交通銀行
BANK OF COMMUNICATIONS

交 通 銀 行 股 份 有 限 公 司

# Bank of Communications Co., Ltd.

*(A joint stock company incorporated in the People's Republic of China with limited liability)*

**(Stock Code: 3328)**

# RESULTS ANNOUNCEMENT FOR THE YEAR ENDED 31 DECEMBER 2008

The Board of Directors of Bank of Communications Co., Ltd. (the "**Bank**") is pleased to announce the audited consolidated results (the "**Annual Results**") of the Bank and its subsidiaries (the "**Group**") for the year ended 31 December 2008 (the "**Reporting Period**"), which have been prepared in accordance with International Financial Reporting Standards promulgated by the International Accounting Standards Board. The Board of Directors of the Bank (the "**Board**") and its audit committee have reviewed and adopted the Annual Results.

## 1. CORPORATE INFORMATION

### 1.1 Stock Exchanges on which shares of the Bank are listed:

A share: Shanghai Stock Exchange
H share: The Stock Exchange of Hong Kong Limited

### 1.2 Stock Name and Stock Code:

A share: Bank of Communications, 601328
H share: BANKCOMM, 3328

### 1.3 Company Secretary: Zhang Jixiang

Contact Address: No.188 Yin Cheng Zhong Lu, Pudong New District, Shanghai, PRC
Telephone: 86-21-58766688
Fax: 86-21-58798398
E-mail: investor@bankcomm.com

# 2. FINANCIAL HIGHLIGHTS

The financial data and indicators in respect of the Group's Annual Results for the year ended 31 December 2008 prepared under International Financial Reporting Standards ("**IFRS**") are as follows:

## 2.1 Major accounting data and financial indicators

| | **2008** | 2007 | 2006 | 2005 | 2004 Adjusted[1] |
|---|---|---|---|---|---|
| **Annual Results** | | | | | *(in millions of RMB)* |
| Net interest income[2] | **65,862** | 53,943 | 39,497 | 31,478 | 25,191 |
| Operating profit before tax | **35,719** | 31,114 | 17,405 | 12,843 | 7,750 |
| Net profit (excluding minority interest) | **28,393** | 20,274 | 12,274 | 9,249 | 1,604 |
| **At year end** | | | | | *(in millions of RMB)* |
| Total assets | **2,682,947** | 2,110,444 | 1,719,483 | 1,423,439 | 1,144,005 |
| Includes: loans and advances to customers[2] | **1,328,590** | 1,104,490 | 924,825 | 769,540 | 638,784 |
| Total liabilities | **2,532,852** | 1,977,123 | 1,628,988 | 1,340,293 | 1,091,902 |
| Includes: due to customers[2] | **1,865,815** | 1,555,599 | 1,344,177 | 1,212,824 | 1,023,334 |
| Shareholders' equity | **150,095** | 133,321 | 90,495 | 83,146 | 52,103 |
| Shareholders' equity (excluding minority interest) | **149,662** | 132,903 | 90,436 | 83,082 | 52,103 |
| **Per share** | | | | | *(in RMB Yuan)* |
| Diluted earnings per share | **0.58** | 0.42 | 0.27 | 0.22 | 0.06 |
| Net assets per share | **3.06** | 2.72 | 1.98 | 1.82 | 1.33 |
| Net assets per share (excluding minority interest) | **3.05** | 2.71 | 1.97 | 1.81 | 1.33 |
| **Major financial ratio** | | | | | % |
| Return on average total assets[3] | **1.19** | 1.06 | 0.78 | 0.72 | 0.15 |
| Return on average shareholders' equity[4] | **20.10** | 18.16 | 14.15 | 13.68 | 4.56 |
| Cost to income ratio[5] | **39.94** | 40.29 | 47.66 | 51.24 | 60.78 |
| Impaired loans ratio[6] | **1.92** | 2.05 | 2.53 | 2.80 | 3.00 |
| Provision coverage of impaired loans (after deducting general reserves after tax)[7] | **116.83** | 95.63 | 72.31 | 57.96 | 44.00 |
| Provision coverage of impaired loans[8] | **166.10** | 142.50 | 91.17 | 57.96 | 44.00 |
| **Capital adequacy ratio** | | | | | % |
| Core capital adequacy ratio[9] | **9.54** | 10.27 | 8.52 | 8.78 | 6.77 |
| Capital adequacy ratio[9] | **13.47** | 14.44 | 10.83 | 11.20 | 9.72 |

*Notes:*

1. In accordance with the provision of IAS 39 (revised 2003), the Group retrospectively adjusted the balance of investment securities as at 1 January 2005. Certain originated loans were reclassified to investment securities — available-for-sale, loans and receivables and financial assets held for trading and retrospective adjustments were also made to revaluation reserve and deferred tax accordingly.

2. The comparative data (including the net interest income, outstanding balances of loans and advances to customers before impairment allowances, impairment allowances and due to customers) are reclassified to conform with the disclosure of financial information for the Reporting Period. (similarly hereinafter)

3. Calculated by dividing net profit of the Reporting Period by the average of total assets at the beginning and at the end of the Reporting Period.

4. Calculated by dividing net profit (excluding the minority interest) of the Reporting Period by the average shareholders' equity (excluding the minority interest) at the beginning and at the end of the Reporting Period.

5. Calculated by dividing other operating expenses by the net operating income (which includes net interest income, net fee and commission income, dividend income, gains less losses from trading activities, gains less losses arising from de-recognition of investment securities and other operating income).

6. Calculated by dividing the outstanding balance of impaired loans by the outstanding balance of loans before impairment allowances at the end of the Reporting Period.

7. Calculated by dividing the outstanding balance of impairment allowances by the outstanding balance of impaired loans at the end of the Reporting Period.

8. Calculated by dividing the outstanding balance of impairment allowances including general reserves after tax by the outstanding balance of impaired loans at the end of the Reporting Period.

9. Calculated in accordance with the relevant regulatory practice in China's banking industry.

## 2.2 Reconciliation of Financial Information between CAS and IFRS

The reconciliation of net assets as at 31 December 2008 and net profit for the year ended 31 December 2008 from Chinese Accounting Standards ("**CAS**") to IFRS is listed as follows:

*(in millions of RMB)*

| | Net Assets (including minority interest) | | Net Profit (including minority interest) | |
|---|---|---|---|---|
| | **31 December 2008** | 31 December 2007 | **2008** | 2007 |
| **CAS figures** | **145,642** | 128,797 | **28,520** | 20,641 |
| Adjustments for accounting standard differences: | | | | |
| 1. Revaluation surplus/deficit from fixed assets | **6,149** | 6,185 | **(234)** | (128) |
| 2. Differences arising from the transfer of the non-performing loans to China Cinda Asset Management Corporation | **(104)** | (329) | **225** | 218 |
| 3. Deferred taxes | **(1,647)** | (1,492) | **69** | (315) |
| 4. Others | **55** | 160 | **(90)** | (14) |
| **IFRS figures** | **150,095** | 133,321 | **28,490** | 20,402 |

Explanation of the adjustments for accounting standard differences:

### *1. Revaluation surplus/deficit from fixed assets*

In 2008, the Group carried out a revaluation exercise on land and buildings for the purpose of the preparation of its IFRS financial statements, which was not a statutory valuation. The valuation surplus/deficit has been reflected in IFRS accounts, while it is not recognised in CAS financial statements. The difference arising from fixed assets valuation exercise has been reflected as an accounting standard difference accordingly. The difference will be depreciated during the remaining beneficiary period.

## 2. *Differences arising from the transfer of the non-performing loans to China Cinda Asset Management Corporation*

On 27 June 2004, the Group disposed of non-performing loans (the "**Transferred Loans**") to China Cinda Asset Management Corporation in exchange for the bills issued by the People's Bank of China (the "**Bills**"). The amount of carrying value of the Transferred Loans in excess of the fair value of the Bills, net of tax, was offset against capital surplus in its IFRS financial statements. But under CAS the Bills were carried at face value. The discount will be amortised and recorded as interest income during the remaining beneficiary period of the Bills.

## 3. *Deferred taxes*

In both CAS and IFRS financial statements prepared by the Group, deferred income tax is provided, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Accordingly, all adjustments on accounting standard differences also gave rise to deferred taxation differences.

## 4. *Others*

All other differences are adjustments with minor amounts.

# 3. DETAILS OF CHANGES IN SHARE CAPITAL AND SHAREHOLDINGS OF SUBSTANTIAL SHAREHOLDERS

## 3.1 Details of Changes in Share Capital

As at 31 December 2008, the Bank has a total of 498,078 shareholders with 450,252 shareholders holding A shares and 47,826 shareholders holding H shares.

| | 1 January 2008 | | Increase/decrease during the Period | | | | | 31 December 2008 | |
|---|---|---|---|---|---|---|---|---|---|
| | Number of shares | Percentage % | Issue of new shares | Bonus shares | Shares transferred from the surplus reserve | Others | Sub-total | Number of shares | Percentage % |
| **1. Shares subject to restriction on sales** | | | | | | | | | |
| 1. State-owned shares | 13,181,997,864 | 26.91 | — | — | — | (3,207,015,216) | (3,207,015,216) | **9,974,982,648** | **20.36** |
| 2. Shares held by state-owned entities | 7,329,448,924 | 14.96 | — | — | — | (7,329,448,924) | (7,329,448,924) | **—** | **—** |
| 3. Shares held by other domestic investors | | | | | | | | | |
| Comprising: | | | | | | | | | |
| Shares held by domestic legal persons | 3,161,532,477 | 6.45 | — | — | — | (3,161,532,477) | (3,161,532,477) | **—** | **—** |
| Shares held by domestic natural persons | — | — | — | — | — | — | — | **—** | **—** |
| 4. Shares held by foreign investors | | | | | | | | | |
| Comprising: | | | | | | | | | |
| Shares held by foreign legal persons | 23,690,961 | 0.05 | — | — | — | (23,690,961) | (23,690,961) | **—** | **—** |
| Shares held by foreign natural persons | — | — | — | — | — | — | — | **—** | **—** |
| **2. Shares not subject to restriction on sales** | | | | | | | | | |
| 1. RMB-denominated ordinary shares | 2,233,245,341 | 4.56 | — | — | — | 13,721,687,578 | 13,721,687,578 | **15,954,932,919** | **32.57** |
| 2. Domestically listed foreign shares | — | — | — | — | — | — | — | **—** | **—** |
| 3. Overseas listed foreign shares | 23,064,468,136 | 47.07 | — | — | — | — | — | **23,064,468,136** | **47.07** |
| 4. Others | — | — | — | — | — | — | — | **—** | **—** |
| **3. Total** | 48,994,383,703 | 100.00 | — | — | — | — | — | **48,994,383,703** | **100.00** |

*Note:* The 13.243 billion and 0.478 billion of A shares which were subject to restriction on sales became tradable on 16 May 2008 and 17 November 2008, respectively. For more details, please refer to the announcements made by the Bank in the "China Securities Journal", "Shanghai Securities News", "Securities Times", the Shanghai Stock Exchange's website (www.sse.com.cn) and the website of The Stock Exchange of Hong Kong Limited (the "**Hong Kong Stock Exchange**") (www.hkexnews.hk) on 14 May 2008 and 12 November 2008, respectively.

### 3.2 Particulars of Shareholdings of the Top 10 Shareholders Subject to Restriction on Sales and Details of the Restriction

As at 31 December 2008, there is only one shareholder of the Bank which shares are subject to restriction on sales and particulars of its shareholdings are as follows:

| Name of shareholder | Number of shares subject to restriction on sales | Date on which shares become tradable | Number of tradable shares | Restrictions |
|---|---|---|---|---|
| Ministry of Finance of the People's Republic of China | 9,974,982,648 | 16 May 2010 | 9,974,982,648 | 36 months |

### 3.3 Particulars of Shareholdings of the Top 10 Shareholders and Top 10 Shareholders not Subject to Restriction on Sales (according to the Bank's register of shareholders maintained at its share registrar)

1. *Shareholding of the Top 10 Shareholders*

| Name of shareholder | Nature of shareholder | Shareholding percentage (%) | Number of shares held | Number of shares subject to restrictions on sales[1] |
|---|---|---|---|---|
| Ministry of Finance of the People's Republic of China[2] | State | 26.48% | 12,974,982,648 | 9,974,982,648 |
| HKSCC Nominees Limited[3] | Foreign-owned | 21.94% | 10,748,914,462 | — |
| The Hongkong and Shanghai Banking Corporation Limited[4] | Foreign-owned | 18.60% | 9,115,002,580 | — |
| Capital Airports Holding (Group) Company | State-owned | 2.01% | 985,447,500 | — |
| State Grid Asset Management Company Limited | State-owned | 0.92% | 451,445,193 | — |
| Shanghai Tobacco (Group) Corp. | State-owned | 0.77% | 378,328,046 | — |
| Yunnan Hongta Group Co. Ltd. | State-owned | 0.71% | 346,787,979 | — |
| Sinopec Finance Company Limited | Domestic legal person | 0.62% | 304,320,800 | — |
| Huaneng Capital Services Corporation Ltd. | State-owned | 0.55% | 268,501,276 | — |
| Daqing Petroleum Administration Bureau | State-owned | 0.48% | 233,151,118 | — |

*Notes:*

1. Based on the knowledge of the Bank, the shares held by the Ministry of Finance of the People's Republic of China and The Hongkong and Shanghai Banking Corporation Limited have not been frozen or pledged. Save as aforementioned, the Bank is not aware of any circumstances where shares held by the above shareholders have been frozen or pledged, or of the existence of any connected relationship between the above shareholders.

2. On 25 March 2008, the Bank received the "Notification in respect of Change in Shareholding" signed by the Ministry of Finance of the People's Republic of China ("**MOF**") and Central Huijin Investments Limited ("**Huijin**"), respectively. Huijin has transferred 3,000,000,000 H shares of the Bank to MOF. Upon completion of the share transfer, MOF holds a total of 12,974,982,648 shares (including 3,000,000,000 H shares) of the Bank, which represents 26.48% of the total issued share capital of the Bank. Please refer to the announcement made by the Bank on 26 March 2008 in "China Securities Journal", "Shanghai Securities News" and "Securities Times" as well as the websites of the Shanghai Stock Exchange (www.sse.com.cn) and the Hong Kong Stock Exchange (www.hkexnews.hk) for details.

3. This represents the aggregate number of H shares held by HKSCC Nominees Limited as nominees for all institutional and individual investors that maintain an account with it as at 31 December 2008. According to the information provided by the National Council for Social Security Fund ("**SSF**"), SSF held 5,555,555,556 H shares of the Bank as at 31 December 2008, representing 11.34% of the total issued share capital of the Bank and all these shares have been transferred to HKSCC Nominees Limited. (similarly hereinafter)

4. According to the Bank's register of shareholders kept by Computershare Hong Kong Investor Services Limited, The Hongkong and Shanghai Banking Corporation Limited ("**HSBC**") held 9,115,002,580 H shares of the Bank as at 31 December 2008. In addition, according to the disclosure of interests forms filed with the Hong Kong Stock Exchange by HSBC Holdings plc, HSBC beneficially held 9,312,013,580 H shares of the Bank, and, through its subsidiaries, indirectly held 69,470,681 H shares of the Bank as at 31 December 2008. In aggregate, HSBC held 9,381,484,261 H shares of the Bank, representing 19.15% of the total issued share capital of the Bank. Please refer to "3.4 Substantial Shareholders and Holders of Interests or Short Positions Required to be Disclosed under Division 2 and 3 of Part XV of the Hong Kong Securities and Futures Ordinance" set out below for details. (similarly hereinafter)

2. *Shareholding of the Top 10 Shareholders not Subject to Restriction on Sales*

| Name of shareholder | Number of shares held | Shareholding percentage | Type of shares |
|---|---|---|---|
| HKSCC Nominees Limited | 10,748,914,462 | 21.94% | H shares |
| The Hongkong and Shanghai Banking Corporation Limited | 9,115,002,580 | 18.60% | H shares |
| Ministry of Finance of the People's Republic of China | 3,000,000,000 | 6.12% | H shares |
| Capital Airports Holding (Group) Company | 985,447,500 | 2.01% | A shares |
| State Grid Asset Management Company Limited | 451,445,193 | 0.92% | A shares |
| Shanghai Tobacco (Group) Corp. | 378,328,046 | 0.77% | A shares |
| Yunnan Hongta Group Co. Ltd. | 346,787,979 | 0.71% | A shares |
| Sinopec Finance Company Limited | 304,320,800 | 0.62% | A shares |
| Huaneng Capital Services Corporation Ltd. | 268,501,276 | 0.55% | A shares |
| Daqing Petroleum Administration Bureau | 233,151,118 | 0.48% | A shares |

Connected relations or concerted actions among the above shareholders: Save and except that certain of the above shareholders are managed by the same legal person, the Bank is not aware of any connected relations among the above shareholders or whether they are parties acting in concert.

### 3.4 Substantial Shareholders and Holders of Interests or Short Positions Required to be Disclosed under Division 2 and 3 of Part XV of the Hong Kong Securities and Futures Ordinance

As at 31 December 2008, the substantial shareholders and other persons (other than the directors, supervisors and chief executive of the Bank) who had interests or short positions in the shares or underlying shares of the Bank as recorded in the register required to be kept pursuant to Section 336 of the Hong Kong Securities and Futures Ordinance (the "**SFO**") are as follows:

| Name of substantial shareholder | Capacity | Number of A shares | Nature of interest[1] | Approximate percentage of issued A shares (%) | Approximate percentage of total issued shares (%) |
|---|---|---|---|---|---|
| Ministry of Finance of the People's Republic of China | Beneficial owner | 9,974,982,648 | Long position | 38.47 | 20.36 |

| Name of substantial shareholder | Capacity | Number of H shares | Nature of interest[1] | Approximate percentage of issued H shares (%) | Approximate percentage of total issued shares (%) |
|---|---|---|---|---|---|
| National Council for Social Security Fund | Beneficial owner | 5,555,555,556 | Long position | 24.09 | 11.34 |
| Ministry of Finance of the People's Republic of China | Beneficial owner | 3,000,000,000 | Long position | 13.01 | 6.12 |
| The Hongkong and Shanghai Banking Corporation Limited | Beneficial owner | 9,312,013,580 | Long position | 40.37 | 19.01 |
| | Interest of controlled corporations[2] | 69,470,681 | Long position | 0.30 | 0.14 |
| | Total: | 9,381,484,261 | | 40.67 | 19.15 |
| HSBC Finance (Netherlands) | Interest of controlled corporations[3] | 9,381,484,261 | Long position | 40.67 | 19.15 |
| HSBC Bank plc | Interest of controlled corporations[4] | 309,481 | Long position | 0.0013 | 0.0006 |
| HSBC Holdings plc | Interest of controlled corporations[5] | 9,381,793,742 | Long position | 40.67 | 19.15 |

*Notes:*

1. Long positions held other than through equity derivatives.

2. HSBC holds 62.14% interest in Hang Seng Bank Limited. Pursuant to the SFO, HSBC is deemed to be interested in the H shares which are held by Hang Seng Bank Limited.

   Hang Seng Bank Limited is deemed to be interested in the 69,470,681 H shares held by its wholly-owned subsidiaries. Such 69,470,681 H shares represent the aggregate of 7,139,564 H shares indirectly held by Hang Seng Bank (Bahamas) Limited, 61,532,838 H shares directly held by Hang Seng Bank Trustee International Limited and 798,279 H shares directly held by Hang Seng Bank (Trustee) Limited.

   Hang Seng Bank (Bahamas) Limited is deemed to be interested in the 7,139,564 H shares held by its wholly-owned subsidiary, Hang Seng Bank Trustee (Bahamas) Limited.

3. HSBC is wholly-owned by HSBC Asia Holdings BV. HSBC Asia Holdings BV is in turn wholly-owned by HSBC Asia Holdings (UK). HSBC Asia Holdings (UK) is in turn wholly-owned by HSBC Holdings BV. HSBC Holdings BV is in turn wholly-owned by HSBC Finance (Netherlands). Pursuant to the SFO, each of HSBC Asia Holdings BV, HSBC Asia Holdings (UK), HSBC Holdings BV and HSBC Finance (Netherlands) is deemed to be interested in the 9,381,484,261 H shares which HSBC has an interest.

4. HSBC Financial Products (France) holds 309,481 H shares. HSBC France owns an equity interest of 58.25% in HSBC Financial Products (France), while the remaining 41.75% equity interest is held by HSBC Securities (France) SA, a wholly-owned subsidiary of HSBC France. HSBC France is in turn wholly-owned by HSBC Bank plc. Pursuant to the SFO, each of HSBC Securities (France) SA, HSBC France and HSBC Bank plc is deemed to be interested in the 309,481 H shares held by HSBC Financial Products (France).

5. HSBC Finance (Netherlands) and HSBC Bank plc are wholly-owned by HSBC Holdings plc. Pursuant to Notes 2, 3, and 4 and the SFO, HSBC Holdings plc is deemed to be interested in the 9,381,484,261 H shares which HSBC has an interest and the 309,481 H shares which HSBC Bank plc has an interest.

Except as disclosed above, no person or corporation was recorded in the register required to be kept under Section 336 of the SFO as holding any interests or short positions in the shares or underlying shares of the Bank that would fall to be disclosed to the Bank and the Hong Kong Stock Exchange pursuant to Divisions 2 and 3 of Part XV of the SFO as at 31 December 2008.

# 4. MANAGEMENT DISCUSSION AND ANALYSIS

In 2008, in addition to the financial tsunami and the recession in global economies triggered by the sub-prime crisis, the Chinese economy also faced daunting challenges, which include declining exports, rising labour costs and revaluation of the RMB and unprecedented large-scale natural disasters. Under the central government's effective macro-control policies and regulatory guidance, the Group continued with its long-standing philosophy of prudent management. It actively responded to the changing market environment and various risk factors. In addition, the Group also continued to strengthen its risk management and internal control while forging ahead with the transformation of its operation development model and realignment of its business structures. These encouraged the sustained and healthy development of its various lines of business.

## 4.1 Operation Overview

The Group's total assets and total liabilities reached RMB2,682.947 billion and RMB2,532.852 billion while shareholder's equity reached RMB149.662 billion as at 31 December 2008, an increase of 27.13%, 28.11% and 12.61%, respectively as compared to the beginning of the year. Net profit for the year was RMB28.393 billion, an increase of 40.05% when compared to the previous year while earnings per share were RMB0.58, an increase of 38.10% when compared to the previous year.

## 4.2 Business Review

*Significant improvements in operating results due to practical response to complex situations*

The Group responded practically to the complex and volatile operating environment in 2008, where it capitalised on opportunities presented while effectively mitigating risks to maintain stable business growth. During the first three quarters, the Group controlled loan disbursements under the tight domestic monetary policy and readjusted the composition of its credit portfolio. In the last two months, the Group accelerated its pace of loan disbursements and increased its credit support for critical sectors such as key national infrastructural projects, small-and-medium enterprises, agricultural sector and disaster-reconstruction. These efforts were made in response to the requirements of the macro-control policy to boost domestic demand and promote economic growth. Given the prudent composition of the Group's assets where its exposure to industries that were significantly affected by the financial crisis was relatively small, the Group was able to minimise the impact of the current global financial crisis on its business. On the other hand, the Group took effective and decisive measures promptly to reduce its exposure to high-risk debt securities since early July, thus further reducing the direct impact of the financial crisis on its business.

As at 31 December 2008, loans to customers (before allowances, and similarly hereinafter unless otherwise stated) increased by 20.29% from the beginning of the year to RMB1,328.590 billion. This included domestic RMB loans which increased by RMB218.747 billion from the beginning of the year, representing an increase of 22.98%, and its market share also increased by 0.24 percentage point from the beginning of the year. Customer deposits increased by 19.94% from the beginning of the year to RMB1,865.815 billion. The Group issued 7.47 million new debit cards and 4.72 million credit cards in the domestic market during the year. Cumulative number of credit cards issued has exceeded 10 million. Moreover, sales of wealth management products also increased significantly during the year, of which, sales of "De Li Bao" increased more than 10 folds while sales of commission insurance products also increased by more than 5 times. The Bank rose by one position in the capital market for RMB-denominated transactions volume and rose by three positions for foreign-currency denominated transactions volume. Thus, the Group continued to maintain its status as one of the most active banks in the market.

The Group achieved relatively strong growth in net profit due to the sound development of its various lines of business. As at 31 December 2008, the Group's operating profit before tax was RMB35.719 billion, an increase of 14.80% when compared to the previous year. Net profit was RMB28.393 billion, an increase of 40.05% when compared to the previous year. Return on average assets was 1.19%, an increase of 0.13 percentage point when compared to the previous year. Return on average shareholders' equity was 20.10%, an increase of 1.94 percentage points when compared to the previous year.

*Significant increase in interest margins due to continued realignment of business structures*

In 2008, the Group focused on the realignment of its business structure and diligently improved its business development and rate of returns.

*Major adjustments to Group's corporate banking business structure.* The Group conscientiously supported the macro-control policy and national policies relating to different industries, and strengthened its management in loan disbursement. This, in turn, resulted in increases in the proportion of loans to electricity, transportation and other energy-related industries. The Group also strengthened its rural financial service and agricultural-related loans increased by 17.7% from the beginning of the year. The Group continued to introduce innovative products and services to small enterprises, which, for example, resulted in strong growth in "Zhan Ye Tong" loans. Meanwhile, the Group continued to implement its differentiated policies for enterprises in different sectors. For instance, loans to industries with over-capacity or those categorised as "heavy-polluting, energy-intensive, resources-dependent and excess capacity sectors" were reduced by RMB3.81 billion. It had better control over the proportion of loans to textile and real estate industries. As at 31 December 2008, customers of domestic corporate loans were classified into 10 classes, with the proportion of the better quality class 1-5 customers at approximately 80.50%, an increase of 6.13 percentage points from the beginning of the year.

*Enhancement to development capacity of retail business.* In addition to improving individual customer stratification system, the Group also introduced its private banking services on a pilot basis. In addition, the Group also enhanced existing wealth management products such as "OTO Fortune" and "BOCOM Fortune". With a new wealth management platform, it effectively upgraded the Group's sales and service capacity. In 2008, new individual deposits for the Group increased by RMB134.118 billion, an increase of 24.77% from the beginning of the year. New individual deposits also made up 36.21% of total customer deposits, an increase of 1.40 percentage points from the beginning of the year. The number and proportion of upper and mid-tier customers increased by 12.18% from the beginning of the year, and 2.47 percentage points, respectively. The newly increased assets from the upper and mid-tier customers accounted for 90.05% of all newly increased individual assets managed by the Group, thus making it a dominant driver of growth.

*Improvement in efficiency of treasury operations.* The types and durations of investments were adjusted and optimised. Among the investment in RMB-denominated debt securities, the proportion of high yield debt securities such as medium-term notes and short-term financing bonds increased by 2.48 and 0.95 percentage points, respectively. The proportion of debt securities investments with a maturity of 5-10 years also increased by 4.1 percentage points. The establishment of the Financial Markets Division enabled the Group to integrate the management of its domestic and foreign currency operations, thereby resulting in a rapid development in the treasury operations. Interest income realised from investment securities during the year reached RMB22.430 billion, an increase of 44.78% compared to last year. Return on investment securities reached 3.99%, placing the Group in a leading position in the industry.

As a result of continued realignment of business structures, the Group's net interest income recorded a significant growth. The Group's net interest income amounted to RMB65.862 billion in 2008, an increase of 22.10% as compared to the previous year. Net interest spread and net interest margin reached 2.88% and 3.02%, respectively, which increased by 10 and 17 basis points as compared to last year. This shows a significant increase in the interest spread.

*Continued growth in fee income due to service upgrading and innovative products*

Facing the downturn in the capital markets in 2008, the Group focused on expanding its fee-based business and endeavored to increase its net fee and commission income, thereby improving its revenue structure.

The Group has further enhanced the level of services and expansion so that traditional fee-based services such as bank cards, custodian, and international settlement services further developed. Income from bank cards and custodian business increased by 45.66% and 25.85%, respectively. The proportion of income from bank cards and custodian business to total fee and commission income increased from 24.46% and 6.43%, respectively, at end of 2007 to 29.03% and 6.59%, respectively, at end of 2008. The total transaction volume of international settlement reached US$200 billion, the increase in which was 10 percentage points higher than the growth of the imports and exports of the foreign trade of the country in the same period.

The Group has increased the innovations in products and services so that the growth of new fee-based business products accelerated. Revenue from guarantee and commitment service, financial consultancy and insurance agency service experienced a faster growth. Fees from guarantee and commitment service increased by 1.29 times over last year, while revenue from consultancy service increased by 3.43 times over last year. It ranked among the top 3 in terms of market share of the underwriting business of short-term financing bonds and medium-term notes.

Through the efforts mentioned above, the Group's net fee and commission income reached RMB8.837 billion for 2008, an increase of 24.55% as compared to last year. The net fee and commission income accounted for 11.44% of net operating income, representing an increase of 0.14 percentage points from last year.

*Accelerated promotion of its strategy and synergies within the Group*

In 2008, due to changes in market environment and operating conditions, the Group further reinforced its strategic objective of being "a first-class public bank group focused on wealth management services by means of international expansion and by providing comprehensive services".

Overseas branches responded actively to the impact from the financial crisis where overall business growth remained steady. Asset size reached US$21.911 billion, an increase of 26.19% compared to the beginning of the year. Non-performing loan ratio, however, still maintained at a relatively low level. The subsidiaries maintained a good growth momentum where operational synergies were gradually shown and the sharing of customer information, resources and cross-functional linkages were enhanced. As at 31 December 2008, the total assets of all subsidiaries reached RMB14.078 billion, and contributed RMB215 million to the Group's profits.

The Group's non-banking license business has been extended to areas such as securities, funds, insurance, trustee and leasing. With seven overseas branches and a representative office, the Group has formed a global service network with "Asia as the core business and Europe and United States as its focus of expansion". With this integrated and globalised organisational structure taking shape, synergies from cross-market and globalisation were expected to be further strengthened.

*Significant increase in operational efficiency due to infrastructure improvement*

The Group continued to improve its business processes, operation efficiency and service quality, as well as to enhance its IT system and upgrade its service outlets. In 2008, the Group implemented transformation of operation system in its newly established provincial branches and the transformation has run smoothly. "Hua Zhong Financial Service Centre" was established to implement the centralised processing of documents and invoices. Six provincial sub-branches have been set up in places including Jiangmen, and a total of 351 OTO retail outlets were also established. Six express banking centres with self-service card issuing machines were built in five branches in a pilot program. 3,035 self-service machines were newly installed, representing an increase of 47% from last year. The rate of calls answered by staff in the customer service centre reached 95%, thus placing the Bank in the leading position in the industry. More than 99% of complaints were resolved in a timely manner. The Bank was the first major bank in the country to successfully implement the switch of operations to the Disaster Recovery Centre in the same city. Wuhan remote data backup centre came online during the year. The initial stage of a "2 places 3 centres" disaster recovery structure was completed. In line with the Group's strategy of globalisation and comprehensive operation, the Group has succeeded in the migration of Hong Kong branch's application system to the head office, laying the foundation for the Group's integration of domestic and overseas data centres. By increasing the pace of system optimisation and product developments and stabilising the operations of the system, the integration between IT and operations management was further enhanced.

Benefiting from the improvement in the businesses management and the continuous enhancement of various cost control measures, the Group has further improved on its operating efficiency. In 2008, the Group's operating expenses amounted to RMB30.867 billion, increased by 22.03% from last year. The increase in the operating expenses was lower than that of the net operating income. The Group's cost to income ratio stood at 39.94%, representing a decrease of 0.35 percentage point as compared to last year. At the same time, the Group's net profit per employee and per outlet reached RMB389,400 and RMB10,824,600, respectively, representing an increase of 23.82% and 39.83% from last year, showing a significant improvement in the operating efficiency.

*Continue to strengthen risk management, asset quality remained stable*

In 2008, the Group continued to enhance its comprehensive risk management system. The Group formulated a brand new 3-year comprehensive risk management plan, and activated the integration plan for the Group's comprehensive risk management system. The management structure was further improved and Risk Management Department was set up based on the original Risk Monitoring Department, with its role and functions of risk management being further expanded. The management on credit risk, market risk, liquidity risk and operational risk was also strengthened. The Group has implemented a consolidated management approach by including the subsidiaries in the comprehensive risk management system. The Bank's work in developing the implementation plan and the target administrative measures for New Basel Capital Accord, places it in a leading position in the industry. Adhering to effective risk management measures in a timely manner reduced the negative impact brought by the global financial crisis upon the Group. The Group has timely reduced the exposure of high risk bonds and made sufficient provisions against foreign currency-denominated bonds showing signs of impairment. The Group also conducted a comprehensive risk analysis on high risk industries including export-oriented industry, and reduced its loan disbursements or requested for additional security based on such analysis. As at 31 December 2008, the impaired loans ratio reduced from 2.05% at the beginning of the year by 0.13 percentage points to arrive at 1.92%; the provision coverage of impaired loans reached 166.10%, an increase of 23.60 percentage points as compared to the beginning of the year[Note].

Note The provision coverage of impaired loans (after deducting general reserves after tax) reached 116.83%, representing an increase of 21.20 percentage points from the beginning of the year.

*Actively fulfilling its social responsibility and significantly improving its in corporate image*

The Group placed great importance in fulfilling its corporate social responsibility and pursued a perfect balance between economic and social benefits, which it considered as an important component of its corporate development strategy. The Group was the first in the industry to implement "Green Credit" project. It categorised its credit customers by the industries they are engaged in in accordance with the environmental impact caused by these customers and industries. The coverage of credit customers and balances that are environmental-friendly reached 99%. In 2008, the Group showed a combined effort to react to combat natural disasters and actively supported disaster relief and reconstruction. Cumulative loans for earthquake relief, disaster relief and reconstruction amounted to RMB16.16 billion. After the successful provision of financial services completion to the Olympics, the Group was awarded more than 100 awards including "Most Effective Bank", "Best State-Owned Bank", "Best Corporate Governance Enterprise", "Best Social Responsible Bank in China" from various authoritative media.

The Group's brand reputation continued to be enhanced. The product "Win To Fortune" integrated all corporate banking products, thus compiling a series of brand names with "intelligent financial services" as the core brand and "9 major services areas + 28 services solutions" as major service contents of the brands. The cash management service brand under this series was awarded the "2008 Best Domestic Bank in China on Cash Management" by Euromoney. "OTO Fortune" and "BOCOM Fortune" and other private banking service brands were awarded the "China's Best Bank for Private Wealth Management" by Euromoney and voted the "Best Private Bank" in the 2008 China Private Wealth Management survey. In July 2008, the Group successfully issued RMB-denominated debt securities in an aggregate amount of RMB3 billion in Hong Kong. The bonds were well received by the Hong Kong investors and were 6.8 times over-subscribed. The Group's reputation in the international market was further enhanced.

## 4.3 Analysis on Major Income Statement Items

### *4.3.1 Operating profit before tax*

In 2008, the Group's operating profit before tax was RMB35.719 billion, representing an increase of RMB4.605 billion or 14.80% as compared to last year. Operating profit before tax was derived mainly from net interest income and net fee and commission income.

The table below shows the significant items which make up the Group's operating profit before tax for the year indicated:

*(in millions of RMB)*

| | **2008** | 2007 |
|---|---|---|
| Net interest income | **65,862** | 53,943 |
| Net fee and commission income | **8,837** | 7,095 |
| Impairment losses on loans and advances | **(10,690)** | (6,380) |
| Operating profit before tax | **35,719** | 31,114 |

### *4.3.2 Net interest income*

In 2008, the Group's net interest income reached RMB65.862 billion, representing an increase of 22.10% as compared to last year. Net interest income is the main component of the Group's operating income, accounting for 85.23% of the Group's net operating income.

The table below shows the average daily balances, associated interest income and expenses, and average yield or average cost of the Group's interest-earning assets and interest-bearing liabilities during the periods indicated:

*(in millions of RMB unless otherwise stated)*

| | **For the 12 months ended 31 December 2008** | | | For the 12 months ended 31 December 2007 | | |
|---|---|---|---|---|---|---|
| | **Average balance**[1] | **Interest income/ (expenses)** | **Average yield/ (cost) ratio** | Average balance[1] | Interest income/ (expenses) | Average yield/ (cost) ratio |
| **ASSETS** | | | | | | |
| Cash and balances with central banks | **296,003** | **4,985** | **1.68%** | 230,754 | 3,438 | 1.49% |
| Due from other banks and financial institutions | **192,410** | **6,907** | **3.59%** | 170,501 | 5,971 | 3.50% |
| Loans and advances to customers | **1,167,624** | **82,784** | **7.09%** | 1,033,547 | 65,417 | 6.33% |
| Of which: Corporate loans | **942,533** | **67,120** | **7.12%** | 833,761 | 53,171 | 6.38% |
| Individual loans | **179,862** | **13,083** | **7.27%** | 143,856 | 9,046 | 6.29% |
| Discounted bills | **45,229** | **2,581** | **5.71%** | 55,930 | 3,200 | 5.72% |
| Investment securities and others | **561,927** | **22,430** | **3.99%** | 468,799 | 15,493 | 3.30% |
| Total interest-earning assets | **2,181,119**[4] | **115,396**[4] | **5.29%** | 1,890,040[4] | 89,658[4] | 4.74% |
| Total non-interest earning assets | **136,485** | | | 89,867 | | |
| **TOTAL ASSETS** | **2,317,604**[4] | | | 1,979,907[4] | | |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | | | | | |
| Due to customers | **1,640,628** | **37,538** | **2.29%** | 1,481,607 | 25,993 | 1.75% |
| Of which: Corporate deposits | **1,093,191** | **24,059** | **2.20%** | 1,044,343 | 16,382 | 1.57% |
| Individual deposits | **547,437** | **13,479** | **2.46%** | 437,264 | 9,611 | 2.20% |
| Due to other banks and financial institutions | **404,398** | **11,817** | **2.92%** | 319,868 | 8,690 | 2.72% |
| Debts issued and others | **43,654** | **1,889** | **4.33%** | 37,966 | 1,693 | 4.46% |
| Total interest-bearing liabilities | **2,051,835**[4] | **49,534**[4] | **2.41%** | 1,825,880[4] | 35,715[4] | 1.96% |
| Shareholders' equity and non-interest bearing liabilities | **265,769** | | | 154,027 | | |
| **TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY** | **2,317,604**[4] | | | 1,979,907[4] | | |
| Net interest income | | **65,862** | | | 53,943 | |
| Net interest spread[2] | | | **2.88%**[4] | | | 2.78%[4] |
| Net interest margin[3] | | | **3.02%**[4] | | | 2.85%[4] |
| Net interest spread[2] | | | **2.97%**[5] | | | 2.85%[5] |
| Net interest margin[3] | | | **3.11%**[5] | | | 2.92%[5] |

*Notes:*

1. Daily average balance calculated under the CAS and adjusted in accordance with IFRS.

2. This ratio represents the difference between the average yield on total average interest-earning assets and the average cost of total average interest-bearing liabilities.

3. This ratio represents the net interest income to total average interest-earning assets.

4. This eliminates the impact of wealth management products.

5. This eliminates the impact of wealth management products and taking into account the tax exemption on the interest income from investments in Government bonds.

In 2008, the Group's net interest spread and net interest margin were 2.88% and 3.02%, respectively, representing an increase of 10 and 17 basis points from last year. The main reasons for the increase in the net interest spread and net interest margin were:

1. In 2007, due to the lagged effect from the 6 times increase in the interest rate by the People's Bank of China ("PBOC") and the continued improvement and optimisation of the quality of the Group's customers and assets structure, the average return on the Group's customer loans significantly increased to 7.09% from 6.33% in last year. However, as a result of the substantial reduction in the interest rate in the fourth quarter, return on loans began to decline.

2. The increase in return from the RMB bond markets and the continued optimisation of the Group's investment portfolio resulted in an increase in the Group's return on securities investment from 3.30% in the previous year to 3.99%.

3. Re-pricing of deposits and capital market volatility caused a trend of backflow of deposits and fixed deposits, thereby resulting in an increase in average cost of deposits from 1.75% in last year to 2.29%.

The table below shows the effect of changes in balances and interest rates on the Group's interest income and interest expense. Changes in balances and interest rates during the periods indicated are calculated based on the changes in average daily balance and the changes in interest rates on interest-earning assets and interest-bearing liabilities during the periods indicated.

*(in millions of RMB)*

| | **Comparison between 2008 and 2007 Increase/(decrease) due to** | | | Comparison between 2007 and 2006 Increase/(decrease) due to | | |
|---|---|---|---|---|---|---|
| | **Volume** | **Interest rate** | **Net increase/ (decrease)** | Volume | Interest rate | Net increase/ (decrease) |
| **Interest-earning Assets** | | | | | | |
| Cash and balances with central banks | **972** | **575** | **1,547** | 1,212 | 130 | 1,342 |
| Due from other banks and financial institutions | **767** | **169** | **936** | 970 | 138 | 1,108 |
| Loans and advances to customers | **8,487** | **8,880** | **17,367** | 12,267 | 6,551 | 18,818 |
| Investment in securities and others | **3,073** | **3,864** | **6,937** | 3,645 | 863 | 4,508 |
| Changes in interest income | **13,299** | **13,488** | **26,787** | 18,094 | 7,682 | 25,776 |
| **Interest-bearing Liabilities** | | | | | | |
| Due to customers | **2,783** | **8,762** | **11,545** | 3,953 | 2,725 | 6,678 |
| Due to other banks and financial institutions | **2,299** | **828** | **3,127** | 4,439 | (600) | 3,839 |
| Debts issued and others | **254** | **(58)** | **196** | 978 | (60) | 918 |
| Changes in interest expenses | **5,336** | **9,532** | **14,868** | 9,370 | 2,065 | 11,435 |
| Changes in net interest income | **7,963** | **3,956** | **11,919** | 8,724 | 5,617 | 14,341 |

In 2008, the Group's net interest income increased by RMB11.919 billion from the previous year, of which, movements in the average balances of various assets and liabilities resulted in an increase in net interest income of RMB7.963 billion and movements in average yield and average cost ratio resulted in an increase in net interest income of RMB3.956 billion. The scale and interest rate factors contributed to the increase in net interest income of 66.81% and 33.19%, respectively.

### 4.3.3 *Net fee and commission income*

Net fee and commission income is a major component of the Group's net operating income. In 2008, the Group overcame the adverse effects of the capital markets by vigorously implementing the strategy of diversification of income structure and expediting products and services innovation, thus resulting in a relatively fast growth of the fee-based business. In 2008, the Group's net fee and commissions income was RMB8.837 billion, representing an increase of 24.55% or RMB1.742 billion from last year, and accounted for 11.44% of the net operating income, representing an increase of 0.14 percentage point as compared to the previous year. New revenue streams such as credit cards, consultancy, and wealth management services are the main driving forces for the growth of the fee-based business.

The table below shows the major components of the Group's net fee and commission income for the periods indicated:

*(in millions of RMB)*

| | **2008** | 2007 |
|---|---|---|
| Settlement and agent service commission income | **2,045** | 1,744 |
| Bank card annual fee and commission income | **2,938** | 2,017 |
| Guarantee and commitment commission income | **912** | 399 |
| Custodian commission income | **667** | 530 |
| Fund sales commission income | **853** | 2,191 |
| Funds management commission income | **590** | 614 |
| Financial consultancy commission income | **1,081** | 244 |
| Other commission income | **1,035** | 506 |
| Total fee and commissions income | **10,121** | 8,245 |
| Less: Fee and commissions expenses | **(1,284)** | (1,150) |
| Net fee and commission income | **8,837** | 7,095 |

### 4.3.4 *Other operating expenses*

The Group expedited the building of the "Process Bank", thereby enhancing its business process and operating efficiency. In 2008, other operating expenses amounted to RMB30.867 billion, increased by 22.03% or RMB5.572 billion as compared to last year. Cost to income ratio was 39.94%, decreased by 0.35 percentage point as compared to the previous year. Affected by the financial crisis, the Group made substantial provision for impairment on bonds denominated in foreign currencies, thus resulting in a corresponding increase in costs. Without taking into account such provision, the Group's cost to income ratio dropped by 2.01 percentage points from last year to 38.28% in 2008.

*4.3.5 Impairment losses on loans and advances*

The Group's impairment losses on loans and advances consisted of impairment losses on loans and advances to customers (less recovery of loans previously written off) and provisions for due from other banks and financial institutions as well as securities purchased under resale agreements.

In 2008, the Group's impairment losses on loans and advances were RMB10.690 billion, representing an increase of RMB4.310 billion from last year. The increase was due to: (i) Considering uncertainties in the domestic and international economy in the future, the Group increased the expected loss on unrecognised risks appropriately. In addition, the rapid growth in the scale of loans also resulted in an increase in the collectively assessed provision by RMB3.839 billion from the previous year to RMB5.855 billion. Such provision includes a special provision of RMB2.012 billion for the financial crisis; (ii) due to the economics downturn and the impact of tightened monetary policy, individually assessed provision was RMB4.860 billion, representing an increase of RMB383 million from last year. In 2008, credit cost ratio was 0.80%, representing an increase of 0.22 percentage point from last year. Without taking into account the special provisions mentioned above, credit cost ratio was 0.65%.

*4.3.6 Income tax*

In 2008, the Group's income tax expense was RMB7.229 billion, representing a decrease of RMB3.483 billion or 32.51% from last year. The effective tax rate was 20.24%, lower than the statutory tax rate of 25%, mainly due to the fact that the Group's interest income from Government bonds is exempted from income tax pursuant to the relevant provisions of the tax law.

The table below shows the Group's current tax and deferred tax for the periods indicated:

*(in millions of RMB)*

| | **2008** | 2007 |
|---|---|---|
| Current Tax | **8,244** | 9,643 |
| Deferred Tax | **(1,015)** | 1,069 |

## 4.4 Analysis on Major Balance Sheet Items

### *4.4.1 Assets*

As at 31 December 2008, the Group's total assets was RMB2,682.947 billion, representing an increase of RMB572.503 billion or 27.13% as compared to the beginning of the year. The Group's assets consist of four principal components, namely loans and advances to customers, investment in securities, cash and balances with central banks and due from other banks and financial institutions, accounting for 48.41%, 23.22%, 13.50% and 12.36% of the Group's total assets, respectively, as at 31 December 2008.

The table below shows the outstanding balances of the principal components of the Group's total assets as at the dates indicated:

*(in millions of RMB)*

| | **31 December 2008** | 31 December 2007 |
|---|---|---|
| Loans and advances to customers | | |
| corporate loans[Note] | **1,053,799** | 900,536 |
| individual loans[Note] | **205,058** | 172,474 |
| discounted bills[Note] | **69,733** | 31,480 |
| Total loans and advances to customers before impairment allowances | **1,328,590** | 1,104,490 |
| Impairment losses on loans and advances | **(29,814)** | (21,702) |
| Loans and advances to customers | **1,298,776** | 1,082,788 |
| Investment in securities | **623,071** | 557,102 |
| Cash and balances with central banks | **362,180** | 261,433 |
| Due from other banks and financial institutions | **331,511** | 156,110 |

*Note:* Corporate loans, individual loans and discounted bills represent amounts before impairment allowances.

(I) Loans Business

Adhering to the macro-control policies, the Group managed to maintain a relatively fast growth in its loan business for the year as a result of its flexible control over the scale and pace of its loan disbursements in 2008. As at 31 December 2008, the total outstanding loans and advances to customers was RMB1,328.590 billion, representing an increase of RMB224.100 billion or 20.29% from the beginning of the year. Of which, loans and advances made by domestic branches increased by RMB218.747 billion, representing an increase of 22.98%. The loans to deposits ratio was 71.21%, representing an increase of 0.21 percentage point from the beginning of the year.

Loan concentration by industries

In 2008, the Group conscientiously supported the macro-control policy and national policies relating to different industries and strengthened the management of its loan disbursements. The Group increased its credit support for critical sectors such as key national infrastructural projects, small-and-medium enterprises, agricultural sector and disaster-reconstruction. The proportion of loans to electricity, transportation and other energy-related industries further increased. The Group also strengthened its rural financial service and agricultural-related loans increased by 17.7% from the beginning of the year. The Group continued to introduce innovative products and services to small enterprises, which, for example, resulted in strong growth in "Zhan Ye Tong" loans. Meanwhile, the Group continued to implement its differentiated policies for enterprises in different sectors. For instance, loans to industries with over-capacity or those categorised as "heavy-polluting, energy-intensive, resources-dependent and excess capacity sectors" were reduced by RMB3.81 billion. It had better control over the proportion of loans to textile and real estate industries.

The table below shows the distribution of the Group's loans and advances to customers by industry as of the dates indicated:

*(in millions of RMB unless otherwise stated)*

| | **31 December 2008** | | 31 December 2007 | |
|---|---|---|---|---|
| | **Outstanding balance** | **Proportion (%)** | Outstanding balance | Proportion (%) |
| Manufacturing | | | | |
| — Petroleum and chemical | **60,331** | **4.54** | 51,599 | 4.67 |
| — Electronics | **23,680** | **1.78** | 22,465 | 2.03 |
| — Steel making and processing | **33,766** | **2.54** | 27,845 | 2.52 |
| — Machinery | **67,141** | **5.05** | 52,823 | 4.78 |
| — Textile | **22,102** | **1.66** | 24,124 | 2.18 |
| — Others | **114,481** | **8.63** | 99,850 | 9.04 |
| Transportation | **148,935** | **11.21** | 121,578 | 11.01 |
| Electricity | **105,541** | **7.94** | 76,751 | 6.95 |
| Wholesale and retail | **108,559** | **8.17** | 95,153 | 8.62 |
| Services | **49,990** | **3.76** | 37,267 | 3.37 |
| Real estate | **88,568** | **6.67** | 77,592 | 7.03 |
| Utilities | **92,207** | **6.94** | 79,411 | 7.19 |
| Construction | **52,261** | **3.93** | 46,206 | 4.18 |
| Energy and mining | **20,279** | **1.53** | 14,451 | 1.31 |
| Recreation and entertainment | **20,560** | **1.55** | 22,065 | 2.00 |
| Accommodation and catering | **13,977** | **1.05** | 10,366 | 0.94 |
| IT and communications service | **8,200** | **0.62** | 12,149 | 1.10 |
| Financial institution | **10,164** | **0.77** | 13,808 | 1.25 |
| Others | **13,057** | **0.98** | 15,033 | 1.36 |
| Total corporate loans | **1,053,799** | **79.32** | 900,536 | 81.53 |
| Mortgage loans | **133,415** | **10.04** | 112,941 | 10.23 |
| Medium-term and long-term working capital loans | **23,873** | **1.80** | 22,709 | 2.06 |
| Short-term working capital loans | **16,883** | **1.27** | 11,333 | 1.03 |
| Car loans | **4,271** | **0.32** | 4,534 | 0.41 |
| Credit card advances | **20,453** | **1.54** | 7,929 | 0.72 |
| Others | **6,163** | **0.46** | 13,028 | 1.17 |
| Total individual loans | **205,058** | **15.43** | 172,474 | 15.62 |
| Discounted bills | **69,733** | **5.25** | 31,480 | 2.85 |
| Gross amount of loans and advances to customers before impairment allowances | **1,328,590** | **100.00** | 1,104,490 | 100.00 |

As at 31 December 2008, the Group's loans to corporate entities amounted to RMB1,053.799 billion, representing an increase of RMB153.263 billion or 17.02% from the beginning for the year. The loans are mainly concentrated in the manufacturing, transportation, wholesale and retail and electricity industries, accounting for 64.96% of the total corporate loans.

As at 31 December 2008, loans to individuals amounted to RMB205.058 billion, representing an increase of RMB32.584 billion or 18.89% from the beginning of the year. The proportion of individual loans to total loans and advances to customers decreased by 0.19 percentage point from the end of the previous year to 15.43%. The increase in mortgage loans, being affected by the decrease in market transaction volume and the global economy downturn, slowed down and increased by RMB20.474 billion or 18.13% as compared to the beginning of the year. The proportion of mortgage loans to total individual loans decreased by 0.42 percentage point. Credit card advances increased by RMB12.524 billion, representing an increase of 157.95% as compared to the beginning of the year. The proportion of credit card advances to total individual loans increased by 5.37 percentage points. The increase was attributed to a higher number of credit cards in issuance and an increase in credit card spending.

Borrowers concentration

Under the prevailing PRC banking regulations, the total outstanding credit exposure to a single group customer must not exceed 15% of the net regulatory capital of a bank whereas the total outstanding loans to a single borrower shall not exceed 10% of the net regulatory capital of a bank. The Group currently complies with these regulatory requirements.

The table below shows the loan balances to the top 10 single borrowers of the Group as at the dates indicated:

*(in millions of RMB unless otherwise stated)*

| | | As at 31 December 2008 | |
|---|---|---|---|
| | **Type of Industry** | **Outstanding loan balance** | **Percentage of total loans and advances (%)** |
| Customer A | Manufacturing — Petroleum and chemical | 6,818 | 0.51 |
| Customer B | Construction | 6,174 | 0.46 |
| Customer C | Transportation | 4,376 | 0.33 |
| Customer D | Wholesale and Retail | 4,100 | 0.31 |
| Customer E | Transportation | 3,560 | 0.27 |
| Customer F | Transportation | 3,450 | 0.26 |
| Customer G | Utilities | 3,067 | 0.23 |
| Customer H | Manufacturing — Petroleum and chemical | 2,930 | 0.23 |
| Customer I | Transportation | 2,720 | 0.20 |
| Customer J | Transportation | 2,600 | 0.20 |
| Total of Top 10 customers | | 39,795 | 3.00 |

Loan concentration by geographical locations

The Group's loans and advances to customers are mainly concentrated in the Yangtze River Delta, the Bohai Rim Economic Zone and the Pearl River Delta. Loans and advances to customers in these three regions increased by 27.15%, 18.86% and 7.80%, respectively, accounting for 65.86% of the Group's total loans and advances to customers outstanding as at 31 December 2008.

Loan quality

The Group continuously improves the quality of its loans. As at 31 December 2008, the impaired loans ratio was 1.92%, representing a decrease of 0.13 percentage point from the beginning of the year. The provision coverage of impaired loans was 166.10%, representing an increase of 23.60 percentage points from the beginning of the year[Note].

Note The provision coverage of impaired loans (after deducting general reserves after tax) reached 116.83%, representing an increase of 21.20 percentage points from the beginning of the year.

The table below shows certain information of the Group's individually identified impaired loans and loans overdue by more than 90 days as at the dates indicated:

*(in millions of RMB unless otherwise stated)*

| | **31 December 2008** | 31 December 2007 |
|---|---|---|
| Individually identified impaired loans | **25,520** | 22,694 |
| Loans overdue by more than 90 days | **20,979** | 19,708 |
| Percentage of impaired loans to gross amount of loans and advances to customers | **1.92%** | 2.05% |

Customer Structure

The Group further optimised its customer structure. Corporate customers of the Group's domestic branches are classified using a 10-class credit rating system. Compared to the beginning of the year, loans outstanding to class 1 to class 5 high quality customers amounted to 80.50% of the total outstanding loan balance, representing an increase of 6.13 percentage points while loans outstanding to class 6 to class 7 customers amounted to 13.62% of the total outstanding loan balance, representing a decrease of 5.94 percentage points, and loans outstanding to class 8 to class 10 high risk customers amounted to 2.12%, representing a decrease of 0.21 percentage point.

(II) Treasury Business

In 2008, the Group set up the Financial Markets Division, which realised the integration of the management of domestic and foreign currency operations. As the Group further strengthened the centralisation of its treasury operations and optimised its investment structure, revenue derived from its treasury operations has further increased. As at 31 December 2008, the Group's outstanding balance of investment securities (after impairment allowances) amounted to RMB623.071 billion, representing an increase of RMB65.969 billion or 11.84% from the previous year. Return on investment securities increased by 69 basis points from last year to 3.99%, thereby effectively improving the profitability of the Group's assets.

*Investment Securities*

The table below shows the distribution of the Group's investment in securities by holding purposes and by type of issuers as of the dates indicated:

— By holding purposes

*(in millions of RMB unless otherwise stated)*

| | **31 December 2008** | | 31 December 2007 | |
|---|---|---|---|---|
| | **Balance** | **Proportion (%)** | Balance | Proportion (%) |
| Investments at fair value through profit or loss | **22,280** | **3.58** | 17,002 | 3.05 |
| Loans and receivables | **90,903** | **14.59** | 66,693 | 11.97 |
| Available-for-sale investments | **142,010** | **22.79** | 146,454 | 26.29 |
| Held-to-maturity investments | **367,878** | **59.04** | 326,953 | 58.69 |
| **Total** | **623,071** | **100.00** | 557,102 | 100.00 |

— By type of issuers

*(in millions of RMB unless otherwise stated)*

| | **31 December 2008** | | 31 December 2007 | |
|---|---|---|---|---|
| | **Balance** | **Proportion (%)** | Balance | Proportion (%) |
| Central governments and central banks | **294,356** | **47.24** | 307,556 | 55.21 |
| Public sector entities | **8,764** | **1.41** | 5,912 | 1.06 |
| Banks and other financial institutions | **225,966** | **36.27** | 209,355 | 37.58 |
| Corporate entities | **93,985** | **15.08** | 34,279 | 6.15 |
| **Total** | **623,071** | **100.00** | 557,102 | 100.00 |

*Foreign currency denominated debt securities*

The Group believes in having a sustainable and sound investment philosophy. The Group has disposed of its holdings of debt securities issued by Fannie Mae, Freddie Mac and Lehman Brothers in a timely manner after the global sub-prime crisis erupted. This improved the Group's exposure to the underlying credit risk in its investment portfolio. As at 31 December 2008, the Group holds US$4.9 billion (approximately RMB33.487 billion) worth of foreign currency denominated debt securities, and this accounted for 1.25% of the Group's total assets.

*4.4.2 Liabilities*

As at the end of 2008, the Group's total liabilities reached RMB2,532.852 billion, increased by RMB555.729 billion or 28.11% from the beginning of the year.

Customer deposits

Customer deposits are the main source of fund for the Group. As at 31 December 2008, the Group's customer deposits balances amounted to RMB1,865.815 billion, increased by RMB310.216 billion or 19.94% as compared to the beginning of the year. The Group has a sound deposit structure. In terms of customers portfolio, corporate deposits accounted for 63.25% of the total deposits, representing a fall of 1.04 percentage points from the beginning of the year; individual deposits accounted for 36.21%, representing an increase of 1.40 percentage points from the beginning of the year. In terms of the term of deposits, current deposits accounted for 47.07% of the total deposits, representing a drop of 12.53 percentage points from the beginning of the year; time deposits accounted for 51.09%, representing an increase of 13.01 percentage points from the beginning of the year. The rise in fixed deposits is due to market fluctuations which trigger customers to place more deposits.

The table below shows the Group's corporate and individual deposits as of the dates indicated:

*(in millions of RMB)*

| | | **31 December 2008** | 31 December 2007 |
|---|---|---|---|
| **Corporate deposits** | | **1,180,207** | 1,000,040 |
| Of which: | Corporate current deposits | **646,894** | 699,289 |
| | Corporate saving deposits | **8,207** | 7,785 |
| | Corporate time deposits | **525,106** | 292,966 |
| **Individual deposits** | | **675,564** | 541,446 |
| Of which: | Individual current deposits | **231,335** | 227,796 |
| | Individual saving deposits | **16,093** | 14,295 |
| | Individual time deposits | **428,136** | 299,355 |

## 4.5 Segment Analysis

*4.5.1 Operating results by geographical segments*

With the exception of its overseas operations, the Group's other geographical segments have all experienced profit growth in 2008. Profits from the Group's overseas operations have declined significantly due to the impact of the sub-prime crisis in the United States which caused relatively significant losses from investments in foreign currency denominated bonds.

The table below shows the net profit and total revenue from each of the Group's geographical segments for the periods indicated:

*(in millions of RMB)*

| | **2008** | | 2007 | |
|---|---|---|---|---|
| | **Net profit/ (loss)** | **Total revenue[1]** | Net profit/ (loss) | Total revenue[1] |
| Northern China[2] | **3,897** | **24,562** | 2,950 | 16,717 |
| North Eastern China[3] | **962** | **7,607** | 829 | 6,002 |
| Eastern China[4] | **11,010** | **49,393** | 7,144 | 36,813 |
| Central and Southern China[5] | **5,730** | **24,130** | 4,313 | 18,702 |
| Western China[6] | **1,794** | **9,547** | 1,376 | 7,412 |
| Overseas[7] | **50** | **5,700** | 960 | 8,651 |
| Head Office | **5,047** | **31,767** | 2,844 | 19,483 |
| Eliminations | **—** | **(22,902)** | (14) | (13,465) |
| **Total[8]** | **28,490** | **129,804** | 20,402 | 100,315 |

*Notes:*

1. Includes interest income, fee and commission income, dividend income, gains less losses from trading activities, gains less losses arising from the de-recognition of investment securities and other operating income.

2. Includes Beijing Municipality, Tianjin Municipality, Hebei Province, Shanxi Province and the Inner Mongolia Autonomous Region.

3. Includes Liaoning Province, Jilin Province and Heilongjiang Province.

4. Includes Shanghai Municipality (excluding Head Office), Jiangsu Province, Zhejiang Province, Anhui Province, Fujian Province, Jiangxi Province and Shandong Province.

5. Includes Henan Province, Hunan Province, Hubei Province, Guangdong Province, Guangxi Autonomous Region and Hainan Province.

6. Includes Chongqing Municipality, Sichuan Province, Guizhou Province, Yunnan Province, Tibet Autonomous Region, Shaanxi Province, Gansu Province, Qinghai Province, Ningxia Autonomous Region and Xinjiang Autonomous Region.

7. Includes overseas subsidiaries and branches in Hong Kong, New York, Singapore, Tokyo, Seoul, Macau and Frankfurt.

8. Includes minority interests.

#### 4.5.2 *Deposits and loans and advances balances by geographical segments*

The table below shows the Group's deposits and loans and advances balances by geographical segments as at the dates indicated:

*(in millions of RMB)*

| | **As at 31 December 2008** | | As at 31 December 2007 | |
|---|---|---|---|---|
| | **Deposit balance** | **Loans and advances balance** | Deposit balance | Loans and advances balance |
| Northern China | **353,576** | **257,720** | 270,655 | 209,844 |
| North Eastern China | **152,496** | **73,961** | 132,207 | 64,102 |
| Eastern China | **712,409** | **530,674** | 605,658 | 440,670 |
| Central and Southern China | **384,419** | **252,763** | 324,907 | 222,589 |
| Western China | **174,069** | **111,579** | 150,311 | 93,660 |
| Overseas | **86,930** | **73,844** | 71,225 | 64,515 |
| Head Office | **1,916** | **28,049** | 636 | 9,110 |
| **Total** | **1,865,815** | **1,328,590** | 1,555,599 | 1,104,490 |

#### 4.5.3 *Operating results by business segments*

The Group's business is mainly divided into four business segments: corporate banking, retail and private banking, treasury and others. The corporate banking segment was the primary source of profit for the Group and operating profit before tax from the corporate banking segment accounted for 81.84% of the Group's total operating profit before tax.

The table below shows the amount of the operating results of each of the Group's business segments for the periods indicated:

*(in millions of RMB)*

| | **Total revenue for the year 2008** | Total revenue for the year 2007 | **Operating profit before tax for the year 2008** |
|---|---|---|---|
| Corporate banking | **75,833** | 60,479 | **29,231** |
| Retail and private Banking | **18,915** | 13,772 | **6,020** |
| Treasury | **33,932** | 25,606 | **2,802** |
| Others | **1,124** | 458 | **(2,334)** |
| **Total** | **129,804** | 100,315 | **35,719** |

## 4.6 Other Financial Information

Set out below are the relevant information disclosed pursuant to the latest requirements of China Securities Regulatory Commission.

### *4.6.1 Fair value measurement related items*

The Group has completed the initial development of an internal control framework which uses fair value measurement as its basis by restructuring its market risk management system in order to satisfy the relevant internal control and information disclosure requirements. This involves all the relevant front office, middle office and back office departments and encompasses fair value valuation, measurement, monitoring and verification. The Group also plans to learn from the experience of its peers in the industry and international practices to further optimise its internal control system relevant to fair value measurement. The Group primarily uses quoted market prices as the fair value of financial instruments traded in active markets and valuation models or third party quotes are used to determine the fair value of financial instruments that are not traded in an active market.

The table below shows the fair value measurement related items of the Group in 2008:

*(in millions of RMB)*

| Item | Opening Balance | Gains/ (losses) on change in fair value | Cumulative Fair value gains/ (losses) recognised in equity | Impairment losses | Closing Balance |
|---|---|---|---|---|---|
| Financial assets | | | | | |
| Includes: | | | | | |
| 1. Financial assets, measured at fair value, changes of which are recorded in profit and loss | 19,340 | 2,703 | — | — | 26,936 |
| Includes: Financial derivatives | 2,338 | 2,318 | — | — | 4,656 |
| 2. Financial assets, available-for-sale | 146,454 | — | 3,647 | (1,085) | 142,010 |
| Total of financial assets | 165,794 | 2,703 | 3,647 | (1,085) | 168,946 |
| Financial liabilities | (10,028) | (2,356) | — | — | (10,013) |
| Investment property | 136 | (19) | — | — | 109 |
| Total | 155,902 | 328 | 3,647 | (1,085) | 159,042 |

### *4.6.2 Holdings in foreign currency denominated financial assets and financial liabilities*

The Group has adopted a strict accounting policy for its financial instruments in 2008, with a particular focus on the accounting policy for its foreign currency denominated financial assets and financial liabilities. The Group has also paid significant attention to the decline in value of its financial assets in view of the continued decline in market prices.

The table below shows the foreign currency denominated financial assets and financial liabilities held by the Group in 2008:

*(in millions of RMB)*

| Item | Opening Balance | Gains/(losses) on change in fair value | Cumulative fair value gains/(losses) recognised in equity | Impairment losses | Closing Balance |
|---|---|---|---|---|---|
| Financial assets | | | | | |
| Includes: | | | | | |
| 1. Financial assets, measured at fair value, changes of which are recorded in profit and loss | 3,322 | 1,818 | — | — | 6,185 |
| Includes: Financial derivatives | 569 | 1,851 | — | — | 2,420 |
| 2. Loans and receivables | 657 | — | — | — | 137 |
| 3. Financial assets, available-for-sale | 33,682 | — | (832) | (1,080) | 28,223 |
| 4. Financial assets, held-to-maturity | 2,811 | — | — | (5) | 1,634 |
| Total of financial assets | 40,472 | 1,818 | (832) | (1,085) | 36,179 |
| Financial liabilities | (9,797) | 507 | — | — | (6,919) |

## 4.7 Risk Management

In 2008, the Group formulated a comprehensive "Three-year Risk Management Plan" (the "**Plan**") that sets out clear blueprint for the development of the Group's risk management and establishes different milestones for the overall development plan. According to the Plan, the Group continued to forge ahead the establishment of the comprehensive risk management framework during the Reporting Period by deepening the structural reforms of the risk management framework and strengthening the technological support for risk management. Further, the Group will promote the development of the risk management team to ensure that risks are controlled at a reasonable level so that different business operations can be carried out safely and prudently.

The Board will be held ultimately responsible for, and makes final decisions on the Group's risk management. It approves the overall risk appetite, determines overall risk management strategy and approves the risk exposure of the Group. The Board also ensures sufficient risk management resources are in place to assess and manage the Group's risk exposures through the risk management committee.

The senior management of the Group is responsible for formulating and implementing appropriate risk policies and procedures and control system based on the risk management strategy approved by the Board. Risk management committee has been established under the senior management. Such risk management committee is comprised of three sub-committees for the management of credit, market and operation risks, respectively. These sub-committees are responsible for the periodic assessments of the risk exposures and the effectiveness of the risk management of the Group.

The Group's Chief Risk Management Officer assumes the duties and responsibilities of implementing the overall risk management on behalf of the senior management. The Chief Risk Management Officer is responsible for the implementation of the risk management strategies, the planning and establishment of a comprehensive risk management system, the coordination and management of the Group's four major risk areas, and the organisation and implementation of various risk management policies and tools.

In 2008, the Group proactively established the risk management system and framework with "Comprehensive, Intensive, Matrix" as its targets and hierarchical risk management structure as its basis. The Group restructured the Risk Monitoring Department at the headquarters to form the Risk Management Department, which assumes the overall risk management functions of all types of risk. As clearly defined in the risk management structure, all risk management departments under each business departments, domestic and overseas branches and subsidiaries will assume the actual risk management functions of all types of risk for different lines of business of the Group as well as regional and subordinate institutions. With a clear division of labour and the establishment of a dual reporting mechanism, a basic risk management model is formed through the "4 layers of defences" composed of business operations, business line management, risk management department and internal audit department.

In 2008, the Group proactively explored the use of stress test management tools, formulated an overall work plan on the use of stress test, and performed various stress tests based on a number of scenarios such as slowdown in economics growth, decline in housing price indices, adjustment to interest rates and change in foreign exchange rates.

*4.7.1 Credit Risk Management*

Credit risk refers to the risk of borrowers or counterparties failing to meet due contractual obligations. Credit risk remains the major risk of the Group at the present stage, and primarily exists in company loans, retail loans, treasury operations, inter-bank transactions and international business.

(1) Methods and procedures on risk classification

For corporate loans, the Group determines impaired credit assets via its asset risk management system daily by using the three-tier risk filtering method and discounted cash flow to estimate the expected loss resulting from each corporate loan. For impaired credit assets, the Group formulates an action plan for each customer and appoints designated personnel to collect or dispose of such assets, and makes provisions for allowance of impairment loss individually according to the expected loss. For non-impaired corporate loans, taking into account customers' credit standings, financial status and repayment capability, the Group uses an internally developed 10-class credit rating system to manage of such corporate loans. Customers with class 1–5 are considered by the Group as high-quality customers, class 6–7 are considered as general customers and class 8–10 are considered as problematic customers. The Group adopts different business strategies depending on customers' different grading.

The Group categorises retail loans based on the overdue status and type of security. With regard to the non-overdue retail customers, the Group strengthens their management through regular visits to customers, and puts potentially higher risk customers into watch lists for exclusive management. For overdue retail customers, the collection approach differs according to overdue duration. Retail loans overdue for longer than a certain period of time are treated as impaired assets for management and impairment provisions are made accordingly.

(2) Risk management and control policies

The Group implements standardised management throughout the whole credit process, including credit check and reporting, credit authorisation investigation and approval, loan drawdown, post-lending supervision and non-performing loan management. During the Reporting Period, the Group practically responded to the challenges brought by the changes in the global and domestic macro-economy and continuously promoted the development and enhancement of the foundation for credit risk management. Reasonable control over the amount and pace of loan disbursements, the adjustment and optimisation of the credit orientation and structure, the enhancement and development of post-lending management as well as the development and promotion of various risk management tools all contributed to the Group's timely and effective identification, measurement, monitoring and management of potential credit risk in various aspects.

*Credit risk management with respect to corporate loans*

During the Reporting Period, the Group implemented a hierarchical approval system comprised of branches, regional credit review centres and head office, which further intensified the centralised control of regional credit review centres and head office over the credit review process, enabling the Group to continuously optimise the customer and loan structure.

During the Reporting Period, in line with the country's macro-control policies, the Group issued guidance on the changes in the government's policy in respect of credit business and strengthened the regional differentiation management. The Group effectively promoted the implementation of "Green Credit" project, increased its loan disbursements to national key projects, small and medium enterprises, three dimensional rural loans and disaster reconstruction, increased its support for transportation, electricity and mechanical industries, and reduced loans to industries categorised as "heavy-polluting, energy-intensive, resources-dependent and excess capacity sectors" and industries with excess capacity, thereby achieving a prudent and balanced credit portfolio.

During the Reporting Period, the Group completed the overall implementation of the internal rating system for its corporate banking business. From the model validation and feedbacks gathered, the model has performed reasonably well and in line with the Group's expectation. The application of internal rating model on credit evaluation and post-lending management has been developed smoothly, thereby playing a significant role in measuring credit risk and evaluating customers' values.

During the Reporting Period, the Group strengthened its post-lending management and achieved positive results. By standardising and optimising the post-lending management system, the Group stepped up its efforts in monitoring and providing guidance to branches on strict implementation of the post-lending management. Through the effective and efficient use of monitoring tools such as risk filters, watch list, migration analysis, risk alert system, the Group further improved its risk monitoring mechanism. By implementing risk monitoring on high risk areas such as group customers, other breaching banks, large credit customers, companies acting as guarantors and private financing, the Group has a comprehensive understanding and control over potential credit risks. With the establishment of a monthly reporting system on high risk customers, the Group further strengthened the follow-up analysis and guidance to management on unexpected credit risk incidents. By developing and promoting the customers' credit risk alert system, the Group can receive advance warnings from the analysis of its customers' group companies correlation patterns and identify potential risks associated with such customers.

The Group has centralised the collection and disposal process on corporate and retail non-performing loans. The Group managed the non-performing loans through various means including collection, restructuring, disposal of collaterals, recourse to guarantors, litigation, arbitration, written-off as allowed under the regulatory requirements.

During the Reporting Period, the Group intensified efforts of the head office in direct and centralised management of non-performing loans, focusing on the collection of non-performing loans for major projects and by particular branches. Through the use of innovative collection methods such as the use of assets for repayment and capital operation to continually enhance the collection and management of non-performing loans, the Group has achieved good results.

*Credit risk management with respect to retail loans*

The Group centrally managed retails loans at branch level based on special features of such loans. The centralised processes include risk verification, review and approval and other intermediary procedures. During the Reporting Period, the Group followed the country's macro-economic control policies and market changes closely so as to monitor the credit provision on retail loans, and strictly controlled the regions, customers and products offered as part of its retail lending business.

In 2008, the Group completed the development and testing of its internal rating model for retail business. The model has been on trial in certain branches, paving the way for full implementation across the bank and integration at a later stage.

In 2008, the Group actively used various tools and measures of pre-intervention to strengthen the monitoring of retail loan risk, including the use of risk alerts and stress test to enhance the ability to identity risks early and provide prompt alert, formulating emergency response protocol to resolve unexpected credit risks; placing customers with high potential risk on a watch list for special management; and implementing different types of collection methods on defaulting retail loan customers depending on the age of the debt. The Group commenced the development and creation of a credit management system for small enterprises, optimised its retail credit system and enhanced systematic management of retail credit risk to ensure the quality of retail loan assets.

The Group has a stand-alone credit card centre which operates and manages credit card business. Credit card business has its own independent risk policies, work flow and credit approval process. Credit risk is evaluated and controlled through means such as customer credit cycle concept, product portfolio management strategy, score card tool, aging analysis, and time series analysis methods.

*Credit risk management with respect to treasury business*

The Group practises centralised review and approval and management of approval limits with respect to the granting of credit to other banking institutions as part of its treasury business. The Group manages its treasury business credit risk through careful selection of clients, timely risk review, giving due consideration to both internal and external credit ratings, hierarchical credit approval system, and the use of its approval limits management system to review and adjust credit limits in a timely manner. During the Reporting Period, the Group's phase one management system in respect of inter-bank credit authorisation has successfully been put into operation, which effectively promoted the control over its risk exposure from its investment and strengthened the monitoring of inter-bank lending.

### 4.7.2 *Liquidity Risk Management*

Liquidity risk refers to the risk of possessing insufficient funds to meet debt obligations as they fall due. The Group's exposure to liquidity risks arises primarily from early or high volume withdrawals by depositors, borrowers delaying their loan repayments and mismatch of the amounts and maturity dates of assets and liabilities.

In 2008, global economic conditions have undergone drastic changes, which caused the Central Government's policy direction to change accordingly. During the Reporting Period, the key factor impacting on the Group's liquidity is the adjustments that were made to the statutory deposit reserve ratio: i) in the first half of 2008, PBOC raised the deposit reserve ratio 6 times by 3 percentage points in aggregate, reducing the Group's available funds and thereby impacting our liquidity; ii) since October 2008, PBOC reduced the deposit reserve ratio 4 times, out of which 3 adjustments (resulting in a total reduction of the ratio by 2 percentage points) are applicable to the Group, freeing up part of the reserve funds and thus enabling the Group to have greater access to funds. All in all, although the numerous adjustments to the deposit reserve ratio have had an impact on the Group during the Reporting Period, the impact has not been significant.

During the Reporting Period, the Group formulated an appropriate liquidity management plan based on our projection on liquidity needs. Besides, the Group conducted periodic analysis of macro-economic situation, PBOC's monetary policies, and money market developments. The Group actively managed liquidity of the Bank by implementing the following measures: i) maintaining stability in liabilities and increasing the proportion of core deposits in total liabilities; ii) setting parameters and limits to monitor and manage the Bank's liquidity position; iii) centralised management at the head office of the use of the Bank's liquidity assets; iv) keeping a healthy ratio of PBOC reserves, overnight inter-bank borrowing and lending, and high liquidity debt investment, as well as actively participating in the operations of open market, money market and bond markets to ensure sound financing capacity in the market; v) reasonably matching maturity dates of assets to reduce liquidity risk through a diversified liquidity portfolio.

During the Reporting Period, by combining the characteristics of the macro-economics situations in 2008, the Group has focused on the implementation of the following two measures to enhance liquidity risk management: i) formulating a liquidity risk emergency plan, setting up periodic monitoring and alerting mechanism, establishing risk assessment and crisis management plan; and ii) enhancing liquidity management on overseas branches, proactively responding to global financial market changes.

As at 31 December 2008, relevant indicators of the Group's liquidity are as follows:

| **Major regulatory indicators** | **31 December 2008** | 31 December 2007 |
|---|---|---|
| Liquidity ratio | | |
| (Local and foreign currencies) | **39.72%** | 27.20% |
| Loan-to-deposit ratio | | |
| (Local and foreign currencies) | **65.29%** | 64.93% |

*Note:* Calculated in accordance with the regulatory requirements applicable to the China banking industry.

*4.7.3 Market Risk Management*

Market risk refers to the risk of on- and off-balance sheet operating losses arising as a result of adverse changes in market price. Market risk exists in the Group's trading book and banking book. The trading book records the Group's tradable financial assets and liabilities with respect to its treasury business including derivative financial instruments. The banking book records the Group's non-tradable financial assets and liabilities.

According to the relevant provisions in "Measures for the Management of Capital Adequacy Ratios of Commercial Banks" promulgated by China regulatory authority, the Group assesses market risk capital regularly, and ensures that capital is adequate to cover its market risk.

During the Reporting Period, the Group has strengthened its centralised management on market risk. The Group has made revisions and improvements to its existing market risk management system, and further standardised market risk limits management and financial tools classification management; continuously expanded the scope of the Bank's periodic market risk assessment, thus reinforcing its importance in decision making; formulated the risk management measures on wealth management products, focused on the standardisation of the procedures for the risk audit of wealth management products and promoted implementation of the requirements on wealth management products risk management.

Under the volatile global financial market environment, the Group is highly concerned about risk control on its investment in foreign currencies bonds during the Reporting Period. By paying close attention to market dynamics, daily real-time monitoring, refining the requirements on classification management, and formulating appropriate control measures, the Group has strengthened the prevention and resolution of potential risk. Through a comprehensive clean up and temporary freeze of the granting of credit to potentially risky business, the Group has effectively prevented the outbreak of potential risk. By enhancing guidance on disposal of high risk bonds and reducing the investment in high risk foreign currencies bond at the best available opportunity, the Group was in a better position to avoid losses in foreign currencies funds brought by the global financial crisis.

Based on the classification of the market risk drivers, the Group's major market risks include interest rate risk, exchange rate risk and other price risk.

(1) Interest Rate Risk Management

Interest rate risk, the Group's largest market risk factor, exists in the Group's trading and banking books. Interest rate risk on trading book mainly reflected the possible negative impact that the changes in interest rate may have on the fair value of the assets under the trading book. Interest rate risk on banking book mainly reflected the risk associated with the changes in interest rate which may result in reducing net interest income for the Group.

The Group implemented limit management on interest rate risk on trading book by setting trading limits, stop-loss limits, exposure limits and sensitivity limits, and systematically monitor such limits. In practice, the Group manages interest rate risks on the trading book through the introduction of parameters such as duration, convexity and value basis point, combined with an analysis of the market environment and position distribution of the Group. Moreover, the Group progressively strengthens the portfolio operation of its trading book, as well as appropriately use financial derivative instruments to control and hedge the interest rate risk on the trading book.

The interest rate risk on banking book mainly arises from the mismatch in the repricing periods of the Group's assets and liabilities. The Group has preliminarily developed a comprehensive banking book's interest rate risk monitoring system, by regularly monitoring the gap in the repricing periods of interest-rate-sensitive assets and liabilities through measures such as gap analysis, taking the initiative to adjust the proportion of floating rate and fixed rate assets and so on, thereby effectively managed banking book's exposure to interest rate risk.

(2) Exchange Rate Risk Management

Exchange rate risk, including exchange rate risk on the trading book arising from the Group's proprietary and agency foreign exchange trading and the structural exchange rate risk arising from the mismatching of the foreign currency denomination of its assets and liabilities, exists in the Group's trading and banking books. The Group continued to enhance its trading system and information management system to manage and control the Bank's exchange rate risk through measures such as restricting and minimising the exposure to exchange rate risk to permissible limits under the Bank's policies by establishing and controlling the relevant limits, strengthening the matching of the currency structure of assets and liabilities by actively adjusting the structure of foreign currency denominated assets, and diverting and hedging against exchange rate risk by suitably utilising financial derivative instruments.

(3) Other Price Risk Management

Other price risk is largely derived from the equity investments held by the Group and other commodity price linked derivatives. Most equity investments were created due to historical reasons or were assets obtained through foreclosure. The Group is of the view that other price risk faced by the Group is not significant.

(4) Risk Analysis

During the Reporting Period, the Group actively promoted the Value at Risk Model (VaR) for monitoring and measuring part of the market risk on the trading book. Sensitivity analysis is currently the main tool that the Group deploys for assessment and quantification of market risks on the trading and banking books.

*Interest rate risk and sensitivity analysis*

The table shows the Group's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates:

*(in millions of RMB)*

| | Non-interest bearing | Less than 1 month | 1–3 months | 3 months–1 year | 1–5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|---|
| Total assets | 80,740 | 1,224,524 | 251,553 | 705,414 | 270,078 | 150,638 | 2,682,947 |
| Total liabilities | (63,498) | (1,441,363) | (250,585) | (524,995) | (225,842) | (26,569) | (2,532,852) |
| Net exposure | 17,242 | (216,839) | 968 | 180,419 | 44,236 | 124,069 | 150,095 |

The table below illustrates the potential impact of a simple 100 basis points (bp) change in the yield on the financial position of the Group at 31 December to the net interest income of the coming year and to the reported equity:

*(in millions of RMB)*

| | Net Interest Income | | Equity | |
|---|---|---|---|---|
| | **For the year ending 31 December 2009** | **For the year ended 31 December 2008** | **As at 31 December 2008** | As at 31 December 2007 |
| Yield increase by 100 bp | **5,175** | **4,477** | **(1,971)** | (1,351) |
| Yield decrease by 100 bp | **(5,175)** | **(4,477)** | **2,088** | 1,380 |

*Exchange rate risk and sensitivity analysis*

As at 31 December 2008, the Group's foreign exchange risk exposure is as follows:

*(in millions of RMB)*

| | **RMB** | **US$ converted to RMB** | **HKD converted to RMB** | **Other currencies converted to RMB** | **Total** |
|---|---|---|---|---|---|
| Total assets | 2,439,425 | 151,072 | 63,579 | 28,871 | 2,682,947 |
| Total liabilities | (2,314,434) | (125,678) | (68,096) | (24,644) | (2,532,852) |
| Net exposure | 124,991 | 25,394 | (4,517) | 4,227 | 150,095 |

The table below illustrates the potential impact from the change of Renminbi against US dollar, HK dollar and other currencies by 5% on the Group's net profit and reported equity:

*(in millions of RMB)*

| | Net Profit/(Loss) | | Equity | |
|---|---|---|---|---|
| | **For the year ended 31 December 2008** | For the year ended 31 December 2007 | **As at 31 December 2008** | As at 31 December 2007 |
| RMB appreciate by 5% | **(903)** | (1,066) | **(196)** | (299) |
| RMB depreciate by 5% | **903** | 1,066 | **196** | 299 |

### *4.7.4 Operational Risk Management*

Operational risk refers to the direct or indirect risk of losses caused by inadequate or improper internal processes, employees and information system in its operations, and external events.

During the Reporting Period, the Group strengthened its centralised management on operational risk. The Group revised and optimised the Bank's operational risk management measures, formulated a comprehensive operational risk management development plan, focused its operational risk management on key areas such as accounting, information technology and anti-fraud. There was no major operational risk related incidents or cases in the Reporting Period, reflecting the safe operations of all lines of business of the Bank.

For accounting operational risk management, the Group has strengthened its management on vault during the Reporting Period, cash, deposit boxes, self-servicing equipment, resulting in a significant improvement on cash and treasury management. The Group also optimised the management on the fund transfer and remittance process, which effectively reduced the associated operational risk. In addition, the Group continuously improved and optimised its accounting risk management tools through the continuous enhancement of its accounting risk monitoring system, vigorously implemented its accounting risk management system by developing a real-time online accounting risk monitoring system, and increased the efficiency of its alert system by expanding its scope.

For information technology risk management, the Group continuously improved the capability of its information technology risk management system through enhancing the system and technical specifications, as well as specifying management requirements and security control points during the Reporting Period. The Group successfully implemented the switch of operations between its data center and the disaster recovery center. The stable operation of its disaster recovery center effectively assured information security during the Olympics and also led to stable operation of various business operating systems and information system. The Group also successfully completed the development of the ISO27001 information security management system and has obtained the ISO27001 international certification on information security.

During the Reporting Period, the Group actively stepped up its efforts on anti-fraud risk management. The Group established anti-fraud management divisions and teams, developed the two-tier anti-fraud management process at the head office and its branches, initiated the development of the anti-fraud information management system, constructed the fraud alert channels, thereby effectively prevented and controlled fraud related risk.

*4.7.5 Anti-money laundering*

The Group has progressively established an Anti-money Laundering (AML) system on the basis of systematic development, together with the focus on its internal control system and the application of its system platform as security measures, thereby further improving its AML related work.

During the Reporting Period, the Group actively advanced its system development, published and revised a number of AML work recommendations and management measures. The Group also continued to achieve system development breakthrough by completing the development of systems such as the offsite AML monitoring system and the customers' risk classification system. The Bank also improved its system governing large and suspicious transactions and implemented the system for automatic perspective data collection and reporting.

## 4.8 Strategic cooperation

In 2008, the strategic cooperation between the Bank and HSBC continued to achieve steady progress. Both parties have achieved significant synergies in areas such as the exchange of technical expertise, credit card business, international business, corporate banking business and custodian and trust business. Through this partnership, the Bank benefited from HSBC's advanced management philosophy and experience. In return, HSBC enjoyed excellent investment returns from the Bank's continued business growth, enhancing further the mutually beneficial relationship between the two banks.

The senior management of HSBC and the Bank maintains close communication through periodic meetings and conferences between the Chairmen and the Chief Executive Officers. This enabled timely and efficient resolution of any issues that arose in the partnership, thereby increasing the depth of cooperation between the two banks.

The Bank's strategy is being "a first-class public bank group focused on wealth management services by means of international expansion and by providing comprehensive services". The Bank continues to focus on the principles of "initiating wisdom" and "establishing policy" while it actively promotes bilateral communication and sharing of technical expertise with HSBC. Both banks have shared among themselves experience in domestic and international banking sector through technical training, staff exchange program and expertise consultation.

Both banks have achieved stellar performances from the cooperation in the following lines of business.

Credit card business:

There had been excellent momentum in the development of the jointly-managed credit card business. As at the end of 2008, the aggregate number of credit cards issued exceeded 10 million and the annual spending on these credit cards reached approximately RMB100 billion. Key performance indicators, such as average level of card spending and total receivables ranked among the top in the industry. This also helped to maintain our lead in other service quality and profitability indicators in the industry.

Corporate banking business:

Both banks jointly provided financial services and credit facilities to reputable global corporations for the purposes of projects that promote environmentally friendly goal. In addition, the second phase of corporate banking system integration between the two banks was completed and commenced operation during the year. This enabled HSBC to make third party enquiries of the Bank's domestic customers, and allowed the Bank to make third party enquiries of HSBC's customers in 11 Asia Pacific countries.

Custodian and trust business:

Both banks cooperated to cross-sell their custodian and trust products and services to potential customers to achieve mutual growth and expansion in the scale of business operations. These include international custody and trust services, insurance and pension funds services.

As a result of the HSBC's confidence in the future development of our Bank and the prospects of the ongoing cooperation between the two banks, despite the lock-up period of the 9.115 billion H shares in the Bank held by HSBC expired on 18 August 2008, both parties reiterated their plans to adopt a long-term approach towards the strategic cooperation between the two banks and HSBC's stance in not reducing its shareholding in the Bank. Going forward, both banks will continue to strengthen communication and coordination to enhance the effectiveness of technical cooperation, and seek to broaden the scope of cooperation in the various lines of business. Through continued collaboration and cooperation with HSBC, the Bank seeks to raise its management standards to international levels. In 2009, both banks will focus on strengthening their co-operation in the following aspects:

— To further increase technical cooperation. Both parties plan to start a new senior management skills development programme in 2009 which will be structured along the different lines of business. Through communication and exchange with HSBC's corresponding lines of business, the Bank seeks to learn from HSBC's strategic development, operational framework, and business innovation and risk management expertise to optimise the utilisation of resources. In addition, the Bank will continue to strengthen technical cooperation with HSBC in other areas, to seek to learn from the experience of HSBC and to share the training resources of the Bank and its knowledge of the China domestic market so as to achieve synergies and mutually beneficial development.

— To expedite the process of incorporating a credit card company. The Pacific credit card centre is the most significant joint venture between the two banks and has achieved excellent results to-date. In accordance with the spirit of the credit card cooperation agreement and within the existing legal and policy framework, both parties will, on the basis of mutual benefits, expedite the negotiations in relation to the incorporation of a credit card company so as to achieve the early establishment of a joint venture credit card company.

— To continue in-depth cooperation in key business areas to achieve ground-breaking future development. As a priority, both banks will focus on strengthening cooperation in the areas of international banking business, corporate banking business, custodian and trust business and cross selling to key clients, integration of systems and RMB international clearing services.

— To promote cooperation in comprehensive operation at an appropriate time. In line with the industry trends and the Bank's strategic development goal of achieving comprehensive operation, both banks will continue to explore the potential of cooperation in the area of comprehensive operation and to conduct cooperation in areas such as securities business, insurance and pension fund business within the legal and regulatory framework.

### 4.9 Outlook for 2009

The global financial crisis is expected to continue to affect the global economy in 2009. The domestic banking industry is also expected to face major challenges with the proliferation of the financial crisis and the macroeconomic downturn. These challenges resulted in greater barrier to achieve rapid development as demand for banking services decline. In addition, as a result of the worsening of the operating conditions for general enterprises, the non-performing assets of the Bank are experiencing an upward pressure which poses significant challenges to the Bank's risk management. The Bank's interest margin is also expected to decline significantly due to increased competition from other banks and financial institutions and the decline in interest rates. At the same time, the Chinese Government has also adopted active fiscal policies to stimulate economic growth. These policies include measures to suitably relax its monetary policy and provide financial support for economic development, all of which will help to create a greater development environment and new opportunities for the Bank.

The Group will continue its development strategy of being "a first-class public bank group focused on wealth management services by means of international expansion and by providing comprehensive services" in the face of future challenges and opportunities by focusing on the following aspects:

1. To fully utilise the Bank's advantage in corporate banking in an environment where the government policy is to stimulate domestic demand and economic growth to raise its overall competitiveness in corporate banking and whole-heartedly devote itself to achieving rapid and healthy growth in corporate banking business.

2. To continue to further optimise its business structure, customer structure and regional structure to enhance the development of its retail banking, fee-based, wealth management and treasury businesses and thus continue to push ahead with the Bank's strategic realignment.

3. To continue to promote innovation in the areas of business management, organisational structure and services so as to further optimise the business process and product development mechanism, raise service quality, continuously improve core competitiveness and actively expand market share.

4. To strengthen micro management while diligently control operating costs and raising operating efficiency.

5. To avoid large declines in interest margins through pro-active asset and liability management.

6. To realise synergies within the Group, to strengthen the operating capability of subsidiaries and to ensure healthy growth of overseas branches.

7. To further strengthen risk management and thus maintain the quality of assets.

# 5. OTHER INFORMATION

## 5.1 Investments in Other Listed Companies and Unlisted Financial Institutions and Sales and Purchase of Shares in Other Listed Companies

### *5.1.1 Holdings of Shares Issued By Other Listed Companies*

| Stock code | Simplified stock name | Initial investment cost (RMB) | Percentage shareholding | Term-end Cost (RMB) | Gains/Losses in the Reporting Period (RMB) | Equity movement in the Reporting Period (RMB) | Accounting items | Source of shares |
|---|---|---|---|---|---|---|---|---|
| 600068 | Gezhouba | 140,315,551.00 | 2.05% | 301,912,520.00 | 21,550,259.47 | (245,588,684.00) | AFS securities | Foreclosed assets |
| 600837 | Haitongzhengquan | 282,242,325.00 | 0.25% | 168,858,537.08 | — | (113,383,787.92) | AFS securities | Foreclosed assets |
| 600000 | Pufayinhang | 6,000,000.00 | 0.14% | 108,570,897.50 | — | (324,073,886.50) | AFS securities | Equity investment |
| 03377 | Sino-Ocean Land | 138,863,720.57 | 0.43% | 62,489,355.39 | — | (109,983,221.20) | AFS securities | Equity investment |
| 00388 | HKEX | 2,371,919.39 | 0.07% | 52,249,626.24 | — | (105,335,394.75) | AFS securities | Equity investment |
| 000979 | ST Keyuan | 12,494,400.00 | 8.84% | 52,060,000.00 | — | (12,384,800.00) | AFS securities | Foreclosed assets |
| 600642 | Shennenggufen | 9,333,333.33 | 0.17% | 29,950,000.00 | 3,106,300.41 | (62,502,500.00) | AFS securities | Equity investment |
| 000686 | Dongbeizhengquan | 3,740,000.00 | 0.38% | 26,663,088.54 | — | (87,464,690.61) | AFS securities | Foreclosed assets |
| 08253 | Tianyuanlvye | 28,289,828.52 | 8.08% | 24,961,613.40 | — | (3,328,215.12) | AFS securities | Equity investment |
| 03808 | Sinotruk | 53,995,928.28 | 0.22% | 23,017,068.00 | — | (30,425,466.00) | AFS securities | Equity investment |
| | Others | 136,367,279.63 | | 190,445,672.27 | 11,291,350.48 | (323,521,906.46) | | |
| | Total | 814,014,285.72 | | 1,041,178,378.42 | 35,947,910.36 | (1,417,992,552.56) | | |

*Notes:*

i) The table sets out the Group's holdings of shares in other listed companies that are classified as investment securities — available-for-sale and financial assets held for trading in the Group's consolidated financial statements.

ii) Gains or losses in the Reporting Period refer to the impact of such investments on the Group's consolidated net profit for the Reporting Period.

### 5.1.2 *Holdings of Shares Issued By Unlisted Financial Institutions*

| Name of institution | Initial investment cost (RMB) | Number of shares held | Percentage shareholding | Term-end Cost (RMB) | Gains/Losses in the Reporting Period (RMB) | Equity movement in the Reporting Period | Accounting Items | Source of shares |
|---|---|---|---|---|---|---|---|---|
| Jiangsu Changsu Rural Commercial Bank Co., Ltd. | 380,000,000.00 | 57,560,225 | 10.00% | 380,000,000.00 | 11,573,082.48 | — | Long-term equity investments | Equity investment |
| China Union Pay Co., Ltd. | 146,250,000.00 | 112,500,000 | 3.90% | 146,250,000.00 | 1,800,000.00 | — | Long-term equity investments | Equity investment |
| **Total** | 526,250,000.00 | 170,060,225 | | 526,250,000.00 | 13,373,082.48 | | | |

### 5.1.3 *Sales and Purchases of Other Listed Equity Shares*

| **Stock name** | **Number of shares held at beginning of period** | **Number of share bought/(sold) during the Reporting Period** | **Number of shares held at end of period** | **Purchase Cost (RMB)** | **Investment Realised Gains/ (Losses) (RMB)** |
|---|---|---|---|---|---|
| Tianyuanlvye | — | 94,350,000 | 94,350,000 | 28,289,828.52 | — |
| Zhongmeinengyuan | — | 340,000 | 340,000 | 6,678,368.82 | — |
| China Mobile | 2,000 | 41,000 | 43,000 | 4,726,137.44 | — |
| Gongshangyinhang | — | 930,000 | 930,000 | 4,710,776.41 | — |
| Shandongchenming | — | 500,000 | 500,000 | 3,980,365.38 | — |
| Zhongguoshenhua | — | 125,000 | 125,000 | 3,663,357.45 | — |
| Zhongguopingan | 60,000 | 167,760 | 227,760 | 3,550,660.53 | — |
| Zhongguotiejian | — | 300,000 | 300,000 | 3,245,251.30 | — |
| Changhangyouyun | — | 200,000 | 200,000 | 2,803,644.41 | — |
| Zhongguotaibao | — | 83,010 | 83,010 | 2,490,300.00 | — |
| Zhongxinyinhang | — | 850,000 | 850,000 | 2,376,225.66 | — |
| Kangmeiyaoye | — | 150,000 | 150,000 | 1,777,338.50 | — |
| Franshion Ppt | 350,000 | 200,000 | 550,000 | 690,335.84 | — |
| Xtep Int'l | — | 200,000 | 200,000 | 578,377.97 | — |
| Hopewell Infra | — | 17,000 | 17,000 | 66,124.89 | — |
| Dazhonggongyong | 1,000,000 | (1,000,000) | — | — | 228,005,570.29 |
| Gezhouba | 35,813,000 | (1,660,000) | 34,153,000 | — | 21,550,259.47 |
| Qingfangcheng | 2,199,068 | (2,199,068) | — | — | 13,596,478.60 |
| ST Lianyou | 10,352,000 | (2,902,000) | 7,450,000 | — | 10,329,961.52 |
| Jidiangufen | 3,000,000 | (3,000,000) | — | — | 7,421,898.35 |
| Shitougufen | 4,178,789 | (4,178,789) | — | — | 7,336,777.57 |
| Boyingtouzi | 646,179 | (646,179) | — | — | 7,286,870.30 |
| ST Tianqiao | 2,938,866 | (2,938,866) | — | — | 5,365,964.51 |
| DongbeiZhiyao | 311,657 | (311,657) | — | — | 5,091,841.25 |
| S*ST Cika | 610,000 | (610,000) | — | — | (3,440,975.63) |
| Shijiguanghua | 236,925 | (236,925) | — | — | 2,812,162.89 |
| Shennenggufen | 5,250,000 | (250,000) | 5,000,000 | — | 1,456,300.41 |

*Note:* Other than disposal of securities obtained by the Bank as security for loans in the ordinary course of business, the remaining movements in securities as shown in the above table are as a result of the trading of listed securities by a subsidiary of the Bank.

## 5.2 Human Resources

### *5.2.1 Number, qualification and education attainment of staff*

As at 31 December 2008, the Bank had a total of 77,734 employees, representing an increase of 14.18% compared to the beginning of the year. Among these employees, 601 (representing 0.77% of the total number of employees) possess advanced professional and technical qualification; 16,370 (representing 21.06% of the total number of employees) possess intermediate professional and technical qualification and 20,711 (representing 26.64% of the total number of employees) possess basic professional and technical qualification. The table below shows the education attainment level of the Bank's employees:

| Education Attainment Level | Number of employees | Proportion (%) |
|---|---|---|
| Doctor | 105 | 0.13 |
| Postgraduate | 2,851 | 3.67 |
| Undergraduate | 37,381 | 48.09 |
| College | 27,604 | 35.51 |
| Junior college | 5,117 | 6.58 |
| High school and below | 4,676 | 6.02 |
| Total | 77,734 | 100.00 |

### *5.2.2 Human Resource Management*

In view of the Bank's strategic objectives, the Bank has further standardised its organisation structure and job designation. Combining the development trends of the market and the industry, the Bank dynamically adjusts its organisation structure, enhancing the connection between the organisation structure, job designations and strategic objectives. The Bank maintains its existing "Pyramid Management Structure" and continues to improve management efficiency. By establishing a job designation model which promotes bilateral management and professional development, the Bank broadens the opportunities for its employees' career development. The allocation of staff highlights the output efficiency, while the full support of operation restructuring, construction of new grid point, standardisation of the Bank's business processes and the promotion of a comprehensive risk management help to provide a strong human resource support for the rapid development of the business.

*5.2.3 Remuneration Policy*

The Bank continued to promote the Bank's unique remuneration and management system of "taking the position as the basis, with the labor market price as target, unifying the job value and performance value"; and continues to design a remuneration system and a management policy that have the characteristics of "a unified approach and standardised operation management throughout the bank" as the main focus of employees' benefits system.

*5.2.4 Performance Management*

The Bank continued to use balanced scorecard and target table as the means to optimise the performance management model. The Bank improved its performance management approach at each level by highlighting the strategic conduction and linkages, clarifying the internal logic of the system and strengthening the examination of the guiding role of the allocation of resources. Revolving around the adjustments to the Bank's organisational structure, following the promotion of globalisation and comprehensive strategy, actively seeking assessment methods and paths for the whole Bank that streamline and differentiate, the Bank will be able to lead the development in the refinement of performance management.

## 5.3 Purchase, Sale or Redemption of the Bank's shares

During the Reporting Period, neither the Bank nor any of its subsidiaries purchased, sold or redeemed any shares of the Bank.

## 5.4 Compliance with the Code on Corporate Governance Practices of the Listing Rules

The Group endeavoured to establish a high standard of corporate governance. The Group believes that effective corporate governance is crucial to maximise shareholder value. In order to maintain a high standard of corporate governance, the Bank established a responsible, professional and accountable Board of Directors, Board of Supervisors and experienced senior management. The members of the Bank's Board of Directors and Board of Supervisors (other than employee supervisors) are elected by the shareholders at the shareholders' general meeting. The Bank has also established five special committees under the Board of Directors, including the Strategy Committee, the Audit Committee, the Risk Management Committee, the Personnel and Compensation Committee and the Social Responsibility Committee. None of the Bank's Directors is aware of any information that would reasonably indicate that the Bank had not, for any time during the period ended 31 December 2008, been in compliance with the Code on Corporate Governance Practices as set out in Appendix 14 to the Listing Rules.

## 5.5 Compliance with the Model Code for Securities Transactions by Directors of Listed Issuers

The Group has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "**Model Code**") as set out in Appendix 10 to the Listing Rules. The Bank made specific enquiries with all its Directors and Supervisors and each of them confirmed that they had complied with the required standards of the Model Code during the Reporting Period.

# 6. FINANCIAL STATEMENTS

## 6.1 CONSOLIDATED PROFIT AND LOSS ACCOUNT

*(in millions of RMB unless otherwise stated)*

| Group | For the year ended 31 December **2008** | 2007 |
|---|---|---|
| Interest income | **117,106** | 90,319 |
| Interest expense | **(51,244)** | (36,376) |
| **Net interest income** | **65,862** | 53,943 |
| Fee and commission income | **10,121** | 8,245 |
| Fee and commission expense | **(1,284)** | (1,150) |
| **Net fee and commission income** | **8,837** | 7,095 |
| Dividend income | **83** | 77 |
| Gains less losses arising from trading activities | **1,557** | 250 |
| Gains less losses arising from de-recognition of investment securities | **226** | 657 |
| Other operating income | **711** | 767 |
| Impairment losses | **(10,690)** | (6,380) |
| Other operating expenses | **(30,867)** | (25,295) |
| **Operating profit before tax** | **35,719** | 31,114 |
| Income tax | **(7,229)** | (10,712) |
| **Net profit for the year** | **28,490** | 20,402 |
| **Attributable to:** | | |
| Shareholders of the Bank | **28,393** | 20,274 |
| Minority interest | **97** | 128 |
| | **28,490** | 20,402 |
| **Basic and diluted earnings per share For profit attributable to the shareholders of the Bank (in RMB)** | **0.58** | 0.42 |
| **Dividends** | | |
| Interim dividends declared during the year | **4,899** | — |
| Final dividends proposed after the balance sheet date | **4,899** | 7,349 |
| | **9,798** | 7,349 |

## 6.2 CONSOLIDATED BALANCE SHEET

*(in millions of RMB)*

| Group | As at 31 December | |
|---|---|---|
| | **2008** | 2007 |
| **ASSETS** | | |
| Cash and balances with central banks | **362,180** | 261,433 |
| Due from other banks and financial institutions | **331,511** | 156,110 |
| Financial assets held for trading | **26,936** | 19,340 |
| Loans and advances to customers | **1,298,776** | 1,082,788 |
| Investment securities — loans and receivables | **90,903** | 66,693 |
| Investment securities — available-for-sale ("AFS") | **142,010** | 146,454 |
| Investment securities — held-to-maturity ("HTM") | **367,878** | 326,953 |
| Property and equipment | **35,279** | 32,199 |
| Deferred tax assets | **2,693** | 2,524 |
| Other assets | **24,781** | 15,950 |
| **Total assets** | **2,682,947** | 2,110,444 |
| **LIABILITIES** | | |
| Due to other banks and financial institutions | **569,453** | 332,556 |
| Financial liabilities held for trading | **10,013** | 10,028 |
| Due to customers | **1,865,815** | 1,555,599 |
| Other liabilities | **43,199** | 35,564 |
| Current taxes | **4,165** | 5,872 |
| Deferred tax liabilities | **207** | 504 |
| Debts issued | **40,000** | 37,000 |
| **Total liabilities** | **2,532,852** | 1,977,123 |
| **EQUITY** | | |
| **Capital and reserves attributable to the Bank's shareholders** | | |
| Share capital | **48,994** | 48,994 |
| Capital surplus | **43,100** | 43,100 |
| Other reserves | **33,443** | 20,422 |
| Retained earnings | **24,125** | 20,387 |
| | **149,662** | 132,903 |
| **Minority Interest** | **433** | 418 |
| **Total equity** | **150,095** | 133,321 |
| **Total equity and liabilities** | **2,682,947** | 2,110,444 |
| **Proposed final dividends in retained earnings** | **4,899** | 7,349 |

# 6.3 CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

*(in millions of RMB)*

| | | | Other reserves | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital | Capital surplus | Statutory reserve | Discretionary reserve | Statutory general reserve | Revaluation reserve for AFS securities | Revaluation reserve for properties | Translation reserve on foreign operations | Retained earnings | Minority interest | Total |
| **Balance at 1 January 2007** | 45,804 | 21,540 | 899 | — | 4,428 | 867 | 4,383 | (213) | 12,728 | 59 | 90,495 |
| Gains from changes in fair value of AFS securities, net of tax | — | — | — | — | — | 1,049 | — | — | — | 51 | 1,100 |
| Transfer to net profit on disposal or impairment of AFS securities, net of tax | — | — | — | — | — | (483) | — | — | — | — | (483) |
| Revaluation of property | — | — | — | — | — | — | 1,236 | — | — | — | 1,236 |
| Realization of revaluation reserve upon disposals | — | — | — | — | — | — | (20) | — | 20 | — | — |
| Translation difference on foreign operations | — | — | — | — | — | — | — | (403) | — | — | (403) |
| Tax rate change impact | — | — | — | — | — | 118 | 506 | — | — | — | 624 |
| Net income/(expense) recognized directly in equity | — | — | — | — | — | 684 | 1,722 | (403) | 20 | 51 | 2,074 |
| Net profit | — | — | — | — | — | — | — | — | 20,274 | 128 | 20,402 |
| Acquisition of new subsidiary | — | — | — | — | — | — | — | — | — | 180 | 180 |
| Dividends | — | — | — | — | — | — | — | — | (4,580) | — | (4,580) |
| Transfer to reserves | — | — | 1,271 | 576 | 6,208 | — | — | — | (8,055) | — | — |
| Issue of shares | 3,190 | 21,560 | — | — | — | — | — | — | — | — | 24,750 |
| **Balance at 31 December 2007** | 48,994 | 43,100 | 2,170 | 576 | 10,636 | 1,551 | 6,105 | (616) | 20,387 | 418 | 133,321 |
| **Balance at 1 January 2008** | **48,994** | **43,100** | **2,170** | **576** | **10,636** | **1,551** | **6,105** | **(616)** | **20,387** | **418** | **133,321** |
| Gains from changes in fair value of AFS securities, net of tax | **—** | **—** | **—** | **—** | **—** | **698** | **—** | **—** | **—** | **(58)** | **640** |
| Transfer to net profit on disposal or impairment of AFS securities, net of tax | **—** | **—** | **—** | **—** | **—** | **487** | **—** | **—** | **—** | **10** | **497** |
| Revaluation of property | **—** | **—** | **—** | **—** | **—** | **—** | **2** | **—** | **—** | **—** | **2** |
| Realization of revaluation reserve upon disposals | **—** | **—** | **—** | **—** | **—** | **—** | **(35)** | **—** | **35** | **—** | **—** |
| Translation difference on foreign operations | **—** | **—** | **—** | **—** | **—** | **—** | **—** | **(596)** | **—** | **—** | **(596)** |
| Tax rate change impact | **—** | **—** | **—** | **—** | **—** | **5** | **18** | **—** | **—** | **—** | **23** |
| Net income/(expense) recognized directly in equity | **—** | **—** | **—** | **—** | **—** | **1,190** | **(15)** | **(596)** | **35** | **(48)** | **566** |
| Net profit | **—** | **—** | **—** | **—** | **—** | **—** | **—** | **—** | **28,393** | **97** | **28,490** |
| Establishment of new subsidiary | **—** | **—** | **—** | **—** | **—** | **—** | **—** | **—** | **—** | **23** | **23** |
| Dividends | **—** | **—** | **—** | **—** | **—** | **—** | **—** | **—** | **(12,248)** | **(57)** | **(12,305)** |
| Transfer to reserves | **—** | **—** | **1,993** | **8,511** | **1,938** | **—** | **—** | **—** | **(12,442)** | **—** | **—** |
| **Balance at 31 December 2008** | **48,994** | **43,100** | **4,163** | **9,087** | **12,574** | **2,741** | **6,090** | **(1,212)** | **24,125** | **433** | **150,095** |

## 6.4 CONSOLIDATED STATEMENT OF CASH FLOWS

*(in millions of RMB)*

| | For the year ended 31 December | |
|---|---|---|
| | **2008** | 2007 |
| **Cash flows from operating activities:** | | |
| Net profit before taxation: | **35,719** | 31,114 |
| Adjustments for: | | |
| Impairment of loans and advances to customers | **10,190** | 5,961 |
| Write-back of due from banks and financial institutions | **(25)** | (113) |
| Reversal of impairment of other receivables | **(67)** | (592) |
| Impairment of investment securities | **1,090** | 692 |
| Depreciation of property and equipment | **3,006** | 2,665 |
| Reversal of revaluation deficit of property and equipment | **(3)** | (70) |
| Amortization of prepaid staff subsidies | **15** | 15 |
| Amortization of land use rights | **6** | 10 |
| Amortization of intangible assets | **228** | 223 |
| Gains less losses arising from de-recognition of investment securities | **(226)** | (657) |
| Gains on disposal of fixed assets | **(47)** | (99) |
| Decrease/(Increase) in the fair value of investment property | **19** | (13) |
| Accrued interest expense on term debt | **1,724** | 1,492 |
| Fee on debt issue | **10** | — |
| Net increase in mandatory reserve deposits | **(52,035)** | (96,069) |
| Net increase in due from other banks and financial institutions | **(94,420)** | (38,456) |
| Net increase in financial assets held for trading | **(7,596)** | (6,450) |
| Net increase in loans and advances to customers | **(226,178)** | (180,948) |
| Net increase in other assets | **(8,691)** | (523) |
| Net increase in due to other banks and financial institutions | **236,897** | 96,449 |
| Net (decrease)/increase in financial liabilities held for trading | **(15)** | 1,304 |
| Net increase in due to customers | **310,216** | 211,422 |
| Net increase in other liabilities | **8,537** | 9,717 |
| Net increase in business tax payable | **199** | 508 |
| Income tax paid | **(9,951)** | (6,272) |
| Net cash from operating activities | **208,602** | 31,310 |
| **Cash flows from investing activities:** | | |
| Acquisition of subsidiary, net of cash acquired | **—** | 11 |
| Purchase of investment securities | **(358,688)** | (536,871) |
| Disposal or redemption of investment securities | **298,726** | 379,441 |
| Acquisition of intangible assets | **(75)** | (191) |
| Purchase of land use rights | **(185)** | (3) |
| Purchase of property and equipment | **(6,983)** | (7,227) |
| Disposal of property and equipment | **1,026** | 636 |

*(in millions of RMB)*

| | For the year ended 31 December **2008** | 2007 |
|---|---|---|
| Net cash used in investing activities | **(66,179)** | (164,204) |
| **Cash flows from financing activities:** | | |
| Issue of shares | **—** | 24,750 |
| Debts issued | **3,000** | 25,000 |
| Fee on debt issue | **(10)** | — |
| Interest paid on debt | **(1,666)** | (577) |
| Dividends paid | **(13,407)** | (5,311) |
| Minority interest — capital contribution | **23** | — |
| Dividends paid to minority interest | **(57)** | — |
| Net cash (used in)/from financing activities | **(12,117)** | 43,862 |
| **Effect of exchange rate changes on cash and cash equivalents** | **(638)** | (627) |
| **Net increase/(decrease) in cash and cash equivalents** | **129,668** | (89,659) |
| **Cash and cash equivalents at the beginning of the period** | **96,064** | 185,723 |
| **Cash and cash equivalents at the end of the period** | **225,732** | 96,064 |
| Supplementary Information | | |
| Interest received | **114,053** | 89,113 |
| Interest paid | **(40,011)** | (31,853) |

## 6.5 NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### 1 Basis of presentation and accounting policies

The consolidated financial statements of the Group have been prepared in accordance with the International Financial Reporting Standards ("IFRS") and disclosure 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 investment securities classified as available for sale, financial assets and financial liabilities held at fair value through profit or loss, property and equipment, investment properties and all derivative contracts, which are carried at fair value.

The Group adopted the following amendments and interpretations that were effective in 2008:

IAS 39 Amendment — Financial Instruments: Recognition and Measurement amendment on reclassification of financial assets permits reclassification of certain financial assets out of the held-for-trading and available-for-sale categories if specified conditions are met. This amendment does not have any impact on the Group's financial statements, as the Group has not reclassified any financial assets.

IFRIC 11 — IFRS 2 Group and treasury share transactions, provides guidance on whether share-based transactions involving treasury shares or involving group entities (for example, options over a parent's shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the stand-alone accounts of the parent and group companies. This interpretation does not have an impact on the Group's financial statements.

IFRIC 14 — IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and Their Interaction, provides guidance on assessing the limit in IAS 19 on the amount of the surplus that can be recognised as an asset. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement. This interpretation does not have an impact on the Group's financial statements.

## 2 Net interest income

*(in millions of RMB)*

| **Group** | **Year ended 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| **Interest income** | | |
| Balances with central banks | **4,985** | 3,438 |
| Due from other banks and financial institutions | **6,907** | 5,971 |
| Loans and advances to customers | **82,784** | 65,417 |
| Investment securities | **22,430** | 15,493 |
| | **117,106** | 90,319 |
| **Interest expense** | | |
| Due to other banks and financial institutions | **(13,541)** | (10,182) |
| Due to customers | **(37,703)** | (26,194) |
| | **(51,244)** | (36,376) |
| **Net interest income** | **65,862** | 53,943 |

*(in millions of RMB)*

| | **Year ended 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Interest income on listed investments | **3,634** | 3,458 |
| Interest income on unlisted investments | **18,796** | 12,035 |
| Interest income accrued on loans and advances to customers individually identified with impairment | **555** | 654 |

## 3 Fee and commission income

*(in millions of RMB)*

| Group | Year ended 31 December | |
|---|---|---|
| | **2008** | 2007 |
| Settlement and agent service commission income | **2,045** | 1,744 |
| Bank card annual fee and commission income | **2,938** | 2,017 |
| Guarantee and commitment commission income | **912** | 399 |
| Custodian commission income | **667** | 530 |
| Fund sales commission income | **853** | 2,191 |
| Fund management commission income | **590** | 614 |
| Financial consulting income | **1,081** | 244 |
| Other commission income | **1,035** | 506 |
| | **10,121** | 8,245 |

*(in millions of RMB)*

| | Year ended 31 December | |
|---|---|---|
| | **2008** | 2007 |
| Fee income, other than amounts included in determining the effective interest rate, arising from financial assets or financial liabilities that are not held for trading nor designated at fair value | **84** | 30 |
| Fee income on trust and other fiduciary activities where the Group holds or invests on behalf of its customers | **667** | 530 |

## 4 Impairment losses

*(in millions of RMB)*

| Group | Year ended 31 December | |
|---|---|---|
| | **2008** | 2007 |
| Due from other banks and financial institutions and securities purchased under resale agreements, net | **(25)** | (113) |
| Loans and advances to customers | | |
| — Collectively assessed provision | **5,855** | 2,016 |
| — Individually assessed provision, net | **4,890** | 4,599 |
| | **10,745** | 6,615 |
| Less: recovery of loans previously written off | **(30)** | (122) |
| | **10,690** | 6,380 |

## 5 Income tax expense

*(in millions of RMB)*

| Group | Year ended 31 December | |
|---|---|---|
| | **2008** | 2007 |
| Current tax | | |
| — Mainland China income tax | **8,285** | 9,346 |
| — Hong Kong profits tax | **11** | 282 |
| — Overseas taxation | **(52)** | 15 |
| | **8,244** | 9,643 |
| Deferred tax | **(1,015)** | 1,069 |
| | **7,229** | 10,712 |

The Corporate Income Tax Law of the People's Republic of China came into effect on 1 January 2008. The applicable income tax rate of the Bank and each of its subsidiaries established in Mainland China has been adjusted to 25%.

Profits earned by the Hong Kong branch or subsidiaries in Hong Kong are subject to Hong Kong profits tax at the rate of 16.5% (2007: 17.5%), on the estimated assessable profit for the year ended 31 December 2008. Taxation on other overseas profits has been calculated on the estimated assessable profit at the rates of taxation prevailing in the countries in which the Group operates during the year ended 31 December 2008.

The taxation on the Group's profit before taxation differs from the theoretical amount that would arise using the taxation rate of the home country of the Group at 25% (2007: 33%). The reconciliation is as follows:

*(in millions of RMB)*

| | Year ended 31 December | |
|---|---|---|
| | **2008** | 2007 |
| Profit before tax | **35,719** | 31,114 |
| Tax calculated at a tax rate of 25% (2007: 33%) | **8,930** | 10,268 |
| Effect of different tax rates in other countries | **10** | 24 |
| Tax credit arising from income not subject to tax(1) | **(1,974)** | (1,332) |
| Tax effect of expenses that are not deductible for tax purposes(2) | **264** | 360 |
| Tax rate change impact | **(1)** | 1,392 |
| Income tax expense | **7,229** | 10,712 |

(1) The income not subject to tax of the Group mainly represents interest income arising from treasury bonds, which is income tax free in accordance with the PRC tax regulation.

(2) The expenses that are not tax deductible of the Group mainly represents a portion of expenditure, such as payroll, entertainment expenses etc, which is over the tax deduction limits in accordance with PRC tax regulation.

## 6 Basic and diluted earnings per share

Basic and diluted earnings per share are calculated by dividing the net profit attributable to shareholders of the Bank by the weighted average number of ordinary shares in issue during the year.

*(in millions of RMB unless otherwise stated)*

| | Year ended 31 December | |
|---|---|---|
| | **2008** | 2007 |
| Profit attributable to shareholders of the Bank | **28,393** | 20,274 |
| Weighted average number of ordinary shares in issue | **48,994** | 47,931 |
| Basic and diluted earnings per share (expressed in RMB per share) | **0.58** | 0.42 |

## 7 Derivative financial instruments

The following derivative instruments are utilized by the Group for trading purpose:

Currency forwards represent commitments to purchase/sell foreign exchanges including unsettled spot transactions. Foreign currency and interest rate futures are contractual obligations to receive or pay a net amount based on changes in currency rates or interest rates or to buy or sell foreign currency or a financial instrument on a future date at a specified price, established in an organised financial market. The credit risk is negligible, as futures contracts are collateralised by cash or marketable securities, and changes in the futures contract value are settled daily with the exchange. Forward rate agreements are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contracted rate of interest and the current market rate, based on a notional principal amount.

Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or interest rates (for example, fixed rate for floating rate) or a combination of all these (i.e. cross-currency interest rate swaps). The Group's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligation. This risk is monitored on an ongoing basis with reference to the current fair value, the notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Group assesses counterparties using the same techniques as for its lending activities.

Foreign currency and interest rate 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 a foreign currency or a financial instrument at a predetermined price. The seller receives a premium from the purchaser in consideration for the assumption of foreign exchange or interest rate risk. Options may be either exchange-traded or negotiated between the Group and a customer (OTC).

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the balance sheet but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Group's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates or foreign exchange rates relative to their terms. The aggregate fair values of derivative financial assets and liabilities can fluctuate significantly from time to time. The fair values of derivative instruments held are set out in the following tables.

*(in millions of RMB)*

| **Group and Bank** | **Contract/ notional Amount** | **Fair values Assets** | **Fair values Liabilities** |
|---|---|---|---|
| **As at 31 December 2008** | | | |
| **Foreign exchange contracts** | **167,252** | **1,995** | **(2,780)** |
| **Interest rate contracts** | **119,649** | **2,661** | **(2,895)** |
| **Total derivatives** | | **4,656** | **(5,675)** |

*(in millions of RMB)*

| **Group and Bank** | **Contract/ notional Amount** | **Fair values Assets** | **Fair values Liabilities** |
|---|---|---|---|
| As at 31 December 2007 | | | |
| Foreign exchange contracts | 154,261 | 1,653 | (2,620) |
| Interest rate contracts | 87,565 | 685 | (699) |
| Others derivative contracts | 14 | — | — |
| Total derivatives | | 2,338 | (3,319) |

The tables above provide a detailed breakdown of the contractual or notional amounts and the fair values of the Group's derivative financial instruments outstanding at year end. These instruments, comprising foreign exchange and interest rate derivatives allow the Group and its customers to transfer, modify or reduce their foreign exchange and interest rate risks.

The Group undertakes its transactions in foreign exchange and interest rate contracts with other financial institutions and customers. Management has established limits of these contracts by counterparties, industry sectors and countries. Actual credit exposures and limits are regularly monitored and controlled by management.

***Credit risk weighted amounts***

*(in millions of RMB)*

| **Group and Bank** | **As at 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Derivatives | | |
| — Exchange rate contracts | **938** | 846 |
| — Interest rate contracts | **625** | 287 |
| — Other derivative contracts | **—** | 2 |
| | **1,563** | 1,135 |

The credit risk weighted amounts are the amounts calculated with reference to the guidelines issued by the China Banking Regulatory Commission ("CBRC") and are dependent on, amongst other factors, the creditworthiness of the counterparty and the maturity characteristics of each type of contract.

***Replacement costs***

*(in millions of RMB)*

| **Group and Bank** | **As at 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Derivatives | | |
| — Exchange rate contracts | **1,995** | 1,653 |
| — Interest rate contracts | **2,661** | 685 |
| | **4,656** | 2,338 |

Replacement cost is the cost of replacing all contracts which have a positive value when marked to market (should the counterparty default on its obligations) and is obtained by marking contracts to market.

The credit risk weighted amounts and replacement costs stated above have taken the effects of netting arrangements into account.

*Notional amounts of derivative financial instruments by original currency*

*(in millions of RMB)*

| Group and Bank | RMB | US Dollars | HK Dollars | Others | Total |
|---|---|---|---|---|---|
| **As at 31 December 2008** | | | | | |
| **Notional amount of derivative financial instruments** | **158,670** | **97,090** | **16,039** | **15,102** | **286,901** |
| As at 31 December 2007 | | | | | |
| Notional amount of derivative financial instruments | 110,038 | 98,854 | 22,673 | 10,275 | 241,840 |

## 8 Dividends

*(in millions of RMB)*

| | Year ended 31 December | |
|---|---|---|
| | **2008** | 2007 |
| Paid in the year | **13,407** | 5,311 |

Under PRC Company Law and the Bank's Articles of Association, the net profit after tax as reported in the PRC statutory financial statements can only be distributed as dividends after allowances for the following:

(i) Making up prior year's cumulative losses, if any;

(ii) Allocations to the non-distributable statutory reserve of 10% of the net profit of the Bank as determined under PRC accounting regulations;

(iii) Allocations to statutory general reserve;

(iv) Allocations to the discretionary revenue reserve fund if approved by the Bank's Annual General Meeting. These funds form part of the shareholders' equity.

In accordance with the relevant regulations, the distributable profit is deemed to be the lesser of (i) the distributable profit determined in accordance with PRC GAAP and (ii) the distributable profit determined in accordance with IFRS.

The dividends are recognized in the balance sheet upon approval by the shareholders at the Annual General Meeting. In accordance with the resolution of the Annual General Meeting on 6 June 2008, the Board of Directors was authorized to approve the profit appropriation plan within 40% of the distributable profit in the first half year of 2008. At 26 August 2008, the directors approved a cash dividend of RMB0.10 per share, amounting to RMB4,899 million.

At 31 December 2008, the aggregate amount of distributable profit was RMB23,334 million, being the distributable profit determined in accordance with IFRS (2007: IFRS) after the distribution of interim dividends. On 18 March 2009, the directors proposed a cash dividend of RMB0.10 (2007: RMB0.15) per share, amounting to RMB4,899 million (2007: RMB7,349 million), which is subject to the approval by shareholders at the Annual General Meeting.

## 9 Financial guarantees and credit related commitments, other commitments and contingent liabilities

***Financial guarantees and credit related commitments***

The following tables indicate the contractual amounts of the Group's financial guarantees and credit related commitments which the Group commits to extend to customers:

*(in millions of RMB)*

| **Group and Bank** | **As at 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Guarantees | **154,918** | 157,771 |
| Letters of credit | **25,637** | 34,779 |
| Acceptances | **193,826** | 172,127 |
| Other commitments with an original maturity of | | |
| — Under 1 year | **95,564** | 59,369 |
| — 1 year and over | **6,937** | 11,907 |
| | **476,882** | 435,953 |

***Capital expenditure commitments***

*(in millions of RMB)*

| **Group** | **As at 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Capital expenditure commitments for buildings | **357** | 203 |

*(in millions of RMB)*

| **Bank** | **As at 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Capital expenditure commitments for buildings | **355** | 203 |

***Operating lease commitments***

Where the Group is the lessee, the future minimum lease payments under non-cancelable operating leases in respect of buildings are as follows:

*(in millions of RMB)*

| **Group** | **As at 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Not later than 1 year | **1,014** | 769 |
| Later than 1 year and not later than 5 years | **2,454** | 1,756 |
| Later than 5 years | **972** | 636 |
| | **4,440** | 3,161 |

*(in millions of RMB)*

| **Bank** | **As at 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Not later than 1 year | **998** | 769 |
| Later than 1 year and not later than 5 years | **2,435** | 1,756 |
| Later than 5 years | **972** | 636 |
| | **4,405** | 3,161 |

***Commitments on security underwriting and bond acceptance***

*(in millions of RMB)*

| **Group and Bank** | **As at 31 December** | |
|---|---|---|
| | **2008** | 2007 |
| Outstanding balance on security underwriting | **6,700** | 6,750 |
| Outstanding balance on bond acceptance(Note 1) | **20,345** | 17,842 |

*Note 1:*

The Bank is entrusted by the Ministry of Finance ("MOF") to underwrite certain Certificates of Treasury Bond. The investors of Certificates of Treasury Bond have a right to redeem the bonds at par any time prior to maturity and the Bank is committed to redeem those bonds. The redemption price is the principal value of the Certificates of Treasury Bond plus unpaid interest.

The original maturities of these bonds vary from 1 to 5 years.

The MOF will not provide funding for the early redemption of these Certificates of Treasury Bond on a back-to-back basis but will pay interest through maturity and repay the principal at maturity.

### *Legal proceedings*

A number of legal proceedings are initiated by third parties against the Group as defendant. The total outstanding claims at end of the year are as follows:

*(in millions of RMB)*

| Group and Bank | As at 31 December | |
|---|---|---|
| | **2008** | 2007 |
| Outstanding claims | **1,298** | 1,785 |
| Provision for losses | **336** | 875 |

## 10 Segmental information

The following table sets out the segmental information of the Group's operating results, assets and liabilities. The geographical segments are:

(i) Northern China — Including the following provinces: Beijing, Tianjin, Hebei, Shanxi, Inner Mongolia;

(ii) North Eastern China — Including the following provinces: Liaoning, Jilin, Heilongjiang;

(iii) Eastern China — Including the following provinces: Shanghai (excluding head office), Jiangsu, Zhejiang, Anhui, Fujian, Jiangxi and Shandong;

(iv) Central & Southern China — Including the following provinces: Henan, Hunan, Hubei, Guangdong, Guangxi, Hainan;

(v) Western China — Including the following provinces: Chongqing, Sichuan, Guizhou, Yunnan, Tibet, Shannxi, Gansu, Qinghai, Ningxia and Xinjiang;

(vi) Head office;

(vii) Overseas — Including overseas subsidiaries and the following branches: Hong Kong, New York, Singapore, Seoul, Tokyo, Frankfurt and Macau.

*(in millions of RMB)*

| As at 31 December 2008 | Northern China | North-eastern China | Eastern China | Central & Southern China | Western China | Head Office | Overseas | Eliminations | Group Total |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| Cash and balances with central banks | 9,682 | 4,087 | 30,922 | 10,306 | 4,580 | 302,138 | 465 | — | 362,180 |
| Due from other banks and financial institutions | 75,584 | 859 | 86,742 | 13,548 | 1,803 | 115,439 | 37,536 | — | 331,511 |
| Financial assets held for trading | — | — | — | 7 | — | 22,350 | 4,579 | — | 26,936 |
| Loans and advances to customers | 252,653 | 70,911 | 518,712 | 247,301 | 108,410 | 28,006 | 72,783 | — | 1,298,776 |
| Investment securities | | | | | | | | | |
| — loans and receivables | 7,032 | 3,285 | 13,015 | 10,755 | 2,851 | 53,965 | — | — | 90,903 |
| — available-for-sale | 7,696 | 144 | 2,789 | 2,500 | 15 | 110,828 | 18,038 | — | 142,010 |
| — held-to-maturity | 7,686 | 11,125 | 21,584 | 15,734 | 4,516 | 305,896 | 1,337 | — | 367,878 |
| Other assets | 207,915 | 77,809 | 312,666 | 161,849 | 76,590 | 46,409 | 16,326 | (836,811) | 62,753 |
| **Segment assets** | 568,248 | 168,220 | 986,430 | 462,000 | 198,765 | 985,031 | 151,064 | (836,811) | 2,682,947 |
| **Liabilities** | | | | | | | | | |
| Due to other banks and financial institutions | (198,738) | (12,430) | (232,468) | (59,740) | (18,921) | (16,339) | (30,817) | — | (569,453) |
| Financial liabilities held for trading | — | — | — | — | — | (4,562) | (5,451) | — | (10,013) |
| Due to customers | (353,576) | (152,496) | (712,409) | (384,419) | (174,069) | (1,916) | (86,930) | — | (1,865,815) |
| Debts issued | — | — | — | — | — | (40,000) | — | — | (40,000) |
| Other liabilities | (10,798) | (5,296) | (25,340) | (11,404) | (5,059) | (801,828) | (24,657) | 836,811 | (47,571) |
| **Segment liabilities** | (563,112) | (170,222) | (970,217) | (455,563) | (198,049) | (864,645) | (147,855) | 836,811 | (2,532,852) |
| **Net on balance sheet position** | 5,136 | (2,002) | 16,213 | 6,437 | 716 | 120,386 | 3,209 | — | 150,095 |
| **Off-balance exposures** | | | | | | | | | |
| Financial guarantees, acceptance and letter of credit | 102,361 | 9,791 | 178,439 | 50,823 | 20,086 | 3,172 | 9,709 | — | 374,381 |
| Other credit related commitments | 13,278 | 7,115 | 35,557 | 18,769 | 9,090 | — | 18,692 | — | 102,501 |
| **Acquisition cost of property and equipment ("PPE") and intangible assets** | (1,012) | (373) | (2,331) | (1,176) | (413) | (1,836) | (101) | — | (7,242) |
| **For the year ended 31 December 2008** | | | | | | | | | |
| Interest income | 22,632 | 7,117 | 44,869 | 22,455 | 9,028 | 28,676 | 5,231 | (22,902) | 117,106 |
| Interest expense | (13,193) | (3,688) | (19,641) | (9,633) | (3,744) | (20,882) | (3,365) | 22,902 | (51,244) |
| **Net interest income** | 9,439 | 3,429 | 25,228 | 12,822 | 5,284 | 7,794 | 1,866 | — | 65,862 |
| Fee and commission income | 1,423 | 337 | 3,014 | 1,363 | 392 | 2,831 | 761 | — | 10,121 |
| Fee and commission expense | (227) | (49) | (499) | (182) | (51) | (96) | (180) | — | (1,284) |
| **Net fee and commission income** | 1,196 | 288 | 2,515 | 1,181 | 341 | 2,735 | 581 | — | 8,837 |
| Dividend income | — | — | 55 | — | 1 | 15 | 12 | — | 83 |
| Gains less losses arising from trading activities | 465 | 112 | 757 | 302 | 77 | (36) | (120) | — | 1,557 |
| Gains less losses arising from investment securities | 28 | 11 | 250 | (52) | 3 | 272 | (286) | — | 226 |
| Other operating income | 14 | 30 | 448 | 62 | 46 | 9 | 102 | — | 711 |
| Reversal/(Impairment losses) on loans and advances | (1,976) | (603) | (4,731) | (1,993) | (1,121) | (23) | (243) | — | (10,690) |
| Other operating expenses | (4,063) | (2,036) | (10,015) | (4,837) | (2,289) | (5,655) | (1,972) | — | (30,867) |
| **Operating profit/(loss) before tax** | 5,103 | 1,231 | 14,507 | 7,485 | 2,342 | 5,111 | (60) | — | 35,719 |
| Income tax | (1,206) | (269) | (3,497) | (1,755) | (548) | (64) | 110 | — | (7,229) |
| **Net profit/(loss) for the year** | 3,897 | 962 | 11,010 | 5,730 | 1,794 | 5,047 | 50 | — | 28,490 |
| **Depreciation and amortization of property and equipment and intangible assets** | (340) | (277) | (980) | (482) | (269) | (751) | (141) | — | (3,240) |

*(in millions of RMB)*

| As at 31 December 2007 | Northern China | North-eastern China | Eastern China | Central & Southern China | Western China | Head Office | Overseas | Eliminations | Group Total |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| Cash and balances with central banks | 11,614 | 3,478 | 21,071 | 8,746 | 4,278 | 211,497 | 749 | — | 261,433 |
| Due from other banks and financial institutions | 19,245 | 1,044 | 41,186 | 5,470 | 2,383 | 65,685 | 25,365 | (4,268) | 156,110 |
| Financial assets held for trading | 128 | 7 | 48 | 23 | 15 | 16,126 | 2,993 | — | 19,340 |
| Loans and advances to customers | 206,479 | 61,380 | 432,436 | 218,590 | 91,232 | 9,091 | 61,188 | 2,392 | 1,082,788 |
| Investment securities | | | | | | | | | |
| — loans and receivables | 6,375 | 3,581 | 13,422 | 10,646 | 2,868 | 29,801 | — | — | 66,693 |
| — available-for-sale | 17,587 | 181 | 48 | 3,206 | 24 | 101,969 | 23,439 | — | 146,454 |
| — held-to-maturity | 10,853 | 13,516 | 29,700 | 22,776 | 8,244 | 239,584 | 2,280 | — | 326,953 |
| Other assets | 33,367 | 8,690 | 40,587 | 27,046 | 9,062 | 15,499 | 14,465 | (98,043) | 50,673 |
| **Segment assets** | 305,648 | 91,877 | 578,498 | 296,503 | 118,106 | 689,252 | 130,479 | (99,919) | 2,110,444 |
| **Liabilities** | | | | | | | | | |
| Due to other banks and financial institutions | (96,262) | (5,408) | (144,743) | (49,396) | (9,259) | (5,155) | (22,333) | — | (332,556) |
| Financial liabilities held for trading | (11) | (2) | (10) | (8) | (6) | (3,002) | (6,989) | — | (10,028) |
| Due to customers | (270,655) | (132,207) | (605,658) | (324,907) | (150,311) | (636) | (71,185) | (40) | (1,555,599) |
| Other liabilities | (6,578) | (2,636) | (97,976) | (6,770) | (3,032) | (35,937) | (25,970) | 99,959 | (78,940) |
| **Segment liabilities** | (373,506) | (140,253) | (848,387) | (381,081) | (162,608) | (44,730) | (126,477) | 99,919 | (1,977,123) |
| **Net on balance sheet position** | (67,858) | (48,376) | (269,889) | (84,578) | (44,502) | 644,522 | 4,002 | — | 133,321 |
| **Off-balance exposures** | | | | | | | | | |
| Financial guarantees, acceptance and letter of credit | 97,774 | 10,222 | 163,335 | 59,544 | 19,382 | 3,199 | 11,221 | — | 364,677 |
| Other credit related commitments | 6,549 | 3,726 | 19,162 | 10,715 | 4,930 | — | 26,194 | — | 71,276 |
| **Acquisition cost of property and equipment (“PPE”) and intangible assets** | (2,449) | (470) | (1,953) | (891) | (285) | (1,176) | (192) | — | (7,416) |
| **For the year ended 31 December 2007** | | | | | | | | | |
| Interest income | 15,595 | 5,608 | 33,576 | 17,223 | 7,012 | 17,464 | 7,329 | (13,488) | 90,319 |
| Interest expense | (7,159) | (2,478) | (13,135) | (6,482) | (2,530) | (12,639) | (5,404) | 13,451 | (36,376) |
| **Net interest income** | 8,436 | 3,130 | 20,441 | 10,741 | 4,482 | 4,825 | 1,925 | (37) | 53,943 |
| Fee and commission income | 623 | 275 | 2,063 | 788 | 307 | 3,144 | 1,045 | — | 8,245 |
| Fee and commission expense | (166) | (51) | (410) | (127) | (56) | (67) | (273) | — | (1,150) |
| **Net fee and commission income** | 457 | 224 | 1,653 | 661 | 251 | 3,077 | 772 | — | 7,095 |
| Dividend income | — | 6 | 61 | — | — | 5 | 5 | — | 77 |
| Gains less losses arising from trading activities | 385 | 98 | 645 | 253 | 65 | (1,208) | 12 | — | 250 |
| Gains less losses arising from investment securities | 85 | — | 232 | 54 | 1 | (2) | 287 | — | 657 |
| Other operating income | 29 | 15 | 236 | 384 | 27 | 80 | (27) | 23 | 767 |
| Reversal/(Impairment losses) on loans and advances | (1,320) | 91 | (3,336) | (1,413) | (284) | (75) | (43) | — | (6,380) |
| Other operating expenses | (3,249) | (2,379) | (8,131) | (4,395) | (2,284) | (3,245) | (1,612) | — | (25,295) |
| **Operating profit/(loss) before tax** | 4,823 | 1,185 | 11,801 | 6,285 | 2,258 | 3,457 | 1,319 | (14) | 31,114 |
| Income tax | (1,873) | (356) | (4,657) | (1,972) | (882) | (613) | (359) | — | (10,712) |
| **Net profit/(loss) for the year** | 2,950 | 829 | 7,144 | 4,313 | 1,376 | 2,844 | 960 | (14) | 20,402 |
| **Depreciation and amortization of property and equipment and intangible assets** | (297) | (280) | (865) | (430) | (254) | (640) | (132) | — | (2,898) |

# 7. PUBLICATION OF ANNUAL RESULTS ANNOUNCEMENT

This results announcement is extracted from the 2008 annual report prepared in accordance with IFRS. The full text of such report is available for shareholders on both the website of the Hong Kong Stock Exchange at www.hkexnews.hk and the website of the Bank at www.bankcomm.com. The full text of the 2008 annual results prepared in accordance with CAS is also available on the website of the Shanghai Stock Exchange at www.sse.com.cn and the website of the Bank at www.bankcomm.com. Investors who wish to understand the annual results in details should also read the full annual report. The Bank's annual report prepared in accordance with IFRS will be despatched to its H shareholders as soon as practicable.

By Order of the Board
**Bank of Communications Co., Ltd.**
**Hu Huaibang**
*Chairman of the Board*

Shenzhen, the PRC, 18 March 2009

*As at the date of this announcement, the directors of the Bank are Mr. Hu Huaibang, Mr. Li Jun, Mr. Peng Chun, Mr. Qian Wenhui, Mr. Zhang Jixiang*, Mr. Hu Huating*, Mr. Qian Hongyi*, Mr. Wong Tung Shun, Peter*, Ms. Laura M. Cha*, Mr. Ji Guoqiang*, Mr. Lei Jun*, Mr. Yang Fenglin*, Mr. Xie Qingjian#, Mr. Ian Ramsay Wilson#, Mr. Thomas Joseph Manning#, Mr. Chen Qingtai#, Dr. Li Ka-Cheung, Eric# and Mr. Gu Mingchao#.*

* *Non-Executive Directors*
\# *Independent Non-Executive Directors*