22,031	-	6,625	-	-	-	28,656
Total liabilities	418,381	324,031	776,616	21,362	2,744	15,218	46,975	1,605,327
Net on-balance sheet position	11,591	119,017	(30,438)	(3,407)	48,347	(9,628)	(2,299)	133,183
Off-balance sheet net notional position*	604	(110,908)	148,444	3,118	(48,403)	9,634	2,402	4,891
Contingent liabilities and commitments	25,032	102,857	253,398	3,572	1,158	857	3,311	390,185

* 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.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.2 Market Risk (continued)

(C) Interest rate risk

Interest rate risk means the risks to a bank's earnings and economic value arising from adverse movements in interest rate and term structures of the bank's asset and liability positions. The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

- Repricing risk: mismatches in the maturity or repricing periods of assets and liabilities that may affect net interest income;
- Basis risk: different pricing basis for different transactions so that the yield on assets and cost of liabilities may change by different amounts within the same repricing period;
- Yield curve risk: non-parallel shifts in the yield curve that may have an adverse impact on net interest income or economic value;
- Option risk: exercise of the options embedded in assets, liabilities or off-balance sheet items that can cause a change in the cash flows of assets and liabilities.

The Group's risk management framework applies also to interest rate risk management. The Assets and Liabilities Management Committee ("ALCO") exercises its oversight of interest rate risk in accordance with "BOCHK Group Banking Book Interest Rate Risk Management Policy" approved by RC. Market Risk Management Division of RMD is responsible for interest rate risk management. With the cooperation of the Asset & Liability Management Division of Financial Management Department and Investment Management, RMD assists the ALCO to manage day-to-day interest rate risk positions. Its roles include, but are not limited to, formulation of management policies, selection of methodologies, setting risk indicators and limits, assessment of target balance sheet, monitoring the compliance with policies and limits, and submission of interest rate risk management reports to RC and senior management, etc.

The Group sets out interest rate risk indicators and limits to identify, measure, monitor and control interest rate risk. The indicators and limits include, but are not limited to, repricing gap limits, basis risk, duration, price value of a basis point (PVBP), Greeks, net interest income sensitivity ratio, economic value sensitivity ratio (including sub-limit for AFS securities), etc. The indicators and limits are classified into three levels, which are approved by RC, ALCO and CRO respectively. Risk-taking business units are required to conduct their business within the boundary of the interest rate risk limits. Before launching a new product or business in the banking book, relevant departments are required to go through a risk assessment process, which includes assessment of underlying interest rate risk and consideration of the adequacy of current risk monitoring mechanism. Any material impact on interest rate risk noted during the risk assessment process will be submitted to RC for approval.

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

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.2 Market Risk (continued)

(C) Interest rate risk (continued)

The Group uses scenario analysis and stress test to assess the banking book interest rate risk the Group would face under adverse circumstances. Scenario analysis and stress test are also devised to assess the impact on net interest income and economic value as well as capital base arising from the optionality of demand and savings deposits, the prepayment of mortgage loans and the prepayment of debt securities with embedded options.

The Group is principally exposed to HK Dollar, US Dollar, onshore and offshore Renminbi in terms of interest rate risk. As at 31 December 2012, if HK Dollar, US Dollar and Renminbi market interest rates had a 100 basis point parallel upward shift of the yield curve in relevant currency with other variables held constant, the impacts on net interest income over a twelve-month period and on reserves would have been as follows:

	Impact on net interest income over the next twelve months at 31 December		Impact on reserves at 31 December	
	2012 HK\$'m	2011 HK\$'m	2012 HK\$'m	2011 HK\$'m
HK Dollar	744	896	(402)	(219)
US Dollar	(834)	(589)	(5,390)	(4,025)
Renminbi	(529)	(560)	(1,128)	(433)

The overall negative impact on net interest income of the above currencies has increased when compared with 2011 and is mainly because of the widened short term negative gaps in relevant currencies. Reserves would have been reduced because of the expected reduction in valuation of available-for-sale portfolio due to the above simulated market rates movement. The reduction of reserves is larger compared with 2011 because the size and duration of available-for-sale portfolio is increased.

The Group uses more severe assumptions when conducting stress test, including a change in the correlation between interest rates of relevant currencies, parallel movement of interest rates, and that in the absence of actions that would be taken to mitigate the impact of interest rates shock, all positions are assumed to run to maturity and reprice or mature simultaneously within a given time band. 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.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.2 Market Risk (continued)

(C) Interest rate risk (continued)

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

	2012						
	Up to 1 month HK\$m	1-3 months HK\$m	3-12 months HK\$m	1-5 years HK\$m	Over 5 years HK\$m	Non- interest bearing HK\$m	Total HK\$m
Assets							
Cash and balances with banks and other financial institutions	188,266	-	-	-	-	10,482	198,748
Placements with banks and other financial institutions maturing between one and twelve months	-	24,152	41,873	-	-	-	66,025
Financial assets at fair value through profit or loss	11,403	4,853	6,732	17,257	7,014	2,073	49,332
Derivative financial instruments	-	-	-	-	-	31,339	31,339
Hong Kong SAR Government certificates of indebtedness	-	-	-	-	-	82,930	82,930
Advances and other accounts	620,505	118,455	64,651	9,495	22	6,611	819,739
Investment in securities							
– Available-for-sale securities	69,387	117,085	66,886	131,589	66,150	3,635	454,732
– Held-to-maturity securities	2,600	5,666	811	7,402	1,919	-	18,398
– Loans and receivables	-	1,558	7,676	-	-	-	9,234
Interests in associates	-	-	-	-	-	259	259
Investment properties	-	-	-	-	-	14,364	14,364
Properties, plant and equipment	-	-	-	-	-	48,743	48,743
Other assets (including deferred tax assets)	-	-	-	-	-	36,920	36,920
Total assets	892,161	271,769	188,629	165,743	75,105	237,356	1,830,763
Liabilities							
Hong Kong SAR currency notes in circulation	-	-	-	-	-	82,930	82,930
Deposits and balances from banks and other financial institutions	159,083	1,483	208	-	-	18,432	179,206
Financial liabilities at fair value through profit or loss	10,017	6,286	3,475	255	139	-	20,172
Derivative financial instruments	-	-	-	-	-	21,214	21,214
Deposits from customers	919,431	129,374	110,938	5,969	38	60,540	1,226,290
Debt securities in issue at amortised cost	4	-	-	5,919	-	-	5,923
Other accounts and provisions (including current and deferred tax liabilities)	13,990	1,710	3,350	25	-	38,187	57,262
Insurance contract liabilities	-	-	-	-	-	53,937	53,937
Subordinated liabilities	-	-	6,749	-	22,006	-	28,755
Total liabilities	1,102,525	138,853	124,720	12,168	22,183	275,240	1,675,689
Interest sensitivity gap	(210,364)	132,916	63,909	153,575	52,922	(37,884)	155,074

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.2 Market Risk (continued)

(C) Interest rate risk (continued)

	2011						
	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	Non- interest bearing HK\$'m	Total HK\$'m
Assets							
Cash and balances with banks and other financial institutions	269,960	–	–	–	–	8,835	278,795
Placements with banks and other financial institutions maturing between one and twelve months	–	48,637	59,273	–	–	–	107,910
Financial assets at fair value through profit or loss	5,732	10,339	5,474	13,080	11,878	2,099	48,602
Derivative financial instruments	–	–	–	–	–	26,787	26,787
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	65,890	65,890
Advances and other accounts	554,348	128,984	54,042	12,563	31	5,261	755,229
Investment in securities							
– Available-for-sale securities	60,433	64,432	42,885	97,200	46,949	4,499	316,398
– Held-to-maturity securities	5,336	14,862	8,299	17,992	7,438	–	53,927
– Loans and receivables	2,033	–	4,640	–	–	–	6,673
Interests in associates	–	–	–	–	–	234	234
Investment properties	–	–	–	–	–	12,441	12,441
Properties, plant and equipment	–	–	–	–	–	39,650	39,650
Other assets (including deferred tax assets)	–	–	–	–	–	25,974	25,974
Total assets	897,842	267,254	174,613	140,835	66,296	191,670	1,738,510
Liabilities							
Hong Kong SAR currency notes in circulation	–	–	–	–	–	65,890	65,890
Deposits and balances from banks and other financial institutions	211,777	1,807	1,429	–	–	21,681	236,694
Financial liabilities at fair value through profit or loss	1,116	802	824	473	22	–	3,237
Derivative financial instruments	–	–	–	–	–	22,281	22,281
Deposits from customers	867,556	138,977	74,731	9,134	162	55,391	1,145,951
Debt securities in issue at amortised cost	96	20	13	5,856	–	–	5,985
Other accounts and provisions (including current and deferred tax liabilities)	13,137	1,001	2,849	–	–	32,426	49,413
Insurance contract liabilities	–	–	–	–	–	47,220	47,220
Subordinated liabilities	–	–	6,625	–	22,031	–	28,656
Total liabilities	1,093,682	142,607	86,471	15,463	22,215	244,889	1,605,327
Interest sensitivity gap	(195,840)	124,647	88,142	125,372	44,081	(53,219)	133,183

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk

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

The Group's liquidity risk management objective is to effectively manage the liquidity of on-balance sheet and off-balance sheet items with reasonable cost based on the liquidity risk appetite to achieve sound operation and sustainable profitability. Customer deposits are the Group's primary source of funds. To ensure stable and sufficient source of funds are in place, the Group actively attracts new deposits, keeps the core deposit and obtains supplementary funding from interbank market or by issuing bills in the capital market. According to different term maturities and the results of funding needs estimated from stressed scenarios, the Group adjusts its asset structure (including loans, bonds investment, interbank placement, etc.) to maintain sufficient liquid assets in support of normal business needs and ensure its ability to raise enough funds at a reasonable cost to serve external claims in case of emergency. The Group is committed to diversify the source of funds and the use of funds to avoid excessive concentration of assets and liabilities and prevent triggering liquidity risk due to the break of funding strand when problem occurred in one concentrated funding source. The Group has established intragroup liquidity risk management guideline to manage the liquidity funding among different entities within the Group, to restrict their reliance of funding on each other. The Group also pays attention to manage liquidity risk created by off-balance sheet activities, such as loan commitments, derivatives, options and other complex structured products. The Group has overall liquidity risk management strategy to cover the liquidity management of foreign currency assets and liabilities, collaterals, intra-day liquidity, intra-group liquidity, the liquidity risk arising from other risks, etc., and has formulated corresponding contingency plan.

RC, a standing committee established by the Board of Directors, is the decision making authority of liquidity risk management, and assumes the ultimate responsibility of liquidity risk management. As authorised by RC, ALCO exercises its oversight of liquidity risk and ensures the daily operations of the Group are in accordance with risk appetite and policies as set by RC. Market Risk Management Division of RMD is responsible for overseeing the Group's liquidity risk. It cooperates with the Asset and Liability Management Division of Financial Management Department, Investment Management, etc. to assist the ALCO to perform liquidity management functions according to their specific responsibilities.

The Group established liquidity risk management indicators and limits to identify, measure, monitor and control liquidity risk on daily basis. Such indicators and limits include, but are not limited to liquidity ratio, loan-to-deposit ratio, Maximum Cumulative Outflow ("MCO") and liquidity buffer asset portfolio. The Group applies cash flow analysis to assess the Group's liquidity condition under normal conditions and also performs liquidity stress test (including institution specific and world wide crisis) and other methods at least on monthly basis to assess the Group's capability to withstand various severe liquidity crises. Also, Assets and Liabilities Management System is developed to provide data and the preparation for regular management reports to facilitate the liquidity risk management duties.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

In accordance with the requirements of Supervisory Policy Manual LM-2 “Sound Systems and controls for Liquidity Risk Management” issued by the HKMA in 2011, the Group has embarked to refine the behavior model and assumptions of existing cash flow analysis and stress test to enhance the Group’s cash flow analysis under both normal and stressed conditions. In cash flow analysis under normal circumstances, assumptions applied to on-balance sheet items such as customer deposits and off-balance sheet items such as loan commitments are being modified. In liquidity stress test, a new combined scenario which is a combination of institution specific and world wide crisis is being set up to assess the Group’s capability to withstand a more severe liquidity crisis, with a more stringent set of assumptions adopted. In addition, the Group has a policy in place to maintain an asset buffer portfolio which includes high quality marketable securities to ensure funding needs even under stressed scenarios. The contingency plan is being established which detailed the conditions to trigger the plan based on stress test results and early warning indicators, the action plans and relevant procedures and responsibility of various departments.

The Group’s liquidity risk management also covers new product or business development. Before launching a new product or business, the relevant departments are required to go through a risk assessment process, which includes the assessment of underlying liquidity risk and consideration of the adequacy of the current risk management mechanism. Any material impact on liquidity risk noted during the risk assessment process will be reported to RC for approval.

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

(A) Liquidity ratio

	2012	2011
Average liquidity ratio	41.20%	36.17%

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

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

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(B) Maturity analysis

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

	2012							Total HK\$'m
	On demand HK\$'m	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	Indefinite HK\$'m	
Assets								
Cash and balances with banks and other financial institutions	145,534	53,214	-	-	-	-	-	198,748
Placements with banks and other financial institutions maturing between one and twelve months	-	-	24,152	41,873	-	-	-	66,025
Financial assets at fair value through profit or loss								
– debt securities held for trading								
– certificates of deposit held	-	67	64	14	-	-	-	145
– others	-	11,075	3,855	3,454	6,585	4,159	-	29,128
– debt securities designated at fair value through profit or loss								
– certificates of deposit held	-	-	509	310	378	-	-	1,197
– others	-	31	369	2,350	11,207	2,832	-	16,789
– fund and equity securities	-	-	-	-	-	-	2,073	2,073
Derivative financial instruments	17,690	2,535	2,032	3,421	1,600	4,061	-	31,339
Hong Kong SAR Government certificates of indebtedness	82,930	-	-	-	-	-	-	82,930
Advances and other accounts								
– advances to customers	60,076	19,055	53,963	138,157	288,680	213,106	1,522	774,559
– trade bills	76	10,150	15,765	19,189	-	-	-	45,180
– advances to banks and other financial institutions	-	-	-	-	-	-	-	-
Investment in securities								
– debt securities held for available-for-sale								
– certificates of deposit held	-	3,001	15,580	45,533	8,708	19	-	72,841
– others	-	49,064	76,254	40,775	143,730	68,424	9	378,256
– debt securities held for held-to-maturity								
– certificates of deposit held	-	465	-	332	77	-	-	874
– others	-	430	2,822	3,792	8,276	2,102	102	17,524
– debt securities held for loans and receivables	-	-	1,558	7,676	-	-	-	9,234
– equity securities	-	-	-	-	-	-	3,635	3,635
Interests in associates	-	-	-	-	-	-	259	259
Investment properties	-	-	-	-	-	-	14,364	14,364
Properties, plant and equipment	-	-	-	-	-	-	48,743	48,743
Other assets (including deferred tax assets)	10,563	13,904	73	47	8,857	3,452	24	36,920
Total assets	316,869	162,991	196,996	306,923	478,098	298,155	70,731	1,830,763
Liabilities								
Hong Kong SAR currency notes in circulation	82,930	-	-	-	-	-	-	82,930
Deposits and balances from banks and other financial institutions	140,245	37,270	1,483	208	-	-	-	179,206
Financial liabilities at fair value through profit or loss								
– certificates of deposit issued	-	-	-	-	-	-	-	-
– others	-	10,017	6,287	3,475	254	139	-	20,172
Derivative financial instruments	13,022	668	865	1,766	3,602	1,291	-	21,214
Deposits from customers	701,678	276,068	129,269	111,327	7,910	38	-	1,226,290
Debt securities in issue at amortised cost	-	4	-	32	5,887	-	-	5,923
Other accounts and provisions (including current and deferred tax liabilities)	28,005	14,148	2,999	4,545	7,559	6	-	57,262
Insurance contract liabilities	3,281	493	3,068	1,070	24,655	21,370	-	53,937
Subordinated liabilities	-	-	418	-	-	28,337	-	28,755
Total liabilities	969,161	338,668	144,389	122,423	49,867	51,181	-	1,675,689
Net liquidity gap	(652,292)	(175,677)	52,607	184,500	428,231	246,974	70,731	155,074

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

	2011							
	On demand HK\$'m	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	Indefinite HK\$'m	Total HK\$'m
Assets								
Cash and balances with banks and other financial institutions	213,787	65,008	-	-	-	-	-	278,795
Placements with banks and other financial institutions maturing between one and twelve months	-	-	48,637	59,273	-	-	-	107,910
Financial assets at fair value through profit or loss								
- debt securities held for trading								
- certificates of deposit held	-	-	-	15	62	-	-	77
- others	-	5,052	9,587	2,740	2,944	4,633	-	24,956
- debt securities designated at fair value through profit or loss								
- certificates of deposit held	-	-	8	7	927	496	-	1,438
- others	-	282	301	2,672	9,661	7,116	-	20,032
- fund and equity securities	-	-	-	-	-	-	2,099	2,099
Derivative financial instruments	18,640	541	732	1,341	1,934	3,599	-	26,787
Hong Kong SAR Government certificates of indebtedness	65,890	-	-	-	-	-	-	65,890
Advances and other accounts								
- advances to customers	55,319	21,353	52,703	140,462	232,840	193,258	614	696,549
- trade bills	31	10,577	21,847	24,046	-	-	5	56,506
- advances to banks and other financial institutions	-	-	155	2,019	-	-	-	2,174
Investment in securities								
- debt securities held for available-for-sale								
- certificates of deposit held	-	3,170	2,316	12,561	9,495	-	-	27,542
- others	-	43,824	44,025	40,829	105,225	50,412	42	284,357
- debt securities held for held-to-maturity								
- certificates of deposit held	-	226	192	2,293	333	-	-	3,044
- others	-	1,510	5,251	10,853	24,187	8,831	251	50,883
- debt securities held for loans and receivables	-	2,033	-	4,640	-	-	-	6,673
- equity securities	-	-	-	-	-	-	4,499	4,499
Interests in associates	-	-	-	-	-	-	234	234
Investment properties	-	-	-	-	-	-	12,441	12,441
Properties, plant and equipment	-	-	-	-	-	-	39,650	39,650
Other assets (including deferred tax assets)	8,749	8,548	21	152	7,350	1,126	28	25,974
Total assets	362,416	162,124	185,775	303,903	394,958	269,471	59,863	1,738,510
Liabilities								
Hong Kong SAR currency notes in circulation	65,890	-	-	-	-	-	-	65,890
Deposits and balances from banks and other financial institutions	216,490	16,968	1,801	1,435	-	-	-	236,694
Financial liabilities at fair value through profit or loss								
- certificates of deposit issued	-	-	-	-	-	-	-	-
- others	-	1,116	802	825	472	22	-	3,237
Derivative financial instruments	13,661	700	771	1,491	3,945	1,713	-	22,281
Deposits from customers	583,005	337,186	137,991	76,830	10,777	162	-	1,145,951
Debt securities in issue at amortised cost	-	96	20	45	5,824	-	-	5,985
Other accounts and provisions (including current and deferred tax liabilities)	30,772	6,137	2,191	4,423	5,890	-	-	49,413
Insurance contract liabilities	1,530	729	866	4,379	26,458	13,258	-	47,220
Subordinated liabilities	-	-	419	1	-	28,236	-	28,656
Total liabilities	911,348	362,932	144,861	89,429	53,366	43,391	-	1,605,327
Net liquidity gap	(548,932)	(200,808)	40,914	214,474	341,592	226,080	59,863	133,183

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(B) Maturity analysis (continued)

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

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

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

(C) Analysis of undiscounted cash flows by contractual maturities

(a) Non-derivative cash flows

The tables below summarise the cash flows of the Group as at 31 December for non-derivative financial liabilities by remaining contractual maturities.

	2012					Total HK\$'m
	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	
Financial liabilities						
Hong Kong SAR currency notes in circulation	82,930	-	-	-	-	82,930
Deposits and balances from banks and other financial institutions	177,516	1,489	221	-	-	179,226
Financial liabilities at fair value through profit or loss	10,018	6,293	3,480	261	137	20,189
Deposits from customers	977,873	129,624	112,716	8,945	53	1,229,211
Debt securities in issue at amortised cost	4	-	218	6,467	-	6,689
Subordinated liabilities	-	538	618	4,622	28,854	34,632
Other financial liabilities	28,700	2,021	3,439	38	6	34,204
Total financial liabilities	1,277,041	139,965	120,692	20,333	29,050	1,587,081

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(a) Non-derivative cash flows (continued)

	2011					
	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	Total HK\$'m
Financial liabilities						
Hong Kong SAR currency notes in circulation	65,890	–	–	–	–	65,890
Deposits and balances from banks and other financial institutions	233,472	1,840	1,450	–	–	236,762
Financial liabilities at fair value through profit or loss	1,116	804	829	477	22	3,248
Deposits from customers	920,349	138,367	77,730	11,752	220	1,148,418
Debt securities in issue at amortised cost	97	21	231	6,701	–	7,050
Subordinated liabilities	–	539	707	4,983	30,069	36,298
Other financial liabilities	29,580	1,312	3,269	6	–	34,167
Total financial liabilities	1,250,504	142,883	84,216	23,919	30,311	1,531,833

(b) Derivative cash flows

(i) Derivatives settled on a net basis

The Group's derivatives that will be settled on a net basis include:

- Exchange rate contracts: non-deliverable OTC currency options, currency futures, non-deliverable currency forwards;
- Interest rate contracts: interest rate swaps;
- Commodity contracts: bullion margin contracts; and
- Equity contracts: exchange traded equity options and equity linked swaps.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(b) Derivative cash flows (continued)

(i) Derivatives settled on a net basis (continued)

The tables below analyse the Group's derivative financial instruments as at 31 December that will be settled on a net basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the tables are the net contractual undiscounted cash flows of derivatives with net negative fair value.

	2012					
	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	Total HK\$'m
Exchange rate contracts	(12,527)	(33)	(84)	-	-	(12,644)
Interest rate contracts	(134)	(343)	(1,299)	(3,153)	(55)	(4,984)
Commodity contracts	(487)	-	-	-	-	(487)
Equity contracts	(3)	-	-	-	-	(3)
	(13,151)	(376)	(1,383)	(3,153)	(55)	(18,118)

	2011					
	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	Total HK\$'m
Exchange rate contracts	(13,030)	(223)	(236)	24	-	(13,465)
Interest rate contracts	(154)	(357)	(1,572)	(3,724)	(192)	(5,999)
Commodity contracts	(717)	-	-	-	-	(717)
Equity contracts	-	(1)	-	-	-	(1)
	(13,901)	(581)	(1,808)	(3,700)	(192)	(20,182)

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(b) Derivative cash flows (continued)

(ii) Derivatives settled on a gross basis

The Group's derivatives that will be settled on a gross basis include OTC currency options, currency forwards, cross currency interest rate swaps, bullion swaps and OTC equity options.

The tables below analyse the Group's derivative financial instruments as at 31 December that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the tables are the gross contractual undiscounted cash flows for all derivatives that are settled on a gross basis.

	2012					
	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	Total HK\$'m
Exchange rate contracts:						
– Outflow	(284,426)	(180,744)	(292,998)	(37,187)	(1,200)	(796,555)
– Inflow	286,321	181,986	294,599	37,191	1,201	801,298
Commodity contracts:						
– Outflow	(4,024)	–	–	–	–	(4,024)
– Inflow	–	–	–	–	–	–
Equity contracts:						
– Outflow	–	–	–	–	–	–
– Inflow	2	–	–	–	–	2
Total outflow	(288,450)	(180,744)	(292,998)	(37,187)	(1,200)	(800,579)
Total inflow	286,323	181,986	294,599	37,191	1,201	801,300

	2011					
	Up to 1 month HK\$'m	1-3 months HK\$'m	3-12 months HK\$'m	1-5 years HK\$'m	Over 5 years HK\$'m	Total HK\$'m
Exchange rate contracts:						
– Outflow	(235,421)	(91,921)	(138,311)	(22,614)	(964)	(489,231)
– Inflow	235,286	91,899	138,285	22,619	962	489,051
Commodity contracts:						
– Outflow	(3,792)	–	–	–	–	(3,792)
– Inflow	–	–	–	–	–	–
Equity contracts:						
– Outflow	(1)	–	–	–	–	(1)
– Inflow	8	1	–	–	–	9
Total outflow	(239,214)	(91,921)	(138,311)	(22,614)	(964)	(493,024)
Total inflow	235,294	91,900	138,285	22,619	962	489,060

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.3 Liquidity Risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(c) Off-balance sheet items

Loan commitments

The contractual amounts of the Group's off-balance sheet financial instruments as at 31 December 2012 that the Group commits to extend credit to customers and other facilities amounting to HK\$392,508 million (2011: HK\$319,768 million). Those loan commitments can be drawn within 1 year.

Financial guarantees and other financial facilities

Financial guarantees and other financial facilities of the Group as at 31 December 2012 amounting to HK\$71,261 million (2011: HK\$70,417 million) are maturing no later than 1 year.

4.4 Insurance Risk

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

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 on 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, whole life 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 to reinsurer under an excess of loss reinsurance arrangement. For some of the insurance liabilities denominated in Renminbi, the Group has entered into reinsurance arrangements that reinsure most of insurance risk.

Uncertainty in the estimation of future benefit payments and premium receipts for long-term insurance contracts arises from the unpredictability of long-term changes in overall levels of mortality, morbidity and persistency. The Group conducted relevant experience studies. The results of the studies are considered in determining the assumptions which include appropriate level of prudential margins.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.5 Capital Management

The major objective of the Group's capital management is to maximise total shareholders' return while maintaining a capital adequacy position in relation to the Group's overall risk profile. The ALCO periodically reviews the Group's capital structure and adjusts the capital mix where appropriate to maintain an optimal balance among risk, return and capital adequacy.

The Group has developed and maintained a sound framework of policies and controls on capital management to support the development of the Group's business and to meet the statutory capital adequacy ratio. The ALCO monitors the Group's capital adequacy. The Group has complied with all the statutory capital requirements of the HKMA for the reported periods in respect of banking operation as further elaborated below.

The Group has adopted the foundation internal ratings-based ("FIRB") approach to calculate the credit risk capital charge for its non-securitisation exposures and internal ratings-based (securitisation) approach to calculate the credit risk capital charge for its securitisation exposures. A small residual credit exposures was approved by HKMA to be exempted from FIRB approach and remained under standardised (credit risk) ("STC") approach.

Since October 2012, the HKMA has approved the Group to adopt the internal models ("IMM") approach to calculate general market risk capital charge for foreign exchange and interest rate exposures and exclude its structural FX positions arising from Nanyang and Chiyu in the calculation of the market risk capital charge. The Group continues to adopt the standardised (market risk) ("STM") approach to calculate the market risk capital charge for remaining exposures.

The Group continues to adopt standardised (operational risk) ("STO") approach to calculate the minimum capital requirement for operational risk in year 2012.

In order to implement Basel II Enhancements, the Banking (Capital) (Amendment) Rules 2011 became effective on 1 January 2012. The amendments were mainly to revise the market risk framework and incorporate other enhancements to the Basel II framework. The Group has calculated the capital charge according to the related regulatory requirements.

The Group has continued to adopt an internal capital adequacy assessment process ("ICAAP") to comply with the HKMA's requirements in the Supervisory Policy Manual "Supervisory Review Process" in 2012. Based on the HKMA's guidelines on Pillar II, ICAAP has been initiated to assess the extra capital needed to cover the material risks not captured under Pillar I, and therefore minimum common equity CAR, minimum core CAR and the minimum CAR are determined. The Group considers this ICAAP process as an on-going process for capital management and periodically reviews and adjusts its capital structure where appropriate in relation to the overall risk profile.

In addition, the capital plan of the Group is drawn up annually and then submitted to the Board for approval after endorsement of the ALCO. The plan is built up by assessing the implications of various factors upon capital adequacy such as the business strategies, return on equity, risk appetite, credit rating, as well as regulatory requirements. Hence, the future capital requirement is determined and capital sources are identified also. The plan is to ensure the Group's capital adequacy and achieve optimal capital structure in order to align with its business development needs and risk profile.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.5 Capital Management (continued)

As a result of the change in the bases of regulatory capital calculation, the amounts shown below are not directly comparable.

(A) Capital adequacy ratio

	2012	2011
Capital adequacy ratio	16.80%	16.90%
Core capital ratio	12.31%	12.51%

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 264.

(B) Components of capital base after deductions

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

	2012 HK\$m	2011 HK\$m
Core capital:		
Paid up ordinary share capital	43,043	43,043
Reserves	38,987	31,947
Profit and loss account	5,820	8,318
Non-controlling interests	1,658	1,605
Deductible item	(25)	–
	89,483	84,913
Deductions from core capital	(387)	(313)
Core capital	89,096	84,600
Supplementary capital:		
Fair value gains arising from holdings of available-for-sale securities	2,067	290
Fair value gains arising from holdings of securities designated at fair value through profit or loss	35	18
Collective loan impairment allowances	192	91
Regulatory reserve	539	253
Surplus provisions	3,963	3,354
Term subordinated debt	26,043	25,961
	32,839	29,967
Deductions from supplementary capital	(387)	(313)
Supplementary capital	32,452	29,654
Total capital base after deductions	121,548	114,254

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.5 Capital Management (continued)

(B) Components of capital base after deductions (continued)

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 261 to 264. 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.

4.6 Fair values of financial assets and liabilities

(A) Financial instruments not measured at fair value

Fair value estimates are made at a specific point in time based on relevant market information and information about various financial instruments. The following methods and assumptions have been used to estimate the fair value of each class of financial instrument as far as practicable.

Balances with banks and other financial institutions and Trade bills

The maturities of these financial assets and liabilities are within one year and the carrying value approximates fair value.

Advances to customers, banks and other financial institutions

Substantially all the advances to customers, banks and other financial institutions are on floating rate terms, bear interest at prevailing market interest rates and their carrying value approximates fair value.

Held-to-maturity securities

Fair value for held-to-maturity securities is based on market prices or broker/dealer price quotations. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics. Their carrying value approximates fair value.

Loans and receivables

A discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity and their carrying value approximates fair value.

Deposits from customers

Substantially all the deposits from customers mature within one year from the balance sheet date and their carrying value approximates fair value.

Debt securities in issue at amortised cost

Fair value for senior notes and other debt securities in issue is based on market prices or broker/dealer price quotations. The carrying value and fair value of senior notes as at 31 December 2012 amounted to HK\$5,919 million (2011: HK\$5,856 million) and HK\$6,317 million (2011: HK\$6,007 million) respectively. The carrying value of other debt securities in issue approximates fair value.

Subordinated liabilities

The subordinated loans are on floating rate terms, bear interest at prevailing market interest rates and their carrying value approximates fair value. Fair value for subordinated notes is based on market prices or broker/dealer price quotations and their carrying value approximates fair value.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.6 Fair values of financial assets and liabilities (continued)

(B) Financial instruments measured at fair value

The Group has an established governance structure and controls framework to ensure that fair values are either determined or validated by control units independent of the front offices. Control units have overall responsibility for independent verification of results from Global Market and Investment Management and all other significant fair value measurements. Specific controls include verification of observable pricing inputs; review and approval for new models and changes to models; calibration and back-testing of models against observed market transactions; analysis and investigation of significant daily valuation movements; review of significant unobservable inputs and valuation adjustments. Significant valuation issues are reported to senior management, Risk Committee and Audit Committee.

Financial instruments measured at fair value are classified into following three levels:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities, including listed equity securities on exchange, debt instruments issued by certain governments and certain foreign exchange derivative contracts.
- Level 2: Valuation technique using inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly. This level includes the majority of the OTC derivative contracts, debt securities with quote from pricing services providers and issued structured deposits.
- Level 3: Valuation technique using inputs for the asset or liability that is not based on observable market data (unobservable inputs). This level includes equity investment and debt instruments with significant unobservable components.

The Group uses valuation techniques or broker/dealer quotations to determine the fair value of financial instruments when unable to obtain the open market quotation in active markets.

The main parameters used in valuation techniques for financial instruments held by the Group include bond prices, interest rates, foreign exchange rates, equity and stock prices, volatilities, counterparty credit spreads and others, which are all observable and obtainable from open market.

For securitisation assets and re-securitisation assets, external prices are obtained from independent third parties. The valuation of security, depending on the nature of transaction, is estimated from market standard cash flow models with input parameter assumptions which include spreads to discount rates, default and recovery rates and prepayment rates that may be observable or unobservable.

For certain illiquid debt securities held by the Group, management obtains valuation quotations from counterparties. The fair value of these financial instruments may be based on unobservable inputs which may have significant impact on the valuation of these financial instruments, and therefore, these instruments have been classified by the Group as level 3. The Group has established internal control procedures to control the Group's exposure to such financial instruments.

There have been no significant transfers between level 1 and 2 during the year 2012 and 2011.

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.6 Fair values of financial assets and liabilities (continued)

(B) Financial instruments measured at fair value (continued)

(i) Fair value hierarchy

	2012			
	Level 1 HK\$m	Level 2 HK\$m	Level 3 HK\$m	Total HK\$m
Financial assets				
Financial assets at fair value through profit or loss				
– Trading securities				
– Debt securities	–	29,273	–	29,273
– Equity securities	13	212	–	225
– Financial assets designated at fair value through profit or loss				
– Debt securities	414	17,239	333	17,986
– Fund	636	–	–	636
– Equity securities	1,212	–	–	1,212
Derivative financial instruments	17,677	13,662	–	31,339
Available-for-sale securities				
– Debt securities	98,350	350,110	2,637	451,097
– Equity securities	2,592	838	205	3,635
Financial liabilities				
Financial liabilities at fair value through profit or loss				
– Trading liabilities	–	17,331	–	17,331
– Financial liabilities designated at fair value through profit or loss	–	2,070	771	2,841
Derivative financial instruments	13,004	8,210	–	21,214

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.6 Fair values of financial assets and liabilities (continued)

(B) Financial instruments measured at fair value (continued)

(i) Fair value hierarchy (continued)

	2011			
	Level 1 HK\$'m	Level 2 HK\$'m	Level 3 HK\$'m	Total HK\$'m
Financial assets				
Financial assets at fair value through profit or loss				
– Trading securities				
– Debt securities	–	25,033	–	25,033
– Equity securities	12	161	–	173
– Financial assets designated at fair value through profit or loss				
– Debt securities	–	21,336	134	21,470
– Fund	1,103	–	–	1,103
– Equity securities	823	–	–	823
Derivative financial instruments	18,611	8,176	–	26,787
Available-for-sale securities				
– Debt securities	65,235	243,842	2,822	311,899
– Equity securities	3,752	563	184	4,499
Financial liabilities				
Financial liabilities at fair value through profit or loss				
– Trading liabilities	–	2,598	–	2,598
– Financial liabilities designated at fair value through profit or loss	–	436	203	639
Derivative financial instruments	13,655	8,626	–	22,281

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.6 Fair values of financial assets and liabilities (continued)

(B) Financial instruments measured at fair value (continued)

(ii) Reconciliation of level 3 items

	2012				
	Financial assets				Financial liabilities
	Financial assets designated at fair value through profit or loss		Available-for-sale securities		Financial liabilities designated at fair value through profit or loss
	Trading securities	Debt securities	Debt securities	Equity securities	
HK\$m	HK\$m	HK\$m	HK\$m	HK\$m	
At 1 January 2012	-	134	2,822	184	203
Gains/(losses)					
– Profit or loss	-	33	-	-	-
– Other comprehensive income	-	-	(10)	21	-
Purchases	-	-	1,860	-	-
Issues	-	-	-	-	771
Sales	-	(5)	(179)	-	-
Settlements	-	-	-	-	(203)
Transfers into/(out) of level 3	-	171	(1,856)	-	-
At 31 December 2012	-	333	2,637	205	771
Total gains for the year included in profit or loss for financial assets and liabilities held as at 31 December 2012	-	33	-	-	-

NOTES TO THE FINANCIAL STATEMENTS

4. Financial risk management (continued)

4.6 Fair values of financial assets and liabilities (continued)

(B) Financial instruments measured at fair value (continued)

(ii) Reconciliation of level 3 items (continued)

	2011				
	Financial assets				Financial liabilities
	Trading securities	Financial assets designated at fair value through profit or loss		Available-for-sale securities	Financial liabilities designated at fair value through profit or loss
		Debt securities HK\$'m	Debt securities HK\$'m		
	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m
At 1 January 2011	100	263	5,955	166	–
(Losses)/gains					
– Profit or loss	–	(10)	(30)	–	–
– Other comprehensive income	–	–	(21)	18	–
Purchases	–	–	1,812	10	–
Issues	–	–	–	–	203
Sales	(100)	(119)	(3,379)	(10)	–
Transfers out of level 3	–	–	(1,515)	–	–
At 31 December 2011	–	134	2,822	184	203
Total losses for the year included in profit or loss for financial assets and liabilities held as at 31 December 2011	–	(10)	–	–	–

Gains/(losses) included in profit or loss for the year as well as gains/(losses) relating to financial assets and liabilities held as at year end are presented in “Net trading gain”, “Net gain/(loss) on financial instruments designated at fair value through profit or loss” or “Net charge of impairment allowances” depending on the nature or the category of the related financial instruments.

NOTES TO THE FINANCIAL STATEMENTS

5. Net interest income

	2012 HK\$'m	2011 HK\$'m
Interest income		
Due from banks and other financial institutions	8,168	8,455
Advances to customers	17,222	13,386
Listed investments	4,542	4,470
Unlisted investments	5,231	5,387
Others	250	233
	35,413	31,931
Interest expense		
Due to banks and other financial institutions	(971)	(2,917)
Deposits from customers	(9,013)	(6,275)
Debt securities in issue	(161)	(26)
Subordinated liabilities	(313)	(562)
Others	(247)	(172)
	(10,705)	(9,952)
Net interest income	24,708	21,979

Included within interest income is HK\$10 million (2011: HK\$3 million) of interest with respect to income recognised on advances classified as impaired for the year ended 31 December 2012. Interest income accrued on impaired investment in securities amounted to HK\$9 million (2011: HK\$16 million).

Included within interest income and interest expense are HK\$35,254 million (2011: HK\$31,850 million) and HK\$11,278 million (2011: HK\$10,573 million), before hedging effect, for financial assets and financial liabilities that are not recognised at fair value through profit or loss respectively.

NOTES TO THE FINANCIAL STATEMENTS

6. Net fee and commission income

	2012 HK\$'m	2011 HK\$'m
Fee and commission income		
Credit card business	3,307	2,887
Securities brokerage	2,114	2,782
Loan commissions	1,628	1,160
Insurance	965	1,097
Bills commissions	736	854
Payment services	667	637
Funds distribution	540	337
Trust and custody services	360	379
Safe deposit box	228	211
Currency exchange	156	156
Others	409	358
	11,110	10,858
Fee and commission expense		
Credit card business	(2,369)	(2,106)
Securities brokerage	(299)	(431)
Payment services	(92)	(91)
Others	(444)	(397)
	(3,204)	(3,025)
Net fee and commission income	7,906	7,833
Of which arise from		
– financial assets or financial liabilities not at fair value through profit or loss		
– Fee and commission income	1,770	1,363
– Fee and commission expense	(7)	(5)
	1,763	1,358
– trust and other fiduciary activities		
– Fee and commission income	550	571
– Fee and commission expense	(14)	(6)
	536	565

NOTES TO THE FINANCIAL STATEMENTS

7. Net trading gain

	2012 HK\$'m	2011 HK\$'m
Net gain from:		
– foreign exchange and foreign exchange products	1,988	1,430
– interest rate instruments and items under fair value hedge	900	12
– commodities	121	186
– equity instruments	120	82
	3,129	1,710

8. Net gain on other financial assets

	2012 HK\$'m	2011 HK\$'m
Net gain on available-for-sale securities	644	469
Net gain/(loss) on held-to-maturity securities	108	(19)
Others	(2)	(142)
	750	308

9. Other operating income

	2012 HK\$'m	2011 HK\$'m
Dividend income from investment in securities		
– listed investments	88	93
– unlisted investments	29	27
Gross rental income from investment properties	436	386
Less: Outgoings in respect of investment properties	(56)	(72)
Others	92	91
	589	525

Included in the "Outgoings in respect of investment properties" is HK\$3 million (2011: HK\$4 million) of direct operating expenses related to investment properties that were not let during the year.

10. Gross insurance benefits and claims

	2012 HK\$'m	2011 HK\$'m
Claims, benefits and surrenders paid	7,515	6,437
Movement in liabilities	6,632	7,407
	14,147	13,844

NOTES TO THE FINANCIAL STATEMENTS

11. Net charge of impairment allowances

	2012 HK\$'m	2011 HK\$'m
Advances to customers		
Individually assessed		
– new allowances	(566)	(146)
– releases	54	134
– recoveries	234	327
Net (charge)/reversal of individually assessed loan impairment allowances (Note 26)	(278)	315
Collectively assessed		
– new allowances	(606)	(720)
– releases	–	–
– recoveries	30	26
Net charge of collectively assessed loan impairment allowances (Note 26)	(576)	(694)
Net charge of loan impairment allowances	(854)	(379)
Available-for-sale securities		
Net reversal of impairment allowances on available-for-sale securities		
– Individually assessed	2	7
Held-to-maturity securities		
Net reversal/(charge) of impairment allowances on held-to-maturity securities		
– Individually assessed (Note 27)	3	(124)
Others	(10)	(10)
Net charge of impairment allowances	(859)	(506)

NOTES TO THE FINANCIAL STATEMENTS

12. Operating expenses

	2012 HK\$'m	2011 HK\$'m
Staff costs (including directors' emoluments)		
– salaries and other costs	5,932	5,606
– pension cost	474	432
	6,406	6,038
Premises and equipment expenses (excluding depreciation)		
– rental of premises	695	613
– information technology	398	429
– others	363	348
	1,456	1,390
Depreciation (Note 31)	1,493	1,277
Auditor's remuneration		
– audit services	33	32
– non-audit services	4	6
Lehman Brothers related products*	(96)	(2,797)
Other operating expenses	2,106	1,916
	11,402	7,862

* The net amount of HK\$97 million recovered by the Group in 2012 from the underlying collateral of the Lehman Brothers minibonds, was credited to operating expenses (2011: HK\$2,854 million).

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

	2012 HK\$'m	2011 HK\$'m
Net gain from disposal of investment properties	4	13
Net gain from fair value adjustments on investment properties (Note 30)	1,885	2,200
	1,889	2,213

14. Net gain/(loss) from disposal/revaluation of properties, plant and equipment

	2012 HK\$'m	2011 HK\$'m
Net gain/(loss) from disposal of premises	118	(2)
Net loss from disposal of other fixed assets	(8)	(32)
Net loss from revaluation of premises (Note 31)	(4)	–
	106	(34)

NOTES TO THE FINANCIAL STATEMENTS

15. Taxation

Taxation in the consolidated income statement represents:

	2012 HK\$'m	2011 HK\$'m
Current tax		
Hong Kong profits tax		
– current year taxation	3,762	3,718
– (over)/under-provision in prior years	(55)	7
	3,707	3,725
Overseas taxation	436	301
	4,143	4,026
Deferred tax credit (Note 39)	(169)	(159)
	3,974	3,867

Hong Kong profits tax has been provided at the rate of 16.5% (2011: 16.5%) on the estimated assessable profits arising in Hong Kong during the year. Taxation on overseas profits has been calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the countries in which the Group operates.

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

	2012 HK\$'m	2011 HK\$'m
Profit before taxation	25,521	24,680
Calculated at a taxation rate of 16.5% (2011: 16.5%)	4,211	4,072
Effect of different taxation rates in other countries	45	37
Income not subject to taxation	(501)	(432)
Expenses not deductible for taxation purposes	105	104
Tax losses not recognised	–	24
Utilisation of previously unrecognised tax losses	(91)	(2)
(Over)/under-provision in prior years	(55)	7
Foreign withholding tax	260	57
Taxation charge	3,974	3,867
Effective tax rate	15.6%	15.7%

16. Profit attributable to the equity holders of the Company

The profit of the Company for the year ended 31 December 2012 attributable to the equity holders of the Company and dealt with in the financial statements of the Company amounted to HK\$12,820 million (2011: HK\$12,823 million).

NOTES TO THE FINANCIAL STATEMENTS

17. Dividends

	2012		2011	
	Per share HK\$	Total HK\$'m	Per share HK\$	Total HK\$'m
Interim dividend paid	0.545	5,762	0.630	6,661
Proposed final dividend	0.693	7,327	0.558	5,899
	1.238	13,089	1.188	12,560

At a meeting held on 23 August 2012, the Board declared an interim dividend of HK\$0.545 per ordinary share for the first half of 2012 amounting to approximately HK\$5,762 million.

At a meeting held on 26 March 2013, the Board proposed to recommend to the Annual General Meeting on 28 May 2013 a final dividend of HK\$0.693 per ordinary share for the year ended 31 December 2012 amounting to approximately HK\$7,327 million. This proposed final dividend is not reflected as a dividend payable in these financial statements, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2013.

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

The calculation of basic earnings per share is based on the consolidated profit attributable to the equity holders of the Company for the year ended 31 December 2012 of approximately HK\$20,930 million (2011: HK\$20,430 million) and on the ordinary shares in issue of 10,572,780,266 shares (2011: 10,572,780,266 ordinary shares).

There was no dilution of earnings per share as no potential ordinary shares were in issue for the year ended 31 December 2012 (2011: Nil).

19. Retirement benefit costs

The principal defined contribution schemes for the Group's employees are ORSO schemes exempted under the MPF Schemes Ordinance and the BOC-Prudential Easy Choice MPF Scheme. Under the ORSO schemes, employees make monthly contributions to the ORSO schemes equal to 5% of their basic salaries, while the employer makes monthly contributions equal to 5% to 15% of the employees' monthly basic salaries, depending on years of service. The employees are entitled to receive 100% of the employer's contributions upon termination of employment after completing 10 years of service, or at a scale ranging from 30% to 90% for employees who have completed between 3 to 10 years of service, on conditions of retirement, early retirement, permanent incapacity and ill-health or termination of employment other than summary dismissal.

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

NOTES TO THE FINANCIAL STATEMENTS

19. Retirement benefit costs (continued)

The Group's total contributions made to the ORSO schemes for the year ended 31 December 2012 amounted to approximately HK\$343 million (2011: approximately HK\$327 million), after a deduction of forfeited contributions of approximately HK\$3 million (2011: approximately HK\$4 million). For the MPF Scheme, the Group contributed approximately HK\$59 million (2011: approximately HK\$51 million) for the year ended 31 December 2012.

20. Share option schemes

(a) *Share Option Scheme and Sharesave Plan*

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

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

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

No options were granted pursuant to the Share Option Scheme or the Sharesave Plan during the year 2012 (2011: Nil). Both the Share Option Scheme and the Sharesave Plan expired in July 2012.

(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 recognition and measurement policies have not been applied to all options granted to employees on or before 7 November 2002.

NOTES TO THE FINANCIAL STATEMENTS

20. Share option schemes (continued)

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

Details of the share options outstanding as at 31 December 2012 and 2011 are disclosed as follows:

	Directors	Senior management	Others*	Total number of share options	Average exercise price (HK\$ per share)
At 1 January 2012	2,530,500	247,300	1,446,000	4,223,800	8.50
Less: Share options exercised during the year	-	(247,300)	-	(247,300)	8.50
Less: Share options lapsed during the year	(2,530,500)	-	(1,446,000)	(3,976,500)	8.50
At 31 December 2012	-	-	-	-	-
Exercisable at 31 December 2012	-	-	-	-	-
At 1 January 2011	3,976,500	247,300	-	4,223,800	8.50
Transfer	(1,446,000)	-	1,446,000	-	8.50
At 31 December 2011	2,530,500	247,300	1,446,000	4,223,800	8.50
Exercisable at 31 December 2011	2,530,500	247,300	1,446,000	4,223,800	8.50

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

Share options were exercised on a regular basis throughout the year and its weighted average share price was HK\$23.70. No share options were exercised during the year of 2011.

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. The valid exercise period of Pre-Listing Share Option Scheme ended on 4 July 2012 and all the non-exercised share options under this scheme have lapsed.

NOTES TO THE FINANCIAL STATEMENTS

21. Directors', senior management's and key personnel's emoluments

(a) Directors' and senior management's emoluments

(i) Directors' emoluments

Details of the emoluments paid to or receivable by the directors of the Company in respect of their services rendered for the Company and managing the subsidiaries within the Group during the year are as follows:

	2012			
	Directors' fee HK\$'000	Basic salaries, allowances and benefits in kind HK\$'000	Bonus HK\$'000	Total HK\$'000
Executive Directors				
HE Guangbei (Chief Executive)	100	7,812	4,024	11,936
GAO Yingxin	100	5,438	2,441	7,979
	200	13,250	6,465	19,915
Non-executive Directors				
XIAO Gang	–	–	–	–
LI Lihui	–	–	–	–
LI Zaohang	–	–	–	–
ZHOU Zaiqun [#]	3,987	–	–	3,987
CHEN Siqing	–	–	–	–
FUNG Victor Kwok King*	301	–	–	301
KOH Beng Seng*	350	–	–	350
NING Gaoning*	89	–	–	89
SHAN Weijian*	350	–	–	350
TUNG Chee Chen*	349	–	–	349
TUNG Savio Wai-Hok*	399	–	–	399
	5,825	–	–	5,825
	6,025	13,250	6,465	25,740

Mr. XIAO Gang resigned as Chairman and Non-executive Director of the Company with effect from 17 March 2013; and Mr. NING Gaoning was appointed as an Independent Non-executive Director of the Company with effect from 24 August 2012.

NOTES TO THE FINANCIAL STATEMENTS

21. Directors', senior management's and key personnel's emoluments (continued)

(a) Directors' and senior management's emoluments (continued)

(i) Directors' emoluments (continued)

	2011			
	Directors' fee HK\$'000	Basic salaries, allowances and benefits in kind HK\$'000	Bonus HK\$'000	Total HK\$'000
Executive Directors				
HE Guangbei (Chief Executive)	100	7,265	4,836	12,201
GAO Yingxin	100	5,077	3,042	8,219
	200	12,342	7,878	20,420
Non-executive Directors				
XIAO Gang	–	–	–	–
LI Lihui	–	–	–	–
LI Zaohang	–	–	–	–
ZHOU Zaiqun [#]	2,435	–	–	2,435
ZHANG Yanling	–	–	–	–
CHEN Siqing	–	–	–	–
FUNG Victor Kwok King [*]	310	–	–	310
KOH Beng Seng [*]	350	–	–	350
SHAN Weijian [*]	350	–	–	350
TUNG Chee Chen [*]	300	–	–	300
TUNG Savio Wai-Hok [*]	350	–	–	350
	4,095	–	–	4,095
	4,295	12,342	7,878	24,515

Note:

[#] Includes fee as Chairman and Non-executive Director of Nanyang Commercial Bank, Limited

^{*} Independent Non-executive Directors

In July 2002, options were granted to several directors of the Company by the immediate holding company, BOC (BVI), under the Pre-Listing Share Option Scheme as set out in Note 20(b). Full details of the scheme are stated in Note 20. During the year, no options were exercised and no benefits arising from the granting of these share options were included in the directors' emoluments disclosed above or recognised in the income statement (2011: Nil).

For the year ended 31 December 2012, certain directors waived emoluments of HK\$2 million (2011: HK\$2 million), which include directors' fee from subsidiaries.

NOTES TO THE FINANCIAL STATEMENTS

21. Directors', senior management's and key personnel's emoluments (continued)

(a) Directors' and senior management's emoluments (continued)

(ii) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include two (2011: two) directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining three (2011: three) individuals during the year are as follows:

	2012 HK\$'m	2011 HK\$'m
Basic salaries and allowances	15	14
Bonus	7	7
Directors' fee from subsidiaries	1	1
	23	22

Emoluments paid to or receivable by individuals during the year with reference to their tenure were within the following bands:

	Number of individuals	
	2012	2011
HK\$5,000,001 – HK\$5,500,000	–	1
HK\$5,500,001 – HK\$6,000,000	2	1
HK\$11,000,001 – HK\$11,500,000	–	1
HK\$11,500,001 – HK\$12,000,000	1	–

(iii) Senior management's emoluments

Emoluments paid to or receivable by individuals during the year with reference to their tenure as senior management were within the following bands:

	Number of individuals	
	2012	2011
HK\$1,500,001 – HK\$2,000,000	–	1
HK\$4,500,001 – HK\$5,000,000	1	1
HK\$5,000,001 – HK\$5,500,000	2	3
HK\$5,500,001 – HK\$6,000,000	2	1
HK\$7,500,001 – HK\$8,000,000	1	–
HK\$8,000,001 – HK\$8,500,000	–	1
HK\$11,000,001 – HK\$11,500,000	–	1
HK\$11,500,001 – HK\$12,000,000	2	–
HK\$12,000,001 – HK\$12,500,000	–	1

NOTES TO THE FINANCIAL STATEMENTS

21. Directors', senior management's and key personnel's emoluments (continued)

(b) Remuneration for Senior Management and Key Personnel under CG-5

Pursuant to CG-5 Guideline on a Sound Remuneration System issued by the HKMA, details of the remuneration for Senior Management and Key Personnel of the Group during the year are as follows:

(i) Remuneration awarded during the year

	2012					
	Senior Management			Key Personnel		
	Non-deferred HK\$m	Deferred HK\$m	Total HK\$m	Non-deferred HK\$m	Deferred HK\$m	Total HK\$m
Fixed remuneration						
Cash	46	–	46	51	–	51
Variable remuneration						
Cash	13	6	19	23	6	29
Total	59	6	65	74	6	80

	2011					
	Senior Management			Key Personnel		
	Non-deferred HK\$m	Deferred HK\$m	Total HK\$m	Non-deferred HK\$m	Deferred HK\$m	Total HK\$m
Fixed remuneration						
Cash	44	–	44	47	–	47
Variable remuneration						
Cash	15	7	22	22	8	30
Total	59	7	66	69	8	77

The remuneration above includes 10 (2011: 11) members of Senior Management and 22 (2011: 21) members of Key Personnel.

NOTES TO THE FINANCIAL STATEMENTS

21. Directors', senior management's and key personnel's emoluments (continued)

(b) Remuneration for Senior Management and Key Personnel under CG-5 (continued)

(ii) Deferred remuneration outstanding

	2012		2011	
	Senior Management HK\$m	Key Personnel HK\$m	Senior Management HK\$m	Key Personnel HK\$m
Deferred remuneration				
Vested	3	3	1	1
Unvested	12	11	9	8
	15	14	10	9
At 1 January	9	8	3	1
Awarded	6	6	7	8
Paid out	(3)	(3)	(1)	(1)
Reduced through performance adjustments	-	-	-	-
At 31 December	12	11	9	8

For the purpose of disclosure, Senior Management and Key Personnel mentioned in this section are defined according to the HKMA's Guideline on a Sound Remuneration System.

Senior Management: The senior executives designated by the Board who are responsible for oversight of the firm-wide strategy or material business lines, including Chief Executive, Deputy Chief Executives, Chief Financial Officer, Chief Risk Officer, Chief Operating Officer, Assistant Chief Executive, Board Secretary and Head of Group Audit.

Key Personnel: The employees whose individual business activities involve the assumption of material risk which may have significant impact on risk exposure, or whose individual responsibilities are directly and materially linked to the risk management, or those who have direct influence to the profit, including heads of material business lines, heads of major subsidiaries, Head of Trading and Chief Dealer, as well as heads of risk control functions.

22. Cash and balances with banks and other financial institutions

	2012 HK\$m	2011 HK\$m
Cash	6,688	6,425
Balances with central banks	84,387	158,950
Balances with banks and other financial institutions	64,735	48,412
Placements with banks and other financial institutions maturing within one month	42,938	65,008
	198,748	278,795

NOTES TO THE FINANCIAL STATEMENTS

23. Financial assets at fair value through profit or loss

	Trading securities		Financial assets designated at fair value through profit or loss		Total	
	2012 HK\$'m	2011 HK\$'m	2012 HK\$'m	2011 HK\$'m	2012 HK\$'m	2011 HK\$'m
At fair value						
Debt securities						
– Listed in Hong Kong	5,378	3,628	959	776	6,337	4,404
– Listed outside Hong Kong	4,982	4,732	7,119	5,376	12,101	10,108
	10,360	8,360	8,078	6,152	18,438	14,512
– Unlisted	18,913	16,673	9,908	15,318	28,821	31,991
	29,273	25,033	17,986	21,470	47,259	46,503
Fund						
– Unlisted	–	–	636	1,103	636	1,103
Equity securities						
– Listed in Hong Kong	13	12	1,126	823	1,139	835
– Listed outside Hong Kong	–	–	86	–	86	–
	13	12	1,212	823	1,225	835
– Unlisted	212	161	–	–	212	161
	225	173	1,212	823	1,437	996
Total	29,498	25,206	19,834	23,396	49,332	48,602

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

	2012 HK\$'m	2011 HK\$'m
Sovereigns	22,729	19,524
Public sector entities*	267	285
Banks and other financial institutions	15,006	17,731
Corporate entities	11,330	11,062
	49,332	48,602

* Included financial assets at fair value through profit or loss of HK\$168 million (2011: HK\$263 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

NOTES TO THE FINANCIAL STATEMENTS

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

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

	2012 HK\$'m	2011 HK\$'m
Treasury bills	17,210	14,691
Certificates of deposit held	1,342	1,515
Other financial assets at fair value through profit or loss	30,780	32,396
	49,332	48,602

24. Derivative financial instruments and hedge accounting

The Group enters into the following exchange rate, interest rate, commodity and equity related derivative financial instrument contracts for trading and risk management purposes:

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments

The Group trades derivative products (both exchange-traded or OTC) mainly for customer business. The Group strictly follows risk management policies in providing derivative products to our customers and in trading of derivative products in the interbank market.

Derivatives are also used to manage the interest rate risk of the banking book. A derivative instrument must be included in the approved product list before any transactions for that instrument can be made. There are limits to control the notional amount of exposure arising from derivative transactions, and the maximum tenor of the deal is set. Every derivative transaction must be input into the relevant system for settlement, mark to market revaluation, reporting and control.

The following tables summarise the contract/notional amounts of each class of derivative financial instrument as at 31 December:

	2012			
	Trading HK\$m	Hedging HK\$m	Not qualified for hedge accounting HK\$m	Total HK\$m
Exchange rate contracts				
Spot, forwards and futures	270,913	–	–	270,913
Swaps	680,377	3,174	7,451	691,002
Foreign currency options				
– Options purchased	4,821	–	–	4,821
– Options written	9,096	–	–	9,096
	965,207	3,174	7,451	975,832
Interest rate contracts				
Futures	235	–	–	235
Swaps	284,906	46,872	8,646	340,424
	285,141	46,872	8,646	340,659
Commodity contracts	20,481	–	–	20,481
Equity contracts	1,507	–	–	1,507
Other contracts	69	–	–	69
Total	1,272,405	50,046	16,097	1,338,548

Not qualified for hedge accounting: 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.

NOTES TO THE FINANCIAL STATEMENTS

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

	2011			
	Trading HK\$'m	Hedging HK\$'m	Not qualified for hedge accounting HK\$'m	Total HK\$'m
Exchange rate contracts				
Spot and forwards	311,393	–	–	311,393
Swaps	394,781	4,234	5,181	404,196
Foreign currency options				
– Options purchased	2,595	–	–	2,595
– Options written	3,556	–	–	3,556
	712,325	4,234	5,181	721,740
Interest rate contracts				
Futures	4,035	–	–	4,035
Swaps	340,641	34,587	49,359	424,587
Interest rate options				
– Swaptions purchased	1,005	–	–	1,005
– Swaptions written	505	–	–	505
	346,186	34,587	49,359	430,132
Commodity contracts	13,010	–	–	13,010
Equity contracts	372	–	–	372
Other contracts	82	–	–	82
Total	1,071,975	38,821	54,540	1,165,336

NOTES TO THE FINANCIAL STATEMENTS

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

The following tables summarise the fair values of each class of derivative financial instrument as at 31 December:

	2012							
	Fair value assets				Fair value liabilities			
	Trading HK\$'m	Hedging HK\$'m	Not qualified for hedge accounting HK\$'m	Total HK\$'m	Trading HK\$'m	Hedging HK\$'m	Not qualified for hedge accounting HK\$'m	Total HK\$'m
Exchange rate contracts								
Spot, forwards and futures	17,257	-	-	17,257	(13,001)	-	-	(13,001)
Swaps	7,476	42	119	7,637	(2,557)	(55)	(136)	(2,748)
Foreign currency options								
- Options purchased	23	-	-	23	-	-	-	-
- Options written	-	-	-	-	(28)	-	-	(28)
	24,756	42	119	24,917	(15,586)	(55)	(136)	(15,777)
Interest rate contracts								
Futures	1	-	-	1	-	-	-	-
Swaps	2,231	3,338	24	5,593	(3,157)	(1,693)	(89)	(4,939)
	2,232	3,338	24	5,594	(3,157)	(1,693)	(89)	(4,939)
Commodity contracts	818	-	-	818	(488)	-	-	(488)
Equity contracts	10	-	-	10	(10)	-	-	(10)
Total	27,816	3,380	143	31,339	(19,241)	(1,748)	(225)	(21,214)

NOTES TO THE FINANCIAL STATEMENTS

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

	2011							
	Fair value assets				Fair value liabilities			
	Trading HK\$m	Hedging HK\$m	Not qualified for hedge accounting HK\$m	Total HK\$m	Trading HK\$m	Hedging HK\$m	Not qualified for hedge accounting HK\$m	Total HK\$m
Exchange rate contracts								
Spot and forwards	18,484	–	–	18,484	(13,804)	–	–	(13,804)
Swaps	1,531	59	89	1,679	(1,553)	(100)	(150)	(1,803)
Foreign currency options								
– Options purchased	18	–	–	18	–	–	–	–
– Options written	–	–	–	–	(23)	–	–	(23)
	20,033	59	89	20,181	(15,380)	(100)	(150)	(15,630)
Interest rate contracts								
Futures	1	–	–	1	(1)	–	–	(1)
Swaps	2,695	2,946	–	5,641	(4,688)	(1,110)	(128)	(5,926)
Interest rate options								
– Swaptions purchased	1	–	–	1	–	–	–	–
– Swaptions written	–	–	–	–	(5)	–	–	(5)
	2,697	2,946	–	5,643	(4,694)	(1,110)	(128)	(5,932)
Commodity contracts	961	–	–	961	(717)	–	–	(717)
Equity contracts	2	–	–	2	(2)	–	–	(2)
Total	23,693	3,005	89	26,787	(20,793)	(1,210)	(278)	(22,281)

NOTES TO THE FINANCIAL STATEMENTS

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

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

	2012 HK\$m	2011 HK\$m
Exchange rate contracts		
Forwards	462	1,487
Swaps	3,746	1,325
Foreign currency options		
– Options purchased	10	2
Interest rate contracts		
Swaps	913	1,733
Commodity contracts	6	14
Equity contracts	38	5
	5,175	4,566

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.

(b) Hedge accounting

The fair values of derivative financial instruments designated as hedging instruments as at 31 December are as follows:

	2012		2011	
	Assets HK\$m	Liabilities HK\$m	Assets HK\$m	Liabilities HK\$m
Fair value hedges	3,338	(1,693)	2,946	(1,110)
Cash flow hedges	42	(55)	59	(100)
	3,380	(1,748)	3,005	(1,210)

NOTES TO THE FINANCIAL STATEMENTS

24. Derivative financial instruments and hedge accounting (continued)

(b) Hedge accounting (continued)

(i) Fair value hedges

The Group uses interest rate swaps to hedge against change in fair value of financial assets and liabilities arising from movements in market interest rates.

Gains or losses on fair value hedges reflected in net trading gain for the year are as follows:

	2012		2011	
	Hedged assets HK\$'m	Hedged liabilities HK\$'m	Hedged assets HK\$'m	Hedged liabilities HK\$'m
Net (loss)/gain				
– hedging instruments	(110)	590	(634)	2,064
– hedged items	86	(426)	589	(2,066)
	(24)	164	(45)	(2)

(ii) Cash flow hedges

The Group hedges a portion of foreign exchange risks that it expects to assume as a result of cash flows from certain fixed income securities using cross-currency interest rate swaps.

There are no gains or losses on ineffective portion recognised in the income statement during the year (2011: Nil).

(iii) Hedges of net investments in foreign operations

As at 31 December 2012, a proportion of the Group's RMB-denominated deposits from customers of HK\$1,834 million (2011: HK\$2,642 million) are designated as a hedging instrument to hedge against the net investments in foreign operations.

There are no gains or losses on ineffective portion recognised in the income statement during the year (2011: Nil).

NOTES TO THE FINANCIAL STATEMENTS

25. Advances and other accounts

	2012 HK\$'m	2011 HK\$'m
Personal loans and advances	238,702	215,715
Corporate loans and advances	539,562	483,664
Advances to customers*	778,264	699,379
Loan impairment allowances		
– Individually assessed	(736)	(259)
– Collectively assessed	(2,969)	(2,571)
	774,559	696,549
Trade bills	45,180	56,506
Advances to banks and other financial institutions	–	2,174
Total	819,739	755,229

As at 31 December 2012, advances to customers included accrued interest of HK\$1,434 million (2011: HK\$1,305 million).

As at 31 December 2012 and 2011, no impairment allowance was made in respect of trade bills and advances to banks and other financial institutions.

* Included advances to customers denominated in HK dollars of HK\$520,638 million (2011: HK\$470,898 million) and US dollars equivalent to HK\$177,027 million (2011: HK\$179,888 million).

26. Loan impairment allowances

	2012		
	Individual assessment		
	Personal HK\$'m	Corporate HK\$'m	Total HK\$'m
At 1 January 2012	28	231	259
(Credited)/charged to income statement (Note 11)	(16)	294	278
Loans written off during the year as uncollectible	(3)	(23)	(26)
Recoveries	17	217	234
Unwind of discount on impairment allowances	–	(10)	(10)
Exchange difference	–	1	1
At 31 December 2012	26	710	736

NOTES TO THE FINANCIAL STATEMENTS

26. Loan impairment allowances (continued)

	2012		
	Collective assessment		
	Personal HK\$'m	Corporate HK\$'m	Total HK\$'m
At 1 January 2012	237	2,334	2,571
Charged to income statement (Note 11)	213	363	576
Loans written off during the year as uncollectible	(211)	(1)	(212)
Recoveries	30	–	30
Exchange difference	–	4	4
At 31 December 2012	269	2,700	2,969

	2011		
	Individual assessment		
	Personal HK\$'m	Corporate HK\$'m	Total HK\$'m
At 1 January 2011	23	303	326
Credited to income statement (Note 11)	(2)	(313)	(315)
Loans written off during the year as uncollectible	(7)	(71)	(78)
Recoveries	14	313	327
Unwind of discount on impairment allowances	–	(3)	(3)
Exchange difference	–	2	2
At 31 December 2011	28	231	259

	2011		
	Collective assessment		
	Personal HK\$'m	Corporate HK\$'m	Total HK\$'m
At 1 January 2011	186	1,799	1,985
Charged to income statement (Note 11)	167	527	694
Loans written off during the year as uncollectible	(142)	(1)	(143)
Recoveries	26	–	26
Exchange difference	–	9	9
At 31 December 2011	237	2,334	2,571

NOTES TO THE FINANCIAL STATEMENTS

27. Investment in securities

	2012 HK\$'m	2011 HK\$'m
The Group		
(a) Available-for-sale securities		
Debt securities, at fair value		
– Listed in Hong Kong	20,252	9,614
– Listed outside Hong Kong	111,969	102,098
	132,221	111,712
– Unlisted	318,876	200,187
	451,097	311,899
Equity securities, at fair value		
– Listed in Hong Kong	2,592	3,660
– Listed outside Hong Kong	–	92
	2,592	3,752
– Unlisted	1,043	747
	3,635	4,499
	454,732	316,398
(b) Held-to-maturity securities		
Listed, at amortised cost		
– in Hong Kong	948	1,164
– outside Hong Kong	7,807	14,125
	8,755	15,289
Unlisted, at amortised cost	9,652	38,663
	18,407	53,952
Impairment allowances	(9)	(25)
	18,398	53,927
(c) Loans and receivables		
Unlisted, at amortised cost	9,234	6,673
Total	482,364	376,998
Market value of listed held-to-maturity securities	8,983	15,288
	2012 HK\$'m	2011 HK\$'m
The Company		
Available-for-sale securities		
Equity securities, at fair value		
– Listed in Hong Kong	2,528	2,506

NOTES TO THE FINANCIAL STATEMENTS

27. Investment in securities (continued)

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

	2012			
	Available-for-sale securities HK\$m	Held-to-maturity securities HK\$m	Loans and receivables HK\$m	Total HK\$m
The Group				
Sovereigns	152,583	3,208	–	155,791
Public sector entities*	39,913	1,278	–	41,191
Banks and other financial institutions	211,561	12,115	8,077	231,753
Corporate entities	50,675	1,797	1,157	53,629
	454,732	18,398	9,234	482,364
	2011			
	Available-for-sale securities HK\$m	Held-to-maturity securities HK\$m	Loans and receivables HK\$m	Total HK\$m
The Group				
Sovereigns	104,799	20,882	–	125,681
Public sector entities*	36,458	6,509	–	42,967
Banks and other financial institutions	148,056	23,107	6,673	177,836
Corporate entities	27,085	3,429	–	30,514
	316,398	53,927	6,673	376,998

* Included available-for-sale securities of HK\$20,974 million (2011: HK\$20,746 million) and held-to-maturity securities of HK\$248 million (2011: HK\$832 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

As at 31 December 2012 and 2011, all of the available-for-sale securities held by the Company are issued by banks and other financial institutions.

NOTES TO THE FINANCIAL STATEMENTS

27. Investment in securities (continued)

The movements in investment in securities are summarised as follows:

	2012		
	Available-for-sale securities HK\$'m	Held-to-maturity securities HK\$'m	Loans and receivables HK\$'m
The Group			
At 1 January 2012	316,398	53,927	6,673
Additions	865,481	12,687	16,446
Disposals, redemptions and maturity	(728,314)	(47,895)	(14,146)
Amortisation	380	(215)	90
Change in fair value	5,484	–	–
Net reversal of impairment allowances (Note 11)	–	3	–
Exchange difference	(4,697)	(109)	171
At 31 December 2012	454,732	18,398	9,234
	2011		
	Available-for-sale securities HK\$'m	Held-to-maturity securities HK\$'m	Loans and receivables HK\$'m
The Group			
At 1 January 2011	286,444	58,384	15,356
Additions	547,949	44,116	18,861
Disposals, redemptions and maturity	(518,880)	(49,523)	(26,852)
Amortisation	(640)	218	127
Change in fair value	41	–	–
Net charge of impairment allowances (Note 11)	–	(124)	–
Exchange difference	1,484	856	(819)
At 31 December 2011	316,398	53,927	6,673

NOTES TO THE FINANCIAL STATEMENTS

27. Investment in securities (continued)

	Available-for-sale securities	
	2012 HK\$'m	2011 HK\$'m
The Company		
At 1 January	2,506	2,775
Change in fair value	22	(269)
At 31 December	2,528	2,506

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

	Available-for-sale securities		Held-to-maturity securities	
	2012 HK\$'m	2011 HK\$'m	2012 HK\$'m	2011 HK\$'m
The Group				
Treasury bills	115,637	72,906	885	6,195
Certificates of deposit held	72,841	27,542	874	3,044
Others	266,254	215,950	16,639	44,688
	454,732	316,398	18,398	53,927

The movements in impairment allowances on held-to-maturity securities are summarised as follows:

	2012 HK\$'m	2011 HK\$'m
The Group		
At 1 January	25	49
(Credited)/charged to income statement (Note 11)	(3)	124
Disposals	(13)	(148)
At 31 December	9	25

NOTES TO THE FINANCIAL STATEMENTS

28. Investment in subsidiaries

	2012 HK\$'m	2011 HK\$'m
The Company		
Unlisted shares, at cost	54,834	54,814

The particulars of all direct and indirect subsidiaries of the Company are set out in the Appendix of this Annual Report, "Subsidiaries of the Company". The following is a list of principal subsidiaries as at 31 December 2012:

Name	Place of incorporation and operation	Particulars of issued share capital	Interest held	Principal activities
Bank of China (Hong Kong) Limited	Hong Kong	43,042,840,858 ordinary shares of HK\$1 each	*100%	Banking business
BOC Group Life Assurance Company Limited	Hong Kong	303,800,000 ordinary shares of HK\$10 each	*51%	Life insurance business
Nanyang Commercial Bank, Limited	Hong Kong	7,000,000 ordinary shares of HK\$100 each	100%	Banking business
Chiyu Banking Corporation Limited	Hong Kong	3,000,000 ordinary shares of HK\$100 each	70.49%	Banking business
BOC Credit Card (International) Limited	Hong Kong	4,800,000 ordinary shares of HK\$100 each	100%	Credit card services
Po Sang Futures Limited	Hong Kong	950,000 ordinary shares of HK\$100 each	100%	Securities and futures brokerage
Nanyang Commercial Bank (China), Limited	PRC	Registered capital RMB6,500,000,000	100%	Banking business

* Shares held directly by the Company

NOTES TO THE FINANCIAL STATEMENTS

29. Interests in associates

	2012 HK\$'m	2011 HK\$'m
At 1 January	234	212
Share of result	35	28
Share of tax	(8)	(5)
Dividend received	(2)	(1)
At 31 December	259	234

The Group's interests in its associates, all of which are unlisted, are as follows:

Name	Joint Electronic Teller Services Limited		BOC Services Company Limited		BOC Expresspay Company Limited	
	Hong Kong		PRC		PRC	
Place of incorporation	Hong Kong		PRC		PRC	
Particulars of issued share capital/registered capital	100,238 ordinary shares of HK\$100 each		Registered capital RMB50,000,000		Registered capital RMB450,000,000	
Principal activities	Operation of a private inter-bank message switching network in respect of ATM services		Credit card back-end service support		Prepay debit card services	
	2012 HK\$'000	2011 HK\$'000	2012 HK\$'000	2011 HK\$'000	2012 HK\$'000	2011 HK\$'000
Assets	375,120	377,539	347,288	272,540	1,775,491	3,083,539
Liabilities	74,411	75,644	192,258	160,334	1,210,013	2,536,960
Revenues	73,040	70,075	858,809	827,296	64,194	36,220
Profit after taxation	26,833	27,677	44,650	28,270	19,134	22,594
	2012	2011	2012	2011	2012	2011
Interest held	19.96%	19.96%	45.00%	45.00%	25.33%	25.33%

NOTES TO THE FINANCIAL STATEMENTS

30. Investment properties

	2012 HK\$'m	2011 HK\$'m
At 1 January	12,441	10,342
Additions	2	14
Disposals	(62)	(25)
Fair value gains (Note 13)	1,885	2,200
Reclassification from/(to) properties, plant and equipment (Note 31)	98	(92)
Exchange difference	–	2
At 31 December	14,364	12,441

The carrying value of investment properties is analysed based on the remaining terms of the leases as follows:

	2012 HK\$'m	2011 HK\$'m
Held in Hong Kong		
On long-term lease (over 50 years)	2,754	2,261
On medium-term lease (10 – 50 years)	11,361	9,944
Held outside Hong Kong		
On long-term lease (over 50 years)	–	2
On medium-term lease (10 – 50 years)	249	234
	14,364	12,441

As at 31 December 2012, investment properties are included in the consolidated balance sheet at valuation carried out at 31 December 2012 on the basis of their fair value by an independent firm of chartered surveyors, Savills Valuation and Professional Services Limited. The fair value represents the estimated amount at which the asset should be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

NOTES TO THE FINANCIAL STATEMENTS

31. Properties, plant and equipment

	Premises HK\$'m	Equipment, fixtures and fittings HK\$'m	Total HK\$'m
Net book value at 1 January 2012	37,049	2,601	39,650
Additions	358	687	1,045
Disposals	(147)	(9)	(156)
Revaluation	9,792	–	9,792
Depreciation for the year (Note 12)	(778)	(715)	(1,493)
Reclassification to investment properties (Note 30)	(98)	–	(98)
Exchange difference	2	1	3
Net book value at 31 December 2012	46,178	2,565	48,743
At 31 December 2012			
Cost or valuation	46,178	7,793	53,971
Accumulated depreciation and impairment	–	(5,228)	(5,228)
Net book value at 31 December 2012	46,178	2,565	48,743
Net book value at 1 January 2011	28,581	2,468	31,049
Additions	83	827	910
Disposals	(95)	(33)	(128)
Revaluation	8,989	–	8,989
Depreciation for the year (Note 12)	(610)	(667)	(1,277)
Reclassification from investment properties (Note 30)	92	–	92
Exchange difference	9	6	15
Net book value at 31 December 2011	37,049	2,601	39,650
At 31 December 2011			
Cost or valuation	37,049	7,414	44,463
Accumulated depreciation and impairment	–	(4,813)	(4,813)
Net book value at 31 December 2011	37,049	2,601	39,650

NOTES TO THE FINANCIAL STATEMENTS

31. Properties, plant and equipment (continued)

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

	Premises HK\$m	Equipment, fixtures and fittings HK\$m	Total HK\$m
At 31 December 2012			
At cost	–	7,793	7,793
At valuation	46,178	–	46,178
	46,178	7,793	53,971
At 31 December 2011			
At cost	–	7,414	7,414
At valuation	37,049	–	37,049
	37,049	7,414	44,463

The carrying value of premises is analysed based on the remaining terms of the leases as follows:

	2012 HK\$m	2011 HK\$m
Held in Hong Kong		
On long-term lease (over 50 years)	16,913	12,792
On medium-term lease (10 – 50 years)	28,547	23,819
Held outside Hong Kong		
On long-term lease (over 50 years)	65	102
On medium-term lease (10 – 50 years)	632	321
On short-term lease (less than 10 years)	21	15
	46,178	37,049

As at 31 December 2012, premises are included in the consolidated balance sheet at valuation carried out at 31 December 2012 on the basis of their fair value by an independent firm of chartered surveyors, Savills Valuation and Professional Services Limited. The fair value represents the estimated amount at which the asset should be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

As a result of the above-mentioned revaluations, changes in value of the Group's premises were recognised in the Group's premises revaluation reserve, the income statement and non-controlling interests as follows:

	2012 HK\$m	2011 HK\$m
Increase in valuation credited to premises revaluation reserve	9,718	8,918
Decrease in valuation charged to income statement (Note 14)	(4)	–
Increase in valuation credited to non-controlling interests	78	71
	9,792	8,989

As at 31 December 2012, the net book value of premises that would have been included in the Group's consolidated balance sheet had the assets been carried at cost less accumulated depreciation and impairment losses was HK\$6,904 million (2011: HK\$6,666 million).

NOTES TO THE FINANCIAL STATEMENTS

32. Other assets

	2012 HK\$'m	2011 HK\$'m
Reposessed assets	18	13
Precious metals	6,610	5,260
Reinsurance assets	14,671	9,022
Accounts receivable and prepayments	15,532	11,469
	36,831	25,764

33. Hong Kong SAR currency notes in circulation

The Hong Kong SAR currency notes in circulation are secured by deposit of funds in respect of which the Hong Kong SAR Government certificates of indebtedness are held.

34. Financial liabilities at fair value through profit or loss

	2012 HK\$'m	2011 HK\$'m
Trading liabilities		
– Short positions in Exchange Fund Bills and Notes	17,331	2,598
Financial liabilities designated at fair value through profit or loss		
– Structured deposits (Note 35)	2,841	639
	20,172	3,237

The carrying amount of financial liabilities designated at fair value through profit or loss as at 31 December 2012 is more than the amount that the Group would be contractually required to pay at maturity to the holders by HK\$1 million (2011: HK\$1 million). The amount of change in the fair values of financial liabilities at fair value through profit or loss, during the year and cumulatively, attributable to changes in own credit risk is insignificant.

NOTES TO THE FINANCIAL STATEMENTS

35. Deposits from customers

	2012 HK\$'m	2011 HK\$'m
Current, savings and other deposit accounts (per consolidated balance sheet)	1,226,290	1,145,951
Structured deposits reported as financial liabilities at fair value through profit or loss (Note 34)	2,841	639
	1,229,131	1,146,590
Analysed by:		
Demand deposits and current accounts		
– corporate	76,742	62,847
– personal	20,553	14,593
	97,295	77,440
Savings deposits		
– corporate	202,846	162,672
– personal	400,719	342,196
	603,565	504,868
Time, call and notice deposits		
– corporate	298,902	334,581
– personal	229,369	229,701
	528,271	564,282
	1,229,131	1,146,590

36. Debt securities in issue at amortised cost

	2012 HK\$'m	2011 HK\$'m
Senior notes under the Medium Term Note Programme	5,919	5,856
Other debt securities	4	129
	5,923	5,985

37. Other accounts and provisions

	2012 HK\$'m	2011 HK\$'m
Other accounts payable	47,639	41,445
Provisions	344	366
	47,983	41,811

NOTES TO THE FINANCIAL STATEMENTS

38. Assets pledged as security

As at 31 December 2012, liabilities of the Group amounting to HK\$18,029 million (2011: HK\$4,614 million) were secured by assets deposited with central depositories to facilitate settlement operations. In addition, the liabilities of the Group amounting to HK\$438 million (2011: HK\$2,005 million) were secured by debt securities and bills related to sale and repurchase arrangements. The amount of assets pledged by the Group to secure these liabilities was HK\$18,596 million (2011: HK\$6,643 million) included in "Trading securities", "Available-for-sale securities" and "Trade bills".

39. Deferred taxation

Deferred tax is recognised in respect of the temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements in accordance with HKAS 12 "Income Taxes".

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

	2012					
	Accelerated tax depreciation HK\$m	Property revaluation HK\$m	Losses HK\$m	Impairment allowance HK\$m	Other temporary differences HK\$m	Total HK\$m
At 1 January 2012	547	5,299	(131)	(451)	(109)	5,155
Charged/(credited) to income statement (Note 15)	17	(128)	(13)	(41)	(4)	(169)
Charged to other comprehensive income	-	1,601	-	-	730	2,331
At 31 December 2012	564	6,772	(144)	(492)	617	7,317
	2011					
	Accelerated tax depreciation HK\$m	Property revaluation HK\$m	Losses HK\$m	Impairment allowance HK\$m	Other temporary differences HK\$m	Total HK\$m
At 1 January 2011	535	3,881	(124)	(333)	90	4,049
Charged/(credited) to income statement (Note 15)	12	(5)	(7)	(116)	(43)	(159)
Charged/(credited) to other comprehensive income	-	1,422	-	-	(156)	1,266
Exchange difference	-	1	-	(2)	-	(1)
At 31 December 2011	547	5,299	(131)	(451)	(109)	5,155

NOTES TO THE FINANCIAL STATEMENTS

39. Deferred taxation (continued)

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

	2012 HK\$'m	2011 HK\$'m
Deferred tax assets	(89)	(210)
Deferred tax liabilities	7,406	5,365
	7,317	5,155
	2012 HK\$'m	2011 HK\$'m
Deferred tax assets to be recovered after more than twelve months	(154)	(141)
Deferred tax liabilities to be settled after more than twelve months	6,847	5,421
	6,693	5,280

As at 31 December 2012, the Group has not recognised deferred tax assets in respect of tax losses amounting to HK\$718 million (2011: HK\$1,264 million). These tax losses do not expire under the current tax legislation.

40. Insurance contract liabilities

	2012 HK\$'m	2011 HK\$'m
At 1 January	47,220	39,807
Benefits paid	(7,169)	(6,037)
Claims incurred and movement in liabilities	13,886	13,450
At 31 December	53,937	47,220

The insurance contract liabilities that are covered by reinsurance arrangements amounted to HK\$14,644 million (2011: HK\$9,012 million) and the associated reinsurance assets of HK\$14,671 million (2011: HK\$9,022 million) are included in "Other assets" (Note 32).

NOTES TO THE FINANCIAL STATEMENTS

41. Subordinated liabilities

	2012 HK\$'m	2011 HK\$'m
Subordinated loans, at amortised cost EUR660m*	6,749	6,625
Subordinated notes, at amortised cost with fair value hedge adjustment USD2,500m**	22,006	22,031
Total	28,755	28,656

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

Amounts qualified as supplementary capital for regulatory purposes are shown in Note 4.5(B).

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

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

42. Share capital

	2012 HK\$'m	2011 HK\$'m
Authorised: 20,000,000,000 ordinary shares of HK\$5 each	100,000	100,000
Issued and fully paid: 10,572,780,266 ordinary shares of HK\$5 each	52,864	52,864

43. Reserves

The Group's and the Company's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity and statement of changes in equity respectively on pages 107 to 108 of the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

44. Notes to consolidated cash flow statement

(a) Reconciliation of operating profit to operating cash outflow before taxation

	2012 HK\$'m	2011 HK\$'m
Operating profit	23,499	22,478
Depreciation	1,493	1,277
Net charge of impairment allowances	859	506
Unwind of discount on impairment allowances	(10)	(3)
Advances written off net of recoveries	26	132
Change in subordinated liabilities	703	2,409
Change in balances with banks and other financial institutions with original maturity over three months	(7,794)	(5,315)
Change in placements with banks and other financial institutions with original maturity over three months	34,466	(66,391)
Change in financial assets at fair value through profit or loss	568	11,924
Change in derivative financial instruments	(5,619)	(2,007)
Change in advances and other accounts	(65,385)	(110,324)
Change in investment in securities	(104,150)	25,445
Change in other assets	(11,077)	(8,133)
Change in deposits and balances from banks and other financial institutions	(57,488)	(77,090)
Change in financial liabilities at fair value through profit or loss	16,935	(22,256)
Change in deposits from customers	80,339	118,918
Change in debt securities in issue at amortised cost	(62)	5,985
Change in other accounts and provisions	6,172	6,331
Change in insurance contract liabilities	6,717	7,413
Effect of changes in exchange rates	3,862	(14,028)
Operating cash outflow before taxation	(75,946)	(102,729)
Cash flows from operating activities included:		
– Interest received	35,297	30,089
– Interest paid	9,704	8,404
– Dividend received	117	120

NOTES TO THE FINANCIAL STATEMENTS

44. Notes to consolidated cash flow statement (continued)

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

	2012 HK\$'m	2011 HK\$'m
Cash and balances with banks and other financial institutions with original maturity within three months	179,311	267,152
Placements with banks and other financial institutions with original maturity within three months	8,152	15,571
Treasury bills with original maturity within three months	53,912	54,544
Certificates of deposit held with original maturity within three months	1,580	3,179
	242,955	340,446

45. Contingent liabilities and commitments

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

	2012 HK\$'m	2011 HK\$'m
Direct credit substitutes	14,168	8,124
Transaction-related contingencies	11,681	11,871
Trade-related contingencies	45,412	50,422
Commitments that are unconditionally cancellable without prior notice	320,777	263,246
Other commitments with an original maturity of		
– up to one year	18,988	11,506
– over one year	52,743	45,016
	463,769	390,185
Credit risk weighted amount	59,008	41,502

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.

NOTES TO THE FINANCIAL STATEMENTS

46. Capital commitments

The Group has the following outstanding capital commitments not provided for in the financial statements:

	2012 HK\$'m	2011 HK\$'m
Authorised and contracted for but not provided for	325	244
Authorised but not contracted for	1	8
	326	252

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

47. Operating lease commitments

(a) The Group as lessee

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

	2012 HK\$'m	2011 HK\$'m
Land and buildings		
– not later than one year	697	598
– later than one year but not later than five years	1,209	1,050
– later than five years	446	299
	2,352	1,947

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

(b) The Group as lessor

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

	2012 HK\$'m	2011 HK\$'m
Land and buildings		
– not later than one year	410	377
– later than one year but not later than five years	272	441
	682	818

The Group leases its investment properties (Note 30) 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 rent adjustments according to the prevailing market conditions at the expiration of the lease.

NOTES TO THE FINANCIAL STATEMENTS

48. Litigation

The Group has been served a number of claims and counterclaims by various independent parties. These claims and counterclaims are in relation to the normal commercial activities of the Group.

No material provision was made against these claims and counterclaims because the directors believe that the Group has meritorious defences against the claimants or the amounts involved in these claims are not expected to be material.

49. Segmental reporting

The Group manages the business mainly from a business segment perspective and over 90% of the Group's revenues, profits before tax and assets are derived from Hong Kong. Currently, four operating segments are identified which 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.

Both Personal Banking and Corporate Banking provide general banking services including various deposit products, overdrafts, loans, credit cards, trade related products and other credit facilities, investment and insurance products, and foreign currency and derivative products, etc. Personal Banking mainly serves retail customers while Corporate Banking mainly deals with corporate customers. Treasury manages the funding and liquidity, and the interest rate and foreign exchange positions of the Group in addition to proprietary trades. The Insurance segment represents business relating to life insurance products, including traditional and unit-linked individual life insurance and group life insurance products. "Others" mainly represents Group's holdings of premises, investment properties, equity investments and interests in associates.

As the Group's major revenue is derived from interest and the senior management relies primarily on net interest income to assess the performance of the segment, interest income and expense for all reportable segments are presented on a net basis. The senior management also assesses the business performance of premium growth and claim expense of the Insurance segment primarily based on net insurance premium income and benefits and claims.

Measurement of segment assets, liabilities, income, expenses, results and capital expenditure is based on the Group's accounting policies. The segment information includes items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group, which is primarily based on market rates with the consideration of specific features of the product.

NOTES TO THE FINANCIAL STATEMENTS

49. Segmental reporting (continued)

	2012							
	Personal Banking HK\$'m	Corporate Banking HK\$'m	Treasury HK\$'m	Insurance HK\$'m	Others HK\$'m	Subtotal HK\$'m	Eliminations HK\$'m	Consolidated HK\$'m
Net interest income/(expense)								
– external	932	8,784	13,229	1,757	6	24,708	–	24,708
– inter-segment	5,725	1,085	(6,288)	–	(522)	–	–	–
	6,657	9,869	6,941	1,757	(516)	24,708	–	24,708
Net fee and commission income/(expense)	4,377	3,420	138	(67)	247	8,115	(209)	7,906
Net insurance premium income	–	–	–	6,466	–	6,466	(15)	6,451
Net trading gain/(loss)	559	364	1,873	359	(34)	3,121	8	3,129
Net gain on financial instruments designated at fair value through profit or loss	–	–	42	705	–	747	–	747
Net (loss)/gain on other financial assets	–	(2)	623	129	–	750	–	750
Other operating income	50	3	8	14	1,429	1,504	(915)	589
Total operating income	11,643	13,654	9,625	9,363	1,126	45,411	(1,131)	44,280
Net insurance benefits and claims	–	–	–	(8,520)	–	(8,520)	–	(8,520)
Net operating income before impairment allowances	11,643	13,654	9,625	843	1,126	36,891	(1,131)	35,760
Net (charge)/reversal of impairment allowances	(214)	(650)	16	(11)	–	(859)	–	(859)
Net operating income	11,429	13,004	9,641	832	1,126	36,032	(1,131)	34,901
Operating expenses	(5,913)	(3,278)	(1,259)	(223)	(1,860)	(12,533)	1,131	(11,402)
Operating profit/(loss)	5,516	9,726	8,382	609	(734)	23,499	–	23,499
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	1,889	1,889	–	1,889
Net (loss)/gain from disposal/revaluation of properties, plant and equipment	(3)	(1)	–	–	110	106	–	106
Share of profits less losses after tax of associates	–	–	–	–	27	27	–	27
Profit before taxation	5,513	9,725	8,382	609	1,292	25,521	–	25,521
Assets								
Segment assets	266,839	573,803	870,488	66,150	65,760	1,843,040	(12,536)	1,830,504
Interests in associates	–	–	–	–	259	259	–	259
	266,839	573,803	870,488	66,150	66,019	1,843,299	(12,536)	1,830,763
Liabilities								
Segment liabilities	716,696	551,508	346,561	61,904	11,556	1,688,225	(12,536)	1,675,689
Other information								
Capital expenditure	27	8	–	15	997	1,047	–	1,047
Depreciation	324	169	90	6	904	1,493	–	1,493
Amortisation of securities	–	–	190	65	–	255	–	255

NOTES TO THE FINANCIAL STATEMENTS

49. Segmental reporting (continued)

	2011							
	Personal Banking HK\$'m	Corporate Banking HK\$'m	Treasury HK\$'m	Insurance HK\$'m	Others HK\$'m	Subtotal HK\$'m	Eliminations HK\$'m	Consolidated HK\$'m
Net interest income/(expense)								
– external	1,386	6,901	11,991	1,697	4	21,979	–	21,979
– inter-segment	4,378	1,757	(5,978)	–	(157)	–	–	–
	5,764	8,658	6,013	1,697	(153)	21,979	–	21,979
Net fee and commission income	4,485	3,015	205	78	143	7,926	(93)	7,833
Net insurance premium income	–	–	–	5,696	–	5,696	(13)	5,683
Net trading gain/(loss)	583	298	724	136	(31)	1,710	–	1,710
Net loss on financial instruments designated at fair value through profit or loss	–	–	(4)	(339)	–	(343)	3	(340)
Net (loss)/gain on other financial assets	(2)	(29)	437	(22)	(76)	308	–	308
Other operating income	36	1	1	15	1,341	1,394	(869)	525
Total operating income	10,866	11,943	7,376	7,261	1,224	38,670	(972)	37,698
Net insurance benefits and claims	–	–	–	(6,852)	–	(6,852)	–	(6,852)
Net operating income before impairment allowances	10,866	11,943	7,376	409	1,224	31,818	(972)	30,846
Net (charge)/reversal of impairment allowances	(176)	(213)	50	(167)	–	(506)	–	(506)
Net operating income	10,690	11,730	7,426	242	1,224	31,312	(972)	30,340
Operating expenses	(5,787)	(3,085)	(911)	(209)	1,158	(8,834)	972	(7,862)
Operating profit	4,903	8,645	6,515	33	2,382	22,478	–	22,478
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	2,213	2,213	–	2,213
Net loss from disposal/revaluation of properties, plant and equipment	(7)	(9)	–	–	(18)	(34)	–	(34)
Share of profits less losses after tax of associates	–	–	–	–	23	23	–	23
Profit before taxation	4,896	8,636	6,515	33	4,600	24,680	–	24,680
Assets								
Segment assets	241,275	536,091	860,848	57,299	61,099	1,756,612	(18,336)	1,738,276
Interests in associates	–	–	–	–	234	234	–	234
	241,275	536,091	860,848	57,299	61,333	1,756,846	(18,336)	1,738,510
Liabilities								
Segment liabilities	676,928	507,852	368,709	54,282	15,892	1,623,663	(18,336)	1,605,327
Other information								
Capital expenditure	26	4	–	20	874	924	–	924
Depreciation	317	153	59	5	743	1,277	–	1,277
Amortisation of securities	–	–	(294)	(1)	–	(295)	–	(295)

NOTES TO THE FINANCIAL STATEMENTS

50. Loans to directors and officers

Particulars of advances made to directors and officers of the Company pursuant to section 161B of the Hong Kong Companies Ordinance are as follows:

	2012 HK\$'m	2011 HK\$'m
Aggregate amount of relevant transactions outstanding at year end	5,865	4,015
Maximum aggregate amount of relevant transactions outstanding during the year	7,316	4,572

51. Significant related party transactions

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

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

General information of the parent companies:

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

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

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

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS

51. Significant related party transactions (continued)

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

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

	2012		2011	
	Associates HK\$m	Other related parties HK\$m	Associates HK\$m	Other related parties HK\$m
Income statement items:				
Administrative services fees received/receivable	–	8	–	8
Balance sheet items:				
Deposits from customers	34	–	173	–
Other accounts and provisions	5	–	–	–
Off-balance sheet items:				
Contingent liabilities and commitments	–	–	20	–

(d) Key management personnel

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

The key management compensation for the year ended 31 December is detailed as follows:

	2012 HK\$m	2011 HK\$m
Salaries and other short-term employee benefits	66	66
Post-employment benefits	1	1
	67	67

NOTES TO THE FINANCIAL STATEMENTS

52. Currency concentrations

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

	2012							
	Equivalent in million of HK\$							
	US Dollars	Japanese Yen	Euro	Australian Dollars	Pound Sterling	Renminbi	Other foreign currencies	Total foreign currencies
Spot assets	480,099	81,033	17,279	24,874	4,336	374,118	17,313	999,052
Spot liabilities	(357,163)	(3,736)	(19,074)	(25,594)	(13,308)	(359,234)	(19,321)	(797,430)
Forward purchases	438,027	39,150	36,876	27,824	32,925	169,229	30,962	774,993
Forward sales	(543,759)	(116,379)	(35,207)	(27,018)	(24,226)	(184,128)	(28,746)	(959,463)
Net options position	(53)	(3)	5	(4)	8	(17)	(21)	(85)
Net long/(short) position	17,151	65	(121)	82	(265)	(32)	187	17,067
Net structural position	321	-	-	-	-	8,583	-	8,904

	2011							
	Equivalent in million of HK\$							
	US Dollars	Japanese Yen	Euro	Australian Dollars	Pound Sterling	Renminbi	Other foreign currencies	Total foreign currencies
Spot assets	451,222	51,268	18,271	32,826	6,108	449,786	16,695	1,026,176
Spot liabilities	(339,118)	(2,921)	(21,407)	(26,183)	(15,738)	(436,987)	(25,490)	(867,844)
Forward purchases	331,290	30,300	30,439	28,440	23,152	126,276	35,522	605,419
Forward sales	(438,296)	(78,706)	(27,604)	(35,125)	(13,500)	(132,354)	(26,524)	(752,109)
Net options position	441	-	(1)	(15)	(11)	(2)	(14)	398
Net long/(short) position	5,539	(59)	(302)	(57)	11	6,719	189	12,040
Net structural position	315	-	-	-	-	5,261	-	5,576

NOTES TO THE FINANCIAL STATEMENTS

53. 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:

	2012			
	Banks HK\$'m	Public sector entities* HK\$'m	Others HK\$'m	Total HK\$'m
Asia, other than Hong Kong				
– Mainland China	272,511	81,892	128,295	482,698
– Japan	7,283	81,320	158	88,761
– Others	49,874	4,410	24,687	78,971
	329,668	167,622	153,140	650,430
North America				
– United States	2,439	46,397	34,290	83,126
– Others	12,990	1,392	276	14,658
	15,429	47,789	34,566	97,784
Total	345,097	215,411	187,706	748,214

	2011			
	Banks HK\$'m	Public sector entities* HK\$'m	Others HK\$'m	Total HK\$'m
Asia, other than Hong Kong				
– Mainland China	246,133	171,336	111,932	529,401
– Japan	14,630	47,527	537	62,694
– Others	43,845	5,095	23,489	72,429
	304,608	223,958	135,958	664,524
North America				
– United States	10,389	42,037	29,949	82,375
– Others	13,590	1,739	245	15,574
	23,979	43,776	30,194	97,949
Total	328,587	267,734	166,152	762,473

* Included United States of HK\$10,442 million (2011: HK\$8,937 million) and other countries in North America of HK\$1,355 million (2011: HK\$1,704 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

NOTES TO THE FINANCIAL STATEMENTS

54. Non-bank Mainland China exposures

The analysis of non-bank Mainland China exposures is based on the categories of non-bank counterparties and the type of direct exposures with reference to the HKMA return for non-bank Mainland China exposures. The Group's exposures in Mainland China arising from non-bank counterparties are summarised as follows:

	2012			
	On-balance sheet exposure HK\$m	Off-balance sheet exposure HK\$m	Total exposure HK\$m	Individually assessed impairment allowances HK\$m
Mainland China entities	317,910	70,998	388,908	142
Companies and individuals outside Mainland China where the credit is granted for use in Mainland China	44,283	16,191	60,474	16
Other non-bank Mainland China exposures	23,213	2,600	25,813	67
	385,406	89,789	475,195	225

	2011			
	On-balance sheet exposure HK\$m	Off-balance sheet exposure HK\$m	Total exposure HK\$m	Individually assessed impairment allowances HK\$m
Mainland China entities	254,105	65,129	319,234	34
Companies and individuals outside Mainland China where the credit is granted for use in Mainland China	34,440	11,941	46,381	14
Other non-bank Mainland China exposures	21,746	2,060	23,806	44
	310,291	79,130	389,421	92

During the year, the basis of the above analyses has been refined and the comparative amounts have been reclassified accordingly.

55. Ultimate holding company

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

56. Approval of financial statements

The financial statements were approved and authorised for issue by the Board of Directors on 26 March 2013.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

1. Capital charge for credit, market and operational risks

The bases of regulatory capital calculation for credit risk, market risk and operational risk are described in Note 4.5 to the Financial Statements in this Annual Report.

As a result of the change in the bases of regulatory capital calculation, the amounts shown below are not directly comparable.

The financial information contained in these supplementary notes has been prepared on a 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. Subsidiaries that are not included in the consolidation for regulatory purposes in respect of calculation of capital adequacy ratio are denoted in "Appendix – Subsidiaries of the Company" on pages 261 to 264.

The table below summarises the capital requirements and capital charge calculated by applying 8% on the risk-weighted amounts, computed on the same consolidation basis for credit, market, and operational risks.

	2012 HK\$'m	2011 HK\$'m
Credit risk	56,343	46,341
Market risk	906	1,625
Operational risk	4,421	4,065
	61,670	52,031

For detail of capital management and capital adequacy ratio of the Group, please refer to Note 4.5 to the Financial Statements in this Annual Report.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

2. Capital requirements for credit risk

The table below shows the capital requirements for credit risk for each class and subclass of exposures as specified in the Banking (Capital) Rules.

	2012 HK\$'m	2011 HK\$'m
Capital required for exposures under the IRB approach		
Corporate		
Specialised lending under supervisory slotting criteria approach		
– Project finance	115	223
Small-and-medium sized corporate	3,726	3,625
Other corporates	31,896	24,054
Bank		
Banks	9,180	9,913
Securities firms	7	7
Retail		
Residential mortgages		
– Individuals	674	702
– Property-holding shell companies	42	46
Qualifying revolving retail	836	779
Small business retail	79	86
Other retail to individuals	403	409
Others		
Cash items	–	–
Other items	5,879	4,870
Securitisation	12	22
Total capital requirements for exposures under the IRB approach	52,849	44,736
Capital required for exposures under the standardised (credit risk) approach		
On-balance sheet exposures		
Sovereigns	1,333	94
Public sector entities	43	36
Multilateral development banks	–	–
Banks	6	3
Securities firms	–	–
Corporate	1,156	779
Regulatory retail	379	271
Residential mortgage loans	231	173
Other exposures which are not past due	105	76
Past due exposures	3	2
Off-balance sheet exposures		
Off-balance sheet exposures other than OTC derivative transactions and credit derivative contracts	231	162
OTC derivative transactions	7	9
Securitisation	–	–
Total capital requirements for exposures under the standardised (credit risk) approach	3,494	1,605
Total capital requirements for credit risk exposures	56,343	46,341

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach

3.1 The internal rating systems and risk components

The Group adopts the foundation internal ratings-based (“FIRB”) approach to calculate the regulatory capital requirements for most of the corporate and bank exposures, and adopts the supervisory slotting criteria approach to project finance exposures under “specialised lending”. The Group adopts retail IRB approach for retail exposures to individuals and small business. The following is the table showing the Group’s different capital calculation approaches to each asset class and sub-classes of exposures.

Asset class	Exposure sub-class	Capital calculation approach
Corporate exposures	Specialised lending under supervisory slotting criteria approach (project finance)	Supervisory Slotting Criteria Approach
	Small-and-medium sized corporates	FIRB Approach
	Other corporates	FIRB Approach
Sovereign exposures	Sovereigns	Standardised (credit risk) Approach
	Sovereign foreign public sector entities	
	Multilateral development banks	
Bank exposures	Banks	FIRB Approach
	Securities firms	FIRB Approach
	Public sector entities (excluding sovereign foreign public sectors entities)	Standardised (credit risk) Approach
Retail exposures	Residential mortgages to individuals	Retail IRB Approach
	Residential mortgages to property-holding shell companies	
	Qualifying revolving retail	
	Small business retail	
	Other retail to individuals	
Equity exposures		Standardised (credit risk) Approach
Other exposures	Cash items	Specific Risk-weight Approach
	Other items	

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.1 *The internal rating systems and risk components (continued)*

(A) **The structure of internal rating systems and the relationship between internal ratings and external ratings**

The Group's internal rating system is a two dimensional rating system that provides separate assessment of borrower and transaction characteristics. For corporate and bank portfolios, the obligor rating dimension reflects exclusively the risk of borrower default and the facility rating dimension reflects transaction specific factors that affect the loss severity in the case of borrower default.

The Group developed statistical models to provide own estimated probability of default ("PD") for its corporate, bank and all retail borrowers, and loss given default ("LGD") and exposure at default ("EAD") for retail exposures under Retail IRB Approach.

The Group uses internal rating system to assess the borrower's likelihood of default for all IRB portfolios. PD estimates the risk of borrower default over a one-year period. A borrower credit grade means a grouping of similar credit-worthiness to which borrowers are assigned on the basis of specified and distinct set of rating criteria, from which the mid-point PD are derived for RWA calculation.

In the process of obligor rating assignment, variables of latest financial performance, management quality, industry risks and group connection of each obligor are assessed as critical factors to predict borrower's ability and willingness to meet with the contractual obligations under different economic conditions.

The borrowers for corporate and bank, and retail PD pools are assigned into eight broad obligor ratings including seven grades for non-defaulted obligors with sub-divisions into 26 minor credit grades and one for defaulted obligors. In the supervisory slotting criteria approach for the project finance exposures, there are four grades for non-defaulted borrowers and one for defaulted borrowers in accordance with the HKMA guidance. The estimates for retail IRB portfolios are pooled by nature of obligors, facility types, collateral types and delinquency status into PD, EAD and LGD pools. This pooling process provides the basis of accurate and consistent estimation for PD, LGD and EAD at the pool level for exposures arising from residential mortgages to both individuals and property-holding shell companies, qualifying revolving retail exposures and other retail exposures to individuals and small business retail exposures. All credit transactions for corporates and banks are assigned facility ratings (in terms of LGD) in accordance with the HKMA guidance. LGD estimates multiplied by the PD estimates produce the expected loss (EL) estimates, which are used to assess credit risk quantitatively.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.1 The internal rating systems and risk components (continued)

(A) The structure of internal rating systems and the relationship between internal ratings and external ratings (continued)

For each internal rating, the equivalent external rating in terms of default risk is as below:

Internal Credit Grades	Definition of Internal Ratings	Standard & Poor's Equivalent
1	The obligors in grades "1" and "2" have extremely low default risk.	AAA
2	The obligor's capacity to meet its financial commitment on the obligation is extremely strong.	AA+
		AA
		AA-
3	The obligors in grade "3" have low default risk but are somewhat susceptible to the adverse effects of changes in circumstances and economic conditions. However, the obligor's capacity to meet its financial commitment on the obligation is very strong.	A+
		A
		A-
4	The obligors in grade "4" have relatively low default risk and are currently under adequate protection. However, adverse economic conditions or changing circumstances are likely to lead to a weakened capacity of the obligor to meet its financial commitment on the obligation.	BBB+
		BBB
		BBB-
5	The obligors in grade "5" have medium default risk which are less vulnerable to nonpayment than other speculative obligors. However, they face major ongoing uncertainties or exposure to adverse business, financial, or economic conditions which could lead to the obligor's inadequate capacity to meet its financial commitment on the obligation.	BB+
		BB
		BB-
6	The obligors in grade "6" have high default risk and are vulnerable to nonpayment. The obligors currently have the capacity to meet its financial commitment on the obligation but adverse business, financial, or economic conditions will very likely impair the obligor's capacity or willingness to meet its financial commitment on the obligation.	B+
		B
		B-
7	The obligors in grade "7" have very high default risk and are currently quite vulnerable to nonpayment. The obligors' ability to meet their financial commitment and obligation are dependent upon favorable business, financial, and economic conditions. In the event of adverse business, financial, or economic conditions, these obligors are not likely to have the capacity to meet its financial commitment on the obligation.	CCC
		CC
		C
8	Obligors rated "8" are in payment default.	D

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.1 The internal rating systems and risk components (continued)

(B) Use of internal estimates

Besides using PD estimates for regulatory capital calculation in corporate and bank exposures, the Group further developed PD estimates for the sovereign exposures, together with the LGD and EAD estimates for corporate, bank and sovereign exposures developed in 2011 for the purpose of enhancing the use of internal rating estimates. From 2012 onwards, each of corporate, bank, and sovereign exposures is estimated by individual LGD and EAD based on the nature of the facility types, collateral types. The estimates of risk components derived from internal rating systems have been used in credit approval, credit monitoring, reporting and analysis of credit risk information, etc.

(C) Process of managing and recognising credit risk mitigation

For those collaterals recognised under capital management, the Group has well-defined policies and procedures for collateral valuation and management which are compliant with the operational requirements for recognised collateral of credit risk mitigation as stated in the Banking (Capital) Rules.

For the credit exposures adopting FIRB approach for capital calculation purpose, the recognised eligible guarantees include the guarantees provided by banks and securities firms with a lower risk weights than the counterparty; and corporates with internal credit ratings which are equivalent to external credit rating A- or above. The Group takes into account the credit risk mitigation effect of recognised collaterals through its determination of the net credit exposures and the effective LGD.

For retail IRB approach, the effect of the credit risk mitigation is incorporated into the internal risk parameters of PD or LGD depending on the nature of the guarantees and collaterals for calculating the risk exposures.

The credit and market risk concentrations within the credit risk mitigation (recognised collateral and guarantees for capital calculation) used by the Group are under a low level.

Up to the date of report, for capital calculation, the Group has not used any recognised credit derivative contracts, on- or off-balance sheet recognised netting for credit risk mitigation yet.

(D) The control mechanisms used for internal rating systems

The Group has established a comprehensive control mechanism to ensure the integrity, accuracy and consistency of the rating systems including the processes for using the risk components in the day-to-day business to assess credit risk.

All of IRB risk models are approved by the Risk Committee ("RC") of the Board on the recommendation of the Group's Basel II Steering Committee ("SC"). The SC supervises the use of these internal rating models for risk identification and assessments in the Group's credit decisions.

In order to achieve reasonably accurate risk ratings assignment, the Group has established a rating approval process which is independent of the sales and marketing units. Since internal rating is one of the key inputs to credit decision making, a control mechanism is put in place to ensure the integrity, accuracy and consistency of the rating assignment. For the wholesale (corporate and bank) portfolio, internal ratings are normally approved by credit officers who are functionally separated from the sales and marketing units. In some cases where the transactions are in small amount and of very low risk, the credit ratings can be assigned and approved by staff within the sales and marketing units, subject to post-approval review of ratings by Risk Management Department.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.1 The internal rating systems and risk components (continued)

(D) The control mechanisms used for internal rating systems (continued)

The rating assignment and risk quantification process of retail portfolio are highly automated. As an integral part of the daily credit assessment process, the accuracy and completeness of data input for automatic rating assignment are verified by units independent from business development function.

The obligor rating assignment is reviewed at least annually as required by the Group's credit risk policy. When credit events occur to the obligor, rating review is triggered promptly in accordance with the Group's credit risk policy.

Rating override is designed to allow the credit analyst to include any other relevant credit information that has not yet been captured in the rating process. For reasons of conservatism and prudential considerations, overrides are unlimited in terms of downgrades but more restricted for better grades (upgrades). All upgrades will be limited to a maximum of two sub-grades supported by a very narrowly pre-defined list of appropriate reasons. All overrides need to be signed off by a higher level of credit approval authority. The internal rating policy sets a trigger point of 10% overrides on rating cases. The use of overrides and override reasons are analysed as part of performance review on IRB rating models.

The performance of internal rating system is put under ongoing periodic monitoring. The senior management periodically reviews the performance and predictive ability of the internal rating system. The effectiveness of the internal rating system and processes are reviewed by independent control functions. The model maintenance unit conducts assessment on the discriminatory power, accuracy and stability of the rating systems while the validation unit performs comprehensive review of the internal rating system. Internal audit reviews the internal rating system and the operations of the related credit risk control units. The results of the review are reported to the Board and senior management regularly.

A model validation team which is independent from the model development unit and rating assignment units, conducts periodic model validations using both qualitative and quantitative analysis. Model acceptance standards are established to ensure the discriminatory power, accuracy and stability of the rating systems meet regulatory and management requirements. Review of a rating model will be triggered if the performance of the model deteriorates materially against pre-determined tolerance limits.

(E) Approach for determining provisions

The approach in determining provisions is in line with the Group's accounting policies. For details, please refer to Note 2.14 "Impairment of financial assets" to the Financial Statements in this Annual Report.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.2 Exposures by IRB calculation approach

The tables below show the Group's exposures other than securitisation exposures (including the EAD of on-balance sheet exposures and off-balance sheet exposures) by each IRB calculation approach.

	2012				
	Foundation IRB Approach HK\$'m	Supervisory Slotting Criteria Approach HK\$'m	Retail IRB Approach HK\$'m	Specific Risk- weight Approach HK\$'m	Total exposures HK\$'m
Corporate	640,927	1,391	–	–	642,318
Bank	429,712	–	–	–	429,712
Retail					
Residential mortgages to individuals and property- holding shell companies	–	–	209,677	–	209,677
Qualifying revolving retail	–	–	55,256	–	55,256
Other retail to individuals and small business retail	–	–	31,938	–	31,938
Others	–	–	–	163,857	163,857
Total	1,070,639	1,391	296,871	163,857	1,532,758

	2011				
	Foundation IRB Approach HK\$'m	Supervisory Slotting Criteria Approach HK\$'m	Retail IRB Approach HK\$'m	Specific Risk- weight Approach HK\$'m	Total exposures HK\$'m
Corporate	540,672	2,875	–	–	543,547
Bank	438,956	–	–	–	438,956
Retail					
Residential mortgages to individuals and property- holding shell companies	–	–	193,566	–	193,566
Qualifying revolving retail	–	–	50,856	–	50,856
Other retail to individuals and small business retail	–	–	30,899	–	30,899
Others	–	–	–	133,623	133,623
Total	979,628	2,875	275,321	133,623	1,391,447

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.3 Exposures subject to supervisory estimates under the IRB approach

By definition, amounts reported under the supervisory slotting criteria approach continue to be subject to supervisory estimates. The table below shows the total EAD of the Group's exposures subject to supervisory estimates under the use of IRB approach.

	2012 HK\$'m	2011 HK\$'m
Corporate	642,318	543,547
Bank	429,712	438,956
Others	163,857	133,623
	1,235,887	1,116,126

3.4 Exposures covered by credit risk mitigation used

(A) Exposures covered by recognised collateral

The table below shows the Group's exposures (after the effect of any on-balance sheet or off-balance sheet recognised netting) which are covered by recognised collateral after the application of haircuts required under the Banking (Capital) Rules. These exposures exclude OTC derivative transactions and repo-style transactions.

	2012 HK\$'m	2011 HK\$'m
Corporate	97,907	89,764
Bank	440	318
Others	–	–
	98,347	90,082

(B) Exposures covered by recognised guarantees

The table below shows the Group's exposures (after the effect of any on-balance sheet or off-balance sheet recognised netting) which are covered by recognised guarantees after the application of haircuts required under the Banking (Capital) Rules. These exposures exclude OTC derivative transactions and repo-style transactions.

	2012 HK\$'m	2011 HK\$'m
Corporate	20,834	18,660
Bank	17,451	20,360
Retail	–	–
Others	–	–
	38,285	39,020

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.5 Risk assessment for corporate and bank exposures under IRB approach

The tables below detail the Group's total EAD of corporate and bank exposures by exposure-weighted average risk-weight and exposure-weighted average PD for each obligor grade as at 31 December.

The EAD and PD disclosed below in respect of corporate and bank exposures have taken into account the effect of recognised guarantees. No recognised netting was adopted by the Group.

For definition of each obligor grade, please refer to page 236.

(A) Corporate exposures (other than specialised lending under supervisory slotting criteria approach)

Internal Credit Grades	2012		
	Exposure at default HK\$m	Exposure-weighted average risk-weight %	Exposure-weighted average PD %
Grade 1	–	–	–
Grade 2	22,607	16.14	0.04
Grade 3	163,693	24.50	0.07
Grade 4	152,425	45.17	0.25
Grade 5	199,136	84.56	1.20
Grade 6	100,041	133.52	5.59
Grade 7	1,272	220.60	26.72
Grade 8/Default	1,753	153.97	100.00
	640,927		

Internal Credit Grades	2011		
	Exposure at default HK\$m	Exposure-weighted average risk-weight %	Exposure-weighted average PD %
Grade 1	–	–	–
Grade 2	17,031	15.25	0.03
Grade 3	145,987	24.55	0.07
Grade 4	128,251	43.87	0.25
Grade 5	183,532	82.03	1.23
Grade 6	62,308	118.60	5.34
Grade 7	2,982	205.70	21.13
Grade 8/Default	581	193.31	100.00
	540,672		

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.5 Risk assessment for corporate and bank exposures under IRB approach (continued)

(B) Corporate exposures (specialised lending under supervisory slotting criteria approach)

Supervisory Rating Grades	2012		2011	
	Exposure at default HK\$'m	Exposure-weighted average risk-weight %	Exposure at default HK\$'m	Exposure-weighted average risk-weight %
Strong	16	70.00	243	70.00
Good	953	90.00	2,001	83.13
Satisfactory	422	115.00	577	115.00
Weak	–	–	54	250.00
Default	–	–	–	–
	1,391		2,875	

The supervisory rating grades and risk-weights of specialised lending are determined in accordance with section 158 of the Banking (Capital) Rules.

(C) Bank exposures

Internal Credit Grades	2012		
	Exposure at default HK\$'m	Exposure-weighted average risk-weight %	Exposure-weighted average PD %
Grade 1	–	–	–
Grade 2	41,148	16.89	0.04
Grade 3	314,401	22.34	0.06
Grade 4	72,441	41.53	0.20
Grade 5	1,711	62.29	0.56
Grade 6	11	53.36	5.02
Grade 7	–	–	–
Grade 8/Default	–	–	–
	429,712		

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.5 Risk assessment for corporate and bank exposures under IRB approach (continued)

(C) Bank exposures (continued)

Internal Credit Grades	2011		
	Exposure at default HK\$'m	Exposure-weighted average risk-weight %	Exposure-weighted average PD %
Grade 1	–	–	–
Grade 2	56,964	16.54	0.04
Grade 3	296,602	23.87	0.07
Grade 4	81,028	41.91	0.20
Grade 5	4,348	64.55	0.75
Grade 6	14	23.68	7.46
Grade 7	–	–	–
Grade 8/Default	–	–	–
	438,956		

3.6 Risk assessment for retail exposures under IRB approach

The tables below show breakdown of retail exposures on a pool basis by expected loss percentage (EL%) range as at 31 December.

Residential mortgages

	2012 HK\$'m	2011 HK\$'m
Up to 1%	208,576	192,602
>1%	969	850
Default	132	114
	209,677	193,566

Qualifying revolving retail

	2012 HK\$'m	2011 HK\$'m
Up to 10%	54,610	50,218
>10%	624	620
Default	22	18
	55,256	50,856

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.6 Risk assessment for retail exposures under IRB approach (continued)

Other retail

	2012 HK\$'m	2011 HK\$'m
Up to 2%	21,895	19,390
>2%	248	479
Default	78	83
	22,221	19,952

Small business retail

	2012 HK\$'m	2011 HK\$'m
Up to 1%	9,459	10,676
>1%	209	218
Default	49	53
	9,717	10,947

3.7 Analysis of actual loss and estimates

The table below shows the actual losses which represent the net charges (including write-offs and individually assessed impairment allowances) made by each class of exposures under the internal ratings-based approach for the year.

	2012 HK\$'m	2011 HK\$'m
Corporate	488	(12)
Bank	–	3
Residential mortgages to individuals and property-holding shell companies	–	–
Qualifying revolving retail	127	93
Other retail to individuals	12	27
Small business retail	12	8
	639	119

Increase in the impairment charge of corporate exposures was mainly caused by the loan restructuring of a few corporate customers leading to loans downgraded.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.7 Analysis of actual loss and estimates (continued)

The table below shows the expected loss which is the estimated loss likely to be incurred arising from the potential default of the obligors in respect of the exposure over a one-year period.

	Expected loss at 31 December 2011 HK\$m	Expected loss at 31 December 2010 HK\$m
Corporate	2,914	2,539
Bank	189	149
Residential mortgages to individuals and property-holding shell companies	93	97
Qualifying revolving retail	309	268
Other retail to individuals	111	126
Small business retail	32	33
	3,648	3,212

The tables below set out the actual default rate compared against the estimated PD of the respective portfolio.

	Actual default rate during 2012 %	Estimated PD at 31 December 2011 %
Corporate	0.49	1.81
Bank	–	0.48
Residential mortgages to individuals and property-holding shell companies	0.04	0.62
Qualifying revolving retail	0.17	0.61
Other retail to individuals	0.76	1.75
Small business retail	0.58	1.34

	Actual default rate during 2011 %	Estimated PD at 31 December 2010 %
Corporate	0.37	1.73
Bank	0.22	0.44
Residential mortgages to individuals and property-holding shell companies	0.03	0.69
Qualifying revolving retail	0.18	0.60
Other retail to individuals	0.72	1.86
Small business retail	0.48	1.40

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

3. Credit risk under the internal ratings-based approach (continued)

3.7 Analysis of actual loss and estimates (continued)

It should be noted that expected loss and actual loss are measured and calculated using different methodologies compliant to relevant regulatory and accounting standards, which are therefore not directly comparable. The limitation arises mainly from the fundamental differences in the definition of “loss”. The expected loss under Basel II which estimates the economic loss arising from the potential default of the obligor by taking into account the time value of money and including the direct and indirect costs associated with the recoveries on the credit exposures, while actual loss is the net individually assessed impairment charges and write-offs made during the year in accordance with the accounting standards.

The actual default rate (actual PD) is measured by using the number of obligors (for wholesale exposures) or number of accounts (for retail exposures) defaulted whereas the estimated probability of default (estimated PD) is an estimate of the long run average default rate over an economic cycle and is the estimated one-year forward-looking PD from the date of rating assignment.

Hence, actual PD in a particular year (“point-in-time”) will typically differ from the estimated PD which is the “through-the-cycle” estimates as economies move above or below the cyclical norms.

The estimated PD is more conservative than the actual default rate for all asset classes.

4. Credit risk under the standardised (credit risk) approach

4.1 Ratings from External Credit Assessment Institutions (“ECAI”)

The Group continues to adopt standardised (credit risk) (“STC”) approach based on external rating to determine the risk weight of the following asset classes of exposures:

- Sovereign
- Public sector entity
- Multilateral development bank

The Group performs the ECAI issuer ratings mapping to its exposures in banking book in accordance with Part 4 of the Banking (Capital) Rules. The ECAIs recognised by the Group include Standard & Poor’s, Moody’s and Fitch.

4.2 Credit risk mitigation

For credit exposures adopting STC approach, the main types of recognised collaterals include cash deposits, debt securities and shares for non-past due exposures. In addition, real estate collateral is also recognised for past due exposures. The treatment of recognised collateral is compliant with the comprehensive approach for credit risk mitigation as mentioned in the Banking (Capital) Rules. For credit exposures under STC approach, the recognised guarantees for capital calculation includes the guarantee given by sovereigns, public sector entities, multilateral development banks with a lower risk weight than the counterparty, and corporate with external rating of A- or above.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

4. Credit risk under the standardised (credit risk) approach (continued)

4.3 Credit risk exposures other than securitisation exposures under the standardised (credit risk) approach

	2012						
	Total Exposures HK\$m	Exposures after CRM*		Risk-weighted amount		Total exposures covered by recognised collateral HK\$m	Total guarantees or recognised credit derivative contracts HK\$m
		Rated	Unrated	Rated	Unrated		
		HK\$m	HK\$m	HK\$m	HK\$m		
On-balance sheet exposures							
Sovereign	237,263	238,873	-	16,662	-	-	-
Public sector entity	24,584	24,437	-	538	-	-	193
Multilateral development bank	21,769	21,769	-	-	-	-	-
Bank	382	382	-	78	-	-	-
Securities firm	-	-	-	-	-	-	-
Corporate	19,683	9,133	8,927	5,520	8,927	206	1,417
Regulatory retail	6,431	-	6,317	-	4,737	114	-
Residential mortgage loans	5,812	-	5,766	-	2,883	-	46
Other exposures which are not past due	1,560	-	1,317	-	1,317	243	-
Past due exposures	31	-	31	-	39	-	-
Total for on-balance sheet exposures	317,515	294,594	22,358	22,798	17,903	563	1,656
Off-balance sheet exposures							
Off-balance sheet exposures other than OTC derivative transactions and credit derivative contracts	4,682	1,924	2,758	231	2,655	754	386
OTC derivative transactions	144	62	82	4	80	-	-
Total for off-balance sheet exposures	4,826	1,986	2,840	235	2,735	754	386
Total for non-securitisation exposures	322,341	296,580	25,198	23,033	20,638	1,317	2,042
Exposures deducted from Core Capital or Supplementary Capital	116						

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4. Credit risk under the standardised (credit risk) approach (continued)

4.3 Credit risk exposures other than securitisation exposures under the standardised (credit risk) approach (continued)

	2011						
	Total Exposures HK\$m	Exposures after CRM*		Risk-weighted amount		Total exposures covered by recognised collateral HK\$m	Total exposures covered by recognised credit derivative contracts HK\$m
		Rated	Unrated	Rated	Unrated		
		HK\$m	HK\$m	HK\$m	HK\$m		
On-balance sheet exposures							
Sovereign	285,206	290,546	–	1,172	–	–	–
Public sector entity	23,204	23,020	–	448	–	–	193
Multilateral development bank	22,491	22,491	–	–	–	–	–
Bank	210	210	–	43	–	–	–
Securities firm	–	–	–	–	–	–	–
Corporate	18,268	6,188	6,615	3,118	6,615	318	5,147
Regulatory retail	4,644	–	4,514	–	3,385	130	–
Residential mortgage loans	4,346	–	4,337	–	2,168	–	9
Other exposures which are not past due	1,078	–	946	–	946	132	–
Past due exposures	15	–	15	–	23	–	–
Total for on-balance sheet exposures	359,462	342,455	16,427	4,781	13,137	580	5,349
Off-balance sheet exposures							
Off-balance sheet exposures other than OTC derivative transactions and credit derivative contracts	3,871	1,954	1,917	226	1,797	556	218
OTC derivative transactions	177	58	119	1	117	–	–
Total for off-balance sheet exposures	4,048	2,012	2,036	227	1,914	556	218
Total for non-securitisation exposures	363,510	344,467	18,463	5,008	15,051	1,136	5,567
Exposures deducted from Core Capital or Supplementary Capital	84						

* Recognised credit risk mitigation satisfying the requirements and conditions set out in the Banking (Capital) Rules.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

5. Counterparty credit risk-related exposures

The Group's counterparty credit risk arising from over-the-counter ("OTC") derivative transactions, repo-style transactions both in trading and banking book is subject to the same risk management framework as mentioned in Note 4 to the Financial Statements in this Annual Report. The Group establishes credit limit through formal credit approval procedures to control the pre-settlement credit risk arising from OTC derivative transactions and settlement limit to control the settlement risk arising from foreign exchange-related transactions in both the trading book and banking book. The Group monitors the risk exposure due to fluctuations in the market by using the current exposure and the potential exposure value of the transactions. Exceptions or excesses are timely and closely identified and monitored by Risk Management Department.

Currently, the Group uses the Current Exposure Method to measure and monitor the counterparty credit exposures, which comprises current exposures and potential future exposures.

The Group establishes prudent eligibility criteria and haircut policy of debt securities being pledged as collateral for repo-style transactions.

The Group formulates policy for classification of credit assets according to the PD of individual counterparty and the period of overdue. If there is objective evidence that an impairment loss has been incurred, impairment allowance will be provided according to HKFRS and regulatory requirements.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

5. Counterparty credit risk-related exposures (continued)

5.1 Counterparty credit risk exposures

The following tables summarise the Group's exposures to counterparty credit risk arising from OTC derivative and repo-style transactions.

(A) Counterparty credit risk exposures under the internal ratings-based approach

	2012 HK\$'m	2011 HK\$'m
OTC derivative:		
Gross total positive fair value	12,884	7,435
Credit equivalent amounts	22,591	14,680
Less: Value of recognised collateral		
– debt securities	–	–
– others	–	–
Net credit equivalent amounts	22,591	14,680
Exposure at default by counterparty type		
Corporate	797	1,521
Banks	21,794	13,159
Retail	–	–
Others	–	–
	22,591	14,680
Risk weighted amounts by counterparty type		
Corporate	509	1,402
Banks	4,443	2,906
Retail	–	–
Others	–	–
	4,952	4,308
Repo-style transactions:		
Net credit exposures	–	3,488
Exposure at default by counterparty type		
Corporate	–	–
Banks	–	3,488
Retail	–	–
Others	–	–
	–	3,488
Risk weighted amounts by counterparty type		
Corporate	–	–
Banks	–	1,852
Retail	–	–
Others	–	–
	–	1,852

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

5. Counterparty credit risk-related exposures (continued)

5.1 Counterparty credit risk exposures (continued)

(B) Counterparty credit risk exposures under the standardised (credit risk) approach

	2012 HK\$'m	2011 HK\$'m
OTC derivative:		
Gross total positive fair value	41	83
Credit equivalent amounts	144	177
Less: Value of recognised collateral		
– debt securities	–	–
– others	–	–
Net credit equivalent amounts	144	177
Credit equivalent amounts net of recognised collateral by counterparty type		
Sovereign	51	57
Public sector entity	5	–
Bank	5	2
Corporate	75	107
Regulatory retail	8	6
Other exposures which are not past due exposures	–	5
Past due exposures	–	–
	144	177
Risk weighted amounts by counterparty type		
Sovereign	–	–
Public sector entity	1	–
Bank	3	1
Corporate	74	107
Regulatory retail	6	5
Other exposures which are not past due exposures	–	5
Past due exposures	–	–
	84	118

There are no outstanding repo-style transactions under the standardised (credit risk) approach as at 31 December 2012 (2011: Nil).

There is no effect of valid bilateral netting agreement on the credit equivalent amounts of the derivative transactions as at 31 December 2012 (2011: Nil).

There are no outstanding credit derivative contracts as at 31 December 2012 (2011: Nil).

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6. Assets securitisation

The Group continues to adopt the ratings-based method under IRB approach to calculate the credit risk for both securitisation and re-securitisation exposures as an investing institution in the year 2012. Since this approach employs mapping of external credit ratings for risk weights calculations, the Group adopts the three ECAs (Standard & Poor's, Moody's and Fitch) recognised by HKMA for this purpose.

The Group monitors the risks inherent in its securitisation assets and re-securitisation assets on an ongoing basis. The external credit ratings, assessment of the underlying assets and market prices are used for managing credit risk associated with the investment. For interest rate risk in its banking book, control measures for asset backed securities and mortgage backed securities include, but not limited to AFS EV and PVBP.

The Group has no outstanding exposures that are held with the intention of transferring exposures booked in the banking book and trading book into securitisation transactions as at 31 December 2012.

Securitisation exposures arising from the Group's investing activities are analysed as follows:

6.1 Securitisation exposures

	2012
	On-balance sheet Banking Book HK\$'m
Residential mortgage loans	1,156
Commercial mortgage loans	–
Student loans	172
Re-securitisations	3
	1,331
	2011*
	HK\$'m
Residential mortgage loans	1,780
Commercial mortgage loans	5
Student loans	467
	2,252

* As a result of the new requirements under Banking (Disclosure) (Amendment) Rules 2011, the amounts shown are not directly comparable with those of 31 December 2012.

There are no on-balance sheet securitisation exposures booked in trading book as at 31 December 2012.

There are no off-balance sheet securitisation exposures booked in banking and trading books as at 31 December 2012.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

6. Assets securitisation (continued)

6.1 Securitisation exposures (continued)

There are no securitisation transactions in trading book subject to the IMM approach as at 31 December 2012.

There are no securitisation exposures deducted from core and/or supplementary capital as at 31 December 2012 and 2011.

The Group has no credit risk mitigations which are treated as part of securitisation and re-securitisation transactions as at 31 December 2012.

The Group has no credit derivative contracts which are treated as part of synthetic securitisation transactions as at 31 December 2011.

6.2 Breakdown by risk-weights of the securitisation exposures (excluding re-securitisation exposures) under internal ratings-based (securitisation) approach

	2012	
	Securitisation exposures HK\$m	Capital requirements HK\$m
7%	1,043	6
8%	51	–
10%	59	1
12%	105	1
15%	–	–
18%	–	–
20%	–	–
25%	–	–
35%	–	–
50%	–	–
60%	50	2
75%	–	–
100%	20	2
250%	–	–
425%	–	–
650%	–	–
Deducted from capital	–	–
	1,328	12

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

6. Assets securitisation (continued)

6.3 Breakdown by risk-weights of the re-securitisation exposures under internal ratings-based (securitisation) approach

	2012	
	Securitisation exposures HK\$m	Capital requirements HK\$m
20%	-	-
25%	-	-
30%	-	-
35%	3	-
40%	-	-
50%	-	-
60%	-	-
65%	-	-
100%	-	-
150%	-	-
200%	-	-
225%	-	-
300%	-	-
500%	-	-
650%	-	-
750%	-	-
850%	-	-
Deducted from capital	-	-
	3	-

6.4 Breakdown by risk-weights of the securitisation exposures (including re-securitisation exposures) under internal ratings-based (securitisation) approach

	2011*		
	Securitisation exposures HK\$m	Risk-weighted amount HK\$m	Capital requirements HK\$m
7%	1,817	134	11
8%	61	5	1
10%	111	12	1
12%	100	13	1
35%	34	13	1
60%	105	67	5
100%	24	26	2
Deducted from capital	-	-	-
	2,252	270	22

* As a result of the new requirements under Banking (Disclosure) (Amendment) Rules 2011, the amounts shown are not directly comparable with those of 31 December 2012.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

6. Assets securitisation (continued)

6.5 Summary of accounting policies for securitisation exposures

The Group held certain securitised debt securities at the end of the reporting period. They are classified and measured for accounting purpose in accordance with the Group's accounting policies as outlined in Note 2.8 "Financial assets". For those investments measured at fair value, further details on their valuation are outlined in Note 4.6(B) "Financial instruments measured at fair value".

7. Capital requirements for market risk

	2012 HK\$'m	2011 HK\$'m
Under the standardised (market risk) approach		
Foreign exchange exposures (net)	–	432
Interest rate exposures		
– non-securitisation exposure	117	240
Equity exposures	36	36
Commodity exposures	6	9
Under the internal models approach		
General foreign exchange and interest rate exposures	747	908
Capital charge for market risk	906	1,625

In 2012, market risk regulatory capital charge is calculated under the Banking (Capital) (Amendment) Rules 2011 to incorporate capital charge for stressed VAR. The following table sets out the IMM VAR and stressed VAR¹ for the general market risk exposure calculated under the IMM approach of the Group.

	Year	At 31 December HK\$'m	Minimum for the year HK\$'m	Maximum for the year HK\$'m	Average for the year HK\$'m
IMM VAR for foreign exchange and interest rate risk	2012	38.5	35.0	105.1	63.9
IMM VAR for foreign exchange risk	2012	19.7	16.2	70.1	36.3
IMM VAR for interest rate risk	2012	24.9	15.5	104.9	44.8
Stressed VAR for foreign exchange and interest rate risk	2012	221.9	140.7	334.6	217.4
Stressed VAR for foreign exchange risk	2012	25.0	24.3	73.2	43.2
Stressed VAR for interest rate risk	2012	216.9	133.2	339.1	218.3

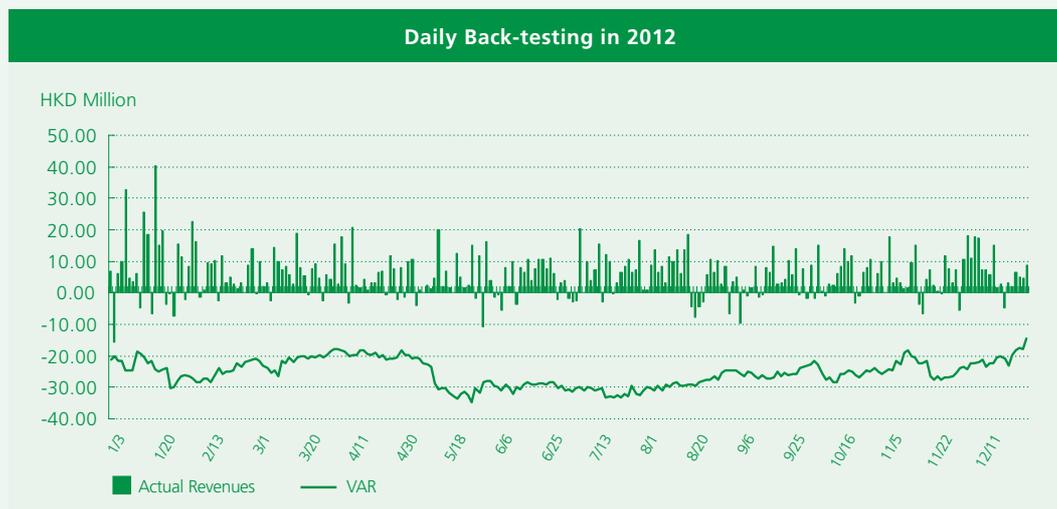
Note:

¹ IMM VAR and stressed VAR measures used for market risk regulatory capital purposes are calculated to a 99% confidence level and use a 10-day holding period. The stressed VAR uses the same methodology as the VAR model and is generated with inputs calibrated to the historical data from a continuous 12-month period of significant financial stress relevant to the Group's portfolio.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

7. Capital requirements for market risk (continued)

The graph below shows the regulatory back-testing result of the Group's market risk under IMM approach.



There were no actual losses exceeding the VAR estimates for the Group in 2012 as shown in the back-testing results.

8. Capital requirements for operational risk

	2012 HK\$'m	2011 HK\$'m
Capital charge for operational risk	4,421	4,065

The Group uses the standardised (operational risk) approach to calculate its operational risk capital charge.

9. Equity exposures in banking book

Equity holdings in other entities are accounted for in accordance with the underlying intentions of holdings at the inception of acquisition. The classifications for equity holdings taken for relationship and strategic purposes will be separated from those taken for other purposes (including capital appreciation). Investments in equity shares which are intended to be held on a continuing basis, but which do not comprise investments in associates, jointly controlled entities or subsidiaries, are classified as available-for-sale securities and are reported in the balance sheet as "Investment in securities".

For equity exposures in banking book other than associates, jointly controlled entities or subsidiaries, the Group applies the same accounting treatment and valuation methodologies as detailed in the Notes 2.8(4) and 2.11 to the Financial Statements. If additional investment is made subsequently such that an investee becomes an associate, jointly controlled entity or subsidiary, then the investment is reclassified in accordance with the Group's accounting policies.

Gains or losses related to equity exposures are summarised below:

	2012 HK\$'m	2011 HK\$'m
Realised gains from sales	6	36
Unrealised gains on revaluation recognised in reserves but not through profit or loss	771	526
Unrealised gains included in supplementary capital	347	237

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

10. Connected transactions

In 2012, BOCHK, a wholly-owned subsidiary of the Company, and its subsidiaries engaged on a regular basis in the usual course of their business in numerous transactions with BOC and its Associates. As BOC is the Company's controlling shareholder and therefore a connected person of the Company, all such transactions constituted connected transactions for the purposes of the Listing Rules. 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. Central Huijin is the ultimate controlling shareholder of the Company. Central Huijin has accepted PRC Government's authorisation in carrying out equity investment in core financial enterprises. For the purposes of this report, therefore, Central Huijin and its Associates have not been treated as connected persons to the Company.

The transactions fell into the following two categories:

1. exempted transactions entered into in the usual course of business and under normal commercial terms. Such transactions were exempted from disclosure and independent shareholder approval by virtue of Rules 14A.31, 14A.33 and 14A.65 of the Listing Rules;
2. certain continuing connected transactions conducted pursuant to the Services and Relationship Agreement entered into among, inter alia, the Company and BOC dated 6 July 2002 (as amended and supplemented from time to time and the latest amendment was for a period of three years commencing 1 January 2011), whereas BOC has agreed to, and agreed to procure its Associates to, enter into all future arrangements with the Group on an arm's length basis, on normal commercial terms and at rates no less favourable than those offered to independent third parties, in relation to certain areas including, among others, information technology services, training services, physical bullion agency services, correspondent banking arrangements, treasury transactions, provision of insurance and syndicated loans, and the Company has agreed to, and agreed to procure its subsidiaries to, enter into all future arrangements on the same basis, provided that the rates offered by the Group to BOC and its Associates will be no more favourable than those offered to independent third parties. The Services and Relationship Agreement is also amended to allow for the provision of (i) call centre services, cash management services and card services and other related business between BOC or its Associates and the Group; and (ii) information technology services by the Group to BOC's worldwide branches and subsidiaries. On 30 December 2010 the Company made an announcement (the "Announcement") in accordance with Rule 14A.47 of the Listing Rules, and has got the approval from the independent shareholders on 25 May 2011. The Announcement listed those continuing connected transactions that exceeded the de minimus threshold and set out caps in respect of such transactions for the three years 2011-2013. These transactions were conducted in the ordinary course of its business and on normal commercial terms. Details of these continuing connected transactions are set out below and are described in the announcements which may be viewed at the Company's website. The Company has complied with the disclosure requirements in accordance with Chapter 14A of the Listing Rules.

Type of Transaction	2012 Cap (HK\$'m)	2012 Actual Amount (HK\$'m)
Information Technology Services	1,000	48
Property Transactions	1,000	137
Bank-note Delivery	1,000	114
Provision of Insurance Cover	1,000	127
Card Services	1,000	104
Custody Business	1,000	36
Call Center Services	1,000	48
Securities Transactions	5,000	226
Fund Distribution Transactions	5,000	39
Insurance Agency	5,000	589
Foreign Exchange Transactions	5,000	195
Trading of Financial Assets	150,000	8,208
Inter-bank Capital Markets	150,000	1,714

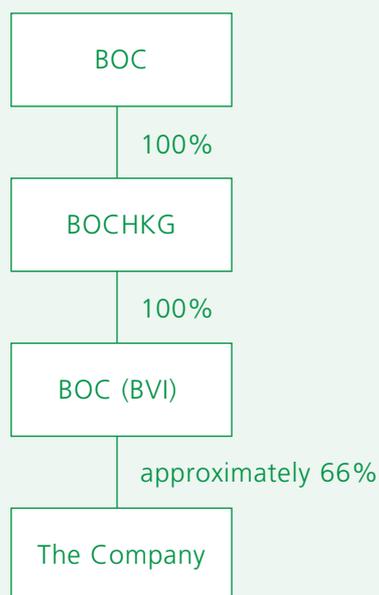
UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

11. Reconciliation between HKFRSs vs IFRS/CAS

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

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

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



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

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

11. Reconciliation between HKFRSs vs IFRS/CAS (continued)

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

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. As the investment securities matured gradually, the related timing difference will be eliminated.

(b) Restatement of carrying value of bank premises

The Company has elected for a revaluation model rather than cost model to account for bank premises and investment properties under HKFRSs. On the contrary, BOC has elected for the cost model for bank premises and revaluation model 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.

As the counterpart of IFRS/CAS to the amendment to HKAS 12 has already been mandatorily effective since 1 January 2012, there is no more difference due to early adoption of the amendment in HKFRSs by the Company.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

11. Reconciliation between HKFRSs vs IFRS/CAS (continued)

Profit after tax/net assets reconciliation

HKFRSs vs IFRS/CAS

	Profit after tax		Net assets	
	2012 HK\$'m	2011 HK\$'m	2012 HK\$'m	2011 HK\$'m
Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under HKFRSs	21,547	20,813	155,074	133,183
Add: IFRS/CAS adjustments				
Re-measurement of carrying value of treasury products	(12)	(27)	–	–
Restatement of carrying value of bank premises	658	488	(35,148)	(26,124)
Deferred tax adjustments	(106)	(33)	5,798	4,305
Effect of early adoption of HKAS 12 (Amendment)	–	(323)	–	(1,778)
Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under IFRS/CAS	22,087	20,918	125,724	109,586

APPENDIX

Subsidiaries of the Company

The particulars of our subsidiaries are as follows:

Name of company	Place and date of incorporation/ operation/ registration	Issued and fully paid up share capital/ registered capital/ units in issue	Interest held	Principal activities
Directly held:				
Bank of China (Hong Kong) Limited	Hong Kong 16 October 1964	Ordinary shares HK\$43,042,840,858	100.00%	Banking business
BOC Group Life Assurance Company Limited*	Hong Kong 12 March 1997	Ordinary shares HK\$3,038,000,000	51.00%	Life insurance business
BOCHK Asset Management (Cayman) Limited*	Cayman Islands 7 October 2010	Ordinary shares HK\$50,000,000	100.00%	Investment holding
Indirectly held:				
Nanyang Commercial Bank, Limited	Hong Kong 2 February 1948	Ordinary shares HK\$700,000,000	100.00%	Banking business
Chiyu Banking Corporation Limited	Hong Kong 24 April 1947	Ordinary shares HK\$300,000,000	70.49%	Banking business
BOC Credit Card (International) Limited	Hong Kong 9 September 1980	Ordinary shares HK\$480,000,000	100.00%	Credit card services
Bank of China (Hong Kong) Nominees Limited*	Hong Kong 1 October 1985	Ordinary shares HK\$2	100.00%	Nominee services
Bank of China (Hong Kong) Trustees Limited*	Hong Kong 6 November 1987	Ordinary shares HK\$3,000,000	100.00%	Trustee and agency services
BNPP Flexi III China Fund*	Luxembourg 15 December 2009	Units in issue HK\$1,774,924,940	51.00%	Investment
BOC Group Trustee Company Limited*	Hong Kong 1 December 1997	Ordinary shares HK\$200,000,000	64.20%	Trustee services
BOC Travel Services Limited*	Hong Kong 24 August 1982	Ordinary shares HK\$2,000,000	100.00%	Travel services
BOCG Life Aggressive Growth Fund*	Hong Kong 8 November 2002	Units in issue US\$2,025,311	51.00%	Investment
BOCG Life Moderate Growth Fund*	Hong Kong 8 November 2002	Units in issue US\$1,459,633	51.00%	Investment
BOCG Life Stable Growth Fund*	Hong Kong 8 November 2002	Units in issue US\$167,586	51.00%	Investment

APPENDIX

Subsidiaries of the Company (continued)

Name of company	Place and date of incorporation/ operation/ registration	Issued and fully paid up share capital/ registered capital/ units in issue	Interest held	Principal activities
BOCG Life Money Market Fund*	Hong Kong 8 November 2002	Units in issue US\$156,228	51.00%	Investment
BOCHK Asset Management Limited*	Hong Kong 28 October 2010	Ordinary shares HK\$39,500,000	100.00%	Asset management
BOCHK Financial Products (Cayman) Limited	Cayman Islands 10 November 2006	Ordinary shares US\$50,000	100.00%	Issuing structured notes
BOCHK Information Technology (Shenzhen) Co., Ltd.*	PRC 16 April 1990	Registered capital HK\$70,000,000	100.00%	Property holding and investment
BOCHK Information Technology Services (Shenzhen) Ltd.*	PRC 26 May 1993	Registered capital HK\$40,000,000	100.00%	Information technology services
BOCI-Prudential Trustee Limited*	Hong Kong 11 October 1999	Ordinary shares HK\$300,000,000	41.10%	Trustee services
Che Hsing (Nominees) Limited*	Hong Kong 23 April 1980	Ordinary shares HK\$10,000	100.00%	Nominee services
Chiyu Banking Corporation (Nominees) Limited*	Hong Kong 3 November 1981	Ordinary shares HK\$100,000	70.49%	Investment holding
Chung Chiat Company Limited	Hong Kong 9 April 1980	Ordinary shares HK\$200	100.00%	Property holding and investment
Grace Charter Limited*	Hong Kong 4 May 2001	Ordinary shares HK\$2	70.49%	Investment holding
G.Z.Y. Microfilm Technology (Shenzhen) Co., Ltd.*	PRC 24 September 1993	Registered capital HK\$40,000,000	100.00%	Property holding and investment
Kincheng Investments & Developments (H.K.) Limited	Hong Kong 15 May 1981	Ordinary shares HK\$6,000	100.00%	Property holding and investment
Kincheng (Nominees) Limited*	Hong Kong 12 December 1980	Ordinary shares HK\$100,000	100.00%	Nominee services
Kiu Nam Investment Corporation Limited*	Hong Kong 9 November 1963	Ordinary shares HK\$2,000,000	100.00%	Property holding and investment
Kwong Li Nam Investment Agency Limited*	Hong Kong 25 May 1984	Ordinary shares HK\$3,050,000	100.00%	Investment agency

Subsidiaries of the Company (continued)

Name of company	Place and date of incorporation/ operation/ registration	Issued and fully paid up share capital/ registered capital/ units in issue	Interest held	Principal activities
Nanyang Commercial Bank (China), Limited	PRC 14 December 2007	Registered capital RMB6,500,000,000	100.00%	Banking business
Nanyang Commercial Bank (Nominees) Limited*	Hong Kong 22 August 1980	Ordinary shares HK\$50,000	100.00%	Nominee services
Nanyang Commercial Bank Trustee Limited*	Hong Kong 22 October 1976	Ordinary shares HK\$3,000,000	100.00%	Trustee services
Po Hay Enterprises Limited*	Hong Kong 2 October 1979	Ordinary shares HK\$100,000	100.00%	Property holding and investment
Po Sang Financial Investment Services Company Limited*	Hong Kong 23 September 1980	Ordinary shares HK\$95,000,000	100.00%	Gold trading and investment holding
Po Sang Futures Limited*	Hong Kong 19 October 1993	Ordinary shares HK\$95,000,000	100.00%	Securities and futures brokerage
Seng Sun Development Company, Limited*	Hong Kong 11 December 1961	Ordinary shares HK\$2,800,000	70.49%	Investment holding
Sin Chiao Enterprises Corporation, Limited*	Hong Kong 13 September 1961	Ordinary shares HK\$3,000,000	100.00%	Property holding and investment
Sin Hua Trustee Limited*	Hong Kong 27 October 1978	Ordinary shares HK\$3,000,000	100.00%	Trustee services
Sin Mei (Nominee) Limited*	Hong Kong 27 April 1982	Ordinary shares HK\$100,000	100.00%	Nominee services
Sin Yeh Shing Company Limited*	Hong Kong 28 November 1980	Ordinary shares HK\$100,000	100.00%	Property holding and investment
Sino Information Services Company Limited*	Hong Kong 11 February 1993	Ordinary shares HK\$7,000,000	100.00%	Information services
The China-South Sea (Nominees) Services Limited*	Hong Kong 13 February 1981	Ordinary shares HK\$100,000	100.00%	Nominee services
Track Link Investment Limited*	Hong Kong 8 February 1994	Ordinary shares HK\$2	100.00%	Property holding and investment

APPENDIX

Subsidiaries of the Company (continued)

G.Z.Y. Microfilm Technology (Shenzhen) Co., Ltd. commenced winding up on 26 December 2011.

Nanyang Finance Company Limited and Nan Song Company, Limited were dissolved on 16 February 2012.

Patson (HK) Limited was dissolved on 19 March 2012.

Dwell Bay Limited and Shenstone Limited were dissolved on 17 July 2012.

Perento Limited was dissolved on 27 July 2012.

Kincheng Investments & Developments (H.K.) Limited commenced members' voluntary winding up on 16 October 2012.

BOC Travel Services Limited commenced members' voluntary winding up on 23 November 2012.

Kincheng Finance (H.K.) Limited was dissolved on 28 December 2012.

Sin Mei (Nominee) Limited, Kincheng (Nominees) Limited, Sin Yeh Shing Company Limited, Track Link Investment Limited, Po Hay Enterprises Limited and Kiu Nam Investment Corporation Limited have been dissolved on 19 January 2013.

Chung Chiat Company Limited and The China-South Sea (Nominees) Services Limited have been dissolved on 23 February 2013.

Remarks:

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

DEFINITIONS

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

Terms	Meanings
"ABS"	Asset-backed Securities
"ADR"	American Depositary Receipt
"ADS(s)"	American Depositary Share(s)
"ALCO"	the Asset and Liability Management Committee
"ATM"	Automated Teller Machine
"Associates"	has the meaning ascribed to "associates" in the Listing Rules
"BOC"	Bank of China Limited, a joint stock commercial bank with limited liability established under the laws of the PRC, the H shares and A shares of which are listed on the Hong Kong Stock Exchange and the Shanghai Stock Exchange respectively
"BOC (BVI)"	BOC Hong Kong (BVI) Limited, a company incorporated under the laws of the British Virgin Islands and a wholly-owned subsidiary of BOCHKG
"BOC-CC"	BOC Credit Card (International) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOCHK
"BOCG Insurance"	Bank of China Group Insurance Company Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOC
"BOCHK Charitable Foundation"	Bank of China (Hong Kong) Limited Charitable Foundation (formerly known as the "Bank of China Group Charitable Foundation"), a charitable foundation being established in July 1994
"BOCHKG"	BOC Hong Kong (Group) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOC
"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
"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
"BOC Life"	BOC Group Life Assurance Company Limited, a company incorporated under the laws of Hong Kong, in which the Group and BOCG Insurance hold equity interests of 51% and 49% respectively
"Board" or "Board of Directors"	the Board of Directors of the Company

DEFINITIONS

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 for Business Enterprises
"CE"	Chief Executive
"CIC"	China Investment Corporation
"CRM"	Credit Risk Mitigation
"CRO"	Chief Risk Officer
"Central Huijin"	Central Huijin Investment Ltd.
"Chiyu"	Chiyu Banking Corporation Limited, a company incorporated under the laws of Hong Kong, in which BOCHK holds an equity interest of 70.49%
"DCE"	Deputy Chief Executive
"EAD"	Exposure at Default
"ECAI(s)"	External Credit Assessment Institution(s)
"EL"	Expected Loss
"EURIBOR"	Euro Interbank Offered Rate
"EV"	Economic Value Sensitivity Ratio
"FIRB"	Foundation Internal Ratings-based
"Fitch"	Fitch Ratings
"GDP"	Gross Domestic Product
"HIBOR"	Hong Kong Interbank Offered Rate
"HKAS(s)"	Hong Kong Accounting Standard(s)
"HKFRS(s)"	Hong Kong Financial Reporting Standard(s)
"HK GAAP"	Generally Accepted Accounting Principles in Hong Kong
"HKICPA"	Hong Kong Institute of Certified Public Accountants
"HK(IFRIC)-Int"	Hong Kong (IFRIC) Interpretation
"HKMA"	Hong Kong Monetary Authority
"HK(SIC)-Int"	Hong Kong (SIC) Interpretation
"Hong Kong" or "Hong Kong SAR"	Hong Kong Special Administrative Region
"ICAAP"	Internal Capital Adequacy Assessment Process
"IFRS"	International Financial Reporting Standards
"IMM"	Internal Models
"IPO"	Initial Public Offering
"IRB"	Internal Ratings-based
"IT"	Information Technology

DEFINITIONS

Terms	Meanings
"LGD"	Loss Given Default
"LIBOR"	London Interbank Offered Rate
"LSC"	Legal Services Centre
"Listing Rules"	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited
"MBS"	Mortgage-backed Securities
"MC"	the Management Committee
"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
"Mainland" or "Mainland China"	the mainland of the PRC
"Medium Term Note Programme"	the medium term note programme was established by BOCHK on 2 September 2011
"Moody's"	Moody's Investors Service
"NCB (China)"	Nanyang Commercial Bank (China), Limited, a company incorporated under the laws of the PRC and a wholly-owned subsidiary of Nanyang
"Nanyang"	Nanyang Commercial Bank, Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOCHK
"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
"PBOC"	People's Bank of China
"PD"	Probability of Default
"PRC"	the People's Republic of China
"PVBP"	Price Value of a Basis Point
"QDIIs"	Qualified Domestic Institutional Investors
"RC"	the Risk Committee
"RMB" or "Renminbi"	Renminbi, the lawful currency of the PRC
"RMB RTGS"	RMB Real Time Gross Settlement
"RMD"	the Risk Management Department
"RQFII"	Renminbi Qualified Foreign Institutional Investors
"RWA"	Risk-weighted Assets
"SC"	Steering Committee
"SFO"	the Securities and Futures Ordinance, Chapter 571 of the Laws of Hong Kong
"SME(s)"	Small and Medium-sized Enterprise(s)
"STC"	Standardised (Credit Risk)
"STM"	Standardised (Market Risk)
"STO"	Standardised (Operational Risk)

DEFINITIONS

Terms	Meanings
"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 "Hong Kong Stock Exchange" or "Stock Exchange of Hong Kong"	The Stock Exchange of Hong Kong Limited
"the Company"	BOC Hong Kong (Holdings) Limited, a company incorporated under the laws of Hong Kong
"the Group"	the Company and its subsidiaries collectively referred as the Group
"UK"	United Kingdom
"US"	the United States of America
"VAR"	Value at Risk

BRANCH NETWORK & CORPORATE BANKING CENTRES

Bank of China (Hong Kong) – Branch Network Hong Kong Island

Branch	Address	Telephone
Central & Western District		
Bank of China Tower Branch	1 Garden Road, Hong Kong	2826 6888
Sheung Wan Branch	252 Des Voeux Road Central, Hong Kong	2541 1601
Queen's Road West (Sheung Wan) Branch	2-12 Queen's Road West, Sheung Wan, Hong Kong	2815 6888
Connaught Road Central Branch	13-14 Connaught Road Central, Hong Kong	2841 0410
Central District Branch	2A Des Voeux Road Central, Hong Kong	2160 8888
Central District (Wing On House) Branch	71 Des Voeux Road Central, Hong Kong	2843 6111
Shek Tong Tsui Branch	534 Queen's Road West, Shek Tong Tsui, Hong Kong	2819 7277
Western District Branch	386-388 Des Voeux Road West, Hong Kong	2549 9828
Shun Tak Centre Branch	Shop 225, 2/F, Shun Tak Centre, 200 Connaught Road Central, Hong Kong	2291 6081
Queen's Road Central Branch	81-83 Queen's Road Central, Hong Kong	2588 1288
Bonham Road Branch	63 Bonham Road, Hong Kong	2517 7066
Kennedy Town Branch	Harbour View Garden, 2-2F Catchick Street, Kennedy Town, Hong Kong	2818 6162
Caine Road Branch	57 Caine Road, Hong Kong	2521 3318
First Street Branch	55A First Street, Sai Ying Pun, Hong Kong	2517 3399
United Centre Branch	Shop 1021, United Centre, 95 Queensway, Hong Kong	2861 1889
Wyndham Street Branch	1-3 Wyndham Street, Central, Hong Kong	2843 2888
Des Voeux Road West Branch	111-119 Des Voeux Road West, Hong Kong	2546 1134
Gilman Street Branch	136 Des Voeux Road Central, Hong Kong	2135 1123
Wan Chai District		
409 Hennessy Road Branch	409-415 Hennessy Road, Wan Chai, Hong Kong	2835 6118
Johnston Road Branch	152-158 Johnston Road, Wan Chai, Hong Kong	2574 8257
Harbour Road Branch	Shop 4, G/F, Causeway Centre, 28 Harbour Road, Wan Chai, Hong Kong	2827 8407
Jardine's Bazaar Branch	G/F, Siki Centre, No.23 Jardine's Bazaar, Causeway Bay, Hong Kong	2882 1383
Happy Valley Wealth Management Centre	Nos. 49-51A, Sing Woo Road, Happy Valley, Hong Kong	3982 8270
Happy Valley Branch	11 King Kwong Street, Happy Valley, Hong Kong	2838 6668
Causeway Bay Branch	505 Hennessy Road, Causeway Bay, Hong Kong	3982 8068
Percival Street Branch	18 Percival Street, Causeway Bay, Hong Kong	2572 4273
Wan Chai (China Overseas Building) Branch	139 Hennessy Road, Wan Chai, Hong Kong	2529 0866
Wan Chai (Wu Chung House) Branch	213 Queen's Road East, Wan Chai, Hong Kong	2892 0909
Hennessy Road (Wan Chai) Branch	310-312 Hennessy Road, Wan Chai, Hong Kong	2923 5628
Eastern District		
Siu Sai Wan Branch	Shop 19, Cheerful Garden, Siu Sai Wan, Hong Kong	2505 2399
Taikoo Shing Branch	Shop P1025-1026, Chi Sing Mansion, Taikoo Shing, Hong Kong	2967 9128
Taikoo Shing Branch Safe Box Service Centre	Shop G1006, Hoi Shing Mansion, Taikoo Shing, Hong Kong	2885 4582
North Point Branch	Roca Centre, 464 King's Road, North Point, Hong Kong	2811 8880
North Point (King's Centre) Branch	193-209 King's Road, North Point, Hong Kong	2286 2000
North Point (Hang Ying Building) Branch	Shop B1, 318-328 King's Road, North Point, Hong Kong	2887 1199
North Point (Kiu Fai Mansion) Branch	413-415 King's Road, North Point, Hong Kong	2562 6108
Sai Wan Ho Branch	142-146 Shau Kei Wan Road, Sai Wan Ho, Hong Kong	2886 3344
Lee Chung Street Branch	29-31 Lee Chung Street, Chai Wan, Hong Kong	2557 3283
Heng Fa Chuen Branch	Shop 205-208, East Wing Shopping Centre, Heng Fa Chuen, Chai Wan, Hong Kong	2897 1131
Kam Wa Street Branch	3 Kam Wa Street, Shau Kei Wan, Hong Kong	2885 9311
City Garden Branch	233 Electric Road, North Point, Hong Kong	2571 2878
King's Road Branch	131-133 King's Road, North Point, Hong Kong	2887 0282
Chai Wan Branch	Block B, Walton Estate, 341-343 Chai Wan Road, Chai Wan, Hong Kong	2558 6433
Chai Wan Branch Safe Box Service Centre	27 Gold Mine Building, 345 Chai Wan Road, Chai Wan, Hong Kong	2557 0248
Healthy Village Branch	Shop 1&2, Healthy Village Phase II, 668 King's Road, North Point, Hong Kong	2563 2278
Sheung On Street Branch	77 Sheung On Street, Chai Wan, Hong Kong	2897 0923
Aldrich Garden Branch	Shop 58, Aldrich Garden, Shau Kei Wan, Hong Kong	3196 4956
Quarry Bay Branch	Parkvale, 1060 King's Road, Quarry Bay, Hong Kong	2564 0333
Shau Kei Wan (Po Man Building) Branch	260-262 Shau Kei Wan Road, Shau Kei Wan, Hong Kong	3550 5000

Branch	Address	Telephone
Southern District		
Tin Wan Branch	2-12 Ka Wo Street, Tin Wan, Hong Kong	2553 0135
Aberdeen Branch	25 Wu Pak Street, Aberdeen, Hong Kong	2553 4165
South Horizons Branch	G38, West Centre Marina Square, South Horizons, Ap Lei Chau, Hong Kong	2580 0345
South Horizons Branch Safe Box Service Centre	Shop 118, Marina Square East Centre, Ap Lei Chau, Hong Kong	2555 7477
Wah Kwai Estate Branch	Shop 17, Shopping Centre, Wah Kwai Estate, Hong Kong	2550 2298
Chi Fu Landmark Branch	Shop 510, Chi Fu Landmark, Pok Fu Lam, Hong Kong	2551 2282
Ap Lei Chau Branch	13-15 Wai Fung Street, Ap Lei Chau, Hong Kong	2554 6487
Stanley Branch	Shop No.301B, Stanley Plaza, Hong Kong	3982 8188

Kowloon

Branch	Address	Telephone
Kowloon City District		
Prince Edward Road (Kowloon City) Branch	382-384 Prince Edward Road, Kowloon City, Kowloon	2926 6038
To Kwa Wan Branch	80N To Kwa Wan Road, To Kwa Wan, Kowloon	2364 4344
Pak Tai Street Branch	4-6 Pak Tai Street, To Kwa Wan, Kowloon	2760 7773
Hung Hom Wealth Management Centre	37-39 Ma Tau Wai Road, Hung Hom, Kowloon	2170 0888
Hung Hom (Eldex Industrial Building) Branch	21 Ma Tau Wai Road, Hung Hom, Kowloon	2764 8363
OUHK Branch	The Open University of Hong Kong, 30 Good Shepherd Street, Ho Man Tin, Kowloon	2760 9099
Ma Tau Kok Road Branch	39-45 Ma Tau Kok Road, To Kwa Wan, Kowloon	2714 9118
Ma Tau Wai Road Branch	47-49 Ma Tau Wai Road, Hung Hom, Kowloon	2926 5123
Site 11 Whampoa Garden Branch	Shop G6, Site 11 Whampoa Garden, Hung Hom, Kowloon	2363 3982
Whampoa Garden Branch	Shop G88, Site 1, Whampoa Garden, Hung Hom, Kowloon	2764 7233
Nga Tsin Wai Road Branch	25 Nga Tsin Wai Road, Kowloon City, Kowloon	2383 2316
Waterloo Road Branch	Shop A2, Man Kee Mansion, 86 Waterloo Road, Kowloon	2363 9231
Wong Tai Sin District		
Tai Yau Street Branch	35 Tai Yau Street, San Po Kong, Kowloon	2328 0087
Chuk Yuen Estate Branch	Shop S1, Chuk Yuen Shopping Centre, Chuk Yuen South Estate, Kowloon	2325 5261
Choi Hung Branch	19 Clear Water Bay Road, Ngau Chi Wan, Kowloon	2327 0271
Choi Hung Road Branch	58-68 Choi Hung Road, San Po Kong, Kowloon	2927 6111
Choi Wan Estate Branch	A3-18 Commercial Complex, Choi Wan Estate, Kowloon	2754 5911
Wong Tai Sin Branch	Shop G13, Wong Tai Sin Plaza, Wong Tai Sin, Kowloon	2327 8147
San Po Kong (Wing Lok Building) Branch	28-34 Tseuk Luk Street, San Po Kong, Kowloon	2328 7915
Yuk Wah Street Branch	46-48 Yuk Wah Street, Tsz Wan Shan, Kowloon	2927 6655
Lok Fu Branch	Shop 2, Lok Fu Plaza II, Lok Fu, Kowloon	2337 0271
Tseuk Luk Street Wealth Management Centre	86 Tseuk Luk Street, San Po Kong, Kowloon	2326 2883
Diamond Hill Branch	G107 Plaza Hollywood, Diamond Hill, Kowloon	2955 5088
Kwun Tong District		
169 Ngau Tau Kok Road Branch	169 Ngau Tau Kok Road, Ngau Tau Kok, Kowloon	2750 7311
177 Ngau Tau Kok Road Branch	177 Ngau Tau Kok Road, Ngau Tau Kok, Kowloon	2927 4321
Wang Kwun Road Branch	Unit G1, Nan Fung Commercial Centre, Wang Kwun Road, Kowloon Bay, Kowloon	2755 0268
Sau Mau Ping Branch	Shop 214, Sau Mau Ping Shopping Centre, Sau Mau Ping, Kowloon	2772 0028
Hip Wo Street Branch	195-197 Hip Wo Street, Kwun Tong, Kowloon	2345 0102
Yau Tong Branch	Shop G1-G27, Ka Fu Arcade, Yau Tong Centre, Kowloon	2349 9191
Hoi Yuen Road Branch	55 Hoi Yuen Road, Kwun Tong, Kowloon	2763 2127
Tsui Ping Estate Branch	Shop 116, 1/F Shopping Circuit, Tsui Ping Estate, Kwun Tong, Kowloon	2345 3238
26 Fu Yan Street Branch	26-32 Fu Yan Street, Kwun Tong, Kowloon	2342 5262
Telford Gardens Wealth Management Centre	Shop P8A, Telford Gardens, Kowloon Bay, Kowloon	2758 3987
Telford Gardens Branch	Shop P2, Telford Gardens, Kowloon Bay, Kowloon	2796 1551
Lam Tin Branch	Shop 12, 49 Kai Tin Road, Lam Tin, Kowloon	2347 1456
Kwun Tong Branch	20-24 Yue Man Square, Kwun Tong, Kowloon	2344 4116

BRANCH NETWORK & CORPORATE BANKING CENTRES

Bank of China (Hong Kong) – Branch Network (continued)

Branch	Address	Telephone
Ngau Tau Kok Road (Kwun Tong) Branch	327 Ngau Tau Kok Road, Kwun Tong, Kowloon	2389 3301
Kwun Tong Plaza Branch	G1 Kwun Tong Plaza, 68 Hoi Yuen Road, Kwun Tong, Kowloon	2342 4295
Kowloon Bay Branch	Shop 2, Telford House, 16 Wang Hoi Road, Kowloon Bay, Kowloon	2759 9339
Yau Tsim Mong District		
Tai Kok Tsui Branch	73-77 Tai Kok Tsui Road, Tai Kok Tsui, Kowloon	2395 3269
Shan Tung Street Branch	42-48 Shan Tung Street, Mong Kok, Kowloon	2332 5461
China Hong Kong City Branch	Shop 28, UG/F, China Hong Kong City, 33 Canton Road, Tsim Sha Tsui, Kowloon	2367 6164
Shanghai Street (Prince Edward) Branch	689-693 Shanghai Street, Mong Kok, Kowloon	2391 0502
Prince Edward Branch	774 Nathan Road, Kowloon	2399 3000
Tsim Sha Tsui Branch	24-28 Carnarvon Road, Tsim Sha Tsui, Kowloon	2721 6242
Tsim Sha Tsui East Branch	Shop G02-03, Inter-Continental Plaza, 94 Granville Road, Tsim Sha Tsui, Kowloon	2739 0308
Jordan Branch	328-330 Nathan Road, Kowloon	2928 6111
Jordan Road Branch	1/F, Sino Cheer Plaza, 23-29 Jordan Road, Kowloon	2730 0883
Shanghai Street (Mong Kok) Branch	611-617 Shanghai Street, Mong Kok, Kowloon	2394 4181
Mong Kok Branch	589 Nathan Road, Mong Kok, Kowloon	2332 0111
Prince Edward Road West (Mong Kok) Branch	116-118 Prince Edward Road West, Mong Kok, Kowloon	2928 4138
Mong Kok Road Branch	50-52 Mong Kok Road, Mong Kok, Kowloon	2395 3263
Mong Kok (Silvercorp Int'l Tower) Branch	Shop B, 707-713 Nathan Road, Mong Kok, Kowloon	2391 6677
Mong Kok (President Commercial Centre) Branch	608 Nathan Road, Mong Kok, Kowloon	2384 7191
Yau Ma Tei Branch	471 Nathan Road, Yau Ma Tei, Kowloon	2780 2307
Kimberley Road Branch	37 Kimberley Road, Tsim Sha Tsui, Kowloon	2739 1886
Cameron Road Wealth Management Centre	30 Cameron Road, Tsim Sha Tsui, Kowloon	2312 0010
Humphrey's Avenue Branch	4-4A Humphrey's Avenue, Tsim Sha Tsui, Kowloon	2311 3822
Olympian City Branch	Shop 133, 1/F, Olympian City 2, 18 Hoi Ting Road, Kowloon	2749 2110
Fuk Tsun Street Branch	32-40 Fuk Tsun Street, Tai Kok Tsui, Kowloon	2391 8468
Canton Road Branch	60 Canton Road, Tsim Sha Tsui, Kowloon	2730 0688
Sham Shui Po District		
Kowloon Plaza Branch	Unit 1, Kowloon Plaza, 485 Castle Peak Road, Kowloon	2370 8928
Festival Walk Branch	Unit LG256, Festival Walk, Kowloon Tong, Kowloon	2265 7288
Yu Chau Street Branch	42-46 Yu Chau Street, Sham Shui Po, Kowloon	2397 1123
Dragon Centre Branch	Shop 206A, Dragon Centre, 37K Yen Chow Street, Sham Shui Po, Kowloon	2788 3238
Lei Cheng Uk Estate Branch	Shop 108, Lei Cheng Uk Commercial Centre, Lei Cheng Uk Estate, Kowloon	2729 8251
Castle Peak Road (Cheung Sha Wan) Branch	365-371 Castle Peak Road, Cheung Sha Wan, Kowloon	2728 3311
108 Cheung Sha Wan Road Branch	108 Cheung Sha Wan Road, Sham Shui Po, Kowloon	2779 0157
194 Cheung Sha Wan Road Branch	194-196 Cheung Sha Wan Road, Sham Shui Po, Kowloon	2728 9389
Cheung Sha Wan Plaza Branch	Shop G08, Cheung Sha Wan Plaza, 833 Cheung Sha Wan Road, Kowloon	2745 7088
223 Nam Cheong Street Branch	223 Nam Cheong Street, Sham Shui Po, Kowloon	2928 2088
Stage 2 Mei Foo Sun Chuen Branch	19 Glee Path, Mei Foo Sun Chuen, Kowloon	2370 8382
Mei Foo Wealth Management VIP Centre	Shop N47-49, Mount Sterling Mall, Mei Foo Sun Chuen, Kowloon	2742 8003
Mei Foo Mount Sterling Mall Branch	17-B Mount Sterling Mall, Mei Foo Sun Chuen, Kowloon	2742 6611
Sham Shui Po Branch	207-211 Nam Cheong Street, Sham Shui Po, Kowloon	2777 0171
Sham Shui Po (On Ning Building) Branch	147-149 Castle Peak Road, Sham Shui Po, Kowloon	2708 3678

New Territories & Outlying Islands

Branch	Address	Telephone
Sha Tin District		
41 Tai Wai Road Branch	41-45 Tai Wai Road, Sha Tin, New Territories	2929 4288
74 Tai Wai Road Branch	74-76 Tai Wai Road, Sha Tin, New Territories	2699 9523
Fo Tan Branch	No 2, 1/F Shatin Galleria, 18-24 Shan Mei Street, Fo Tan, New Territories	2691 7193
Lucky Plaza Branch	Lucky Plaza, Wang Pok Street, Sha Tin, New Territories	2605 6556

Branch	Address	Telephone
Sha Tin Wealth Management VIP Centre	Shop 18, L1, Shatin Plaza, Sha Tin, New Territories	2688 7668
Sha Kok Estate Branch	Shop 39, Sha Kok Shopping Centre, Sha Kok Estate, Sha Tin, New Territories	2648 0302
Heng On Estate Branch	Shop 203, Commercial Centre, Heng On Estate, Ma On Shan, New Territories	2642 0111
Ma On Shan Plaza Branch	Shop 2103, Level 2, Ma On Shan Plaza, Sai Sha Road, Ma On Shan, New Territories	2631 0063
Lung Hang Estate Branch	103 Lung Hang Commercial Centre, Sha Tin, New Territories	2605 8618
New Town Plaza Branch	Shop 608, Level 6 Phase One, New Town Plaza, Sha Tin, New Territories	2606 6163
Lek Yuen Branch	No 1, Fook Hoi House, Lek Yuen Estate, Sha Tin, New Territories	2605 3021
City One Sha Tin Branch	Shop Nos. 24-25, Ngan Shing Commercial Centre, City One, Sha Tin, New Territories	2648 8083
Tai Po District		
Tai Po Branch	68-70 Po Heung Street, Tai Po Market, New Territories	2657 2121
Tai Po Plaza Branch	Unit 4, Level 1 Tai Po Plaza, 1 On Tai Road, Tai Po, New Territories	2665 5890
On Chee Road Branch	Shop 10-11, Jade Plaza, 3 On Chee Road, Tai Po, New Territories	2665 1966
Fu Heng Estate Branch	Shop 1-2, Fu Heng Shopping Centre, Tai Po, New Territories	2661 6278
Fu Shin Estate Branch	Shop G11, Fu Shin Shopping Centre, Tai Po, New Territories	2663 2788
Kwong Fuk Road Branch	40-50 Kwong Fuk Road, Tai Po Market, New Territories	2658 2268
Sai Kung District		
East Point City Branch	Shop 101, East Point City, Tseung Kwan O, New Territories	2628 7238
HKUST Branch	The Hong Kong University of Science & Technology, Clear Water Bay Road, New Territories	2358 2345
Tseung Kwan O Plaza Branch	Shop 112-125, Level 1, Tseung Kwan O Plaza, Tseung Kwan O, New Territories	2702 0282
Metro City Branch	Shop 209, Level 2, Metro City Phase 1, Tseung Kwan O, New Territories	2701 4962
Hau Tak Estate Branch Securities Services Centre	Shop 15, Hau Tak Shopping Centre, Tseung Kwan O, New Territories	2703 5749
Sai Kung Branch	Shop No. 56 & 58, Sai Kung Town Centre, 22-40 Fuk Man Road, Sai Kung, New Territories	2792 1465
Tsuen Wan District		
Clague Garden Branch	Shop 1-3, Commercial Complex, Clague Garden Estate, 24 Hoi Shing Road, Tsuen Wan, New Territories	2412 2202
Citywalk Branch	Shop 65, G/F, Citywalk, 1 Yeung Uk Road, Tsuen Wan, New Territories	2920 3211
Tsuen Wan Branch	297-299 & 313 Sha Tsui Road, Tsuen Wan, New Territories	2411 1321
Castle Peak Road (Tsuen Wan) Branch	201-207 Castle Peak Road, Tsuen Wan, New Territories	2416 6577
Sham Tseng Branch	Shop G1 & G2, Rhine Garden, Sham Tseng, New Territories	2491 0038
Texaco Road Branch	Shop A112, East Asia Gardens, 36 Texaco Road, Tsuen Wan, New Territories	2414 4287
Castle Peak Road (Tsuen Wan) Branch Securities Services Centre	167 Castle Peak Road, Tsuen Wan, New Territories	2406 1746
Kwai Tsing District		
Ha Kwai Chung Branch	192-194 Hing Fong Road, Kwai Chung, New Territories	2424 9823
Sheung Kwai Chung Branch	7-11 Shek Yi Road, Sheung Kwai Chung, New Territories	2480 6161
Cheung Hong Estate Branch	201-202 Commercial Centre No 2, Cheung Hong Estate, Tsing Yi Island, New Territories	2497 7718
Cheung Fat Estate Branch	Shop 317, Cheung Fat Shopping Centre, Tsing Yi Island, New Territories	2433 1689
Cheung Hong Estate Commercial Centre Branch	2 G/F, Commercial Centre, Cheung Hong Estate, Tsing Yi Island, New Territories	2497 0325
Maritime Square Branch	Shop 115, Maritime Square, Tsing Yi Island, New Territories	2436 9298
Lei Muk Shue Branch	Shop 22, Lei Muk Shue Shopping Centre, Kwai Chung, New Territories	2428 5731
Metroplaza Branch	Shop 260-265, Metroplaza, 223 Hing Fong Road, Kwai Chung, New Territories	2420 2686

BRANCH NETWORK & CORPORATE BANKING CENTRES

Bank of China (Hong Kong) – Branch Network (continued)

Branch	Address	Telephone
Kwai Cheong Road Branch	40 Kwai Cheong Road, Kwai Chung, New Territories	2480 3311
Kwai Chung Road Branch	1009 Kwai Chung Road, Kwai Chung, New Territories	2424 3021
Kwai Chung Plaza Branch	A18-20, G/F Kwai Chung Plaza, 7-11 Kwai Foo Road, Kwai Chung, New Territories	2920 2468
Tuen Mun District		
Tuen Mun Wealth Management Centre	Shop 5, Level 1, North Wing, Trend Plaza, Tuen Mun, New Territories	2404 9777
Tuen Mun Town Plaza Branch	Shop 2, Tuen Mun Town Plaza phase II, Tuen Mun, New Territories	2450 8877
Tuen Mun Fa Yuen Branch	Shop G & H, 6 Tsing Hoi Circuit, Tuen Mun, New Territories	2458 1033
Tuen Mun San Hui Branch	G13-G14 Eldo Court, Heung Sze Wui Road, Tuen Mun, New Territories	2457 3501
Siu Hong Court Branch	226 Commercial Centre, Siu Hong Court, Tuen Mun, New Territories	2466 6703
Kin Wing Street Branch	24-30 Kin Wing Street, Tuen Mun, New Territories	2465 2212
Venice Gardens Branch	Shop13-15, G/F Venice Gardens, Leung Tak Street, Tuen Mun, New Territories	2455 1288
Butterfly Estate Branch	Shop Nos. L187-195, Level 1, Butterfly Plaza, Tuen Mun, New Territories	2920 5188
Leung King Estate Branch	Shop No. L221 and L222, Level 2, Leung King Plaza, Leung King Estate, 31 Tin King Road, Tuen Mun, New Territories	2463 3855
Yuen Long District		
Tai Tong Road Branch	Shop A135, 1/F Hop Yick Plaza, 23 Tai Tong Road, Yuen Long, New Territories	2479 2113
Yuen Long Branch	102-108 Castle Peak Road, Yuen Long, New Territories	2474 2211
Castle Peak Road (Yuen Long) Branch	162 Castle Peak Road, Yuen Long, New Territories	2476 2193
Yuen Long (Hang Fat Mansion) Branch	8-18 Castle Peak Road, Yuen Long, New Territories	2475 3777
Kau Yuk Road Branch	18-24 Kau Yuk Road, Yuen Long, New Territories	2473 2833
Kingswood Villas Branch	A189 Kingswood Richly Plaza, Tin Shui Wai, New Territories	2448 3313
Kingswood Ginza Branch	Shop G64, Phase 1 Kingswood Ginza, Tin Shui Wai, New Territories	2616 4233
Tin Shui Estate Branch	Shop No. G30, Tin Shui Shopping Centre, Tin Shui Wai, New Territories	2445 8728
North District		
Sheung Shui Centre Branch	Shop 1007-1009, Level 1, Sheung Shui Centre, Sheung Shui, New Territories	2670 3131
Sheung Shui Branch	61 San Fung Avenue, Sheung Shui, New Territories	2671 0155
Sha Tau Kok Branch	Block 16-18, Sha Tau Kok Chuen, Sha Tau Kok, New Territories	2674 4011
Flora Plaza Branch	Shop 28, Flora Plaza, 88 Pak Wo Road, Fanling, New Territories	2675 6683
Fanling Centre Branch	Shop 2D-E & H, Fanling Centre, Fanling, New Territories	2669 7899
Luen Wo Market Branch	17-19 Wo Fung Street, Luen Wo Market, Fanling, New Territories	2675 5113
Luen Wo Market Branch Safe Box Service Centre	Shop B, 10-16 Luen Shing Street, Luen Wo Market, Fanling, New Territories	2683 1662
Sheung Shui Branch Securities Services Centre	136 San Fung Avenue, Sheung Shui, New Territories	2672 3738
Choi Yuen Plaza Branch	Shop 3, 3/F, Choi Yuen Plaza, Sheung Shui, New Territories	2671 6783
Outlying Island District		
Cheung Chau Branch	53-55 Tai Sun Street, Cheung Chau, New Territories	2981 0021
Hong Kong International Airport Branch	Unit 77075, Passenger Terminal Building, Hong Kong International Airport	2326 1883

Corporate Banking Centres & SME Centres

Network & Centres	Address	Telephone
Corporate Finance	10/F, Bank of China Tower, 1 Garden Road, Hong Kong	3982 7078
Corporate Business I	10/F, Bank of China Tower, 1 Garden Road, Hong Kong	2826 6889
Corporate Business II	9/F, Bank of China Tower, 1 Garden Road, Hong Kong	3982 6509
Commercial Business I	Unit 701-706, The Gateway Tower 3 (Prudential Tower), 21 Canton Road, Tsim Sha Tsui, Kowloon	3982 7300
Commercial Business II	9/F, Bank of China Tower, 1 Garden Road, Hong Kong	3982 6555

Network & Centres	Address	Telephone
Hong Kong Central and West Commercial Centre	24/F, Bank of China Tower, 1 Garden Road, Hong Kong	3982 6513
Hong Kong Central and West SME Centre		
Hong Kong East Commercial Centre	13/F, Cambridge House, Taikoo Place, 981 King's Road, Island East, Hong Kong	3982 7398
Hong Kong East SME Centre		
Kowloon East Commercial Centre	25/F, Millennium City 5, 418 Kwun Tong Road, Kwun Tong, Kowloon	3982 7600
Kowloon East SME Centre		
Kowloon West Commercial Centre	9/F, BOC Mongkok Commercial Centre, 589 Nathan Road, Mongkok, Kowloon	3982 7700
Kowloon West SME Centre		
New Territories East Commercial Centre	3/F, 68-70 Po Heung Street, Tai Po Market, New Territories	3982 7888
New Territories East SME Centre		
Fo Tan Commercial Centre	Room 1408, 14/F, Shatin Galleria, 18-24 Shan Mei Street, Fo Tan, Shatin, New Territories	3982 7800
Fo Tan SME Centre		
New Territories West Commercial Centre	Unit 1316-1325, Level 13, Metroplaza Tower 1, 223 Hing Fong Road, Kwai Chung, New Territories	3982 7900
New Territories West SME Centre		
Financial Institutions	33/F, Bank of China Tower, 1 Garden Road, Hong Kong	2903 6666
Trade Product	5/F, Bank of China Centre, Olympian City, 11 Hoi Fai Road, West Kowloon	3198 3544

Nanyang Commercial Bank – Branch Network

Branch	Address	Telephone
Head Office	151 Des Voeux Road, Central, Hong Kong	2852 0888
Hong Kong Island		
Western Branch	1/F & 2/F, 359-361 Queen's Road Central, Hong Kong	2851 1100
Causeway Bay Branch	472 Hennessy Road, Causeway Bay, Hong Kong	2832 9888
Happy Valley Branch	29 Wong Nei Chung Road, Happy Valley, Hong Kong	2893 3383
Kennedy Town Branch	86 Belcher's Street, Kennedy Town, Hong Kong	2817 1946
Quarry Bay Branch	1014 King's Road, Quarry Bay, Hong Kong	2563 2286
Des Voeux Road West Branch	334 Des Voeux Road West, Hong Kong	2540 4532
Aberdeen Branch	Shop A, 171 Aberdeen Main Road, Aberdeen, Hong Kong	2553 4115
North Point Branch	351 King's Road, North Point, Hong Kong	2566 8116
Sai Wan Ho Branch	63 Shaukeiwan Road, Sai Wan Ho, Hong Kong	2567 0315
Wanchai Branch	123 Johnston Road, Wanchai, Hong Kong	2574 8118
Causeway Centre Branch	Shop Nos 9-10, Ground Floor, Causeway Centre, 28 Harbour Road, Wanchai, Hong Kong	2827 6338
Central District Branch	2/F Century Square, 1-13 D'Aguiar Street, Central, Hong Kong	2522 5011
Sunning Road Branch	8 Sunning Road, Causeway Bay, Hong Kong	2882 7668
Kowloon		
Mongkok Branch	727 Nathan Road, Mongkok, Kowloon	2394 8206
Yaumati Branch	309 Nathan Road, Yaumati, Kowloon	2782 9888
Ferry Point Branch	Offices B-D, 10/F and Shops D-F, G/F, Best-O-Best Commercial Centre, 32-36 Ferry Street, Yaumati, Kowloon	2332 0738
Homantin Branch	G/F-2/F, 67B Waterloo Road, Kowloon	2715 7518
Nathan Road Branch	570 Nathan Road, Mongkok, Kowloon	2780 0166
Laichikok Road Branch	236 Laichikok Road, Shamshuipo, Kowloon	2396 4164
Jordan Road Branch	20 Jordan Road, Yaumati, Kowloon	2735 3301
Tokwawan Branch	62 Tokwawan Road, Kowloon	2764 6666
Kwun Tong Branch	G/F Shop 1, 1/F Shop 2, 410 Kwun Tong Road, Kowloon	2389 6266
Tsimshatsui Branch	G/F, Cheong Hing Building, 72 Nathan Road, Tsim Sha Tsui, Kowloon	2376 3988
Hungghom Branch	69A Wuhu Street, Hungghom, Kowloon	2362 2301
Shamshuipo Branch	198-200 Tai Po Road, Shamshuipo, Kowloon	2777 0147
Yee On Street Branch	Shops 4-6, G/F, Yee On Centre, 45 Hong Ning Road, Kowloon	2790 6688
Peninsula Centre Branch	Shop G48 Peninsula Centre, 67 Mody Road, Tsimshatsui, Kowloon	2722 0823
San Po Kong Branch	41-45, Yin Hing Street, San Po Kong, Kowloon	2328 5555
Kowloon City Branch	86 Nga Tsin Wai Road, Kowloon City, Kowloon	2716 6033
Laguna City Branch	Shop No. 26, Phase 1 Laguna City, Cha Kwo Ling Road, Kowloon	2772 3336
Kowloon Bay Branch	Shop 2, G/F, Shun Fat Industrial Building, 17 Wang Hoi Road, Kowloon Bay, Kowloon	2769 6268

BRANCH NETWORK & CORPORATE BANKING CENTRES

Nanyang Commercial Bank – Branch Network (continued)

Branch	Address	Telephone
New Territories		
Kwai Chung Branch	100 Lei Muk Road, Kwai Chung, New Territories	2480 1118
Tai Po Branch	Shop No. 11, G/F, Treasure Garden, 1 On Chee Road, Tai Po, New Territories	2656 5201
Yuen Long Branch	G/F, Tung Yik Building, Tai Tong Road, Yuen Long, New Territories	2479 0231
Ha Kwai Chung Branch	180 Hing Fong Road, Kwai Chung, New Territories	2429 4242
Tsuen Wan Branch	78 Chung On Street, Tsuen Wan, New Territories	2492 0243
Sheung Shui Branch	31 Fu Hing Street, Sheung Shui, New Territories	2679 4333
Tuen Mun Branch	Forward Mansion, Yan Ching Circuit, Tuen Mun, New Territories	2459 8181
Shatin Branch	Shop 7-8, Lucky Plaza, Shatin, New Territories	2605 9188
Fou Wah Centre Branch	Shop A, 2/F, Fou Wah Centre, 210 Castle Peak Road, Tsuen Wan, New Territories	2498 4411
Sai Kung Branch	Shop 11-12 Sai Kung Garden, Man Nin Street, New Territories	2791 1122
Offshore		
Shanghai Branch	Block A, F6, Nanyang Commercial Bank Building, No.800 Century Avenue, Shanghai, China	(86-21) 6887 9801
San Francisco Branch	505 Montgomery Street, Suite 1200, San Francisco, CA94111, USA	(1-415) 398 8866

Chiyu Banking Corporation – Branch Network

Branch	Address	Telephone
Hong Kong Island		
Central Branch	78, Des Voeux Road Central, Hong Kong	2843 0187
North Point Branch	390-394 King's Road, North Point, Hong Kong	2570 6381
Wanchai Branch	325 Hennessy Road, Wanchai, Hong Kong	2572 2823
Sheung Wan Branch	Shop 3, G/F, Lee Fung Building, 315-319 Queen's Road Central, Hong Kong	2544 1678
Western Branch	443 Queen's Road West, Hong Kong	2548 2298
Quarry Bay Branch	967-967A, King's Road, Quarry Bay, Hong Kong	2811 3131
Aberdeen Branch	G/F, 138-140, Aberdeen Main Road, Aberdeen, Hong Kong	2553 0603
Kowloon		
Hung Hom Branch	23-25 Gillies Avenue, Hung Hom, Kowloon	2362 0051
Kwun Tong Branch	Factory A, G/F, Lucky (Kwun Tong) Industrial Building, 398-402 Kwun Tong Road, Kowloon	2343 4174
Sham Shui Po Branch	235-237 Laichikok Road, Kowloon	2789 8668
San Po Kong Branch	61-63 Hong Keung Street, San Po Kong, Kowloon	2328 5691
Yau Ma Tei Branch	117-119 Shanghai Street, Yau Ma Tei, Kowloon	2332 2533
Castle Peak Road Branch	G/F, 226-228 Castle Peak Road, Kowloon	2720 5187
Kowloon Bay Branch	Shop10, G/F, Kai Lok House, Kai Yip Estate, Kowloon Bay, Kowloon	2796 8968
Tokwawan Branch	G/F, Shop 11-13, 78 Tokwawan Road, Kowloon	2765 6118
Tsz Wan Shan Branch	Shop 703A, 7/F, Tsz Wan Shan Shopping Centre, 23 Yuk Wah Street, Tsz Wan Shan, Kowloon	2322 3313
New Territories		
Yau Oi Estate Branch	Shop 103-104, G/F, Restaurant Block, Yau Oi Estate, Tuen Mun, New Territories	2452 3666
Kwai Hing Estate Branch	Shop 1, G/F, Hing Yat House, Kwai Hing Estate, Kwai Chung, New Territories	2487 3332
Tai Wo Estate Branch	Shop 112-114, G/F, On Wo House, Tai Wo Estate, Tai Po, New Territories	2656 3386
Belvedere Garden Branch	Shop 5A, G/F, Belvedere Square, Tsuen Wan, New Territories	2411 6789
Tsuen Wan Branch	Shop 1 & 1D, Level 2, Discovery Park Commercial Centre, Tsuen Wan, New Territories	2413 8111
Sui Wo Court Branch	Shop F7, Commercial Centre, Sui Wo Court, Shatin, New Territories	2601 5888
Ma On Shan Branch	Shop 313, Level 3, Ma On Shan Plaza, Bayshore Tower, Ma On Shan, New Territories	2640 0733
Sheung Tak Estate Branch	Shop 238, Sheung Tak Shopping Centre, Sheung Tak Estate, Tseung Kwan O, New Territories	2178 2278
The Mainland of China		
Fuzhou Branch	1/F, International Building, 210 Wusi Road, Fuzhou, Fujian Province, China	(86-591) 8781 0078
Xiamen Branch	1/F, Unit 111-113, No.861 Xiah Road, Xiamen, Fujian Province, China	(86-592) 585 7690

Branch	Address	Telephone
Xiamen Jimel Sub-Branch	No.68-71, Lehai Bei Li, Jimel District, Xiamen, Fujian Province, China	(86-592) 619 3302
Guanyinshan Sub-Branch	Unit 1702E, 1703A, No. 9 Building, 170 Tapu East Road, Guanyinshan CBD, Xiamen, Fujian Province, China	(86-592) 599 0520

Nanyang Commercial Bank (China) – Branch Network

Branch	Address	Telephone
The Mainland of China		
Head Office	Nanyang Commercial Bank Building, No.800 Century Avenue, Pudong District, Shanghai, China	(86-21) 3856 6666
Shenzhen Branch	L140-142, Tower 4, Excellence Century Center, Fuhua 3rd Road, Futian District, Shenzhen, China	(86-755) 8233 0230
Shenzhen Shekou Sub-Branch	G/F, Finance Centre, No.22 Taizi Road, Shekou, Nanshan District, Shenzhen, China	(86-755) 2682 8788
Shenzhen Luohu Sub-Branch	G/F, The Kwangtung Provincial Bank Building, No.1013, South Ren Min Road, Luohu District, Shenzhen, China	(86-755) 2515 6333
Shenzhen Futian Sub-Branch	1/F, Shen Ye Garden Club House, Caitian Road, Futian District, Shenzhen, China	(86-755) 8294 2929
Shenzhen Baoan Sub-Branch	Unit 108 Xushida Garden, Xin An Si Road, Baoan District 34-2, Shenzhen, China	(86-755) 2785 3302
Shenzhen Jiabin Sub-Branch	1/F, Block C, Nanyang Mansion, No.2002 Jianshe Road, Luohu District, Shenzhen, China	(86-755) 8220 9955
Shenzhen Houhai Sub-Branch	L184-185, Tiley Central Plaza II, Central Area, Nanshan District, Shenzhen, China	(86-755) 8663 6200
Dongguan Sub-Branch	No.C-112, C-204, Dingfeng International Plaza, No.19 Dongguan Avenue, Dongcheng District, Dongguan, China	(86-769) 2662 6888
Haikou Branch	1/F, Time Square, No.2 Guomao Road, Haikou, Hainan, China	(86-898) 6650 0038
Guangzhou Branch	Room 402 & R03-04, Skygalleria CITIC Plaza, No.233 North Tianhe Road, Tianhe District, Guangzhou, China	(86-20) 3891 2668
Guangzhou Panyu Sub-Branch	C001-C008 & C101-C106, No.2 West Fuhua Road, Shiqiao, Panyu District, Guangzhou, China	(86-20) 3451 0228
Guangzhou Yuexiu Sub-Branch	Room 01, Huayitai Plaza, No.418 Dong Feng Zhong Road, Yuexiu District, Guangzhou, China	(86-20) 8378 2668
Foshan Sub-Branch	Room 403-405 and Ground Floor P5/P6, Jinhai Plaza, No. 21 Jihua Wu Road Chancheng District, Foshan, China	(86-757) 8290 3368
Dalian Branch	1/F, Anho Building, No.87 Renmin Road, Dalian, China	(86-411) 3984 8888
Beijing Branch	1/F A, B, C, D Areas and 2F, Tower B, Jiacheng Plaza, 18 Xiaguangli, North Dongsanhuan Road, Chao Yang District, Beijing, China	(86-10) 5839 0888
Beijing Jianguomen Sub-Branch	Level 1A, No.88 Jianguomen Wai Da Jie, Chaoyang District, Beijing, China	(86-10) 6568 4728
Beijing Zhongguancun Sub-Branch	Room 105 & 106, Ground Floor, No.8 North Haidian Second Street, Haidian District, Beijing, China	(86-10) 5971 8565
Beijing Jinrongjie Sub-Branch	G/F, Business No.2 Fortune Time Plaza, No.11 Fenghui Garden, Xicheng District, Beijing, China	(86-10) 5836 2188
Shanghai Branch	1/F, 2/F & M/F, Nanyang Commercial Bank Building, No.800 Century Avenue, Pudong District, Shanghai, China	(86-21) 2033 7500
Shanghai Xuhui Sub-Branch	Huafucheng Mansion, No.2 Lane 498 Tianyaoqiao Road, Xuhui District, Shanghai, China	(86-21) 6468 1999
Shanghai Zhabei Sub-Branch	Unit 102, Block 7, Daning Central Square, No.700 Wanrong Road, Zhabei District, Shanghai, China	(86-21) 5308 8888
Shanghai Hongqiao Sub-Branch	Unit 105-106, No.107 Zunyi Road, Changning District, Shanghai, China	(86-21) 6237 5000
Shanghai Huangpu Sub-Branch	Room A103-A107, Tomorrow Square, No.389 West Nanjing Road, Huangpu District, Shanghai, China	(86-21) 6375 5858
Hangzhou Branch	Room 101-201, Building 2, Tong Ce Square, No.3688 Jiang Nan Avenue, Binjiang District, Hangzhou, China	(86-571) 8778 6000
Hangzhou Chengzhong Sub-Branch	1-2F Guo Mao Building, No.195-1 Qingchun Road, Hangzhou, China	(86-571) 8703 8080
Nanning Branch	1/F, Kings Wealth CBD Modern Town, No.63 Jinhu Road, Nanning, China	(86-771) 555 8333
Shantou Branch	G/F, No.3 Yingbin Road, Shantou, China	(86-754) 8826 8266
Qingdao Branch	South Door, No.66 Nanjing Road, Qingdao, China	(86-532) 6670 7676
Qingdao Economic and Technical Development Zone Sub-Branch	No.218 Middle Changjiang Road, Economic & Technical Development Zone, Qingdao, Shandong, China	(86-532) 6805 5618
Qingdao Qiling Road Sub-Branch	1-2/F, Unit 12-13, Jinling Century Garden, Xianxiang Road, Laoshan District, Qingdao, China	(86-532) 8395 0878
Chengdu Branch	M/F, 1/F, Dong Du INTL., 70 Section 2, Middle Renmin Road, Chengdu, China	(86-28) 8628 2777
Chengdu Chuangye Road Sub-Branch	No.7-9, 10-12, 13-16, 1 F, 4 Building, No.49 Chuangye Road, Hi-tech Zone, Chengdu, China	(86-28) 6155 8822
Wuxi Branch	Vanke Homes, No.28 North Changjiang Road, Wuxi New District, Wuxi, China	(86-510) 8119 1666

REVIEW OF ANNUAL RESULTS

The 2012 annual results have been reviewed by the Audit Committee of the Company.

By Order of the Board
CHAN Chun Ying
Company Secretary

Hong Kong, 26 March 2013

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

* *Non-executive Directors*

** *Independent Non-executive Directors*