

REPORT OF THE BOARD OF DIRECTORS

The board of directors of China Construction Bank Corporation is pleased to present its report together with the audited financial statements of the Bank and its subsidiaries (collectively “the Group”) prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2005 as set forth in the “Financial Statements”.

PRINCIPAL ACTIVITIES

The Group is engaged in the provision of a range of banking products and services and related financial services.

PROFITS AND DIVIDENDS

The profit of the Group for the year ended 31 December 2005 and the state of the Bank’s and the Group’s affairs as at that date are set out in the “Financial Statements” on pages 102 to 204.

During the year 2005, the Board declared a cash dividend to our promoters as at 30 June 2005 in an aggregate amount of RMB 168 million and a special dividend in an aggregate amount of RMB 3,100 million to our shareholders as at 26 October 2005, which were approved by an extraordinary meeting of shareholders on 27 August 2005.

The Board now recommend the payment of a final dividend in the amount of RMB 0.015 per share, totalling approximately RMB 3,370 million in respect of the financial year ended 31 December 2005, subject to the approval of shareholders at the forthcoming annual general meeting. If approved, the final dividend will be paid to shareholders whose names appear on the register of members of the Bank as of Monday, 22 May 2006.

RESERVES

Please refer to the consolidated statement of changes in equity for details of the movements in the reserves of the Group. Other details of the reserves are set out in notes 27 and 28 to the “Financial Statements”.

SUMMARY OF FINANCIAL INFORMATION

Please refer to the “Four-Year Financial Summary” for the summary of the operating results, assets and liabilities of the Group for the four years ended 31 December 2005.

DONATIONS

Donations made by the Group during the year for charitable and community purposes amounted to RMB 6 million.

PROPERTY AND EQUIPMENT

Please refer to note 19 of the “Financial Statements” for details of movements in the property and equipment of the Group for the year ended 31 December 2005.

ULTIMATE PARENT AND ITS SUBSIDIARIES

Please refer to notes 38 and 18(f) to the “Financial Statements” for details of the Bank’s ultimate parent and its subsidiaries respectively as at 31 December 2005.

REPORT OF THE BOARD OF DIRECTORS

SHARE CAPITAL AND PUBLIC FLOAT

Please refer to note 27(a) to the “Financial Statements” for details of the movements in share capital of the Bank during the financial year.

Shares were issued during the year on the Bank’s global IPO and all of the Bank’s shares were listed on the Hong Kong Stock Exchange.

Based on publicly available information at the latest practicable date prior to the publication of this report, the public float of the Bank was 25.75%. Accordingly, the Board believes that the Bank has sufficient public float.

PURCHASE, SALE AND REDEMPTION OF SHARES

There was no purchase, sale or redemption by the Bank or any of its subsidiaries of the listed securities of the Bank during the reporting period.

RETIREMENT BENEFITS

Please refer to note 25 of the “Financial Statements” for details of the retirement benefits provided to employees of the Group.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights in the Articles of Association requiring the Bank to offer new shares to existing shareholders in proportion to their shareholdings. The Articles of Association provides that if the Bank wishes to increase its capital, it may issue new shares to non-specified investors, may issue shares to existing shareholders or issue shares by way of distribution to existing shareholders, may transfer capital from its capital accumulation fund to issue new shares, or through other means permitted by law or regulation. There are no compulsory provisions for shareholders to exercise their pre-emptive rights.

MAJOR CUSTOMERS

For the year ended 31 December 2005, the total of interest income and other operating income from the five largest customers of the Group represented an amount not exceeding 30% of the total of interest income and other operating income of the Group.

USE OF PROCEEDS FROM THE IPO

In 2005, the Bank completed its IPO and issued 30,458,834,000 H shares at an issue price of HK\$2.35 per share, raising HK\$71,578 million. The proceeds have been used in accordance with the purposes disclosed in the prospectus of the Bank dated 14 October 2005 for strengthening the Bank’s capital base to support the ongoing growth of our businesses.

REPORT OF THE BOARD OF DIRECTORS

DIRECTORS AND SUPERVISORS

During the financial year, our directors were as follows:

Name	Position	Date of appointment
Guo Shuqing	Chairman and executive director	25 March 2005
Chang Zhenming	Vice chairman, executive director and president	15 September 2004
Liu Shulan ¹	Executive director and vice president	15 September 2004
Zhao Lin	Executive director and vice president	15 September 2004
Zhu Zhenmin	Non-executive director	15 September 2004
Jing Xuecheng	Non-executive director	15 September 2004
Wang Shumin	Non-executive director	15 September 2004
Wang Yonggang	Non-executive director	15 September 2004
Liu Xianghui	Non-executive director	29 November 2004
Zhang Xiangdong	Non-executive director	29 November 2004
Gregory L. Curl	Non-executive director	27 August 2005
Song Fengming	Independent non-executive director	15 September 2004
Yashiro Masamoto	Independent non-executive director	15 September 2004
Tse Hau Yin, Aloysius	Independent non-executive director	29 November 2004
Elaine La Roche	Independent non-executive director	6 June 2005

1. Ms. Liu Shulan resigned from the post of executive director effective on 6 April 2006 because she has reached retirement age.

On 16 March 2005, the first extraordinary meeting of shareholders for 2005 and fourth meeting of the first session of our Board passed resolutions accepting the resignation of Mr. Zhang Enzhao as chairman and director of the Bank.

During the financial year, our supervisors were as follows:

Name	Position	Date of appointment
Xie Duyang	Chairman of the board of supervisors	15 September 2004
Liu Jin	Supervisor	15 September 2004
Jin Panshi	Supervisor	15 September 2004
Chen Yueming	Supervisor	15 September 2004
Cheng Meifen	Supervisor	15 December 2004
Cui Jianmin	External supervisor	25 March 2005
Guo Feng	External supervisor	25 March 2005

The biographical details of the directors and supervisors of the Bank are set out in the "Profiles of Directors, Supervisors and Senior Management".

Each of our directors (including non-executive directors) has a service term of three years (commencing from the date of their appointment by election and ending on the date of the annual general meeting of the final year of the term of his/her office), and may be re-elected upon expiry of their term.

REPORT OF THE BOARD OF DIRECTORS

MATERIAL INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES OF THE BANK

As at 31 December 2005, the interests and short positions of substantial shareholders and other persons of the Bank in the shares and underlying shares of the Bank as recorded in the register required to be kept under section 336 of the Securities and Futures Ordinance (“SFO”) were as follows:

Name	Number of H shares held		Total holding issued shares	% of total
	Held directly	Held indirectly		
(i) Huijin ¹	138,150,047,904	20,692,250,000	158,842,297,904	70.69%
(ii) Jianyin ¹	20,692,250,000	—	20,692,250,000	9.21%
(iii) Bank of America ²	19,132,974,346	—	19,132,974,346	8.52%
(iv) Temasek ³	—	13,576,203,750	13,576,203,750	6.04%
(v) AFH ⁴	13,207,316,750	—	13,207,316,750	5.88%

1. As Huijin directly controls one-third or more of the voting rights in the shareholders’ meetings of Jianyin, in accordance with the SFO, the interests directly held by Jianyin are deemed to be indirect interests of Huijin.
2. Bank of America holds an option to acquire our shares representing a total of 19.90% of our issued share capital (excluding any shares already held by Bank of America as at that date), which is in the form of a physically settled unlisted derivative.
3. Temasek’s interests in us are held through its indirect interests in the following entities, the respective direct shareholdings of which are set out below:

Entity	Number of H shares held
AFH	13,207,316,750
Aranda Investments Pte Ltd	360,700,000
CESMA International Private Limited	62,000
Fullerton (Private) Limited	862,000
PSA Corporation Pte Ltd	291,000
PSA International Pte Ltd	583,000
Singapore Technologies Marine Ltd	606,000
The Rohatyn Group Asia Opportunity Fund, Ltd	3,887,000
Vision Tech Investment Pte Ltd	1,896,000

4. As AFH is a wholly-owned subsidiary of Temasek, in accordance with the SFO, the interests directly held by AFH are deemed to be indirect interests of Temasek.

Save as disclosed above, as at 31 December 2005, in the register required to be kept under Section 336 of the SFO, no other persons were recorded as holding any interests or short positions in the shares or underlying shares of the Bank that would fall to be disclosed by the Bank under Division 2 and 3 of Part XV of the SFO.

An analysis of the Bank’s shareholdings as at 31 December 2005 is set out in the “Corporate Governance Report”.

DIRECTORS’ FINANCIAL, BUSINESS AND FAMILY RELATIONSHIPS

There are no relationships among the directors of the Bank, including financial, business, family or other material relationships.

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DIRECTORS' AND SUPERVISORS' INTERESTS IN CONTRACTS AND SERVICE CONTRACTS

For the year ended 31 December 2005, no director or supervisor of the Group had any material interest, whether directly or indirectly, in any contract of significance entered into by the Bank, any of its holding companies or subsidiaries or subsidiaries of the Bank's holding companies, apart from service contracts.

None of the directors and supervisors has entered into a service contract with the Bank which is not terminable by the Bank within one year without payment of compensation (other than statutory compensation).

DIRECTORS' AND SUPERVISORS' INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at 31 December 2005, none of the directors and supervisors of the Group had any interests or short positions in the shares, underlying shares of equity derivatives or debentures of the Bank or its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Bank and the Stock Exchange of Hong Kong Limited pursuant to Appendix 10 of *Model Code for Securities Transactions by Directors of Listed Issuers* of the Listing Rules.

As at 31 December 2005, the Group has not granted its directors or supervisors, or their respective spouses or children below the age of 18 any rights to subscribe for the shares or debentures of the Bank or any of its associated corporations and none of them has ever exercised any such right to subscribe for shares or debentures.

DIRECTORS' INTERESTS IN COMPETING BUSINESSES

None of the directors of the Bank directly or indirectly has any interest which constitutes or may constitute a competing business of the Bank.

CONTRACT OF SIGNIFICANCE

The Bank has entered into an agreement with Huijin, its controlling shareholder, on 12 January 2005 pursuant to which the Bank purchased from Huijin an option to sell to Huijin a maximum of US\$22.5 billion in U.S. dollars for RMB at a fixed exchange rate of US\$1 to RMB 8.2769. This option can be exercised in 2007 in twelve equal monthly instalments. The Bank will pay Huijin a total of approximately RMB 5,587 million in twelve equal monthly instalments as consideration for this option in 2007.

MATERIAL LEGAL PROCEEDINGS

As at 31 December 2005, as far as the Board is aware, the Bank was not involved in any material litigation or arbitration and no material litigation claims were pending or threatened or made against the Bank.

CONNECTED TRANSACTIONS

Transactions between us and Jianyin and its subsidiaries and other connected persons constitute connected transactions for us under Chapter 14A of the Listing Rules. Details of these transactions are set out below.

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Exempt continuing connected transactions

Continuing connected transactions between us and Jiayin

Pursuant to the restructuring, the assets and liabilities of the former China Construction Bank were divided between us and Jiayin. Following the separation, we entered into various agreements on a continuing basis with Jiayin to regulate the continuing business relationships between us. These continuing connected transactions with Jiayin are divided into the following categories:

- *Asset management services provided by us to Jiayin.* We provide Jiayin with various asset management services pursuant to the asset management services agreements entered into between us and Jiayin, relating to the management of properties, motor vehicles and equipment, entrusted loans, corporate bonds and the assets and liabilities of the former China Agricultural Development and Trust Investment Corporation.
- *Comprehensive services provided by Jiayin to us.* Jiayin provides us with various ancillary services pursuant to the comprehensive services agreements entered into between us and Jiayin. These agreements relate to, among others, the provision of catering services, security guard and cash-in-transit services, conference services, gardening services, office cleaning services and maintenance services for our equipment and facilities. The above services are in the nature of support services for our branch network and, as such, are not directly related to our core business operations.
- *Leasing of motor vehicles and equipment by Jiayin to us.* Jiayin leases to us certain motor vehicles and equipment pursuant to the leasing agreements entered into between us and Jiayin.
- *Consultancy services provided by Jiayin to us.* Pursuant to a consultancy services framework agreement effective as at 9 March 2005 and entered into between us and China Investment Consultancy Company, a subsidiary of Jiayin, China Investment Consultancy Company provides us with consultancy services in respect of our infrastructure lending business.
- *Leasing of properties by Jiayin to us.* We lease properties from Jiayin for our business operations.
- *Property management services provided by Jiayin to us.* Jiayin provides us with property management services for various properties occupied by us for our business operations.

For each category of transaction we have entered into with Jiayin, the respective amounts have not resulted in the percentage ratios set out in Chapter 14 of the Listing Rules (other than the profit ratio, which does not apply) exceeding 0.1%. Accordingly, these connected transactions are exempt continuing connected transactions under Rule 14A.33(3) of the Listing Rules, and thus are exempt from the reporting, announcement and independent shareholders' approval requirements of the Listing Rules.

Continuing connected transactions between us and State Grid

State Grid Corporation of China ("State Grid"), one of our promoters, and its subsidiaries, provide electricity supplies to our business operations in certain locations in Mainland China, and we pay tariffs to them in accordance with rates prescribed by the PRC government.

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The acquisition as a consumer in the ordinary and usual course of business of electricity supplies, being consumer goods or consumer services, by us from State Grid and its subsidiaries on normal commercial terms is exempt continuing connected transactions under Rule 14A.33(1) of the Listing Rules, and thus is exempt from the reporting, announcement and independent shareholders' approval requirements of the Listing Rules.

Other exempt continuing connected transactions

Commercial banking services and products provided by us in the ordinary and usual course of business

We provide commercial banking services and products to our customers in the ordinary and usual course of our business. Such services and products include taking deposits (including time, demand and call deposits) and the provision of long-term loans, short-term loans, consumer loans and mortgages by our Bank. Customers who place deposits with us include our substantial shareholders, directors, supervisors and chief executive officers and those of our subsidiaries, each ex-director of us and our subsidiaries who was a director within 12 months preceding the date of listing of our H shares, and our promoters, namely, Jianyin, State Grid, Shanghai Baosteel and Yangtze Power and their respective associates, each of whom is a connected person of us under Chapter 14A of the Hong Kong Listing Rules.

The provision of commercial banking services and products by us to our connected persons in the ordinary and usual course of our business and on normal commercial terms that are comparable or no more favourable than those offered to independent third parties is exempt continuing connected transactions under Rule 14A.65(4) of the Listing Rules, and thus is exempt from the reporting, announcement and independent shareholders' approval requirements of the Listing Rules.

Loans and credit facilities granted by us to connected persons

We extend loans and credit facilities (including provision of guarantees, security for third party loans, comfort letters and discounted bills) to our customers in the ordinary and usual course of our business on normal commercial terms with reference to prevailing market rates. Customers who utilise our Bank's loans and credit facilities include our substantial shareholders, directors, supervisors and chief executive officers and those of our subsidiaries, each ex-director of us and our subsidiaries who was a director within 12 months preceding the date of listing of our H shares, and our promoters, namely, Jianyin, State Grid, Shanghai Baosteel and Yangtze Power, and their respective associates, each of whom is a connected person of us under Chapter 14A of the Listing Rules.

The provision of loans and credit facilities by us to our connected persons in the ordinary and usual course of our business and on normal commercial terms that are comparable or no more favourable than those offered to independent third parties are exempt continuing connected transactions under Rule 14A.65(1) of the Listing Rules, and thus are exempt from all reporting, announcement and independent shareholders' approval requirements of the Listing Rules.

Service contracts between us and our directors and supervisors

We entered into a service contract with each of our directors and supervisors for a term of three years (commencing from the date of their election and ending on the date of the annual general meeting of the final year of the term of their office). Each service contract contains indemnification provisions covering losses in connection with the services of the relevant director or supervisor, except for any losses arising from

REPORT OF THE BOARD OF DIRECTORS

his or her gross negligence, wilful misconduct or dishonesty. These contracts are exempt connected transactions under Rule 14A.31(6) of the Listing Rules, and thus are exempt from the reporting, announcement and independent shareholders' approval requirements of the Listing Rules.

CORPORATE GOVERNANCE

We are committed to maintaining the highest standard of corporate governance practices. Information on the corporate governance practices adopted by the Bank and our compliance with the Model Code is set out in the "Corporate Governance Report".

REMUNERATION POLICY FOR THE DIRECTORS, SUPERVISORS AND SENIOR MANAGEMENT

We have established, and continually seek to improve a fair and transparent performance evaluation system and incentive mechanism for our directors, supervisors and senior management.

We have a remuneration package comprising salary, annual bonus and long-term incentive scheme for the chairman and vice-chairman of our Board, chairman of the board of supervisors, other executive directors and employee supervisors representing shareholders. Non-executive directors, non-employee supervisors representing shareholders, external supervisors and supervisors representing employees are remunerated by way of a stipend. The Bank participates in the relevant PRC mandatory retirement schemes for its directors, supervisors and senior management.

We have established interim provisions for the remuneration of directors, supervisors and senior management. Details of the remuneration of our directors, supervisors and senior management are set out in notes 10 and 36(c) of the "Financial Statements".

The Bank's long term incentive scheme (including a management share appreciation rights scheme and employee shares policy) was approved by its shareholders in 2005 which will be implemented subject to obtaining the necessary approvals.

COMPLIANCE WITH HKMA SUPERVISORY POLICY MANUAL ON FINANCIAL DISCLOSURE BY LOCALLY INCORPORATED AUTHORISED INSTITUTIONS

In preparing the financial statements for 2005, the Bank has fully complied with the guidelines set out in the *Supervisory Policy Manual on Financial Disclosure by Locally Incorporated Authorised Institutions* ("Guidelines") issued by the HKMA except for the following:

- The Guidelines require separate disclosure of the movements in the allowances for loan impairment losses for individually assessed loans and for collectively assessed loans. We did not break down the movements in the allowances for loan impairment losses into allowances for individually assessed loans and collectively assessed loans, however, we disclosed the movements on an aggregate basis in the notes to our financial statements.
- The Guidelines require separate disclosure of the amount of new allowances charged to the income statement and the amount of allowances released back to the income statement in the movement of allowances for loan impairment losses. We did not segregate the amount of new allowances from the amount of allowances released back, and, in lieu of that, we disclosed these two amounts on a net basis in the notes to our financial statements.

The Bank expects to be able to make such disclosures by 31 December 2006.

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AUDITORS

KPMG were appointed as the international auditors of the Bank for the year ended 31 December 2005. A resolution for the reappointment of KPMG as the auditors of the Bank for the year ended 31 December 2006 will be proposed at the forthcoming annual general meeting of the Bank.

By order of the Board of Directors



Chairman

6 April 2006

REPORT OF THE BOARD OF SUPERVISORS

In 2005, pursuant to the relevant provisions of the *Company Law of the People's Republic of China* and the Articles of Association, the Board of supervisors performed its duties faithfully and conducted supervision and checks earnestly in order to safeguard the interests of shareholders and the Bank.

In 2005, five meetings of board of supervisors were held and fourteen proposals were reviewed, seven of which were submitted to the shareholders' general meeting for consideration. Two new external supervisors were elected. Two new committees, namely performance and due diligence supervision committee and financial and internal control supervision committee, were established under the board of supervisors. Relevant rules and regulations of the board of supervisors and their rules of procedure were formulated, amended, and refined. The board of supervisors considered the final accounts of the Bank and its profit distribution plan. The supervisors attended shareholders' general meetings and meetings of the board of directors as observers. Some supervisors attended the relevant meetings of the special committees of the board of directors and the meetings of the senior management as observers.

In 2005, the board of supervisors performed its duties under the Articles of Association by focusing on the performance and due diligence of the board of directors and senior management and their members, as well as financial and internal control, and conducted a series of supervision and inspection. By attending meetings as observers, and conducting work related interviews, supervisory assessment, research and investigation, and documents review, the board of supervisors carried out supervision on the performance and due diligence of the board of directors, senior management, directors and senior executives. Regarding financial and internal control supervision, selective off-site supervision was conducted. Regarding the classification of the risks associated with credit assets, risk management and internal control, specific investigations and researches were carried out on selective key issues. With attention on related transactions of the Bank, the supervisors communicated with the related party transactions committee of the board of directors and various relevant departments.

The board of supervisors addressed the issues found in the course of supervision and investigations, gave opinions and suggestions promptly; and also consulted with and advised the board of directors and the senior management on important matters, thus improving and pushing forward relevant works.

With the introduction of strategic investors, and successful listing in Hong Kong, the Bank's businesses developed in a healthy manner, operating efficiency grew steadily, and financial position improved further with non-performing assets maintained at a lower level. The board of directors performed their duties pursuant to relevant laws, implemented resolutions adopted by the shareholders' general meeting, and exercised their power in deciding on the improvements to the Articles of Association, formulating development strategies, formulating financial budget and profit distribution plan, and promoting the reform of the management system and various departments. The senior management carried out operating activities pursuant to relevant laws, organised the implementation of board of directors' resolutions, confirmed and put into practice the customer-focused culture, strengthened operation and management, and promoted business development and growth of efficiency. The current directors and senior executives were diligent in carrying out bank-wide reform and development, and enquiries revealed that they did not contravene any laws, regulations or the Articles of Association, neither did they commit any acts detrimental to the interests of shareholders and the Bank during the reporting period.

KPMG conducted an audit of the financial statements of the Bank for the year 2005 in accordance with the *Hong Kong Standards on Auditing*, and issued a standard and unqualified audit report, stating that the financial statements gave a true and fair view of the financial position, operating results, and cash flow.

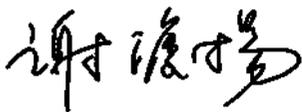
In 2005, the board of supervisors are not aware of any related transactions conducted by the Bank against fair and reasonable principle. The Bank did not carry out any material acquisition or asset sale.

REPORT OF THE BOARD OF SUPERVISORS

Looking forward to the coming year, the board of directors, the board of supervisors, and the senior management will work together to further improve the Bank's corporate governance and rationalise the communication channels and operating mechanism. The board of directors should further enhance the quality of its decision-making, playing a bigger role in guiding the Bank to grow steadily and healthily. The senior management should strengthen macroeconomic policies analysis and industry research, increase the momentum for products and services innovation, further reengineer business operations continuously, improve grassroots level management, enhance internal control, improve asset quality steadily, and enhance the capabilities of the Bank to compete in the market and withstand risks.

The board of supervisors will continue to perform its duties earnestly, properly supervise the board of directors, the senior management and their members to perform their duties, and enhance the financial and internal control of the Bank, so as to contribute to the steady development of the Bank in compliance with the relevant laws and regulations.

By order of the Board of Supervisors



Chairman of the Board of Supervisors

6 April 2006

AUDITORS' REPORT



To the shareholders of China Construction Bank Corporation

(established in the People's Republic of China with limited liability)

We have audited the financial statements of China Construction Bank Corporation (the "Bank") and its subsidiaries (collectively the "Group") on pages 102 to 204 which have been prepared in accordance with International Financial Reporting Standards promulgated by the International Accounting Standards Board.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Bank's directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view it is fundamental that appropriate accounting policies are selected and applied consistently, that judgements and estimates are made which are prudent and reasonable and that the reasons for any significant departure from applicable accounting standards are stated.

It is our responsibility to form an independent opinion, based on our audit, on those financial statements and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

BASIS OF OPINION

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the circumstances of the Bank and of the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

OPINION

In our opinion, the financial statements give a true and fair view of the state of affairs of the Bank and of the Group as at 31 December 2005 and of the profit and cash flows of the Group for the year then ended and have been properly prepared in accordance with International Financial Reporting Standards promulgated by the International Accounting Standards Board and the disclosure requirements of the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

Hong Kong, 6 April 2006

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2005 (Expressed in millions of Renminbi unless otherwise stated)

	Note	2005	2004
Interest income		173,601	147,196
Interest expense		(57,050)	(45,708)
Net interest income	3	<u>116,551</u>	<u>101,488</u>
Fee and commission income	4	9,261	7,352
Fee and commission expense		(806)	(881)
Net fee and commission income		<u>8,455</u>	<u>6,471</u>
Dividend income	5	546	777
Net gain arising from dealing securities	6	455	306
Net gain arising from investment securities	7	1,927	2,701
Net (loss)/gain arising from foreign currency dealing		(1,306)	509
Other income		2,086	1,724
Operating income		<u>128,714</u>	<u>113,976</u>
General and administrative expenses	8	(58,092)	(53,419)
Provisions for impairment losses on			
— loans and advances to customers	17(b)	(13,706)	(6,109)
— others	9	(1,552)	(3,249)
Operating expenses		<u>(73,350)</u>	<u>(62,777)</u>
Profit before tax		55,364	51,199
Income tax	13(a)	(8,268)	(2,159)
Net profit		<u>47,096</u>	<u>49,040</u>
Attributable to:			
Shareholders of the Bank		47,103	49,042
Minority interests		(7)	(2)
Net profit		<u>47,096</u>	<u>49,040</u>
Cash dividends payable to shareholders of the Bank			
Interim dividend declared during the year	28(a)	168	—
Final dividend declared during the year		—	2,914
Special dividend declared during the year	28(a)	3,100	—
Final dividend proposed after the balance sheet date	28(a)	3,370	—
		<u>6,638</u>	<u>2,914</u>
Basic and diluted earnings per share (in RMB)	14	<u>0.24</u>	<u>0.26</u>

The notes on pages 108 to 204 form part of these financial statements.

CONSOLIDATED BALANCE SHEET

As at 31 December 2005 (Expressed in millions of Renminbi)

	Note	2005	2004
Assets			
Cash and balances with central banks	15	480,136	399,366
Amounts due from banks and non-bank financial institutions	16	190,108	112,531
Loans and advances to customers	17	2,395,313	2,173,562
Investments	18	1,413,871	1,107,636
Property and equipment	19	49,961	48,444
Deferred tax assets	20	420	—
Other assets	21	55,933	68,381
Total assets		4,585,742	3,909,920
Liabilities			
Amounts due to central banks		21	2,247
Amounts due to banks and non-bank financial institutions	22	164,524	112,039
Deposits from customers	23	4,006,046	3,491,121
Certificates of deposit issued		5,429	3,741
Current tax liabilities		5,648	1,750
Deferred tax liabilities	20	—	388
Other liabilities and provisions	24	76,490	63,187
Subordinated bonds issued	26	39,907	39,896
Total liabilities		4,298,065	3,714,369
Equity			
Share capital	27	224,689	194,230
Reserves	27	62,890	1,286
Total equity attributable to shareholders of the Bank		287,579	195,516
Minority interests		98	35
Total equity		287,677	195,551
Total equity and liabilities		4,585,742	3,909,920

Approved and authorised for issue by the board of directors on 6 April 2006.

Chang Zhenming
Vice chairman and
executive director

Jing Xuecheng
Director

Wang Shumin
Director

The notes on pages 108 to 204 form part of these financial statements.

BALANCE SHEET OF THE BANK

As at 31 December 2005 (Expressed in millions of Renminbi)

	Note	2005	2004
Assets			
Cash and balances with central banks		480,136	399,366
Amounts due from banks and non-bank financial institutions		190,018	112,531
Loans and advances to customers		2,393,226	2,171,781
Investments		1,412,114	1,105,673
Investments in subsidiaries	18(f)	640	531
Property and equipment		49,884	48,377
Deferred tax assets		420	—
Amounts due from subsidiaries		1,943	1,752
Other assets		55,773	68,049
Total assets		4,584,154	3,908,060
Liabilities			
Amounts due to central banks		21	2,247
Amounts due to banks and non-bank financial institutions		164,308	112,015
Amounts due to subsidiaries		891	209
Deposits from customers		4,004,228	3,489,376
Certificates of deposit issued		5,429	3,741
Current tax liabilities		5,616	1,741
Deferred tax liabilities		—	377
Other liabilities and provisions		76,370	62,948
Subordinated bonds issued		39,907	39,896
Total liabilities		4,296,770	3,712,550
Equity			
Share capital		224,689	194,230
Reserves		62,695	1,280
Total equity		287,384	195,510
Total equity and liabilities		4,584,154	3,908,060

Approved and authorised for issue by the board of directors on 6 April 2006.

Chang Zhenming
 Vice chairman and
 executive director

Jing Xuecheng
 Director

Wang Shumin
 Director

The notes on pages 108 to 204 form part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2005 (Expressed in millions of Renminbi)

Note	Share capital	Capital reserve	Statutory		Investment revaluation reserve	General reserve	Exchange reserve	Retained earnings	(Note) Others	Minority interests	Total equity
			surplus reserve	public welfare fund							
As at 1 January 2004	—	—	—	—	544	—	—	394	186,230	37	187,205
Shares issued upon incorporation of the Bank	27(a) 194,230	—	—	—	—	—	—	—	(186,230)	—	8,000
Net profit	—	—	—	—	—	—	—	49,042	—	(2)	49,040
Net change in fair value of available-for-sale investments	27(d) —	—	—	—	(642)	—	—	—	—	—	(642)
Net gain realised on disposal of available-for-sale investments	27(d) —	—	—	—	(178)	—	—	—	—	—	(178)
Appropriations to statutory reserves	—	—	343	171	—	—	—	(514)	—	—	—
Profit distributions	—	—	—	—	—	—	—	(47,874)	—	—	(47,874)
As at 31 December 2004	194,230	—	343	171	(276)	—	—	1,048	—	35	195,551
As at 1 January 2005	194,230	—	343	171	(276)	—	—	1,048	—	35	195,551
Shares issued	27(a) 30,459	—	—	—	—	—	—	—	—	—	30,459
Share premium arising from shares issued	27(b) —	42,091	—	—	—	—	—	—	—	—	42,091
Minority interest in a new subsidiary	—	—	—	—	—	—	—	—	—	70	70
Net profit	—	—	—	—	—	—	—	47,103	—	(7)	47,096
Net change in fair value of available-for-sale investments	27(d) —	—	—	—	(859)	—	—	—	—	—	(859)
Net loss realised on disposal of available-for-sale investments	27(d) —	—	—	—	312	—	—	—	—	—	312
Appropriations to statutory reserves and general reserve	27(c), 27(e), 28 —	—	3,991	1,996	—	10,332	—	(16,319)	—	—	—
Exchange differences	27(f) —	—	—	—	—	—	6	—	—	—	6
Profit distributions	28 —	—	—	—	—	—	—	(27,049)	—	—	(27,049)
As at 31 December 2005	224,689	42,091	4,334	2,167	(823)	10,332	6	4,783	—	98	287,677

Note: Upon incorporation on 17 September 2004, the Bank issued a total of 186,230 million promoters' shares at a par value of RMB 1 each as consideration for the businesses of China Construction Bank succeeded by it, and transferred the balance of others in equity to share capital. Others in equity mainly represented contributions made by the owner and statutory reserve of China Construction Bank prior to its restructuring as at 31 December 2003.

The notes on pages 108 to 204 form part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2005 (Expressed in millions of Renminbi)

	Note	2005	2004
Operating activities			
Net profit		47,096	49,040
Adjustments for:			
— Interest income from special government bond	18(a)	—	(3,242)
— Dividend income		(546)	(777)
— Revaluation (gain)/loss on investments and derivatives	6	(210)	174
— Net gain on disposal of investments, property and equipment, land use rights, and other assets		(1,969)	(2,491)
— Unrealised foreign exchange losses		1,575	12
— Depreciation and amortisation	8	6,686	8,532
— Provisions for impairment losses		15,258	9,358
— Income tax	13(a)	8,268	2,159
— Interest expense on subordinated bonds issued	3	1,850	414
		<u>78,008</u>	<u>63,179</u>
<i>Changes in operating assets and liabilities:</i>			
Increase in balances with central banks		(94,582)	(42,707)
Increase in amounts due from banks and non-bank financial institutions		(3,130)	(20,424)
Increase in loans and advances to customers		(240,302)	(236,312)
(Increase)/decrease in other operating assets		(10,718)	75,953
Decrease in amounts due to central banks		(2,226)	(3,449)
Increase in amounts due to banks and non-bank financial institutions		52,485	2,865
Increase in deposits from customers		514,925	295,448
Increase/(decrease) in certificates of deposit issued		1,688	(605)
Income tax paid		(4,867)	(140)
Increase/(decrease) in other operating liabilities		12,163	(15,456)
		<u>303,444</u>	<u>118,352</u>
Net cash from operating activities		303,444	118,352

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2005 (Expressed in millions of Renminbi)

	Note	2005	2004
Investing activities			
Proceeds from disposal and redemption of investments		591,361	542,163
Proceeds from disposal of property and equipment, land use rights, and other assets		1,345	2,701
Payments on acquisition of investments		(895,920)	(824,114)
Payments on acquisition of property and equipment, and land use rights		(8,992)	(7,099)
Investment in a new subsidiary	29(c)	70	—
Dividend received		540	777
		<u>540</u>	<u>777</u>
Net cash used in investing activities		<u>(311,596)</u>	<u>(285,572)</u>
Financing activities			
Proceeds from shares issuance	27(a), 27(b)	74,639	8,000
Proceeds from securitisation of retail mortgages		2,920	—
Dividend paid		(2,914)	—
Cost of issuing shares, net of interest income	27(b)	(2,089)	—
Interest paid on subordinated bonds issued		(1,846)	—
Proceeds from subordinated bonds issued	26	—	40,000
Transaction costs on bonds issued		—	(106)
		<u>—</u>	<u>(106)</u>
Net cash from financing activities		<u>70,710</u>	<u>47,894</u>
Net increase/(decrease) in cash and cash equivalents		62,558	(119,326)
Cash and cash equivalents as at 1 January		220,106	339,435
Effect of exchange rate changes on cash held		(1,907)	(3)
		<u>(1,907)</u>	<u>(3)</u>
Cash and cash equivalents as at 31 December	29(a)	<u>280,757</u>	<u>220,106</u>
Cash flows from operating activities include:			
Interest received		169,177	139,928
		<u>169,177</u>	<u>139,928</u>
Interest paid, excluding interest expense on subordinated bonds issued		(52,552)	(43,948)
		<u>(52,552)</u>	<u>(43,948)</u>

The notes on pages 108 to 204 form part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

1 BACKGROUND

With the approval of the State Council, China Construction Bank (“CCB”) underwent a restructuring (the “Restructuring”) on 30 December 2003. China Construction Bank Corporation (the “Bank”) is a joint stock company with limited liability incorporated in the People’s Republic of China (the “PRC”) on 17 September 2004 as part of the Restructuring of CCB. The registered office of the Bank is located at No. 25, Finance Street, Xicheng District, Beijing, the PRC. Pursuant to the Restructuring, CCB was separated into the Bank and China Jianyin Investment Limited (“Jianyin”). The China Banking Regulatory Commission (the “CBRC”) issued a financial services certificate to the Bank on 15 September 2004. The State Administration for Industry and Commerce of the PRC issued a business licence to the Bank on 17 September 2004.

On 27 October 2005, all of the Bank’s shares were listed on the Main Board of the Stock Exchange of Hong Kong Limited (the “SEHK”).

The principal activities of the Bank and its subsidiaries (collectively the “Group”) are the provision of corporate and personal banking services, conducting treasury business and corresponding banking business, and the provision of asset management and trustee services.

For the purpose of these financial statements, Mainland China excludes the Hong Kong Special Administrative Region of the PRC (“Hong Kong”), the Macau Special Administrative Region of the PRC (“Macau”) and Taiwan.

2 SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) and its interpretations promulgated by the International Accounting Standards Board, and the disclosure requirements of the Hong Kong Companies Ordinance. These financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

All IFRS in issue which are relevant to the Group have been applied, except for IFRS 7 Financial Instruments: Disclosures (“IFRS 7”) and the amendment to IAS 1 Presentation of Financial Statements: Capital Disclosures (“IAS 1 Amendment”) both of which were issued in August 2005 and are effective for the period beginning 1 January 2007.

IFRS 7 requires more detailed qualitative and quantitative disclosure primarily on fair value information and risk management. The Group has assessed the impact of IFRS 7 and concluded that IFRS 7 would only affect the level of details in the disclosure of the financial statements, and would not have financial impact nor result in a change in the Group’s accounting policies.

The disclosures required by IAS 1 Amendment on how the Group manages its capital and complies with external capital requirements, are mostly contained in the Annual Report.

The accounting policies set out below have been applied consistently by the Group in the preparation of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(b) Basis of preparation of the financial statements

These financial statements have been prepared to reflect the restructuring of a business under common control in which all of the consolidated entities are ultimately controlled by the PRC government both before and after the Restructuring, and that control is not transitory. The financial statements for the year ended 31 December 2004 reflect the income and expenses and the cash flows of the Group as if the Group had been in existence throughout the year from 1 January 2004 to 31 December 2004 and as if the Group had succeeded to the businesses of CCB as of 31 December 2003 as part of the Restructuring.

The financial statements are presented in Renminbi ("RMB"), which is the Group's functional and presentation currency, rounded to the nearest million.

The financial statements are prepared using the historical cost basis, except for the following assets and liabilities which are stated at their fair value: financial assets and financial liabilities at fair value through profit or loss and available-for-sale assets, except those for which a reliable measure of fair value is not available; and certain non-financial assets which are stated at deemed cost.

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

The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the year in which the estimate is revised if the revision affects only that year, or in the year of the revision and future years if the revision affects both current and future years.

Judgements made by management in the application of IFRS that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the subsequent period are discussed in Note 35.

(c) Basis of consolidation

The consolidated financial statements include the financial statements of the Bank and its subsidiaries. Subsidiaries are those enterprises controlled by the Bank. Control exists when the Bank has the power, directly or indirectly, to govern the financial and operational policies of an enterprise so as to obtain benefits from its activities. The results and affairs of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(c) Basis of consolidation (Cont'd)

The Group does not consolidate Special Purpose Entities ("SPEs") that it does not control. As it can sometimes be difficult to determine whether the Group exercises control over SPEs, it makes judgments about risks and rewards as well as the ability to make operational decisions for the SPEs. In many instances, elements are present that, considered in isolation, indicate control or lack of control over a SPE, but when considered together make it difficult to reach a clear conclusion. When assessing whether the Group has to consolidate a SPE, the Group evaluates a range of factors, including whether (a) the Group will obtain the majority of the benefits of the activities of a SPE, (b) the Group retains the majority of the residual ownership risks related to the assets in order to obtain the benefits from its activities, (c) the Group has the decision-making powers to obtain the majority of the benefits, or (d) the activities of the SPE are being conducted on behalf and according to the Group's specific business needs so that the Group obtains the benefits from the SPE's operations. The Group consolidates a SPE if an assessment of the relevant factors indicates that the Group obtains the majority of the benefits of its activities.

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

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

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

In the Bank's balance sheet, an investment in a subsidiary is stated at cost less allowances for impairment losses.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(d) Foreign currency translations

Transactions in foreign currencies are translated into Renminbi at the foreign exchange rates ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the foreign exchange rates ruling at that date. Non-monetary assets and liabilities that are measured at historical cost in foreign currencies are translated using the foreign exchange rates at the date of the transaction. Non-monetary assets and liabilities that are measured at fair value in foreign currencies are translated using the foreign exchange rates at the date the fair value is determined. When the gain or loss on a non-monetary item is recognised directly in equity, any exchange component of that gain or loss is recognised directly in equity, and all other foreign exchange differences arising from settlement and translation of monetary and non-monetary assets and liabilities are recognised in the income statement.

The assets and liabilities of overseas operations are translated into Renminbi at the foreign exchange rates ruling at the balance sheet date. The revenue and expenses and cash flows of overseas operations are translated into Renminbi at rates approximating the foreign exchange rates ruling at the date of the transaction. Foreign exchange differences arising from translation are recognised directly in equity.

(e) Financial instruments

(i) *Recognition and measurement*

All financial assets and financial liabilities are recognised in the balance sheet, when and only when, the Group or the Bank, as appropriate, becomes a party to the contractual provisions of the instrument. Financial assets are derecognised on the date when the contractual rights to the cash flows expire or substantially all the risks and rewards of ownership are transferred. Financial liabilities are derecognised on the date when the obligations specified in the contracts are discharged, cancelled or expire. A regular way purchase or sale of financial asset is recognised using trade date accounting. From this date, any gains and losses arising from changes in fair value of the financial assets or financial liabilities are recorded.

At initial recognition, all financial assets and financial liabilities are measured at fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include observable market data. Transaction costs for financial assets and financial liabilities at fair value through profit or loss are expensed immediately.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(e) Financial instruments (Cont'd)

(i) *Recognition and measurement* (Cont'd)

Financial assets and financial liabilities are categorised as follows:

- financial assets and financial liabilities at fair value through profit or loss include those financial assets and financial liabilities held principally for the purpose of short term profit taking and those financial assets and financial liabilities that are designated by the Group upon recognition as at fair value through profit or loss.

All derivatives not qualified for hedging purposes are included in this category and are carried as assets when their fair value is positive and as liabilities when their fair value is negative;

- held-to-maturity assets are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intent and ability to hold to maturity, other than those that meet the definition of loans and receivables, or that the Group designated as at fair value through profit or loss or as available-for-sale;
- loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market, other than those that the Group intends to sell immediately or in the near term, and those that are designated as available for sale upon initial recognition, or those where the Group may not recover substantially all of its initial investment, other than because of credit determination, which will be classified as available-for-sale; and
- available-for-sale assets are non-derivative financial assets that are designated as available for sale or are not classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity assets.

Subsequent to initial recognition, financial assets and financial liabilities are measured at fair value, without any deduction for transaction costs that may occur on sale or other disposal except for loans and receivables, held-to-maturity financial assets and financial liabilities not designated at fair value through profit or loss, which are measured at amortised cost using the effective interest rate method. Financial assets and financial liabilities that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are stated at cost.

Gains and losses from changes in the fair value of financial instruments at fair value through profit or loss are included in the income statement when they arise. Gains and losses arising from a change in the fair value of available-for-sale assets are recognised directly in equity, except for impairment losses and foreign exchange gains and losses, until the financial asset is derecognised at which time the cumulative gains or losses previously recognised in equity will be recognised in the income statement. For financial assets and financial liabilities carried at amortised cost, a gain or loss is recognised in the income statement when the financial asset or financial liability is derecognised or impaired, and through the amortisation process.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(e) Financial instruments (Cont'd)

(ii) *Impairment*

Financial assets are assessed at each balance sheet date to determine whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset and that event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The carrying amount of asset is reduced through the use of an allowance for impairment losses and a corresponding provision for impairment losses is recognised in the income statement.

Losses expected as a result of future events, no matter how likely, are not recognised because the necessary loss event has not yet occurred.

— *Loans and receivables and held-to-maturity assets*

The Group uses two methods of assessing impairment losses: those assessed individually and those assessed on a collective basis.

(ii-1) Individually assessed financial assets

Loans and receivables and held-to-maturity assets, which are considered individually significant, are assessed individually for impairment. This includes all loans and advances in the corporate lending portfolios.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity assets carried at amortised cost has been incurred on an individual basis, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate.

Loans and advances which are assessed individually for impairment are assessed in the light of the objective evidence of loss events, for example:

- Significant financial difficulty of the borrower
- A breach of contract, such as default or delinquency in interest or principal payments
- For economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the Group would not otherwise consider
- It is probable that the borrower will become bankrupt or go through other forms of financial reorganisation

Individually impaired loans and advances are graded at a minimum at doubtful (see Note 34(a) for the definitions of the loan classification).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(e) Financial instruments (Cont'd)

(ii) **Impairment** (Cont'd)

— *Loans and receivables and held-to-maturity assets* (Cont'd)

(ii-1) Individually assessed financial assets (Cont'd)

It may not be possible to identify a single, discrete event that caused the impairment but it may be possible to identify impairment through the combined effect of several events.

Cash flows relating to short term loans and receivables are not discounted if the effect of discounting is immaterial.

The calculation of the present value of the estimated future cash flows of a collateralised loan or receivable reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

(ii-2) Collectively assessed financial assets

Loans and receivables and held-to-maturity assets, which include the following, are assessed for impairment losses on a collective basis:

- Homogeneous groups of loans not considered individually significant
- Individually assessed loans with no objective evidence of impairment on an individual basis

For the purpose of collective assessment, assets are grouped on the basis of historical loss experience for similar credit risk characteristics that are indicative of the debtors' ability to pay all amounts due according to the contractual terms.

Loans and advances which are assessed collectively for impairment are assessed in the light of the objective evidence of impairment that there is observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of loans and advances since the initial recognition of those assets including:

- adverse changes in the payment status of borrowers in the group; or
- national or local economic conditions that correlate with defaults on the assets in the group.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(e) Financial instruments (Cont'd)

(ii) **Impairment** (Cont'd)

— *Loans and receivables and held-to-maturity assets* (Cont'd)

(ii-2) Collectively assessed financial assets (Cont'd)

Homogeneous groups of loans not considered individually significant

For homogeneous groups of loans, including all of the retail lending portfolio, that are not considered individually significant, the Group adopts a flow rate methodology to assess impairment losses on a collective basis. This methodology utilises a statistical analysis of historical trends of probability of default and amount of consequential loss as well as an evaluation of current economic conditions that may have a consequential impact on inherent losses in the portfolio.

Individually assessed loans with no objective evidence of impairment on an individual basis

Where loans are individually significant and therefore have been individually assessed but for which no impairment can be identified individually, either due to the absence of any loss events or due to an inability to measure reliably the impact of potential loss events on future cash flows, these loans are grouped together in portfolios of similar credit risk characteristics for the purpose of assessing a collective impairment loss. These loans include all the corporate loans and advances which are graded at normal, special mention or substandard (see Note 34(a) for the definitions of the loan classification). This loss covers those loans and advances that were impaired at the balance sheet date but which will not be individually identified as such until some time in the future.

The collective impairment loss is assessed after taking into account:

- Historical loss experience in portfolios of similar risk characteristics;
- The emergence period between a loss occurring and that loss being identified; and
- The current economic and credit environments and whether in management's experience these indicate that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(e) Financial instruments (Cont'd)

(ii) *Impairment* (Cont'd)

— *Loans and receivables and held-to-maturity assets* (Cont'd)

(ii-2) Collectively assessed financial assets (Cont'd)

The emergence period between a loss occurring and its identification is determined by management based on the historical experience of the markets where the Group operates.

Impairment losses recognised on a collective basis represent an interim step pending the identification of impairment losses on individual assets (which are subject to individual assessment) in the pool of financial assets that are collectively assessed for impairment.

As soon as information is available that specifically identifies objective evidence of impairment on individual assets in a pool, those assets are removed from the pool of financial assets. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment for impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. The reversal shall not result in a carrying amount of the financial asset that exceeds the amortised cost at the date of the reversal had the impairment not been recognised. The amount of the reversal is recognised in the income statement.

When the borrower or the guarantor fails to repay the loan principal and interest, and repossessed assets are received by the Group for recovery of the impaired loans, the carrying value of the impaired loans is adjusted, if necessary, to the estimated fair value of the repossessed assets through impairment allowances. The adjusted carrying value of the impaired loans is transferred to repossessed assets, net of impairment allowances.

When management determine that a loan has no reasonable prospect of recovery after the Group has completed all the necessary legal or other proceedings, the loan is written off against its allowance for impairment losses. If in a subsequent period the loan written off is recovered, the amount recovered will be recognised in the income statement through impairment allowances.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(e) Financial instruments (Cont'd)

(ii) **Impairment** (Cont'd)

— *Available-for-sale assets*

When a decline in the fair value of an available-for-sale asset has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised directly in equity is removed from equity and recognised in the income statement even though the financial asset has not been derecognised.

The amount of the cumulative loss that is removed from equity and recognised in the income statement is the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that financial asset previously recognised in the income statement. For an available-for-sale asset that is not carried at fair value because its fair value cannot be reliably measured, such as an unquoted equity instrument, the amount of any impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed, with the amount of the reversal being recognised in the income statement. Impairment losses recognised in the income statement for an investment in an equity instrument classified as available-for-sale are not reversed through the income statement. Any increase in the fair value of such assets is recognised directly in equity.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(e) Financial instruments (Cont'd)

(iii) *Fair value measurement*

The fair value of financial assets is based on their quoted market price in an active market at the valuation date without any deduction for transaction costs. A quoted market price is from an active market where price information is readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and that price information represents actual and regularly occurring market transactions on an arm's length basis. If a quoted market price is not available, the fair value of the financial assets is established using valuation techniques.

Valuation techniques applied include recent arm's length market transactions between knowledgeable and willing parties referenced to the fair value of another instrument that is substantially the same, discounted cash flow analysis and option pricing models. Periodically the Group calibrates the valuation techniques and tests them for validity.

In estimating the fair value of a financial asset and financial liability, the Group considers all factors, including but not limited to, interest rate, credit risk, foreign currency exchange price and market volatility, that are likely to affect the fair value of the financial asset and financial liability.

The Group obtains market data in the same market where the financial instrument was originated or purchased.

(iv) *Derivative financial instruments*

The Group uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from its investment activities. In accordance with its treasury policy, the Group generally does not hold or issue derivative financial instruments for trading purposes. However, derivatives that do not qualify for hedge accounting are accounted for as financial assets and financial liabilities at fair value through profit or loss.

Derivative financial instruments are recognised at fair value. The gain or loss on re-measurement to fair value is recognised immediately in the income statement. However, where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(e) Financial instruments (Cont'd)

(v) *Hedge accounting*

It is the Group's policy to document the relationship between the hedging instruments and hedged items, as well as the risk management objective and strategy for undertaking the hedge, upon the inception of that relationship qualified for hedge accounting. Such policies also require documentation of the assessment, both at hedge inception and on any ongoing basis, of whether the derivatives are highly effective in offsetting changes in fair values attributed to the hedged risks. The Group discontinues prospectively hedge accounting when (i) the hedging instrument expires or is sold, terminated or exercised; (ii) the hedge no longer meets the criteria for hedge accounting; or (iii) the Group revokes the designation.

Fair value hedges

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

The hedging instrument is measured at fair value, with fair value changes recognised in the income statement. Changes in the fair value of the hedged item which are attributable to the risks hedged with the hedging instrument are reflected as adjustments to the carrying value of the hedged item. This adjustment is recognised in the income statement to offset the effect of the gain or loss on the hedging instrument.

(f) Repurchase and resale agreements

Assets purchased subject to commitments to resell them at future dates are not recognised. The amounts paid are accounted for as balances with central banks, amounts due from banks and non-bank financial institutions or loans and advances to customers depending on the identity of the counterparty.

Assets sold under repurchase agreements continue to be recognised in the financial statements and are measured in accordance with the accounting policy for these assets. The proceeds from the sale of the assets are reported as amounts due to central banks, banks or non-bank financial institutions.

The difference between the purchase and resale consideration or the sale and repurchase consideration is amortised over the period of the transaction and is included in interest income or expense, as appropriate.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(g) Property and equipment

(i) Cost

Items of property and equipment (including construction in progress) are stated at cost, or deemed cost, less accumulated depreciation and impairment losses. The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of attributable indirect costs.

Construction in progress represents property under construction and is stated at cost less impairment losses. Capitalisation of these costs ceases and the construction in progress is transferred to an appropriate class of property and equipment when the asset is substantially ready for its intended use.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Pursuant to the Restructuring, all property and equipment were revalued to fair value on 31 December 2003 by an independent professional valuer in the PRC, China Consultants of Accounting and Financial Management Co., Ltd ("CCAFM"). The revalued amount was adopted as the deemed cost of the property and equipment on 31 December 2003.

(ii) Subsequent costs

The Group recognises in the carrying amount of an item of property and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised in the income statement as an expense when incurred.

(iii) Depreciation

Depreciation is calculated to write off the cost or deemed cost, less residual value if applicable, of property and equipment and is charged to the income statement on a straight-line basis over the estimated useful lives of each part of an item of property and equipment. The estimated useful lives are as follows:

	<i>Estimated useful lives</i>
Bank premises	30–35 years
Computer equipment	3–8 years
Others	4–11 years

No depreciation is provided in respect of construction in progress.

The residual value, if not insignificant, is reassessed annually.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(g) Property and equipment (Cont'd)

(iv) *Impairment*

The carrying amount of property and equipment is reviewed periodically in order to assess whether the recoverable amount has declined below the carrying amount. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The amount of the reduction is recognised in the income statement. The recoverable amount is the greater of the net selling price and value in use.

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

(v) *Disposal and retirement*

Gains or losses arising from the disposal or retirement of property and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the income statement on the date of disposal or retirement.

(h) Land use rights

Land use rights are stated at cost or deemed cost, being the fair value on 31 December 2003 determined by CCAF, using the comparable market basis.

Land use rights are amortised on a straight-line basis over the respective periods of grant of 30–50 years.

(i) Repossessed assets

Repossessed assets are initially recognised at the carrying value of the loan principal and interest receivable, net of respective allowances for impairment losses, upon the seizure of these assets in lieu of the rights on the loans and advances and interest receivable. An impairment loss is recognised in the income statement whenever the carrying amount of such an asset exceeds its recoverable amount.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(j) **Fiduciary activities**

The Group acts in a fiduciary capacity as a custodian, trustee or an agent for customers. Assets held by the Group and the related undertakings to return such assets to customers are excluded from the financial statements as the risks and rewards of the assets reside with the customers.

Entrusted lending is one of the principal fiduciary activities of the Group. The Group enters into entrusted loan agreements with a number of customers, whereby the customers provide funding (the "entrusted funds") to the Group, and the Group grants loans to third parties (the "entrusted loans") at the instruction of the customers. As the Group does not assume the risks and rewards of the entrusted loans and the corresponding entrusted funds, entrusted loans and funds are recorded as off-balance sheet items at their principal amounts and no impairment assessments are made for these entrusted loans.

(k) **Provisions and contingent liabilities**

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

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

(l) **Employee benefits**

(i) **Employment benefits**

Salaries and bonuses, housing benefits and costs for social security benefits are accrued in the year in which the services are rendered by employees of the Group. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(I) Employee benefits (Cont'd)

(ii) *Post employment benefits*

Post employment benefits of the Group mainly include retirement benefits, and supplementary retirement benefits to the employees who retired on or before 31 December 2003.

Defined contribution retirement schemes

Obligations for contributions to defined contribution retirement schemes are recognised as an expense in the income statement as incurred for current employees.

Supplementary retirement benefits

The Group's obligations in respect of supplementary retirement benefits are calculated by estimating the amount of future benefits that the Group is committed to pay to the employees after their retirement using actuarial techniques. Such benefits are discounted to determine their present values. The discount rate is the yield on PRC government bonds at the balance sheet date, the maturity dates of which approximate to the terms of the Group's obligations. In calculating the Group's obligations, to the extent that any cumulative unrecognised gains or losses exceed 10% of the present value of the obligation at the balance sheet date, that portion is recognised in the income statement. Otherwise, the gain or loss is not recognised.

(m) Income recognition

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

(i) *Interest income*

Interest income for all interest-bearing assets is recognised as interest income in the income statement using the effective interest method or an applicable floating rate. Interest income includes the amortisation of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis.

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(m) Income recognition (Cont'd)

(i) *Interest income* (Cont'd)

The accrual of interest income of a loan where principal or interest of which is overdue over 90 days based on the original terms of the claim is discontinued. Instead, interest will continue to be recognised on the impaired financial assets using the rate of interest used to discount future cash flows ("unwinding of discount") for the purpose of measuring the related impairment loss.

(ii) *Fee and commission income*

Fee and commission income is recognised in the income statement when the corresponding service is provided.

Origination or commitment fees received by the Group which result in the creation or acquisition of a financial asset are deferred and recognised as an adjustment to the effective interest rate. If the commitment expires without the Group making a loan, the fee is recognised as revenue on expiry.

(iii) *Dividend income*

Dividend income is recognised in the income statement on the date when the Group's right to receive payment is established. Dividend income from listed investments is recognised when the share price of the investment goes ex-dividend.

(n) Offsetting

Financial assets and financial liabilities are offset and the net amount is reported in the balance sheet when the Group has a legally enforceable right to set off the recognised amounts and the transactions are intended to be settled on a net basis, or realise the asset and settle the liability simultaneously.

(o) Cash and cash equivalents

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise cash, non-restricted balances with central banks, banks and non-bank financial institutions, and short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

(p) Operating lease payments

Payments made under operating leases are recognised in the income statement on a straight-line basis over the terms of the leases.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

2 SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

(q) Income tax

Income tax in the income statement comprises current tax and movements in deferred tax balances. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

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

Deferred tax is provided using the balance sheet liability method, for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date. Deferred tax assets also arise from unused tax losses and unused tax credits.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(r) Dividends or profit distributions

Dividends or profit distributions are recognised as a liability in the year in which they are approved and declared.

(s) Related parties

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

(t) Segment reporting

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

3 NET INTEREST INCOME

	2005	2004
Interest income arises from:		
Balances with central banks	6,675	6,119
Amounts due from banks and non-bank financial institutions	3,442	2,027
Loans and advances to customers (note (i))		
— corporate loans	97,975	86,540
— personal loans	23,789	19,224
— discounted bills	5,341	4,839
Investments in debt securities (note (ii))	36,379	28,196
Others	—	251
	<u>173,601</u>	<u>147,196</u>
Interest expense arises from:		
Amounts due to banks and non-bank financial institutions	(2,920)	(1,805)
Deposits from customers	(52,084)	(43,051)
Subordinated bonds issued	(1,850)	(414)
Others	(196)	(438)
	<u>(57,050)</u>	<u>(45,708)</u>
Net interest income	<u>116,551</u>	<u>101,488</u>

Notes:

(i) Interest income arising from loans and advances to customers includes interest income accrued on individually assessed impaired loans and advances to customers of RMB 809 million for the year ended 31 December 2005 (2004: RMB 650 million), which includes interest income on the unwinding of discount of allowances for loan impairment losses of RMB 725 million for the year ended 31 December 2005 (2004: RMB 520 million) (Note 17(b)).

(ii) Interest income from investments in debt securities is mainly derived from unlisted investments.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

4 FEE AND COMMISSION INCOME

	2005	2004
Bank card fees	2,618	2,316
Remittance, settlement and account management fees	2,116	1,486
Agency fee for securities, foreign currency dealing and insurance services	1,927	1,472
Commission on trust business	946	702
Consultancy and advisory fees	848	732
Guarantee fees	290	233
Payment and collection services fees	246	192
Others	270	219
	<u>9,261</u>	<u>7,352</u>

5 DIVIDEND INCOME

The Group's dividend income was mainly derived from unlisted equity investments.

6 NET GAIN ARISING FROM DEALING SECURITIES

	2005	2004
Net gain on debt securities dealing	12	110
Revaluation gain/(loss) on investments and derivatives	210	(174)
Others	233	370
	<u>455</u>	<u>306</u>

7 NET GAIN ARISING FROM INVESTMENT SECURITIES

	2005	2004
Net gain on disposal	2,392	2,436
Net revaluation (loss)/gain transferred from equity on disposal	(465)	265
	<u>1,927</u>	<u>2,701</u>

Net gain on disposal primarily relates to available-for-sale securities.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

8 GENERAL AND ADMINISTRATIVE EXPENSES

	2005	2004
Staff costs		
— salaries, bonuses and staff welfare expenses	19,569	16,091
— contributions to defined contribution retirement schemes	2,149	1,700
— housing allowance	1,602	455
— supplementary retirement benefits	239	—
— staff termination costs	369	1,457
— others	3,370	2,468
	<u>27,298</u>	<u>22,171</u>
Property and equipment expense		
— depreciation	5,643	7,497
— rent and property management expenses	2,249	2,104
— utilities	993	942
— maintenance	937	937
— others	730	614
	<u>10,552</u>	<u>12,094</u>
Other general and administrative expenses (note (i))	11,798	11,450
Business tax and surcharges (note (ii))	7,401	6,459
Amortisation expense	1,043	1,035
Loss on disposal of property and equipment, land use rights, and other assets	—	210
	<u>58,092</u>	<u>53,419</u>

Notes:

(i) The amount includes auditors' remuneration of RMB 141 million for the year ended 31 December 2005 (2004: RMB 113 million).

(ii) Business tax of 5% is levied primarily on interest income from loans and advances to customers, and fee and commission income.

The surcharges, which include education surcharges and city construction tax, are charged at 3% and between 1% and 7% of business tax paid respectively.

9 PROVISIONS FOR IMPAIRMENT LOSSES ON ASSETS OTHER THAN LOANS AND ADVANCES TO CUSTOMERS

	2005	2004
Available-for-sale securities	948	1,876
Property and equipment	293	406
Others	311	967
	<u>1,552</u>	<u>3,249</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

10 DIRECTORS' AND SUPERVISORS' EMOLUMENTS

The aggregate of the emoluments in respect of the Directors and Supervisors who held office during the year is as follows:

	2005						Total RMB'000
	Paid in 2005					(note(i)) Discretionary bonus and other emoluments payable RMB'000	
	Fees RMB'000	Salaries and other emoluments RMB'000	Discretionary bonus RMB'000	Contributions to defined contribution retirement schemes RMB'000	Sub-total RMB'000		
Executive directors							
Guo Shuqing	—	425	180	13	618	236	854
Chang Zhenming	—	543	235	16	794	311	1,105
Liu Shulan	—	483	211	16	710	269	979
Zhao Lin	—	483	211	16	710	276	986
Independent non-executive directors							
Song Fengming	287	—	—	—	287	—	287
Yashiro Masamoto	273	—	—	—	273	—	273
Tse Hau Yin, Aloysius	268	—	—	—	268	—	268
Elaine La Roche	123	—	—	—	123	—	123
Non-executive directors							
Zhu Zhenmin (note (ii))	—	—	—	—	—	227	227
Jing Xuecheng (note (ii))	—	—	—	—	—	227	227
Wang Shumin (note (ii))	—	—	—	—	—	227	227
Wang Yonggang (note (ii))	—	—	—	—	—	227	227
Liu Xianghui (note (ii))	—	—	—	—	—	227	227
Zhang Xiangdong (note (ii))	—	—	—	—	—	240	240
Gregory L. Curl (note (iii))	—	—	—	—	—	87	87
Supervisors							
Xie Duyang	—	523	221	16	760	288	1,048
Liu Jin	—	301	128	16	445	163	608
Jin Panshi	—	331	120	16	467	170	637
Cheng Meifen (note (iv))	—	328	135	16	479	—	479
Cui Jianmin	150	—	—	—	150	—	150
Guo Feng	120	—	—	—	120	—	120
Chen Yueming (note (v))	—	—	—	—	—	200	200
	1,221	3,417	1,441	125	6,204	3,375	9,579
Former executive director resigned in 2005							
Zhang Enzhao	—	74	—	5	79	—	79
	1,221	3,491	1,441	130	6,283	3,375	9,658

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

10 DIRECTORS' AND SUPERVISORS' EMOLUMENTS (Cont'd)

	2004				Total RMB'000
	Fees RMB'000	Salaries and other emoluments RMB'000	Discretionary bonus RMB'000	Contributions to defined contribution retirement schemes RMB'000	
Executive directors					
Chang Zhenming	—	52	233	5	290
Liu Shulan	—	199	460	14	673
Zhao Lin	—	199	460	14	673
Independent non-executive directors					
Song Fengming	57	—	—	—	57
Yashiro Masamoto	55	—	—	—	55
Tse Hau Yin, Aloysius	21	—	—	—	21
Supervisors					
Xie Duyang	—	51	206	4	261
Liu Jin	—	16	15	1	32
Jin Panshi	—	194	150	14	358
	133	711	1,524	52	2,420
Former executive director resigned in 2005					
Zhang Enzhao	—	231	503	14	748
	133	942	2,027	66	3,168

Notes:

- (i) The amounts of discretionary bonus and other emoluments payable at 31 December 2005 in respect of the services rendered by the Directors and Supervisors are subject to approval of the Bank's shareholders in the Annual General Meeting to be held on 15 June 2006.
- (ii) The amounts will be payable to China SAFE Investments Limited ("Huijin") for the services of the respective Directors in 2005 after the approval of the Bank's shareholders as mentioned in note (i). No such payment was made in 2004.
- (iii) The amount will be payable to Bank of America Corporation for his services as Director in 2005 after the approval of the Bank's shareholders as mentioned in note (i).
- (iv) Ms. Cheng Meifen has been a Supervisor since December 2004. She did not receive any Supervisor's emoluments from the Group in 2004.
- (v) The amount will be payable to State Grid Corporation of China for her services as Supervisor in 2005 after the approval of the Bank's shareholders as mentioned in note (i). No such payment was made in 2004.
- (vi) None of the Directors and Supervisors received any inducements, or compensation for loss of office, or waived any emoluments during the years ended 31 December 2005 and 2004.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

11 INDIVIDUALS WITH HIGHEST EMOLUMENTS

Of the five individuals with the highest emoluments, none of them are Directors or Supervisors whose emoluments are disclosed in Note 10 above. The aggregate of the emoluments in respect of the five highest paid individuals during the year is as follows:

	2005 RMB'000	2004 RMB'000
Salaries and other emoluments	10,400	9,099
Discretionary bonuses	5,481	2,471
Contributions to defined contribution retirement schemes	681	797
	<u>16,562</u>	<u>12,367</u>

The number of these individuals whose emoluments are within the following bands is set out below.

	2005	2004
RMB 1,500,001–RMB 2,000,000	—	1
RMB 2,000,001–RMB 2,500,000	—	2
RMB 2,500,001–RMB 3,000,000	2	2
RMB 3,000,001–RMB 3,500,000	1	—
RMB 3,500,001–RMB 4,000,000	1	—
RMB 4,000,001–RMB 4,500,000	1	—

None of these individuals received any inducements, or compensation for loss of office, or waived any emoluments during the years ended 31 December 2005 and 2004.

12 LOANS TO DIRECTORS, SUPERVISORS AND OFFICERS

There were no loans to the Directors, Supervisors and Officers (and their affiliates) of the Bank as defined under section 161B of the Hong Kong Companies Ordinance during the years ended 31 December 2005 and 2004.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

13 INCOME TAX

(a) Recognised in the income statement

	2005	2004
Current tax		
— Mainland China	8,668	1,771
— Hong Kong	87	63
— Overseas	10	4
	<u>8,765</u>	<u>1,838</u>
Deferred tax (Note 20)	(497)	321
	<u>8,268</u>	<u>2,159</u>

(b) Reconciliation of profit before tax to income tax

	2005	2004
Profit before tax	<u>55,364</u>	<u>51,199</u>
Expected PRC income tax charged at statutory tax rate of 33% (note (i))	<u>18,270</u>	<u>16,896</u>
Non-deductible expenses (note (ii))		
— Staff costs	403	3,906
— Impairment losses	373	802
— Others	233	1,334
	<u>1,009</u>	<u>6,042</u>
Non-taxable income (note (iii))		
— Interest income from PRC government bonds	(2,772)	(3,162)
— Interest income from bond issued by Cinda	—	(1,834)
— Others	(391)	(310)
	<u>(3,163)</u>	<u>(5,306)</u>
	<u>16,116</u>	<u>17,632</u>
Less: Tax exemption (note (iv))	<u>(7,848)</u>	<u>(15,473)</u>
Income tax	<u>8,268</u>	<u>2,159</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

13 INCOME TAX (Cont'd)

(b) Reconciliation of profit before tax to income tax (Cont'd)

Notes:

- (i) *The provision for PRC income tax of the Group is calculated based on the statutory tax rate of 33% in accordance with the relevant PRC income tax rules and regulations.*
- (ii) *Amounts primarily represent impairment losses on assets (such as property and equipment, and repossessed assets) in excess of the deductible amount, and entertainment expenses, depreciation and amortisation charges which are not tax deductible.*
- (iii) *Amounts primarily comprise interest income from PRC government bonds and the bond issued by China Cinda Asset Management Company ("Cinda") for the purpose of acquiring CCB's impaired loans and advances in 1999 (Note 18(a)(iii)).*

According to a notice issued by the Ministry of Finance of the PRC (the "MOF"), interest income from the bond issued by Cinda is subject to income tax from 1 January 2005 onwards.

- (iv) *According to an approval notice issued by the MOF and the State Administration of Taxation of the PRC in June 2005, substantial amounts of the Group's income tax for each of the year ended 31 December 2004 and for the six months ended 30 June 2005 were exempted. The amounts of income tax exempted for the year ended 31 December 2005 were RMB 7,848 million (2004: RMB 15,473 million).*

14 EARNINGS PER SHARE

As part of the Restructuring, CCB received a capital injection of USD 22,500 million (equivalent to RMB 186,230 million) from Huijin on 30 December 2003. Upon incorporation on 17 September 2004, the Bank issued a total of 186,230 million promoters' shares at a par value of RMB 1 each to Huijin and Jianyin as consideration for the business succeeded from CCB, and 8,000 million promoters' shares at par value of RMB 1 each to three promoters for cash received.

Basic earnings per share for the year ended 31 December 2005 have been computed by dividing the net profit attributable to shareholders of the Bank by 199,542 million shares, being the weighted average of 194,230 million shares that were in issue and outstanding up to 26 October 2005, the date immediately before the completion of the Initial Public Offering (the "IPO"), 220,716 million shares in issue and outstanding between 27 October 2005 and 13 November 2005, the date immediately before the issuance of an additional 3,973 million shares upon the exercise of the over-allotment option, and 224,689 million shares in issue and outstanding since 14 November 2005.

Basic earnings per share for the year ended 31 December 2004 have been computed by dividing the net profits attributable to shareholders of the Bank by 188,547 million shares, being the weighted average number of shares calculated on the basis that 186,230 million shares were in issue and outstanding up to 16 September 2004 and 194,230 million shares were in issue and outstanding during the period from 17 September 2004 to 31 December 2004.

There was no difference between basic and diluted earnings per share as there were no potential dilutive shares outstanding during the years ended 31 December 2005 and 2004.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

15 CASH AND BALANCES WITH CENTRAL BANKS

	2005	2004
Cash	28,413	27,080
Balances with central banks		
— Statutory deposit reserve funds (note (i))	281,783	245,208
— Surplus deposit reserve funds (note (ii))	108,395	123,540
— Fiscal deposits	4,175	3,538
— Balances under resale agreement	57,370	—
	<u>451,723</u>	<u>372,286</u>
Total	<u>480,136</u>	<u>399,366</u>

Notes:

- (i) The Group places statutory deposit reserve funds with the People's Bank of China (the "PBOC") and the central banks of certain overseas countries where it has operations. The statutory deposit reserve funds are not available for the Group's daily business.

Statutory deposit reserve funds placed with the PBOC were calculated at 7% of eligible Renminbi deposits for domestic branches of the Bank prior to 25 April 2004 and 7.5% thereafter. The Bank was also required to deposit an amount equivalent to 2% of its foreign currency deposits from domestic branch customers as statutory deposit reserve funds prior to 15 January 2005. This was increased to 3% on 15 January 2005.

The amounts of statutory deposit reserve funds placed with the central banks of overseas countries are determined by local jurisdiction.

- (ii) The surplus deposit reserve funds were maintained with the PBOC for the purposes of clearing.

16 AMOUNTS DUE FROM BANKS AND NON-BANK FINANCIAL INSTITUTIONS

(a) Analysed by nature

	2005	2004
Money market placements	155,728	71,262
Balances under resale agreements	13,808	37,033
Deposits	22,036	6,886
Gross balances	191,572	115,181
Less: Allowances for impairment losses (Note 16(d))	(1,464)	(2,650)
Net balances	<u>190,108</u>	<u>112,531</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

16 AMOUNTS DUE FROM BANKS AND NON-BANK FINANCIAL INSTITUTIONS (Cont'd)

(b) Analysed by geographical location

	2005	2004
Balances with		
— Banks in Mainland China	24,366	34,861
— Non-bank financial institutions in Mainland China (note)	19,440	17,220
	<u>43,806</u>	<u>52,081</u>
Balances with banks outside Mainland China	147,766	63,100
	<u>191,572</u>	<u>115,181</u>
Gross balances		
Gross balances with banks and non-bank financial institutions		
— maturing within one month	108,230	83,979
— maturing between one month and one year	81,522	28,322
— maturing after one year	1,820	2,880
	<u>191,572</u>	<u>115,181</u>

Note: Non-bank financial institutions in Mainland China represent financial institutions, registered with and under the supervision of the CBRC, other than banks in Mainland China.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

16 AMOUNTS DUE FROM BANKS AND NON-BANK FINANCIAL INSTITUTIONS (Cont'd)

(c) Analysed by legal form of counterparty

	2005	2004
Balances with		
— PRC policy banks	1,292	—
— PRC state-owned banks and non-bank financial institutions	14,766	22,468
— PRC joint-stock banks and non-bank financial institutions	29,554	29,613
— Foreign-invested banks and non-bank financial institutions	145,960	63,100
	<u>191,572</u>	<u>115,181</u>
Gross balances		
Less: Allowances for impairment losses on balances with		
— PRC state-owned banks and non-bank financial institutions	(1,011)	(1,143)
— PRC joint-stock banks and non-bank financial institutions	(453)	(1,507)
	<u>(1,464)</u>	<u>(2,650)</u>
Total allowances for impairment losses		
Net balances	<u>190,108</u>	<u>112,531</u>

(d) Movements of allowances for impairment losses

	2005	2004
As at 1 January	2,650	3,847
Charge for the year	16	203
Write-offs	(1,202)	(1,400)
	<u>1,464</u>	<u>2,650</u>
As at 31 December		

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

17 LOANS AND ADVANCES TO CUSTOMERS

(a) Analysed by nature

	2005	2004
Corporate loans	1,809,836	1,657,460
Personal loans	454,253	412,647
Discounted bills	194,309	157,319
	<u>2,458,398</u>	<u>2,227,426</u>
Gross loans and advances to customers		
Less: Allowances for impairment losses (Note 17(b))	(63,085)	(53,864)
	<u>2,395,313</u>	<u>2,173,562</u>
Net loans and advances to customers		

(b) Movements of allowances for impairment losses

	2005	2004
As at 1 January	53,864	54,395
Charge for the year	13,706	6,109
Unwinding of discount	(725)	(520)
Transfers out (note)	(93)	(432)
Write-offs	(3,784)	(6,342)
Recoveries of loans and advances previously written off	117	654
	<u>63,085</u>	<u>53,864</u>
As at 31 December		

Note: Transfers out include the net transfer of allowances for impairment losses to/from repossessed assets and debt equity swap investments.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

17 LOANS AND ADVANCES TO CUSTOMERS (Cont'd)

(c) Loans and advances to customers and allowances

	2005			Total	Gross impaired loans and advances as a % of gross total loans and advances
	(note (i)) Loans and advances for which allowances are collectively assessed	(note (ii)) Impaired loans and advances for which allowances are collectively assessed			
Gross loans and advances to					
— financial institutions	782	—	—	782	—
— non-financial institution customers	2,363,147	46,989	47,480	2,457,616	3.84%
	<u>2,363,929</u>	<u>46,989</u>	<u>47,480</u>	<u>2,458,398</u>	<u>3.84%</u>
Less: Allowances for impairment losses on loans and advances to					
— financial institutions	(2)	—	—	(2)	
— non-financial institution customers	(19,427)	(13,234)	(30,422)	(63,083)	
	<u>(19,429)</u>	<u>(13,234)</u>	<u>(30,422)</u>	<u>(63,085)</u>	
Net loans and advances to					
— financial institutions	780	—	—	780	
— non-financial institution customers	2,343,720	33,755	17,058	2,394,533	
	<u>2,344,500</u>	<u>33,755</u>	<u>17,058</u>	<u>2,395,313</u>	

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

17 LOANS AND ADVANCES TO CUSTOMERS (Cont'd)

(c) Loans and advances to customers and allowances (Cont'd)

	2004			Total	Gross impaired loans and advances as a % of gross total loans and advances
	(note (i))	(note (ii))			
	Loans and advances for which allowances are collectively assessed	Impaired loans and advances for which allowances are collectively assessed	Impaired loans and advances for which allowances are individually assessed		
Gross loans and advances to					
— financial institutions	648	—	—	648	—
— non-financial institution customers	2,139,398	53,847	33,533	2,226,778	3.92%
	<u>2,140,046</u>	<u>53,847</u>	<u>33,533</u>	<u>2,227,426</u>	<u>3.92%</u>
Less: Allowances for impairment losses on loans and advances to					
— financial institutions	(4)	—	—	(4)	
— non-financial institution customers	(19,496)	(14,102)	(20,262)	(53,860)	
	<u>(19,500)</u>	<u>(14,102)</u>	<u>(20,262)</u>	<u>(53,864)</u>	
Net loans and advances to					
— financial institutions	644	—	—	644	
— non-financial institution customers	2,119,902	39,745	13,271	2,172,918	
	<u>2,120,546</u>	<u>39,745</u>	<u>13,271</u>	<u>2,173,562</u>	

Notes:

- (i) Loans and advances assessed on a collective basis for impairment bear relatively insignificant impairment losses as a proportion of the total portfolio. These loans and advances include those which are graded normal or special-mention.
- (ii) Impaired loans and advances include loans for which objective evidence of impairment exists and which have been assessed as bearing significant impairment losses. These loans include loans for which objective evidence of impairment has been identified:
- individually (including corporate loans and advances which are graded doubtful or loss); or
 - collectively; that is portfolios of homogeneous loans (including retail loans and advances which are graded substandard, doubtful or loss) and portfolios of loans which have been individually assessed but for which no impairment can be identified individually (including corporate loans and advances which are graded substandard).
- (iii) The definitions of the loan classification stated in notes (i) and (ii) above are described in Note 34(a).
- (iv) There were no impaired loans and advances to financial institutions as at 31 December 2005 and 2004.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

17 LOANS AND ADVANCES TO CUSTOMERS (Cont'd)

(d) Analysed by legal form of borrowers

	2005	2004
Corporate loans to		
— State-owned enterprises	844,404	838,864
— Joint-stock enterprises	374,427	350,150
— Private enterprises	214,509	152,490
— Foreign invested enterprises	183,486	147,863
— Collectively-controlled enterprises	42,963	44,278
— Jointly-owned enterprises	18,698	14,204
— Others	131,349	109,611
	<hr/>	<hr/>
Subtotal	1,809,836	1,657,460
Personal loans	454,253	412,647
Discounted bills	194,309	157,319
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Gross loans and advances to customers	2,458,398	2,227,426
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Less: Allowances for impairment losses on		
Corporate loans to		
— State-owned enterprises	(20,555)	(19,571)
— Joint-stock enterprises	(13,866)	(11,718)
— Private enterprises	(8,765)	(5,656)
— Foreign invested enterprises	(6,096)	(5,047)
— Collectively-controlled enterprises	(2,778)	(3,051)
— Jointly-owned enterprises	(782)	(633)
— Others	(2,577)	(2,583)
	<hr/>	<hr/>
Subtotal	(55,419)	(48,259)
Personal loans	(7,480)	(5,465)
Discounted bills	(186)	(140)
	<hr/>	<hr/>
Total allowances for impairment losses	(63,085)	(53,864)
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Net loans and advances to customers	2,395,313	2,173,562
	<hr/>	<hr/>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

18 INVESTMENTS

	2005	2004
Receivables (Note 18(a))	443,729	433,858
Held-to-maturity debt securities (Note 18(b))	643,978	489,791
Available-for-sale		
— debt securities (Note 18(c))	312,059	166,917
— equity investments (Note 18(d))	11,672	16,355
	323,731	183,272
Debt securities at fair value through profit or loss (Note 18(e))	2,433	715
Total	1,413,871	1,107,636

The Group's debt securities at fair value through profit or loss are held for trading purposes.

(a) Receivables

	2005	2004
<i>Due from issuers in Mainland China:</i>		
Government		
— Special government bond (note (i))	49,200	49,200
— Others	530	563
The PBOC (note (ii))	94,197	84,354
Policy banks	49,872	52,671
Cinda (note (iii))	247,000	247,000
Banks	2,930	70
Total	443,729	433,858

Notes:

- (i) This represents a non-negotiable bond of nominal value of RMB 49,200 million issued by the MOF in 1998 to strengthen the capital base of CCB. The bond matures in 2028 and originally bore interest at a fixed rate of 7.2% per annum. The interest rate of the bond was revised to a fixed interest rate of 2.25% per annum with effect from 1 December 2004 as part of the Restructuring. This substantial modification of the terms of the special government bond has been accounted for as a derecognition of the original bond with an interest rate of 7.2% per annum and the recognition of a new bond that matures in 2028 and bears an interest rate of 2.25% per annum to reflect the substance of the Restructuring of CCB.

Interest receivable on the bond from the date of issue to 30 November 2004 was settled by CCB's or the Bank's profit distribution as per a notice of the MOF. From 1 December 2004, interest receivable on the bond is settled by cash on an annual basis.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

18 INVESTMENTS (Cont'd)

(a) Receivables (Cont'd)

Notes: (Cont'd)

(ii) Due from the PBOC includes:

- a non-transferable bill of nominal value of RMB 63,354 million issued specifically to CCB as part of the Restructuring. The majority of the proceeds paid by Cinda on the disposal of impaired loans and advances were used to subscribe for a PBOC bill of nominal value of RMB 63,354 million. The bill matures in June 2009 and bears a fixed interest rate of 1.89% per annum. The PBOC has the right to early settle the bill; and
- a non-transferable bill of nominal value of RMB 21,000 million issued for settlement of CCB's receivables arising from its appointment by the State Council and the PBOC to act as the receiver in respect of the liquidation of a trust and investment company (Note 24(b)). The bill matures in June 2007 and bears a fixed interest rate of 1.89% per annum. The PBOC has an early redemption right on this bill subject to certain conditions.

(iii) Cinda issued a bond specifically to CCB in 1999 for the acquisition of CCB's impaired loans and advances at their original book value. The bond has a nominal value of RMB 247,000 million and matures in September 2009. It bears a fixed interest rate of 2.25% per annum. According to a notice issued by the MOF, starting from 1 January 2005, the MOF will provide financial support if Cinda is unable to repay the interest in full. The MOF will also provide support for the repayment of bond principal, if necessary.

(iv) As part of the Restructuring, the PBOC approved the Bank's use of the special government bond and the bill of nominal value of RMB 63,354 million issued by the PBOC as eligible assets equivalent to the surplus deposit reserve funds for the purpose of clearing.

(v) All debt securities included as Receivables are unlisted.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

18 INVESTMENTS (Cont'd)

(b) Held-to-maturity debt securities

	2005	2004
<i>Issued by:</i>		
Governments		
— in Mainland China	205,649	202,436
— outside Mainland China	161	165
The PBOC	218,354	105,589
Policy banks		
— in Mainland China	144,507	118,473
— outside Mainland China	1,630	82
Banks and non-bank financial institutions		
— in Mainland China	17,115	4,940
— outside Mainland China	37,934	31,989
Public sector entities outside Mainland China	17,938	23,120
Others		
— in Mainland China	176	—
— outside Mainland China	514	2,997
Total	<u>643,978</u>	<u>489,791</u>
Listed in Hong Kong	1,849	—
Listed outside Hong Kong	27,787	30,744
Unlisted	<u>614,342</u>	<u>459,047</u>
Total	<u>643,978</u>	<u>489,791</u>
Market value of listed securities	<u>28,920</u>	<u>30,463</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

18 INVESTMENTS (Cont'd)

(c) Available-for-sale debt securities

	2005	2004
<i>At fair value and issued by:</i>		
Governments		
— in Mainland China	13,404	8,073
— outside Mainland China	44,061	45,344
The PBOC	110,114	14,339
Central banks outside Mainland China	310	—
Policy banks		
— in Mainland China	10,429	4,132
— outside Mainland China	5,512	5,637
Banks and non-bank financial institutions		
— in Mainland China	—	529
— outside Mainland China	87,950	28,883
Public sector entities outside Mainland China	23,086	45,918
Others		
— in Mainland China (note)	13,245	—
— outside Mainland China	3,948	14,062
Total	312,059	166,917
Listed in Hong Kong	1,863	1,237
Listed outside Hong Kong	74,562	58,858
Unlisted	235,634	106,822
Total	312,059	166,917

Note: Others in Mainland China as at 31 December 2005 include debt securities issued by state-owned enterprises and joint-stock enterprises of RMB 3,424 million (2004: Nil) and RMB 9,821 million (2004: Nil) respectively.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

18 INVESTMENTS (Cont'd)

(d) Available-for-sale equity investments

	2005	2004
<i>At fair value:</i>		
Debt equity swap investments (note)	10,886	15,421
Other equity investments	786	934
Total	11,672	16,355
Listed in Hong Kong	563	638
Listed outside Hong Kong	17	28
Unlisted	11,092	15,689
Total	11,672	16,355

Note: Pursuant to the arrangement by the PRC government in 1999, the Group acquired unlisted legal person shares ("debt equity swap investments") in certain corporate borrowers in lieu of repayments of loans granted to them. Pursuant to a notice (the "Notice") jointly issued by the State Economic & Trade Commission of the PRC and the PBOC on 5 July 1999, commercial banks are prohibited from being involved in management of the operation of these corporate borrowers although the banks hold equity interests through the above debt equity swap arrangement.

Prior to 30 April 2005, the Group appointed Cinda to hold and manage these debt equity swap investments. The Group has ownership and right of disposal and retains the risks and rewards associated with them. These shares were registered under the name of Cinda which acted on behalf of the Group and earned a management fee in return. On 30 April 2005, the Group entered into an agreement (the "Termination Agreement") with Cinda to terminate the appointment of Cinda to manage these investments on its behalf. Pursuant to the Termination Agreement, Cinda would transfer the legal titles of these investments to the Group. Notwithstanding this change, the Group is still required to comply with the Notice and the Group will continue not to participate in the financial and operating policy decisions of these corporate borrowers nor exert significant influence over these policies. In substance, the Group does not have any control or significant influence over these corporate borrowers. The Group has been advised by its external legal counsel that such direct ownership in these investments does not violate any of the prevailing laws and regulations in the PRC.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

18 INVESTMENTS (Cont'd)

(e) Debt securities at fair value through profit or loss

	2005	2004
<i>Issued by:</i>		
Governments		
— in Mainland China	361	88
— outside Mainland China	234	248
The PBOC	49	196
Policy banks		
— in Mainland China	718	—
— outside Mainland China	142	—
Banks and non-bank financial institutions outside Mainland China	615	183
Public sector entities outside Mainland China	244	—
Others outside Mainland China	70	—
	2,433	715

All the above securities are unlisted and held for trading purposes.

(f) Investments in subsidiaries

The following list contains only the particulars of subsidiaries which principally affected the results, assets or liabilities of the Group. All of these companies are subsidiaries as defined under Note 2(c) and have been included in the scope of the consolidated financial statements of the Group.

Name of company	Place of incorporation and operation	Particulars of the issued and paid up capital	% of ownership directly held by the Bank	Principal activities
China Construction Bank (Asia) Limited (formerly Jian Sing Bank Limited)	Hong Kong	300 million shares of HK\$ 1 each	100%	Commercial banking and related financial services
Sino-German Bausparkasse Corporation Limited	PRC, limited liability company	150 million shares of RMB 1 each	75.1%	Home mortgage loan and deposit taking business
CCB Principal Asset Management Co., Ltd. ("CCB Principal")	PRC, limited liability company	200 million shares of RMB 1 each	65%	Fund management services

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

19 PROPERTY AND EQUIPMENT

	Bank premises (Note 19(a))	Construction in progress	Computer equipment	Others	Total
Cost or deemed cost:					
As at 1 January 2005	38,352	764	9,576	5,000	53,692
Additions	1,103	2,225	2,434	2,593	8,355
Disposals	(701)	(2)	(705)	(1,615)	(3,023)
Transfers	233	(643)	64	346	—
As at 31 December 2005	<u>38,987</u>	<u>2,344</u>	<u>11,369</u>	<u>6,324</u>	<u>59,024</u>
Accumulated depreciation and impairment losses:					
As at 1 January 2005	(2,024)	—	(2,947)	(277)	(5,248)
Depreciation charges	(1,624)	—	(2,434)	(1,585)	(5,643)
Impairment losses	(234)	(50)	(4)	(5)	(293)
Disposals	224	1	678	1,218	2,121
As at 31 December 2005	<u>(3,658)</u>	<u>(49)</u>	<u>(4,707)</u>	<u>(649)</u>	<u>(9,063)</u>
Net carrying value:					
As at 31 December 2005	<u>35,329</u>	<u>2,295</u>	<u>6,662</u>	<u>5,675</u>	<u>49,961</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

19 PROPERTY AND EQUIPMENT (Cont'd)

	Bank premises (Note 19(a))	Construction in progress	Computer equipment	Others	Total
Cost or deemed cost:					
As at 1 January 2004	38,208	964	6,548	6,016	51,736
Additions	973	719	2,689	1,733	6,114
Disposals	(941)	(72)	(387)	(2,758)	(4,158)
Transfers	112	(847)	726	9	—
As at 31 December 2004	38,352	764	9,576	5,000	53,692
Accumulated depreciation and impairment losses:					
As at 1 January 2004	—	—	—	—	—
Depreciation charges	(1,714)	—	(3,182)	(2,601)	(7,497)
Impairment losses	(388)	—	(9)	(9)	(406)
Disposals	78	—	244	2,333	2,655
As at 31 December 2004	(2,024)	—	(2,947)	(277)	(5,248)
Net carrying value:					
As at 31 December 2004	36,328	764	6,629	4,723	48,444

Note: As at 31 December 2005, ownership documentation for the Group's bank premises with a net carrying value of RMB 1,152 million (31 December 2004: RMB 1,112 million) was being finalised.

(a) Analysed by remaining term of leases

The net carrying value of Group's bank premises at the balance sheet date is analysed by the remaining terms of the leases as follows:

	2005	2004
Long term leases (over 50 years), held in Hong Kong	102	105
Medium term leases (10–50 years), held in Mainland China	35,012	36,141
Short term leases (less than 10 years), held in Mainland China	215	82
Total	35,329	36,328

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

19 PROPERTY AND EQUIPMENT (Cont'd)

(b) Valuation

As required by the relevant PRC rules and regulations with respect to the Restructuring, the property and equipment of CCB as at 31 December 2003 were valued by CCAFMM on a depreciated replacement cost or a comparable market basis as appropriate.

The Group's bank premises were also valued separately by Chesterton Petty Limited, an independent qualified valuer in Hong Kong as at 31 December 2003. The value arrived at by them was approximately the same as that arrived at by CCAFMM.

The effect of this valuation was to increase the depreciation charges of property and equipment by approximately RMB 394 million for the year ended 31 December 2005 (2004: RMB 394 million).

The valuation was a one-off event driven by the Restructuring. Other than this revaluation, which was carried out in compliance with relevant PRC rules and regulations, the Group has no plans to revalue its property and equipment on a regular basis. Accordingly, the property and equipment are to be stated at cost or deemed cost, less accumulated depreciation and impairment losses.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

20 DEFERRED TAX

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

	In Mainland China			Outside Mainland China	
	Interest recognition for short-term debt securities (note (i))	Deferral or amortisation of subordinated bonds issue costs	Fair value adjustments for securities and derivatives (note (ii))	Fair value adjustments for securities and derivatives (note (ii))	Deferred tax assets/(liabilities)
As at 1 January 2004	(179)	—	(249)	(43)	(471)
Recognised in income statement	(343)	(35)	60	(3)	(321)
Recognised in equity	—	—	420	(16)	404
As at 31 December 2004	<u>(522)</u>	<u>(35)</u>	<u>231</u>	<u>(62)</u>	<u>(388)</u>
As at 1 January 2005	(522)	(35)	231	(62)	(388)
Recognised in income statement	522	4	(55)	26	497
Recognised in equity	—	—	268	43	311
As at 31 December 2005	<u>—</u>	<u>(31)</u>	<u>444</u>	<u>7</u>	<u>420</u>

Notes:

(i) Interest income for certain debt investments was taxed on disposal or maturity of these investments in 2004.

Starting from 1 January 2005, interest income from such debt investments as recognised in the financial statements is taxed on an accrual basis.

(ii) Unrealised gains or losses arising from fair value adjustments for securities and derivatives are subject to tax when realised in 2004.

Starting from 1 January 2005, unrealised gains or losses arising from fair value adjustments for securities at fair value through profit or loss and derivatives are taxed when recognised. Fair value adjustments for available-for-sale securities are subject to tax when realised.

(iii) The Group did not have significant unrecognised deferred taxation arising at the balance sheet date.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

21 OTHER ASSETS

	2005	2004
Interest receivable		
— debt securities	11,695	8,695
— loans and advances to customers	4,294	3,612
— others	1,080	338
	<u>17,069</u>	<u>12,645</u>
Land use rights (Note 21(a))	18,449	18,986
Positive fair value of derivatives (Notes 21(b) and 34(f))	12,146	1,624
Repossessed assets (Note 21(c))	1,877	2,862
Intangible assets	978	969
Government receivable (Note 21(d))	—	23,781
Others	5,414	7,514
	<u>55,933</u>	<u>68,381</u>
Total		

(a) Valuation of land use rights

As required by the relevant PRC rules and regulations with respect to the Restructuring, the land use rights of CCB as at 31 December 2003 were valued by CCAF on a comparable market basis.

The effect of this valuation was to increase the amortisation charges of land use rights by approximately RMB 230 million for the year ended 31 December 2005 (2004: RMB 230 million).

(b) Positive fair value of derivatives

The balance as at 31 December 2005 includes the fair value of the foreign exchange option, amounting to RMB 9,545 million (2004: Nil), which was purchased to hedge the currency risk arising from the separately managed US dollar denominated investment portfolio (Note 34(d)).

The premium payable in respect of the above option purchased is stated at a discounted value of RMB 5,348 million (2004: Nil) and is included under other liabilities and provisions (Note 24).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

21 OTHER ASSETS (Cont'd)

(c) Repossessed assets

On 30 June 2004, CCB entered into sale and purchase agreements (the "S&P Agreements") to dispose of certain repossessed assets for a consideration of RMB 1,098 million. The completion dates of these transactions, which were initially set on 27 December 2004, were deferred to and finalised on 30 March 2005 and 30 May 2005 respectively upon request from the buyers. As at 31 December 2004, the Group considered that the uncertainty on completion was insignificant and these repossessed assets were therefore derecognised. Pursuant to the S&P Agreements, all gains or losses arising from these repossessed assets after the date of the S&P Agreements belong to the buyers. However, the Group has an obligation to buy back those assets which are found to be with defects within nine months from the completion dates, or for assets whose titles fail to be transferred to the buyers, within three years from the completion dates. As at 31 December 2005, the Group considered that the potential buy-back amounts would be immaterial.

(d) Government receivable

As part of the Restructuring, the PRC government agreed to replenish the remaining accumulated losses of CCB as at 31 December 2003. The government receivable is non-interest-bearing and an amount of RMB 41,718 million was settled by the Bank's profit distribution of the profit for the year ended 31 December 2004 as approved by the shareholders in the general meeting on 27 December 2004. The remaining balance was settled by the Bank's profit distribution of the profit for the six months ended 30 June 2005 as approved by the shareholders in the general meeting on 6 June 2005 (Note 28).

22 AMOUNTS DUE TO BANKS AND NON-BANK FINANCIAL INSTITUTIONS

(a) Analysed by nature

	2005	2004
Balances under repurchase agreements	21,189	100
Money market takings	17,540	23,085
Deposits	125,795	88,854
Total	164,524	112,039

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

22 AMOUNTS DUE TO BANKS AND NON-BANK FINANCIAL INSTITUTIONS (Cont'd)

(b) Analysed by geographical location

	2005	2004
Balances payable on demand		
— Banks in Mainland China	6,591	6,615
— Non-bank financial institutions in Mainland China	<u>78,726</u>	<u>73,736</u>
	<u>85,317</u>	<u>80,351</u>
— Banks outside Mainland China	<u>322</u>	<u>4,348</u>
Term deposits		
— Banks in Mainland China	10,849	7,099
— Non-bank financial institutions in Mainland China	<u>33,922</u>	<u>2,614</u>
	<u>44,771</u>	<u>9,713</u>
— Banks outside Mainland China	20,612	17,627
— Non-bank financial institutions outside Mainland China	<u>13,502</u>	<u>—</u>
	<u>34,114</u>	<u>17,627</u>
Total	<u>164,524</u>	<u>112,039</u>

(c) Analysed by legal form of counterparty

	2005	2004
Balances with		
— PRC policy banks	137	45
— PRC state-owned banks and non-bank financial institutions	106,219	69,773
— PRC joint-stock banks and non-bank financial institutions	19,389	20,246
— Foreign-invested banks and non-bank financial institutions	<u>38,779</u>	<u>21,975</u>
Total	<u>164,524</u>	<u>112,039</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

23 DEPOSITS FROM CUSTOMERS

(a) Analysed by nature

	2005	2004
Demand deposits		
— Corporate customers	1,475,119	1,389,355
— Personal customers	709,026	633,765
	<u>2,184,145</u>	<u>2,023,120</u>
Time deposits		
— Corporate customers	632,350	452,689
— Personal customers	1,189,551	1,015,312
	<u>1,821,901</u>	<u>1,468,001</u>
Total	<u>4,006,046</u>	<u>3,491,121</u>

(b) Analysed by geographical segments

	2005	2004
Yangtze River Delta	828,647	726,774
Pearl River Delta	620,375	544,452
Bohai Rim	802,270	698,108
Central	687,258	604,301
Western	671,263	597,300
Northeastern	322,758	280,177
Head office	58,897	29,698
Overseas	14,578	10,311
Total	<u>4,006,046</u>	<u>3,491,121</u>

See Note 33(b) for the definitions of geographical segments.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

24 OTHER LIABILITIES AND PROVISIONS

	2005	2004
Interest payable		
— deposits from customers	25,205	22,976
— others	927	504
	<u>26,132</u>	<u>23,480</u>
Salaries and welfare payables (Note 24(a))	9,505	7,209
Supplementary retirement benefit obligations (Note 25(b))	5,621	5,743
Foreign exchange option premium payable (Note 21(b))	5,348	—
Payables to Jianyin (Notes 24(b) and 36(a))	5,211	6,405
Business and other tax payables	3,451	2,705
Dormant accounts	2,860	1,104
Negative fair value of derivatives (Note 34(f))	2,490	1,816
Bond redemption payable	2,063	1,717
Litigation provision (Note 24(c))	1,802	2,107
Payment and collection clearance account	1,333	1,358
Settlement accounts	897	1,287
Dividend payable (Note 28(a))	3,268	2,914
Others	6,509	5,342
	<u>76,490</u>	<u>63,187</u>
Total		

(a) Salaries and welfare payables

Included under salaries and welfare payables, the Group has the following payables to defined contribution retirement schemes at the balance sheet date:

	2005	2004
As at 31 December	<u>1,082</u>	<u>1,231</u>

(b) Payables to Jianyin

The balance as at 31 December 2005 represented a payable of RMB 5,211 million (2004: RMB 5,113 million) to Jianyin, arising from the receipt of a bill issued by the PBOC with a nominal value of RMB 21,000 million (Note 18(a)), which exceeded net advances made by CCB for the liquidation of a trust and investment company, plus the interest accrual on such excess portion.

The balance as at 31 December 2004 also included the proceeds from the disposal of assets owned by Jianyin collected by the Group on behalf of Jianyin.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

24 OTHER LIABILITIES AND PROVISIONS (Cont'd)

(c) Litigation provision

	2005	2004
As at 1 January	2,107	2,587
Charge for the year	5	707
Payments made	(310)	(1,187)
	<u>1,802</u>	<u>2,107</u>
As at 31 December		

25 RETIREMENT BENEFITS

(a) Statutory retirement schemes

In accordance with the labour regulations of the PRC, the Group participates in various defined contribution retirement schemes organised by the municipal and provincial governments for its employees in Mainland China. The Group is required to make contributions to a separate entity which could be the government or publicly administered retirement schemes at certain rates of the salaries, bonuses and certain allowances of its employees. A member of the schemes is entitled to a pension equal to a fixed proportion of the salary prevailing at his or her retirement date.

For its employees outside Mainland China, the Group participates in various defined contribution retirement schemes at funding rates determined in accordance with the local practices and regulations.

The Group has no other material obligations for the payment of its employees' retirement and other post retirement benefits other than the contributions described above and in Note 25(b) below.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

25 RETIREMENT BENEFITS (Cont'd)

(b) Supplementary retirement benefits

The Group pays supplementary retirement benefits for its employees in Mainland China who retired on or before 31 December 2003 ("Eligible Employees"). The amounts recognised in the balance sheet represent the present value of unfunded obligations.

The Group's obligations in respect of the supplementary retirement benefits at the balance sheet date were reviewed by an independent actuary, Towers, Perrin, Forster & Crosby, Inc., Hong Kong, using the projected unit credit actuarial cost method. They are members of the Society of Actuaries of the United States of America.

Net liabilities recognised in the balance sheet represent:

	2005	2004
Present value of the obligations	5,758	5,221
Unrecognised actuarial (losses)/gains	(137)	522
As at 31 December	<u>5,621</u>	<u>5,743</u>

Movements in the net liabilities recognised in the balance sheet are as follows:

	2005	2004
As at 1 January	5,743	6,367
Payments made	(361)	(348)
Net expense/(net income) recognised in the income statement	<u>239</u>	<u>(276)</u>
As at 31 December	<u>5,621</u>	<u>5,743</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

25 RETIREMENT BENEFITS (Cont'd)

(b) Supplementary retirement benefits (Cont'd)

Net expense/(net income) recognised as staff cost/(other income) in the income statement comprises:

	2005	2004
Interest cost	239	219
Actuarial gain recognised	—	(495)
Net expense/(net income)	<u>239</u>	<u>(276)</u>

Actuarial gain recognised in the year ended 31 December 2004 arose mainly from the change in the discount rate.

Principal actuarial assumptions at the balance sheet date are as follows:

	2005	2004
Discount rate	3.50%	4.75%
Health care cost increases	7.00%	7.00%
Average expected future lifetime of Eligible Employees	<u>15.1 years</u>	<u>15.5 years</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

26 SUBORDINATED BONDS ISSUED

During the year ended 31 December 2004, the Group issued the following subordinated bonds upon the approval of the PBOC and the CBRC. The carrying value of the Group's subordinated bonds at the balance sheet date represents:

	Note	2005	2004
4.87% subordinated fixed rate bonds maturing in August 2014	(i)	11,140	11,140
Subordinated floating rate bonds maturing in August 2014	(ii)	3,860	3,860
4.95% subordinated convertible fixed rate bonds maturing in September 2014	(iii)	8,300	8,300
Subordinated floating rate bonds maturing in December 2014	(iv)	6,078	6,078
4.95% subordinated convertible fixed rate bonds maturing in December 2014	(v)	10,622	10,622
Total nominal value		40,000	40,000
Less: Unamortised issue cost		(93)	(104)
Net carrying value		39,907	39,896

Notes:

- (i) The interest rate per annum on the subordinated fixed rate bonds is 4.87%. The Group has an option to redeem the bonds on 1 August 2009. If they are not redeemed early, the interest rate of the bonds will increase in August 2009 to 7.67% per annum for the next five years.
- (ii) The interest rate per annum on the subordinated floating rate bonds is the PBOC one-year fixed deposit rate, which is reset annually, plus an interest margin of 2.00%. The Group has an option to redeem the bonds on 1 August 2009. If they are not redeemed early, the interest margin of the bonds will increase to 2.75% from August 2009 for the next five years.
- (iii) The interest rate per annum on the subordinated convertible fixed rate bonds is 4.95%. The bondholders may convert the interest rate into a floating rate, being the PBOC one-year fixed deposit rate plus an interest margin of 1.80%, on 22 September 2006. The interest rate is reset annually. The Group has an option to redeem the bonds on 22 September 2009. Fixed rate bonds not redeemed early by the Group on 22 September 2009 will start to pay 7.95% per annum for the next five years. For floating rate bonds not redeemed early by the Group on 22 September 2009, the interest margin of the bonds will increase to 2.80% for the next five years.
- (iv) The interest rate per annum on the subordinated floating rate bonds is the benchmark rate plus an interest margin of 2.00%. The benchmark rate is the PRC interbank money market 7-days repo rate, which is reset and payable every six months. The Group has an option to redeem the bonds on 27 December 2009. If they are not redeemed early, the interest margin of the bonds will increase to 3.00% from December 2009 for the next five years.
- (v) The interest rate per annum on the subordinated convertible fixed rate bonds is 4.95%. The bondholders may convert the interest rate into a floating rate, being the PBOC one-year fixed deposit rate plus an interest margin of 1.80%, on 27 December 2006. The interest rate is reset annually. The Group has an option to redeem the bonds on 27 December 2009. Fixed rate bonds not redeemed early by the Group on 27 December 2009 will start to pay 7.95% per annum for the next five years. For floating rate bonds not redeemed by the Group on 27 December 2009, the interest margin of the bonds will increase to 2.80% for the next five years.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

27 EQUITY

(a) Share capital

	2005		2004	
	No. of shares	Amount	No. of shares	Amount
Registered, issued and fully paid:				
<i>Ordinary shares of RMB 1 each</i>				
At 1 January	194,230	194,230	—	—
Shares issued	<u>30,459</u>	<u>30,459</u>	<u>194,230</u>	<u>194,230</u>
At 31 December	<u>224,689</u>	<u>224,689</u>	<u>194,230</u>	<u>194,230</u>

On 17 September 2004, the Bank was incorporated with a registered and paid up capital of RMB 194,230 million divided into 194,230 million shares with a par value of RMB 1 each. 186,230 million shares were issued to Huijin and Jianyin in consideration for the business transferred to the Bank, and 8,000 million shares were issued to other promoters at RMB 1 per share for cash. These shares are collectively referred to as Original Unlisted Shares.

The conversion of the Bank's Original Unlisted Shares into H shares was approved by its shareholders in general meetings on 5 June 2005 and 6 June 2005, and by the State Council and the China Securities Regulatory Commission on 9 June 2005 and 20 September 2005 respectively. Upon completion of the IPO on 27 October 2005, all the Original Unlisted Shares were converted into H shares which are listed on the SEHK.

On 27 October 2005, a total of 26,486 million H shares with a par value of RMB 1 each were issued by the Bank at a subscription price of HK\$ 2.35 per share as part of the IPO.

On 14 November 2005, a total of 3,973 million H shares with a par value of RMB 1 each were issued by the Bank at a subscription price of HK\$ 2.35 per share as a result of the exercise of the over-allotment option.

All H shares are ordinary shares and rank pari passu with the same rights and benefits.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

27 EQUITY (Cont'd)

(b) Capital reserve

Capital reserve generally records transactions of the following nature:

- (i) share premium arising from the issuance of shares at prices in excess of their par value; and
- (ii) any other item required by PRC regulations to be so treated.

Capital reserve may be used for increasing paid-in capital as approved by the shareholders.

	2005
Gross proceeds upon issue of shares	74,639
Shares at par value	<u>(30,459)</u>
Share premium before costs of issuing shares	44,180
Costs of issuing shares	<u>(2,089)</u>
Share premium recognised in capital reserve	<u>42,091</u>

As described in Note 27(a), the Bank issued a total of 30,459 million ordinary shares of RMB 1 each at a total consideration of RMB 74,639 million in 2005. After accounting for interest income and costs directly associated with the share issues, the Bank credited the share premium of RMB 42,091 million to the capital reserve.

(c) Surplus reserves

Surplus reserves consist of statutory surplus reserve, discretionary surplus reserve and statutory public welfare fund.

- (i) *Statutory surplus reserve and discretionary surplus reserve*

The Bank is required to appropriate 10% of its net profit, as determined under the Accounting Standards for Business Enterprises, the *Accounting Regulations for Financial Enterprises* (2001) and other relevant regulations issued by the MOF (collectively "PRC GAAP"), to the statutory surplus reserve until the reserve balance reaches 50% of the registered capital. After making the appropriation to the statutory surplus reserve, the Bank may also appropriate its net profit to the discretionary surplus reserve upon approval by shareholders in general meeting.

Subject to the approval of shareholders, statutory and discretionary surplus reserves may be used to make good prior year losses, if any, and may be converted into capital, provided that the balance of statutory surplus reserve after such capitalisation is not less than 25% of the registered capital before such capitalisation.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

27 EQUITY (Cont'd)

(c) Surplus reserves (Cont'd)

(ii) Statutory public welfare fund

Prior to 1 January 2006, the Bank is required to appropriate 5% to 10% of its net profit, as determined under PRC GAAP, to the statutory public welfare fund. In accordance with *The Company Law of the PRC (Revised in 2005)*, which was issued on 27 October 2005 and effective from 1 January 2006, the Bank is no longer required to make further appropriation to the statutory public welfare fund with effect from 1 January 2006.

This fund can only be used to purchase capital items for the collective benefit of the Bank's employees such as the construction of canteen and other staff welfare facilities.

The fund is non-distributable other than in liquidation.

(d) Investment revaluation reserve

Investment revaluation reserve has been accounted for in accordance with the accounting policies adopted for the measurement of the available-for-sale investments at fair value.

(e) General reserve

The general reserve at 31 December 2005 comprises:

(i) An amount of RMB 10,284 million set up under the MOF's requirements

Pursuant to a notice, Cai Jin [2005] No. 49, issued by the MOF on 17 May 2005 and which became effective on 1 July 2005, banks and certain non-bank financial institutions in Mainland China, including the Bank, are required to maintain a general reserve (in addition to allowances for impairment losses) to cover potential losses against their assets. The general reserve is in principle not less than 1% of the aggregate amount of risk-bearing assets, before allowances for impairment losses, at the balance sheet date. The general reserve forms part of the equity of the financial institution, and transfers to it are made through appropriations of profit after taxation.

The MOF issued another notice, Cai Jin [2005] No. 90 on 5 September 2005. This notice requires financial institutions to set aside the required general reserve within a transitional period of approximately three years, but not more than five years, from 1 July 2005. Management consider that the Bank will comply with the requirements of these notices before 30 June 2010.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

27 EQUITY (Cont'd)

(e) General reserve (Cont'd)

- (ii) *An amount of RMB 48 million set up under requirements of the Hong Kong Banking Ordinance*

Paragraph 9 of the Seventh Schedule to the Hong Kong Banking Ordinance requires the Bank's Hong Kong Branch to set aside amounts in a regulatory reserve in respect of losses which it will, or may, incur on loans and advances to customers, in addition to impairment losses recognised in accordance with the accounting policies of the Group. Transfers to and from the regulatory reserve are made directly through retained earnings.

(f) Exchange reserve

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

28 PROFIT DISTRIBUTIONS

(a) Profit distributions for the year ended 31 December 2005

The Bank's profit appropriations for the year ended 31 December 2005 are as follows:

	For the six months ended		For the	Total
	30 June 2005	31 December 2005	six months ended 31 December 2005	
	(note (i))	(note (ii))	(note (ii))	
Appropriations to				
— Statutory surplus reserve	1,931	—	2,060	3,991
— Statutory public welfare fund	966	—	1,030	1,996
— General reserve (Note 27(e))	—	312	10,020	10,332
	<u>2,897</u>	<u>312</u>	<u>13,110</u>	<u>16,319</u>
Profit distributions				
— settlement of government receivable	23,781	—	—	23,781
— interim dividend declared during the year	—	168	—	168
— special dividend declared during the year	—	—	3,100	3,100
	<u>23,781</u>	<u>168</u>	<u>3,100</u>	<u>27,049</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

28 PROFIT DISTRIBUTIONS (Cont'd)

(a) Profit distributions for the year ended 31 December 2005 (Cont'd)

Notes:

- (i) At the general meeting of shareholders held on 6 June 2005, the shareholders approved the Bank's profit distribution policy for the six months ended 30 June 2005. On 27 August 2005, the Bank's shareholders confirmed the amounts of the Bank's profit appropriations for the six months ended 30 June 2005.

The Bank appropriated 10% and 5% of its adjusted net profit for the six months ended 30 June 2005, which is calculated as if no income tax exemption was granted to the Bank, to the statutory surplus reserve and statutory public welfare fund respectively. The Bank's external legal counsel has confirmed the appropriateness of such basis of calculation. No appropriation was made to the discretionary surplus reserve.

- (ii) The shareholders approved the following profit appropriations of the Bank for the year ending 31 December 2005 at the extraordinary general meeting held on 27 August 2005:

(ii-1) The Bank appropriates 65% of its retained earnings of RMB 480 million, which is determined under PRC GAAP, as at 30 June 2005 to the general reserve. The remaining 35% of the retained earnings, or RMB 168 million, will be distributed to the five promoters in the form of cash dividend;

(ii-2) The Bank appropriates 50%, 10% and 5% of its profit after tax, under PRC GAAP, for the six months ending 31 December 2005 to the general reserve, statutory surplus reserve and statutory public welfare fund respectively;

(ii-3) RMB 3,100 million of the profit after tax for the period from and including 1 July 2005 to 26 October 2005, being the date immediately preceding the first date when the Bank's shares were listed (the "listing date"), was distributed in the form of cash dividend (the "special dividend") to those shareholders immediately preceding the listing date; and

(ii-4) 35% of the profit after tax for the six months ending 31 December 2005, as determined under PRC GAAP or IFRS, whichever is lower, less the special dividend, will be distributed in the form of cash dividend to the Bank's shareholders as at the relevant record date.

On 6 April 2006 the Directors proposed a final cash dividend of RMB 0.015 per share in respect of the year ended 31 December 2005. Subject to the agreement of the shareholders in the Annual General Meeting to be held on 15 June 2006, the total amount of approximately RMB 3,370 million is payable to those on the register of shareholders as of 22 May 2006. This dividend has not been recognised as a liability at the balance sheet date (Note 37).

- (iii) In the preparation of the Bank's PRC statutory financial statements for the year ended 31 December 2005, the Bank changed its accounting policies mainly relating to the measurement and recognition of financial assets, and the new accounting policies have been applied retrospectively. The change in accounting policies resulted in an increase of the Bank's retained earnings, as determined under PRC GAAP, as at 31 December 2004. The Bank accordingly increased its appropriations to the statutory surplus reserve and the statutory public welfare fund by RMB 65 million and RMB 33 million respectively in 2005.

(b) Distributability of reserves

At 31 December 2005, the aggregate amount of reserves available for distribution to shareholders of the Bank was RMB 4,607 million (2004: RMB 1,018 million).

(c) Profit attributable to shareholders of the Bank

The consolidated profit attributable to shareholders of the Bank includes a profit of RMB 46,957 million (2004: RMB 49,033 million) which has been dealt with in the financial statements of the Bank.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

29 NOTES TO CONSOLIDATED CASH FLOW STATEMENT

(a) Cash and cash equivalents

	2005	2004
Cash	28,413	27,080
Surplus deposit reserve funds	108,395	123,540
Amounts due from banks and non-bank financial institutions	190,108	112,531
Less:		
— amounts due over three months when acquired	(32,362)	(6,023)
— balances under resale agreements	(13,797)	(37,022)
	143,949	69,486
Total	280,757	220,106

(b) Significant non-cash transactions

- (i) Transfer of the receivable arising from the liquidation of a trust and investment company by a bill of nominal value of RMB 21,000 million issued by the PBOC in 2004 (Notes 18(a) and 24(b)).
- (ii) Settlement of the interest receivable arising from the Group's investment in the special government bond in 2004 (Note 18(a)).
- (iii) Settlement of the government receivable in 2004 and 2005 (Notes 21(d) and 28(a)).

(c) Investment in a new subsidiary

CCB Principal was established by the Bank, Principal Financial Services, Inc and China Huadian Group Corporation in 2005. On 19 September 2005 the Bank and the above two shareholders of CCB Principal paid cash of RMB 130 million and RMB 70 million as the initial capital of CCB Principal respectively. The Bank owns 65% of CCB Principal's registered capital at 31 December 2005.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

30 COMMITMENTS AND CONTINGENT LIABILITIES

(a) Credit commitments

At any given time the Group has outstanding commitments to extend credit. These commitments take the form of approved loans and credit card limits.

The Group provides financial guarantees and letters of credit to guarantee the performance of customers to third parties.

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers. The Group expects most acceptances to be settled simultaneously with the reimbursement from the customers.

The contractual amounts of commitments and contingent liabilities are set out in the following table by category. The amounts reflected in the table for commitments assume that amounts are fully advanced. The amount reflected in the table for guarantees and letters of credit represents the maximum potential loss that would be recognised at the balance sheet date if counterparties failed completely to perform as contracted.

	2005	2004
Contractual amount		
Loan commitments		
— with an original maturity of under one year	16,961	24,397
— with an original maturity of one year or over	144,871	140,471
	<u>161,832</u>	<u>164,868</u>
Guarantees and letters of credit	183,638	136,481
Acceptances	138,826	113,073
Credit card commitments	37,421	25,044
Others	20,429	771
	<u>542,146</u>	<u>440,237</u>

These commitments and contingent liabilities have off-balance sheet credit risk. Before the commitments are fulfilled or expire, management assess and make allowances for any probable losses accordingly. As the facilities may expire without being drawn upon, the total of the contractual amounts is not representative of expected future cash outflows.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

30 COMMITMENTS AND CONTINGENT LIABILITIES (Cont'd)

(a) Credit commitments (Cont'd)

Credit risk weighted amount of contingent liabilities and commitments

	2005	2004
Contingent liabilities and commitments	<u>242,057</u>	<u>203,201</u>

The credit risk weighted amount refers to the amount as computed in accordance with the rules set out by the CBRC and depends on the status of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% of contingent liabilities and commitments.

There are no relevant standards prescribed by IFRS in calculating the above credit risk weighted amounts.

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

(b) Capital commitments

The Group had the following authorised capital commitments at the balance sheet date:

	2005	2004
Purchase of property and equipment		
— Contracted for	296	777
— Not contracted for	<u>967</u>	<u>1,528</u>
Total	<u>1,263</u>	<u>2,305</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

30 COMMITMENTS AND CONTINGENT LIABILITIES (Cont'd)

(c) Operating lease commitments

The Group leases certain properties under operating leases, which typically run for an initial period of one to five years and may include an option to renew the lease when all terms are renegotiated. At the balance sheet date, the Group's future minimum lease payments under non-cancellable operating leases for premises were as follows:

	2005	2004
Within one year	1,387	956
After one year but within five years	3,020	2,234
After five years	1,087	942
Total	5,494	4,132

(d) Outstanding litigation and disputes

As at 31 December 2005, the Group was the defendant in certain pending litigations and disputes with gross claims of RMB 2,607 million (2004: RMB 3,268 million). Provision has been made for the estimated losses of these litigations based upon the opinions of the Group's internal and external legal counsel (Note 24(c)). The Group considers that the provisions made are reasonable and adequate.

(e) Underwriting obligations

At the balance sheet date, the unexpired underwriting commitments of PRC government bonds were as follows:

	2005	2004
Underwriting obligations	1,980	6,870

(f) Redemption obligations

As an underwriting agent of PRC government bonds, the Group has the responsibility to buy back those bonds sold by it should the holders decide to early redeem the bonds held. The redemption price for the bonds at any time before their maturity date is based on the coupon value plus any interest unpaid and accrued up to the redemption date. Accrued interest payables to the bond holders are calculated in accordance with relevant rules of the MOF and the PBOC. The redemption price may be different from the fair value of similar instruments traded at the redemption date.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

30 COMMITMENTS AND CONTINGENT LIABILITIES (Cont'd)

(f) Redemption obligations (Cont'd)

The redemption obligations below represent the nominal value of government bonds underwritten and sold by the Group, but not yet matured at the balance sheet date:

	2005	2004
Redemption obligations	<u>102,079</u>	<u>97,158</u>

The Group expects the amount of redemption before the maturity date of these government bonds through the Group will not be material.

(g) Provision against commitments and contingent liabilities

The Group has assessed and made provision for any probable outflow of economic benefits in relation to the above commitments and contingent liabilities in accordance with the accounting policies. Except for the provisions made against outstanding litigations and disputes (Note 24(c)), the Group has not made other provisions in respect of the above commitments and contingent liabilities at the balance sheet date.

31 ASSETS PLEDGED AS SECURITY

The following assets have been pledged as security for bills rediscounting transactions and securities sold under repurchase agreements. The related secured liabilities are recorded as amounts due to central banks, or banks and non-bank financial institutions of approximately similar carrying value at the balance sheet date.

	2005	2004
Available-for-sale debt securities	20,882	—
Discounted bills	<u>—</u>	<u>125</u>
Total	<u>20,882</u>	<u>125</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

32 ENTRUSTED LENDING BUSINESS

The Group provides entrusted lending business services to government agencies and corporations. All entrusted loans are made under the instruction or at the direction of these entities and are funded by entrusted funds from them.

For entrusted assets and liabilities and entrusted provident housing fund mortgage business, the Group generally does not take on credit risk in relation to these transactions. The Group acts as an agent to hold and manage these assets and liabilities at the direction of the entrustor and receives fee income for the services provided.

Trust assets are not assets of the Group and are not recognised in the balance sheet. Surplus funding is accounted for as deposits from customers. Income received and receivable for providing these services is included in the income statement as fee income.

At the balance sheet date, the entrusted assets and liabilities were as follows:

	2005	2004
Entrusted loans	<u>255,012</u>	<u>194,418</u>
Entrusted funds	<u>255,012</u>	<u>194,418</u>

33 SEGMENT REPORTING

Segment information is presented in respect of the Group's business and geographical segments. Historically, the Group managed its business primarily along geographical locations. In recent years, the Group has begun to reorganise the management structure along the business segments of corporate banking, personal banking and treasury business. This new management structure, upon full implementation, is expected to enhance the Group's ability to assess and monitor the financial performance of business segments. During the year ended 31 December 2005, the Group has been in a transitional phase of reorganisation in which it has managed its business both along business segments and geographical segments. Accordingly, both business and geographical segment information are presented as the Group's primary segment reporting formats.

Measurement of segment assets and liabilities and segment revenues and results is based on the Group's accounting policies.

Transactions between segments are conducted under normal commercial terms and conditions. Internal charges and transfer pricing adjustments are determined with reference to market rates and have been reflected in the performance of each segment. Net interest income and expenses arising on internal charges and transfer pricing adjustments are referred to as "internal net interest income/expenses". Interest income and expenses earned from third parties are referred to as "external net interest income/expenses".

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

33 SEGMENT REPORTING (Cont'd)

Segment revenues, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Segment revenue, expenses, assets, and liabilities are determined before intra-group balances and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between Group entities within a single segment. Segment capital expenditure is the total cost incurred during the year to acquire segment assets (both tangible and intangible) that are expected to be used for more than one year.

(a) Business segments

The Group comprises the following main business segments:

Corporate banking

This segment represents the provision of a range of financial products and services to corporations, government agencies and financial institutions. The products and services include corporate loans, trade financing, deposit taking activities, agency services, consulting and advisory services, cash management services, remittance and settlement services, custody services and guarantee services.

Personal banking

This segment represents the provision of a range of financial products and services to individual customers. The products and services comprise personal loans, deposit taking activities, card business, personal wealth management services, remittance services and securities agency services.

Treasury business

This segment covers the Group's treasury operations. The treasury enters into inter-bank money market transactions and repurchase transactions, and invests in debt instruments. It also trades in debt instruments, derivatives and foreign currency for its own account. The treasury carries out customer driven derivatives, foreign currency and precious metal trading. Its function also includes the management of the Group's overall liquidity position, including the issuance of subordinated bonds.

Others and unallocated

These represent equity investments, overseas operations and head office assets, liabilities, income and expenses that are not directly attributable to a segment or cannot be allocated on a reasonable basis.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

33 SEGMENT REPORTING (Cont'd)

(a) Business segments (Cont'd)

	Corporate banking	Personal banking	2005		Elimination	Total
			Treasury business	Others and unallocated		
External net interest income/ (expense)	86,375	(7,342)	36,504	1,014	—	116,551
Internal net interest (expense)/income	(21,869)	36,875	(13,799)	(1,207)	—	—
Net interest income/ (expense)	64,506	29,533	22,705	(193)	—	116,551
Net fee and commission income/(expense)	3,176	4,133	1,154	(8)	—	8,455
Dividend income	—	—	—	546	—	546
Net gain arising from dealing securities	—	—	451	4	—	455
Net gain arising from investment securities	—	—	913	1,014	—	1,927
Net loss arising from foreign currency dealing	—	—	(1,259)	(47)	—	(1,306)
Other income	751	147	—	1,188	—	2,086
Operating income	68,433	33,813	23,964	2,504	—	128,714
General and administrative expenses						
— depreciation and amortisation	(1,723)	(2,383)	(674)	(1,906)	—	(6,686)
— others	(19,245)	(18,109)	(4,009)	(10,043)	—	(51,406)
	(20,968)	(20,492)	(4,683)	(11,949)	—	(58,092)
Provisions for impairment losses	(11,953)	(2,258)	(9)	(1,038)	—	(15,258)
Operating expenses	(32,921)	(22,750)	(4,692)	(12,987)	—	(73,350)
Profit/(loss) before tax	35,512	11,063	19,272	(10,483)	—	55,364
Capital expenditure	1,503	3,544	206	3,511	—	8,764
Segment assets	2,240,910	493,493	1,664,996	215,578	(29,235)	4,585,742
Segment liabilities	2,041,994	2,105,639	73,935	105,732	(29,235)	4,298,065

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

33 SEGMENT REPORTING (Cont'd)

(a) Business segments (Cont'd)

	2004				Elimination	Total
	Corporate banking	Personal banking	Treasury business	Others and unallocated		
External net interest income/ (expense)	75,488	(3,938)	29,225	713	—	101,488
Internal net interest (expense)/income	(13,113)	31,917	(16,534)	(2,270)	—	—
Net interest income/ (expense)	62,375	27,979	12,691	(1,557)	—	101,488
Net fee and commission income/(expense)	2,786	3,248	580	(143)	—	6,471
Dividend income	—	—	—	777	—	777
Net gain arising from dealing securities	—	—	296	10	—	306
Net gain arising from investment securities	—	—	1,080	1,621	—	2,701
Net gain arising from foreign currency dealing	—	—	500	9	—	509
Other income	251	10	—	1,463	—	1,724
Operating income	65,412	31,237	15,147	2,180	—	113,976
General and administrative expenses						
— depreciation and amortisation	(2,081)	(3,327)	(242)	(2,882)	—	(8,532)
— others	(19,757)	(12,912)	(3,461)	(8,757)	—	(44,887)
	(21,838)	(16,239)	(3,703)	(11,639)	—	(53,419)
Provisions for impairment losses	(4,868)	(1,621)	(220)	(2,649)	—	(9,358)
Operating expenses	(26,706)	(17,860)	(3,923)	(14,288)	—	(62,777)
Profit/(loss) before tax	38,706	13,377	11,224	(12,108)	—	51,199
Capital expenditure	1,569	2,509	183	2,168	—	6,429
Segment assets	2,062,841	438,260	1,279,176	156,393	(26,750)	3,909,920
Segment liabilities	1,936,788	1,653,998	52,391	97,942	(26,750)	3,714,369

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

33 SEGMENT REPORTING (Cont'd)

(b) Geographical segments

The Group operates principally in Mainland China with branches located in 31 provinces, autonomous regions and municipalities directly under the central government, and two subsidiaries located in Bohai Rim. The Group also has bank branch operations outside Mainland China in Hong Kong, Singapore, Frankfurt, Johannesburg, Tokyo and Seoul, and subsidiaries operating in Hong Kong.

In presenting information on the basis of geographical segments, operating income is allocated based on the location of the branches and subsidiaries that generated the revenue. Segment assets and capital expenditure are allocated based on the geographical location of the underlying assets.

Geographical segments, as defined for management reporting purposes, are as follows:

- “Yangtze River Delta” refers to the following areas serviced by the tier-1 branches of the Group: Shanghai Municipality, Jiangsu Province, Zhejiang Province, City of Ningbo and City of Suzhou;
- “Pearl River Delta” refers to the following areas serviced by the tier-1 branches of the Group: Guangdong Province, City of Shenzhen, Fujian Province and City of Xiamen;
- “Bohai Rim” refers to the following areas serviced by the subsidiaries and tier-1 branches of the Group: Beijing Municipality, Shandong Province, Tianjin Municipality, Hebei Province and City of Qingdao;
- the “Central” region refers to the following areas serviced by the tier-1 branches of the Group: Shanxi Province, Guangxi Autonomous Region, Hubei Province, Henan Province, Hunan Province, Jiangxi Province, Hainan Province, Anhui Province and the Three Gorges Area;
- the “Western” region refers to the following areas serviced by the tier-1 branches of the Group: Sichuan Province, Chongqing Municipality, Guizhou Province, Yunnan Province, Tibet Autonomous Region, Inner Mongolia Autonomous Region, Shaanxi Province, Gansu Province, Qinghai Province, Ningxia Autonomous Region and Xinjiang Autonomous Region; and
- the “Northeastern” region refers to the following areas serviced by the tier-1 branches of the Group: Liaoning Province, Jilin Province, Heilongjiang Province and City of Dalian.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

33 SEGMENT REPORTING (Cont'd)

(b) Geographical segments (Cont'd)

	Yangtze River Delta	Pearl River Delta	Bohai Rim	Central	Western	2005 North- eastern	Head office	Overseas	Elimination	Total
External net interest income	21,877	8,203	13,591	11,994	12,608	2,982	44,056	1,240	—	116,551
Internal net interest income/(expense)	4,766	6,272	7,584	5,599	5,715	3,376	(32,684)	(628)	—	—
Net interest income	26,643	14,475	21,175	17,593	18,323	6,358	11,372	612	—	116,551
Net fee and commission income	1,833	1,606	1,426	1,419	1,120	548	430	73	—	8,455
Dividend income	15	17	33	237	57	109	78	—	—	546
Net gain arising from dealing securities	—	—	—	—	—	—	451	4	—	455
Net gain arising from investment securities	41	109	176	325	43	80	1,070	83	—	1,927
Net gain/(loss) arising from foreign currency dealing	43	(10)	51	21	8	21	(1,393)	(47)	—	(1,306)
Other income	200	297	158	264	477	170	274	246	—	2,086
Operating income	28,775	16,494	23,019	19,859	20,028	7,286	12,282	971	—	128,714
General and administrative expenses										
— depreciation and amortisation	(1,265)	(957)	(1,047)	(1,231)	(1,075)	(523)	(570)	(18)	—	(6,686)
— others	(10,069)	(7,270)	(9,154)	(9,871)	(9,071)	(4,279)	(1,382)	(310)	—	(51,406)
Provisions for impairment losses	(11,334)	(8,227)	(10,201)	(11,102)	(10,146)	(4,802)	(1,952)	(328)	—	(58,092)
Operating expenses	(13,204)	(10,771)	(13,599)	(13,880)	(13,497)	(5,846)	(2,217)	(336)	—	(73,350)
Profit before tax	15,571	5,723	9,420	5,979	6,531	1,440	10,065	635	—	55,364
Capital expenditure	1,523	925	1,242	1,106	1,093	555	2,203	117	—	8,764
Segment assets	863,654	643,197	857,832	703,969	684,549	328,658	1,886,307	68,561	(1,450,985)	4,585,742
Segment liabilities	860,461	642,324	855,680	703,607	684,500	328,913	1,606,345	67,220	(1,450,985)	4,298,065
Off-balance sheet credit commitments	148,964	67,183	92,659	93,666	77,747	32,880	14,279	14,768	—	542,146

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

33 SEGMENT REPORTING (Cont'd)

(b) Geographical segments (Cont'd)

	Yangtze River Delta	Pearl River Delta	Bohai Rim	Central	2004		Head office	Overseas	Elimination	Total
					Western	North- eastern				
External net interest income	17,266	7,327	8,779	8,856	11,293	2,623	44,617	727	—	101,488
Internal net interest income/ (expense)	5,542	6,250	10,980	6,217	5,691	3,341	(38,059)	38	—	—
Net interest income	22,808	13,577	19,759	15,073	16,984	5,964	6,558	765	—	101,488
Net fee and commission income	1,348	1,261	1,184	1,138	890	504	38	108	—	6,471
Dividend income	81	106	64	288	100	38	98	2	—	777
Net gain arising from dealing securities	—	—	—	—	1	—	295	10	—	306
Net gain arising from investment securities	18	63	32	45	13	14	2,513	3	—	2,701
Net gain arising from foreign currency dealing	52	86	85	44	23	30	180	9	—	509
Other income	275	190	224	278	278	68	342	69	—	1,724
Operating income	24,582	15,283	21,348	16,866	18,289	6,618	10,024	966	—	113,976
General and administrative expenses										
— depreciation and amortisation	(1,590)	(1,279)	(1,501)	(1,629)	(1,464)	(745)	(297)	(27)	—	(8,532)
— others	(7,728)	(6,434)	(7,669)	(8,856)	(8,607)	(4,183)	(1,121)	(289)	—	(44,887)
Provisions for impairment losses	(9,318)	(7,713)	(9,170)	(10,485)	(10,071)	(4,928)	(1,418)	(316)	—	(53,419)
Operating expenses	(9,783)	(9,168)	(10,625)	(11,972)	(13,907)	(5,251)	(1,721)	(350)	—	(62,777)
Profit before tax	14,799	6,115	10,723	4,894	4,382	1,367	8,303	616	—	51,199
Capital expenditure	1,170	869	1,000	1,160	913	398	904	15	—	6,429
Segment assets	752,004	559,086	734,521	619,657	608,884	289,589	1,444,466	62,446	(1,160,733)	3,909,920
Segment liabilities	748,983	558,583	732,385	619,167	609,618	289,252	1,254,883	62,231	(1,160,733)	3,714,369
Off-balance sheet credit commitments	117,568	49,774	75,535	75,709	66,228	20,837	19,999	14,587	—	440,237

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT

(a) Credit risk

Credit risk represents the potential loss that may arise from the failure of a debtor to meet its obligation or commitment to the Group. It arises primarily from the Group's credit asset portfolios.

To identify, evaluate, monitor and manage credit risk, the Group designs the particular organisation framework, credit policies and processes required for effective credit risk management, which have been implemented in the whole Group upon approval of the Risk Management and Internal Control Committee and of the President. The Risk Management and Internal Control Committee are responsible for supervising and evaluating the set-up, organisational structure, work process and effectiveness of various risk management functions. To mitigate risk, the Group may obtain collateral and guarantees where appropriate.

With respect to daily operations, the Risk Management Department, as directed by the Risk Management and Internal Control Committee, monitors, shares and coordinates the work of other risk management functions, including the Corporate Banking Department, the Housing Finance & Personal Lending Department, the Special Assets Resolution Department and the Legal Department.

In respect of the loans portfolios, the Group adopts a risk-based loan classification methodology and classifies loans into five categories: normal, special-mention, substandard, doubtful and loss. The last three categories are considered as impaired loans and advances for which objective evidence of impairment exists based on a loss event or several events and which bear significant impairment losses. The allowances for impairment losses for the impaired loans and advances are assessed collectively or individually as appropriate.

The definitions of the five categories of loans and advances are set out below:

Normal	Borrowers can honour the terms of their loans. There is no reason to doubt their ability to repay principal and interest in full on a timely basis.
Special mention	Borrowers are able to service their loans currently, although repayment may be adversely affected by specific factors.
Substandard	Borrowers' abilities to service their loans are in question as they cannot rely entirely on normal business revenues to repay principal and interest. Losses may ensue even when collateral or guarantees are invoked.
Doubtful	Borrowers cannot repay principal and interest in full and significant losses will need to be recognised even when collateral or guarantees are invoked.
Loss	Only a small portion or no principal and interest can be recovered after taking all possible measures and exhausting all legal remedies.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(a) Credit risk (Cont'd)

Loans and advances to customers analysed by economic sector concentrations at the balance sheet date are presented in the table below:

	2005		2004	
		%		%
Domestic operations				
Corporate loans				
— Manufacturing	433,104	17.87	396,631	18.08
— Transportation, storage and postal services	278,532	11.49	236,033	10.76
— Production and supply of electric power, gas and water	265,647	10.96	231,590	10.56
— Property development	256,396	10.58	244,036	11.12
— Construction	86,855	3.58	82,139	3.74
— Water, environment and public utility management	75,959	3.13	54,814	2.50
— Education	63,395	2.62	51,309	2.34
— Wholesale and retail trade	63,179	2.61	56,863	2.59
— Telecommunications, computer services and software	60,304	2.48	72,163	3.29
— Mining	49,332	2.04	52,637	2.40
— Other customers	143,088	5.90	146,204	6.66
Subtotal	1,775,791		1,624,419	
Personal loans	453,889	18.73	412,275	18.79
Discounted bills	194,122	8.01	157,275	7.17
Gross loans and advances to customers	2,423,802	100.00	2,193,969	100.00
Less: Allowances for impairment losses	(62,949)		(53,643)	
Net loans and advances to customers	2,360,853		2,140,326	

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(a) Credit risk (Cont'd)

	2005		2004	
		%		%
Overseas operations:				
Corporate loans				
— Manufacturing	8,550	24.71	5,432	16.24
— Transportation, storage and postal services	7,314	21.14	8,455	25.27
— Property development	4,984	14.41	5,055	15.11
— Telecommunications, computer services and software	4,379	12.66	5,065	15.14
— Production and supply of electric power, gas and water	1,652	4.78	907	2.71
— Wholesale and retail trade	1,225	3.54	1,050	3.14
— Construction	467	1.35	401	1.20
— Other customers	5,474	15.82	6,676	19.95
	<u>34,045</u>		<u>33,041</u>	
Subtotal	34,045		33,041	
Personal loans	364	1.05	372	1.11
Discounted bills	187	0.54	44	0.13
	<u>34,596</u>	<u>100.00</u>	<u>33,457</u>	<u>100.00</u>
Gross loans and advances to customers	34,596	100.00	33,457	100.00
Less: Allowances for impairment losses	<u>(136)</u>		<u>(221)</u>	
Net loans and advances to customers	<u>34,460</u>		<u>33,236</u>	
Total net loans and advances to customers	<u>2,395,313</u>		<u>2,173,562</u>	

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(a) Credit risk (Cont'd)

Loans and advances to customers analysed by geographical sector risk concentrations at the balance sheet date are presented in the table below:

	2005		2004	
		%		%
Yangtze River Delta	608,384	24.75	547,351	24.57
Pearl River Delta	328,399	13.36	288,515	12.95
Bohai Rim	494,216	20.10	457,796	20.55
Central	405,956	16.51	362,218	16.26
Western	398,664	16.22	357,460	16.05
Northeastern	152,762	6.21	136,689	6.15
Head office	35,421	1.44	43,940	1.97
Overseas	34,596	1.41	33,457	1.50
Gross loans and advances to customers	<u>2,458,398</u>	<u>100.00</u>	<u>2,227,426</u>	<u>100.00</u>
Less: Allowances for impairment losses	<u>(63,085)</u>		<u>(53,864)</u>	
Net loans and advances to customers	<u>2,395,313</u>		<u>2,173,562</u>	

See Note 33(b) for the definitions of geographical segments.

The table below shows a breakdown of total credit extended by the Group by type of collaterals:

	2005	2004
Loans secured by monetary assets	202,546	163,452
Loans secured by tangible assets, other than monetary assets	935,706	790,675
Guaranteed loans	633,180	662,237
Unsecured loans	<u>686,966</u>	<u>611,062</u>
Gross loans and advances to customers	<u>2,458,398</u>	<u>2,227,426</u>
Less: Allowances for impairment losses	<u>(63,085)</u>	<u>(53,864)</u>
Net loans and advances to customers	<u>2,395,313</u>	<u>2,173,562</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(b) Market risk

Market risk is the risk of loss, in respect of the Group's on and off-balance sheet activities, arising from adverse movements in market rates including interest rates, foreign exchange rates and stock prices etc. Market risk would arise from both the Group's trading and non-trading business.

The Risk Management Department is responsible for formulating the Group's market risk management policies, and managing its overall market risk exposures. The Asset and Liability Management Department ("ALM") of the Bank is responsible for managing the size and structure of the balance sheet, and risk of interest rates and foreign exchange rates, according to the Group's risk management policies. The Treasury Department manages the Bank's RMB and foreign currency investment portfolios, conducts proprietary and customer-driven trades, implements market risk management policies and rules and performs daily identification, measurement, assessment and control of risks.

Value-at-risk ("VaR") analysis, sensitivity analysis and stress testing are the key indicators used by the Group to measure and monitor the market risk of its trading business. Gap analysis and economic value added are the key indicators used by the Group to monitor the market risk of its non-trading business.

VaR is a technique which estimates the potential losses that could occur on risk positions taken, due to movements in market rates and prices over a specified time horizon and to a given level of confidence. The Treasury Department calculates interest rate VaR across its foreign currency debt investments. Currently, this technique is extending to debt investment portfolio denominated in RMB. It uses historical movements in market rates and prices, at 99% confidence level, with a 1-day holding period. VaR is calculated on a daily basis for foreign currency portfolios.

The results of stress testing are assessed against a set of forward-looking scenarios using stress moves in market variables, which are regularly reviewed.

Gap analysis is a technique to project future cash flows in order to quantify the differences, at all future dates, between assets and liabilities.

The Group considers that any market risk arising from its proprietary trading is not material.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(c) Interest rate risk

The Group's interest rate exposures mainly comprise those originating in its commercial banking structural interest rate exposure, and its trading positions.

(i) *Structural interest rate risk*

Interest rate risk is inherent in many of the Group's businesses and arises from factors such as differences in timing between contractual maturities or repricing of assets and liabilities.

ALM regularly monitors such interest rate risk positions. In terms of measuring and managing the risk, the Group regularly calculates interest rate gap and market value effect of these interest rate positions in different interest scenarios. The primary objective of such interest rate risk management is to limit potential adverse effects of interest rate movements on net interest income.

(ii) *Trading interest rate risk*

The major part of this risk arises from the treasury's investment portfolios. The interest rate risk is monitored using the VaR method described above. Complementary methods are also applied, to capture the sensitivities to interest rate movements, expressed as the fair value change due to one basis point (0.01%) change in interest rates.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(c) Interest rate risk (Cont'd)

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

	Effective interest rate (note (i))	Total	Non-interest bearing	2005			
				Less than three months	Between three months and one year	Between one and five years	More than five years
Assets							
Cash and balances with central banks	1.63%	480,136	28,413	451,723	—	—	—
Amounts due from banks and non-bank financial institutions	2.14%	190,108	—	147,801	42,031	276	—
Loans and advances to customers (note (ii))	5.39%	2,395,313	86	1,028,552	1,312,723	38,971	14,981
Investments	2.88%	1,413,871	11,672	140,108	420,801	621,237	220,053
Other	—	106,314	106,314	—	—	—	—
Total assets	4.14%	4,585,742	146,485	1,768,184	1,775,555	660,484	235,034
Liabilities							
Amounts due to central banks	1.89%	21	—	21	—	—	—
Amounts due to banks and non-bank financial institutions	1.77%	164,524	—	136,089	27,814	621	—
Deposits from customers	1.39%	4,006,046	40,789	2,770,313	905,529	276,616	12,799
Certificates of deposit issued	2.82%	5,429	—	4,198	527	704	—
Other	—	82,138	82,138	—	—	—	—
Subordinated bonds issued	4.63%	39,907	—	—	9,915	29,992	—
Total liabilities	1.44%	4,298,065	122,927	2,910,621	943,785	307,933	12,799
Asset-liability gap	2.70%	287,677	23,558	(1,142,437)	831,770	352,551	222,235

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(c) Interest rate risk (Cont'd)

	Effective interest rate (note (i))	Total	2004				
			Non-interest bearing	Less than three months	Between three months and one year	Between one and five years	More than five years
Assets							
Cash and balances with central banks	1.80%	399,366	27,080	372,286	—	—	—
Amounts due from banks and non-bank financial institutions	1.64%	112,531	—	111,215	1,008	308	—
Loans and advances to customers (note (ii))	5.18%	2,173,562	193	852,554	1,287,709	18,555	14,551
Investments	2.84%	1,107,636	16,355	120,771	236,426	544,450	189,634
Other	—	116,825	116,825	—	—	—	—
Total assets	4.09%	3,909,920	160,453	1,456,826	1,525,143	563,313	204,185
Liabilities							
Amounts due to central banks	1.91%	2,247	—	2,247	—	—	—
Amounts due to banks and non-bank financial institutions	1.63%	112,039	—	109,595	2,301	103	40
Deposits from customers	1.29%	3,491,121	42,004	2,565,071	631,210	236,133	16,703
Certificates of deposit issued	2.29%	3,741	—	2,715	644	382	—
Other	—	65,325	65,325	—	—	—	—
Subordinated bonds issued	4.73%	39,896	—	—	9,912	29,984	—
Total liabilities	1.32%	3,714,369	107,329	2,679,628	644,067	266,602	16,743
Asset-liability gap	2.77%	195,551	53,124	(1,222,802)	881,076	296,711	187,442

Notes:

(i) Effective interest rate represents the ratio of interest income/expense to average interest bearing assets/liabilities.

(ii) For loans and advances to customers, the above "Less than three months" category includes overdue amounts (net of allowances for impairment losses) of RMB 68,412 million as at 31 December 2005 (2004: RMB 73,999 million). Overdue amounts represent loans, of which the whole or part of the principals was overdue, or interest was overdue for more than 90 days but for which principal was not yet due.

(d) Currency risk

The Group's foreign exchange exposure mainly comprises exposures that arise from foreign currency portfolio within the treasury's proprietary investments and currency exposures originated by the Group's overseas branches.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(d) Currency risk (Cont'd)

The Group has invested the capital injection of USD 22,500 million in debt investments and money market instruments denominated in U.S. dollars. The investment portfolio is managed separately from other investments held by the Group. On 12 January 2005, the Bank entered into an agreement with Huijin, pursuant to which the Bank purchased from Huijin an option to sell to Huijin a maximum of USD 22,500 million in exchange for Renminbi at a pre-determined exchange rate of USD 1 to RMB 8.2769. The option is exercisable in 2007 in twelve equal monthly instalments. The Group will pay a total option premium of RMB 5,587 million to Huijin in twelve equal monthly instalments in 2007.

The option was purchased to hedge currency risk arising from the separate fund mentioned above. This option is qualified as a fair value hedge in accordance with IFRS. The change in the fair value of the option and the change in the fair value of the assets in the separate fund due to foreign exchange fluctuation are recognised as net (loss)/gain arising from foreign currency dealing.

The Group values the option using the Garman Kohlhagen Option model, which is commonly used by market participants to value currency options. The parameters used for the valuation include relevant market interest rates of RMB and USD, the spot exchange rates of RMB against USD sourced from the PBOC, and the foreign exchange volatility, which is based on that of non-deliverable forwards of RMB against USD, adjusted for the fact that the PRC foreign exchange market is regulated.

The fair value of the option as at 31 December 2005 was approximately RMB 9,545 million, which is included in other assets (Note 21(b)). The premium payable in respect of the option is stated at its discounted value of approximately RMB 5,348 million as at 31 December 2005 and is included under other liabilities and provisions (Note 24).

The change in the fair value of the option recognised as net (loss)/gain arising from foreign currency dealing for the year ended 31 December 2005 was approximately RMB 4,197 million.

On 5 December 2005, the Bank entered into a USD/RMB foreign currency swap with the PBOC pursuant to which the Bank will sell USD 8,969 million and buy RMB at a pre-determined forward rate on 7 December 2006 to cover the currency risk arising from certain assets denominated in U.S. dollars.

The unrealised loss of RMB 46 million has been recognised as net (loss)/gain arising from foreign currency dealing of the year ended 31 December 2005 and included in other liabilities and provisions as at 31 December 2005.

The Group manages other currency risk by spot and forward foreign exchange transactions and matching its foreign currency denominated assets with corresponding liabilities in the same currencies.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(d) Currency risk (Cont'd)

The Group's total equity is denominated in RMB, which is its functional currency. The currency exposures of the Group's assets and liabilities at the balance sheet date were as follows:

	2005			Total
	RMB	USD	Others	
Assets				
Cash and balances with central banks	473,590	4,260	2,286	480,136
Amounts due from banks and non-bank financial institutions	32,438	127,205	30,465	190,108
Loans and advances to customers	2,278,785	82,727	33,801	2,395,313
Investments	1,183,101	214,555	16,215	1,413,871
Other	99,871	4,970	1,473	106,314
Total assets	4,067,785	433,717	84,240	4,585,742
Liabilities				
Amounts due to central banks	21	—	—	21
Amounts due to banks and non-bank financial institutions	118,870	40,288	5,366	164,524
Deposits from customers	3,856,445	106,308	43,293	4,006,046
Certificates of deposit issued	—	377	5,052	5,429
Other	77,269	4,298	571	82,138
Subordinated bonds issued	39,907	—	—	39,907
Total liabilities	4,092,512	151,271	54,282	4,298,065
Net position	(24,727)	282,446	29,958	287,677
Notional amount of hedging currency option and foreign currency swap contracts	253,963	(253,963)	—	—
Off-balance sheet credit commitments	460,151	60,086	21,909	542,146

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(d) Currency risk (Cont'd)

	2004			Total
	RMB	USD	Others	
Assets				
Cash and balances with central banks	393,995	3,459	1,912	399,366
Amounts due from banks and non-bank financial institutions	47,461	59,080	5,990	112,531
Loans and advances to customers	2,054,975	78,777	39,810	2,173,562
Investments	903,463	188,147	16,026	1,107,636
Other	113,449	2,486	890	116,825
Total assets	<u>3,513,343</u>	<u>331,949</u>	<u>64,628</u>	<u>3,909,920</u>
Liabilities				
Amounts due to central banks	2,247	—	—	2,247
Amounts due to banks and non-bank financial institutions	83,437	15,254	13,348	112,039
Deposits from customers	3,364,350	96,690	30,081	3,491,121
Certificates of deposit issued	—	—	3,741	3,741
Other	60,071	3,418	1,836	65,325
Subordinated bonds issued	39,896	—	—	39,896
Total liabilities	<u>3,550,001</u>	<u>115,362</u>	<u>49,006</u>	<u>3,714,369</u>
Net position	<u>(36,658)</u>	<u>216,587</u>	<u>15,622</u>	<u>195,551</u>
Off-balance sheet credit commitments	<u>364,555</u>	<u>56,593</u>	<u>19,089</u>	<u>440,237</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(e) Liquidity risk

Liquidity risk is the risk that funds will not be available to meet liabilities as they fall due. It is caused by mismatches in the amount and maturity of assets and liabilities. At the local level, in line with policy, the day to day monitoring of future cash flows takes place and suitable levels of easily marketable assets are maintained by the businesses.

On the Group level, liquidity is managed through ALM. ALM is responsible for both regulatory and prudential liquidity. These are managed through the liquidity policies which are coordinated by ALM and include:

- optimising the Group's asset and liability structure with the principle of matching funding operations with its sources of income;
- maintenance of strong balance sheet liquidity ratios;
- projecting cash flows and assessing the level of liquid assets in relation thereto; and
- maintenance of sufficient surplus funds through internal transfer pricing.

A substantial portion of the Group's assets are funded by customer deposits made up of savings accounts and other short-term deposits. These customer deposits, which have been growing in recent years, are widely diversified by type and maturity and represent a stable source of funds.

In terms of measuring liquidity risk, the Group principally uses liquidity gap analysis, although currently such analysis is restricted to cash flow projections of within one year. Different scenarios are then applied to assess the impact on both trading and client businesses.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(e) Liquidity risk (Cont'd)

The following tables provide an analysis of the assets and liabilities of the Group into relevant maturity groupings based on the remaining periods to repayment at the balance sheet date.

	2005						Total
	Overdue/ repayable on demand	Less than three months	Between three months and one year	Between one and five years	More than five years	Undated	
Assets							
Cash and balances with central banks (note (i))	136,808	57,370	—	—	—	285,958	480,136
Amounts due from banks and non-bank financial institutions	11,379	136,422	42,031	276	—	—	190,108
Loans and advances to customers (note (ii))	71,195	332,389	783,035	657,218	551,476	—	2,395,313
Investments							
— Receivables	—	—	30,482	349,457	63,790	—	443,729
— Held-to-maturity debt securities	—	67,346	135,556	315,950	125,126	—	643,978
— Available-for-sale investments	—	17,932	138,310	76,353	79,464	11,672	323,731
— Debt securities at fair value through profit or loss (note (iii))	—	—	828	977	628	—	2,433
Other	2,948	10,161	8,295	12,149	508	72,253	106,314
Total assets	222,330	621,620	1,138,537	1,412,380	820,992	369,883	4,585,742
Liabilities							
Amounts due to central banks	21	—	—	—	—	—	21
Amounts due to banks and non-bank financial institutions	85,860	50,229	27,814	621	—	—	164,524
Deposits from customers	2,226,495	583,304	904,671	277,301	14,275	—	4,006,046
Certificates of deposit issued	—	420	2,018	2,991	—	—	5,429
Other	28,204	16,474	21,063	11,697	4,700	—	82,138
Subordinated bonds issued	—	—	—	—	39,907	—	39,907
Total liabilities	2,340,580	650,427	955,566	292,610	58,882	—	4,298,065
Long/(short) position	(2,118,250)	(28,807)	182,971	1,119,770	762,110	369,883	287,677

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(e) Liquidity risk (Cont'd)

	Overdue/ repayable on demand	Less than three months	2004			Undated	Total
			Between three months and one year	Between one and five years	More than five years		
Assets							
Cash and balances with central banks (note (i))	150,620	—	—	—	—	248,746	399,366
Amounts due from banks and non-bank financial institutions	6,821	104,394	1,008	308	—	—	112,531
Loans and advances to customers (note (ii))	69,733	294,498	756,263	589,055	464,013	—	2,173,562
Investments							
— Receivables	—	—	2,853	361,344	69,661	—	433,858
— Held-to-maturity debt securities	—	63,850	71,554	219,835	134,552	—	489,791
— Available-for-sale investments	—	18,508	27,708	58,608	62,093	16,355	183,272
— Debt securities at fair value through profit or loss (note (iii))	—	64	315	27	309	—	715
Other	4,696	7,528	31,901	877	93	71,730	116,825
Total assets	231,870	488,842	891,602	1,230,054	730,721	336,831	3,909,920
Liabilities							
Amounts due to central banks	2,222	25	—	—	—	—	2,247
Amounts due to banks and non-bank financial institutions	84,699	24,896	2,301	103	40	—	112,039
Deposits from customers	2,238,796	364,976	633,002	234,428	19,919	—	3,491,121
Certificates of deposit issued	—	107	969	2,665	—	—	3,741
Other	25,049	14,438	16,050	5,560	4,228	—	65,325
Subordinated bonds issued	—	—	—	—	39,896	—	39,896
Total liabilities	2,350,766	404,442	652,322	242,756	64,083	—	3,714,369
Long/(short) position	(2,118,896)	84,400	239,280	987,298	666,638	336,831	195,551

Notes:

- (i) For cash and balances with central banks, undated amount represents statutory deposit reserve funds and fiscal balances maintained with the PBOC.
- (ii) For loans and advances to customers, overdue amount included in the above "overdue/repayable on demand" category represents loans of which principals were overdue, and excludes loans of which interests were overdue but the principals were not yet due. The overdue amount is stated net of appropriate allowances for impairment losses.
- (iii) For debt securities held for trading purposes, the remaining term to maturities does not represent the Group's intention to hold them to final maturity.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(f) Use of derivatives

Derivatives include forward, swap and option transactions undertaken by the Group in the foreign exchange and interest rate markets. The Group, through the operations of its branch network, acts as an intermediary between a wide range of customers structuring deals to produce risk management products to suit individual customer needs. These positions are actively managed through entering offsetting deals with external parties to ensure the Group's net exposures are within acceptable risk levels. No significant proprietary positions are maintained by the Group at the balance sheet date. The Group also uses derivatives (principally foreign exchange options and swaps, and interest rate swaps) in the management of its own asset and liability portfolios and structural positions.

The primary derivatives utilised by the Group are shown in the following table.

Derivatives	Description
Cross-currency, foreign exchange and interest rate swaps	Cross-currency, foreign exchange 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 for cross-currency swaps.
Foreign currency and interest rate options	Foreign currency and interest rate options are contractual agreements under which the seller grants the purchaser the right, but not the obligation, either to buy or sell at or by a predetermined date or during a predetermined 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 over the counter.
Currency forwards	Currency forwards represent commitments to purchase or sell foreign exchanges at the certain date in the future.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(f) Use of derivatives (Cont'd)

The following tables provide an analysis of the notional amounts of derivatives of the Group by relevant maturity groupings based on the remaining periods to settlement and the corresponding fair values at the balance sheet date. The notional amounts of the derivatives indicate the volume of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

	2005					Fair values	
	Notional amounts with remaining life of					Assets	Liabilities
	less than three months	between three months and one year	between one year and five years	more than five years	Total		
Interest rate derivatives							
Interest rate swaps	21,254	16,536	33,464	18,440	89,694	1,193	1,199
Cross-currency swaps	512	3,684	1,892	288	6,376	662	695
Interest futures	—	104	—	—	104	—	—
Interest rate options purchased	—	—	—	—	—	—	—
Interest rate options written	1,372	—	—	—	1,372	—	12
	<u>23,138</u>	<u>20,324</u>	<u>35,356</u>	<u>18,728</u>	<u>97,546</u>	<u>1,855</u>	<u>1,906</u>
Currency derivatives							
Spot	2,943	—	—	—	2,943	—	—
Forwards	44,235	32,339	1,904	—	78,478	483	394
Foreign exchange swaps	30,884	79,710	—	—	110,594	249	178
Currency options purchased	101	155	181,580	—	181,836	9,550	3
Currency options written	269	2,448	—	—	2,717	9	9
	<u>78,432</u>	<u>114,652</u>	<u>183,484</u>	<u>—</u>	<u>376,568</u>	<u>10,291</u>	<u>584</u>
Total						<u>12,146</u>	<u>2,490</u>
						(Note 21)	(Note 24)

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(f) Use of derivatives (Cont'd)

	2004					Fair values	
	Notional amounts with remaining life of					Assets	Liabilities
	less than three months	between three months and one year	between one year and five years	more than five years	Total		
Interest rate derivatives							
Interest rate swaps	5,097	5,856	38,350	17,977	67,280	745	802
Cross-currency swaps	662	6,898	1,159	577	9,296	319	318
Interest rate options							
purchased	—	—	6	—	6	—	—
Interest rate options written	22,760	—	4	—	22,764	—	212
	<u>28,519</u>	<u>12,754</u>	<u>39,519</u>	<u>18,554</u>	<u>99,346</u>	<u>1,064</u>	<u>1,332</u>
Currency derivatives							
Spot	2,268	—	—	—	2,268	—	—
Forwards	7,933	9,124	616	—	17,673	113	401
Foreign exchange swaps	17,911	4,897	51	—	22,859	446	83
Currency options purchased	17	—	—	—	17	—	—
Currency options written	3	83	—	—	86	1	—
	<u>28,132</u>	<u>14,104</u>	<u>667</u>	<u>—</u>	<u>42,903</u>	<u>560</u>	<u>484</u>
Total						<u>1,624</u>	<u>1,816</u>
						(Note 21)	(Note 24)

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(f) Use of derivatives (Cont'd)

The replacement costs and credit risk weighted amounts in respect of these derivatives are as follows. These amounts have taken into account the effects of bilateral netting arrangements.

Replacement costs

	2005	2004
Interest rate derivatives	1,855	1,064
Currency derivatives, net of option premium payable	4,943	560
	<u>6,798</u>	<u>1,624</u>

Replacement cost represents the cost of replacing all contracts which have a positive value when marked to market. Replacement cost is a close approximation of the credit risk for these derivative contracts as at the balance sheet date.

Credit risk weighted amounts

	2005	2004
Interest rate derivatives	2,458	1,702
Currency derivatives	1,914	1,016
	<u>4,372</u>	<u>2,718</u>

The credit risk weighted amount refers to the amount as computed in accordance with the rules set out by the CBRC and depends on the status of the counterparty and the maturity characteristics.

In accordance with the rules set out by the CBRC, the credit risk weight assigned to the PBOC and Huijin, which is a government agency, is zero. Therefore, the credit risk weighted amount of the currency option purchased from Huijin and foreign currency swap with the PBOC (Note 34(d)) is zero.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(g) Operational risk

Operational risk includes the risk of direct or indirect loss due to an event or action causing failure of technology, processes, infrastructure and personnel, and other risks having an operational impact.

The Group manages this risk through a controls-based environment by establishing a framework of policies and procedures in order to identify, assess, control, manage and report risks. The framework covers all business functions ranging from finance, credit, accounting, settlement, savings, treasury, intermediary business, computer applications and management, special assets resolution and legal affairs. This has allowed the Group to identify and address comprehensively the operational risk inherent in all key products, activities, processes and systems. Key controls include:

- authorisation limits for various business activities to branches are delegated after consideration of their respective business scope, risk management capabilities and credit approval procedures. Such authorities are revised on a timely basis to reflect changes in market conditions and business development and risk management needs;
- the use of the single legal responsibility framework and strict disciplinary measures in order to ensure accountability;
- systems and procedures to identify, control and report on the major risks: credit, market, liquidity and operational;
- promotion of a risk management culture throughout the organisation by building a team of risk management professionals, providing formal training and having an appraisal system in place, to raise the overall risk awareness among the Group's employees;
- a dedicated anti-money laundering division under the Compliance Department responsible for overseeing that cash management and account management are in compliance with the relevant regulations, and for improving training on anti-money laundering to ensure our employees are well-equipped with the necessary knowledge and basic skills to combat money laundering since May 2005. Prior to this, the Legal Department was responsible for this function;
- the review and approval by senior management of comprehensive financial and operating plans which are prepared by branches;
- the assessment of individual branches' financial performance against the comprehensive financial and operating plan; and
- the maintenance of contingent facilities (including backup systems and disaster recovery schemes) to support all major operations, especially back office operations, in the event of an unforeseen interruption. Insurance cover is arranged to mitigate potential losses associated with certain operational events.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

34 RISK MANAGEMENT (Cont'd)

(h) Fair value

(i) *Financial assets*

The Group's financial assets mainly include cash, amounts due from central banks, banks and non-bank financial institutions, loans and advances to customers, and investments.

Amounts due from central banks, banks and non-bank financial institutions

Amounts due from central banks, banks and non-bank financial institutions are mainly priced at market interest rates and mature within one year. Accordingly, the carrying values approximate the fair values.

Loans and advances to customers

Loans and advances to customers are mostly priced at floating rates close to the PBOC rates. Accordingly, their carrying values approximate the fair values.

Investments

Available-for-sale investments and debt securities at fair value through profit or loss are stated at fair value in the financial statements. The following table summarises the carrying values and the fair values of receivables and held-to-maturity debt securities which are not presented on the balance sheet at their fair values.

	Carrying values		Fair values	
	2005	2004	2005	2004
Receivables	<u>443,729</u>	<u>433,858</u>	<u>444,056</u>	<u>414,724</u>
Held-to-maturity debt securities	<u>643,978</u>	<u>489,791</u>	<u>653,514</u>	<u>483,866</u>

(ii) *Financial liabilities*

The Group's financial liabilities mainly include amounts due to banks and non-bank financial institutions, deposits from customers, certificates of deposit issued and subordinated bonds issued. The carrying values of financial liabilities approximated their fair values at the balance sheet date, except that the fair value of subordinated bonds issued as at 31 December 2005 was RMB 41,431 million (2004: RMB 39,896 million), which was higher than their carrying value of RMB 39,907 million (2004: RMB 39,896 million).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

35 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

In determining the carrying amounts of some assets and liabilities, the Group makes assumptions of the effects of uncertain future events on those assets and liabilities at the balance sheet date. These estimates involve assumptions about such items as risk adjustment to cash flows or discount rates used and future changes in prices affecting other costs. The Group's estimates and assumptions are based on historical experience and expectations of future events and are reviewed periodically. In addition to assumptions and estimations of future events, judgements are also made during the process of applying the Group's accounting policies.

(a) Impairment losses on loans and advances

Loan portfolios are assessed periodically to assess whether impairment losses exist and if they exist, the amounts of impairment losses. Objective evidence for impairment includes observable data indicating that there is a measurable decrease in the estimated future cash flows identified with an individual loan. It also includes observable data indicating adverse changes in the repayment status of borrowers in the loan portfolio or national or local or economic conditions that correlate with defaults on the loans in the portfolio. The impairment loss for a loan that is individually evaluated for impairment is the decrease in the estimated future cash flow of that loan. When loans and advances are collectively evaluated for impairment, the estimate is based on historical loss experience for assets with credit risk characteristics similar to the loans and advances. Historical loss experience is adjusted on the basis of the relevant observable data that reflect current economic conditions. Management review the methodology and assumptions used in estimating future cash flows regularly to reduce any difference between loss estimates and actual loss experience.

(b) Impairment of available-for-sale equity investments

For available-for-sale equity investments, a significant or prolonged decline in fair value below cost is considered to be objective evidence of impairment. Judgement is required when determining whether a decline in fair value has been significant or prolonged. In making this judgement, the historical data on market volatility as well as in the share price of the specific equity investment are taken into account. The Group also takes into account other factors, such as industry and sector performance and financial information regarding the investee.

(c) Fair value of financial instruments

For a number of financial instruments, no quoted prices from an active market exist. The fair values for these financial instruments are established by using valuation techniques. These techniques include using recent arm's length market transactions, reference to the current fair value of similar instruments and discounted cash flow analysis and option pricing models. The Group has established a process to ensure that valuation techniques are constructed by qualified personnel and are validated and reviewed by personnel independent of the area that constructed the valuation techniques. Valuation techniques are certified before being implemented for valuation and are calibrated to ensure that outputs reflect actual market conditions. Valuation models established by the Group make the maximum use of market inputs and rely as little as possible on Group-specific data. However, it should be noted that some inputs, such as credit and counterparty risk, and risk correlations, require management estimates. Management estimates and assumptions are reviewed periodically and are adjusted if necessary.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

35 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (Cont'd)

(d) Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity investments if the Group has the intention and ability to hold them until maturity. In evaluating whether the requirements to classify a financial asset as held-to-maturity are met, management make significant judgements. Failure in correctly assessing the Group's intention and ability to hold specific investments until maturity may result in reclassification of the whole portfolio as available-for-sale.

(e) Income taxes

Determining income tax provisions involves judgement on the future tax treatment of certain transactions. The Group carefully evaluates tax implications of transactions and tax provisions are set up accordingly. The tax treatment of such transactions is reconsidered periodically to take into account all changes in tax legislations. Deferred tax assets are recognised for tax losses not yet used and temporary deductible differences. As those deferred tax assets can only be recognised to the extent that it is probable that future taxable profit will be available against which the unused tax credits can be utilised, management's judgement is required to assess the probability of future taxable profits. Management's assessment is constantly reviewed and additional deferred tax assets are recognised if it becomes probable that future taxable profits will allow the deferred tax asset to be recovered.

36 RELATED PARTIES

(a) Huijin and companies under Huijin

(i) *Huijin*

Huijin directly and indirectly owned 70.69% (2004: 95.88%) of the issued share capital of the Bank as at 31 December 2005. Huijin was incorporated on 16 December 2003 as a wholly state-owned investment company with the approval of the State Council. Huijin is a government agency, and was established to hold certain equity investments on behalf of the State Council. Huijin represents the PRC government in exercising its investors' rights and obligations in certain financial institutions such as the Bank. As part of the Restructuring, the Group carried out the following transactions with Huijin:

- Huijin has undertaken to assume all the debts, obligations and liabilities relating to the business acquired by the Bank, which arose for any reason prior to 31 December 2003 and were not succeeded by the Bank at Restructuring; and
- Huijin entered into a foreign exchange option agreement with the Bank on 12 January 2005 (Note 34(d)). The purpose of the option is to hedge against the Bank's currency risk arising from capital contributed by Huijin of USD 22,500 million.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

36 RELATED PARTIES (Cont'd)

(a) Huijin and companies under Huijin (Cont'd)

(i) Huijin (Cont'd)

Transactions during the year and the corresponding balances outstanding at the balance sheet date with Huijin are as follows:

	2005	2004
Interest expense arising during the year from:		
Deposits from customers	195	—
	<u>195</u>	<u>—</u>
Liabilities at the balance sheet date:		
Deposits from customers	18,334	—
Interest payable	27	—
	<u>18,361</u>	<u>—</u>

(ii) Jianyin

As part of the Restructuring, CCB was separated into the Bank and Jianyin, a limited liability company directly and wholly owned by Huijin. Jianyin directly owns 9.21% (2004: 10.65%) of the issued share capital of the Bank. Its principal activities include the holding of equity investments, asset management and other business activities as approved by the relevant PRC government authorities.

Jianyin entered into certain services and operating lease agreements with the Group subsequent to the Restructuring. Transactions during the year and the corresponding balances outstanding at the balance sheet date with Jianyin are as follows:

	2005	2004
Income or expenses arising during the year from:		
Other income (note (ii-1))	53	5
Operating expenses (note (ii-2))	200	190
Interest expenses	6	—
	<u>259</u>	<u>195</u>
Assets or liabilities at the balance sheet date:		
Other assets	20	—
	<u>20</u>	<u>—</u>
Amounts due to banks and non-bank financial institutions	233	—
Deposits from customers	462	—
Other liabilities and provisions (Note 24)	5,211	6,405
	<u>5,906</u>	<u>6,405</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

36 RELATED PARTIES (Cont'd)

(a) Huijin and companies under Huijin (Cont'd)

(ii) Jianyin (Cont'd)

Notes:

(ii-1) This included custody management fee income earned by the Group for managing assets on behalf of Jianyin and income from disposal of fixed assets to Jianyin.

(ii-2) This mainly represents rental expenses paid by the Group for leasing assets, including properties and motor vehicles, owned by Jianyin, and fees for supporting services provided by Jianyin.

(ii-3) Amounts due from/to Jianyin are unsecured and are repayable under normal commercial terms. No allowance for impairment losses was made in respect of amounts due from Jianyin.

(iii) Other companies under Huijin

Huijin also has controlling equity interests in certain other banks and non-bank financial institutions in Mainland China. The Group enters into banking transactions with these companies in the normal course of its banking business at market rates. These include sale and purchase of debt securities, conducting money market transactions and inter-bank clearing. Transactions during the year and corresponding balances outstanding at the balance sheet date with these companies are as follows:

	2005	2004
Interest income arising during the year from:		
Debt securities issued by these banks and non-bank financial institutions	600	68
Amounts due from these banks and non-bank financial institutions	<u>54</u>	<u>30</u>
	<u>654</u>	<u>98</u>
Interest expense arising during the year from:		
Amounts due to these banks and non-bank financial institutions	<u>91</u>	<u>25</u>
Assets or liabilities at the balance sheet date:		
Debt securities issued by these banks and non-bank financial institutions	31,191	3,109
Amounts due from these banks and non-bank financial institutions	<u>4,374</u>	<u>1,656</u>
	<u>35,565</u>	<u>4,765</u>
Amounts due to these banks and non-bank financial institutions	<u>5,726</u>	<u>2,256</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

36 RELATED PARTIES (Cont'd)

(a) Huijin and companies under Huijin (Cont'd)

(iii) *Other companies under Huijin* (Cont'd)

The Group issued subordinated bonds with a nominal value of RMB 40,000 million during the year ended 31 December 2004. One of the subsidiaries of Huijin underwrote the Group's subordinated bonds with a nominal value of RMB 3,320 million upon their issuance. These bonds are bearer bonds and are traded in the secondary market. Accordingly, the Group has no information in respect of the amount of bonds held by such bank at the balance sheet date.

(b) Transactions with other PRC state-owned entities

The Group operates in an economic regime currently predominated by entities directly or indirectly owned by the PRC government through its government authorities, agencies, affiliations and other organisations ("state-owned entities").

Transactions with other state-owned entities include but are not limited to the following:

- lending and deposit taking;
- taking and placing of inter-bank balances;
- entrusted lending and other custody services;
- insurance and securities agency, and other intermediary services;
- sale, purchase, underwriting and redemption of bonds issued by other state-owned entities;
- purchase, sale and leases of property and other assets; and
- rendering and receiving of utilities and other services.

These transactions are conducted in the ordinary course of the Group's banking business on terms similar to those that would have been entered into with non-state-owned entities. The Group has also established its pricing strategy and approval processes for major products and services, such as loans, deposits and commission income. Such pricing strategy and approval processes do not depend on whether the customers are state-owned entities or not. Having due regard to the substance of the relationships, the Directors are of the opinion that none of these transactions are material related party transactions that require separate disclosure.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

36 RELATED PARTIES (Cont'd)

(c) Key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including Directors, Supervisors and Executive Officers.

The aggregate of the compensations in respect of Directors and Supervisors is disclosed in Note 10. The Executive Officers' annual compensations during the year are as follows:

	2005			Total RMB'000
	Salaries and other emoluments RMB'000	Discretionary bonus RMB'000	Contributions to defined contribution retirement schemes RMB'000	
Vice president				
Luo Zhefu	470	482	16	968
Xin Shusen (appointed in July 2005)	479	487	16	982
Chen Zuofu (appointed in July 2005)	467	482	16	965
Fan Yifei (appointed in July 2005)	505	483	16	1,004
Chief audit officer				
Yu Yongshun (appointed in July 2005)	171	164	7	342
Secretary to the board of directors				
Xuan Changneng	408	348	16	772
Company secretary				
Ha Yiu Fai (appointed in August 2005)	2,575	1,001	94	3,670
Qualified accountant				
Yuen Yiu Leung (appointed in August 2005)	1,072	474	67	1,613
	<u>6,147</u>	<u>3,921</u>	<u>248</u>	<u>10,316</u>

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

36 RELATED PARTIES (Cont'd)

(c) Key management personnel (Cont'd)

	2004			
	Salaries and other emoluments RMB'000	Discretionary bonus RMB'000	Contributions to defined contribution retirement schemes RMB'000	Total RMB'000
Vice president				
Luo Zhefu	185	460	14	659
Zheng Zhijie	236	460	14	710
Chief compliance officer				
Xin Shusen	192	460	14	666
Assistant president				
Chen Zuofu	185	419	14	618
Fan Yifei	221	419	14	654
Secretary to the board of directors				
Xuan Changneng (appointed in November 2004)	67	63	4	134
	<u>1,086</u>	<u>2,281</u>	<u>74</u>	<u>3,441</u>

(d) Contributions to defined contribution retirement schemes

The Group participates in various defined contribution retirement schemes organised by municipal and provincial governments for its employees in Mainland China. For its employees outside Mainland China, the Group participates in various defined contribution retirement schemes at funding rates determined in accordance with the local practices and regulations. The details of the Group's defined contribution retirement schemes are described in Notes 24(a) and 25(a).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in millions of Renminbi unless otherwise stated)

37 EVENTS AFTER THE BALANCE SHEET DATE

After the balance sheet date, the Directors proposed a final dividend. Further details are disclosed in Note 28(a)(ii).

38 ULTIMATE PARENT

The Group is owned and controlled by the PRC government. The majority of the Group's shares are held by Huijin, a government agency.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

Year ended 31 December 2005 (Expressed in millions of Renminbi unless otherwise stated)

The information set out below does not form part of the audited financial statements, and is included herein for information purposes only.

(a) Differences between the financial statements prepared under IFRS and those prepared in accordance with PRC GAAP

China Construction Bank Corporation (the "Bank") prepares consolidated financial statements, which include the financial statements of the Bank and its subsidiaries (collectively the "Group"), in accordance with International Financial Reporting Standards ("IFRS") and its interpretations promulgated by the International Accounting Standards Board and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

As a financial institution incorporated in the People's Republic of China (the "PRC"), the Bank also prepares its statutory financial statements for the year ended 31 December 2005 in accordance with the Accounting Standards for Business Enterprises, the *Accounting Regulations for Financial Enterprises* (2001) and other relevant regulations issued by the Ministry of Finance of the PRC (collectively "PRC GAAP"). In the preparation of the Bank's PRC statutory financial statements for the year ended 31 December 2005, the Bank changed its accounting policies, which are mainly relating to the measurement and recognition of financial assets, and the new accounting policies have been applied retrospectively.

There is no difference in the net profit attributable to shareholders of the Bank for the year ended 31 December 2005 or total equity attributable to shareholders of the Bank as at 31 December 2005 between the Group's consolidated financial statements prepared under IFRS and the Bank's statutory financial statements prepared under PRC GAAP.

(b) Liquidity ratios

	2005	2004
Renminbi current assets to Renminbi current liabilities	<u>59.08%</u>	<u>51.37%</u>
Foreign currency current assets to foreign currency current liabilities	<u>108.68%</u>	<u>71.15%</u>

The above liquidity ratios are calculated in accordance with the formula promulgated by the People's Bank of China and China Banking Regulatory Commission and based on the Bank's financial statements prepared under PRC GAAP.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

Year ended 31 December 2005 (Expressed in millions of Renminbi unless otherwise stated)

(c) Capital adequacy ratio

The capital adequacy ratio is prepared on a solo basis in accordance with the guideline *Regulation Governing Capital Adequacy of Commercial Banks* [Order (2004) No. 2] effective on 1 March 2004, which may have significant differences with the relevant requirements in the Hong Kong Special Administrative Region ("Hong Kong") of the PRC or other countries.

The capital adequacy ratios and the related components of the Bank at balance sheet date, calculated based on PRC GAAP, were as follows:

	2005	2004
Core capital adequacy ratio (note (i))	<u>11.08%</u>	<u>8.57%</u>
Capital adequacy ratio (note (ii))	<u>13.57%</u>	<u>11.29%</u>
<i>Components of capital base</i>		
Core capital:		
— Paid up ordinary share capital	224,689	194,230
— Reserves	<u>59,520</u>	<u>514</u>
	<u>284,209</u>	<u>194,744</u>
Supplementary capital:		
— General provision for doubtful debts	24,563	22,256
— Term subordinated bonds	<u>40,000</u>	<u>40,000</u>
— Total supplementary capital	<u>64,563</u>	<u>62,256</u>
Total capital base before deductions	348,772	257,000
Deductions:		
— Unconsolidated equity investments	<u>(1,528)</u>	<u>(1,012)</u>
Total capital base after deductions	<u>347,244</u>	<u>255,988</u>
Risk weighted assets	<u>2,558,956</u>	<u>2,267,467</u>

Notes:

- (i) Core capital adequacy ratio is calculated by dividing the net amount of core capital after deductions of 50% of unconsolidated equity investments by risk weighted assets.
- (ii) Capital adequacy ratio is calculated by dividing the total capital base after deductions by risk weighed assets.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

Year ended 31 December 2005 (Expressed in millions of Renminbi unless otherwise stated)

(d) Currency concentrations

	2005			Total
	US Dollars	HK Dollars	Others	
Spot assets	433,717	48,014	36,011	517,742
Spot liabilities	(151,271)	(30,922)	(23,360)	(205,553)
Forward purchases	100,048	6,513	7,368	113,929
Forward sales	(135,922)	(22,627)	(14,389)	(172,938)
Net option position	(181,580)	—	—	(181,580)
Net long position	64,992	978	5,630	71,600
Net structural position	—	203	12	215

	2004			Total
	US Dollars	HK Dollars	Others	
Spot assets	331,949	13,336	51,156	396,441
Spot liabilities	(115,362)	(13,911)	(35,095)	(164,368)
Forward purchases	29,827	5,312	3,631	38,770
Forward sales	(9,624)	(4,514)	(18,744)	(32,882)
Net option position	1	—	—	1
Net long position	236,791	223	948	237,962
Net structural position	—	121	15	136

The net option position is calculated using the delta equivalent approach required by the Hong Kong Monetary Authority (the "HKMA"). The net structural position of the Group includes the structural positions of the Bank's overseas branches, banking subsidiaries and other subsidiaries substantially involved in foreign exchange. Structural assets and liabilities include:

- Investments in fixed assets and premises, net of depreciation charges;
- Capital and statutory reserves of overseas branches; and
- Investments in overseas subsidiaries and related companies.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

Year ended 31 December 2005 (Expressed in millions of Renminbi unless otherwise stated)

(e) Cross-border claims

The Group is principally engaged in business operations within Mainland China, and regards all claims on third parties outside Mainland China as cross-border claims.

For the purpose of these unaudited supplementary financial information, Mainland China excludes Hong Kong, the Macau Special Administrative Region of the PRC and Taiwan.

Cross-border claims include loans and advances, balances and placements with banks and non-bank financial institutions, holdings of trade bills and certificates of deposit and investment securities.

Cross-border claims have been disclosed by country or geographical area. A country or geographical area is reported where it constitutes 10% or more of the aggregate amount of cross-border claims, after taking into account any risk transfers. Risk transfers are only made if the claims are guaranteed by a party in a country which is different from that of the counterparty or if the claims are on an overseas branch of a bank whose head office is located in another country.

	2005			Total
	Banks and non-bank financial institutions	Public sector entities	Others	
Asia Pacific excluding Mainland China	123,597	1,479	17,183	142,259
— of which attributed to Hong Kong	83,578	903	6,165	90,646
Europe	74,108	3,805	5,897	83,810
North and South America	85,507	81,085	6,818	173,410
	<u>283,212</u>	<u>86,369</u>	<u>29,898</u>	<u>399,479</u>

	2004			Total
	Banks and non-bank financial institutions	Public sector entities	Others	
Asia Pacific excluding Mainland China	60,365	4,120	15,302	79,787
— of which attributed to Hong Kong	26,204	2,869	4,726	33,799
Europe	30,104	3,669	4,532	38,305
North and South America	48,486	107,006	6,718	162,210
	<u>138,955</u>	<u>114,795</u>	<u>26,552</u>	<u>280,302</u>

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

Year ended 31 December 2005 (Expressed in millions of Renminbi unless otherwise stated)

(f) Overdue loans and advances to customers by geographic sector

	2005	2004
Yangtze River Delta	8,395	6,843
Pearl River Delta	13,965	14,944
Bohai Rim	18,178	13,999
Central	11,443	8,068
Western	14,019	9,990
Northeastern	6,181	5,938
Head office	2,234	2,399
Overseas	77	216
Total	74,492	62,397

Note: The above analysis includes loans and advances overdue for more than 90 days as required by the HKMA.

Loans and advances with a specific repayment date are classified as overdue when the principal or interest is overdue.

For loans and advances repayable by regular instalments, if part of the instalments is overdue, the whole amount of these loans would be classified as overdue.

Loans and advances repayable on demand are classified as overdue when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instructions. If the loans and advances repayable on demand are outside the approved limit that was advised to the borrower, they are also considered as overdue.

(g) Gross amount of overdue loans and advances to customers

	2005	2004
Gross loans and advances to customers which have been overdue with respect to either principal or interest for periods of:		
— between 3 and 6 months	11,475	14,883
— between 6 and 12 months	15,567	14,313
— over 12 months	47,450	33,201
Total	74,492	62,397
As a percentage of total gross loans and advances to customers:		
— between 3 and 6 months	0.47%	0.67%
— between 6 and 12 months	0.63%	0.64%
— over 12 months	1.93%	1.49%
Total	3.03%	2.80%

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

Year ended 31 December 2005 (Expressed in millions of Renminbi unless otherwise stated)

(g) Gross amount of overdue loans and advances to customers (Cont'd)

Notes:

(i) *The above analysis includes loans and advances overdue for more than 90 days as required by the HKMA.*

Loans and advances with a specific repayment date are classified as overdue when the principal or interest is overdue.

For loans and advances repayable by regular instalments, if part of the instalments is overdue, the whole amount of these loans would be classified as overdue.

Loans and advances repayable on demand are classified as overdue when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instructions. If the loans and advances repayable on demand are outside the approved limit that was advised to the borrower, they are also considered as overdue.

(ii) *There were no overdue loans and advances to financial institutions as of 31 December 2005 and 2004.*

(h) Rescheduled loans and advances to customers

	2005		2004	
		% of total loans and advances		% of total loans and advances
Rescheduled loans and advances to customers	5,012	0.20%	2,563	0.12%
Less:				
— rescheduled loans and advances to customers but overdue more than 90 days	<u>1,319</u>	0.05%	<u>1,128</u>	0.05%
Rescheduled loans and advances to customers overdue less than 90 days	<u>3,693</u>	0.15%	<u>1,435</u>	0.07%

BRANCHES AND SUBSIDIARIES

TIER-1 BRANCHES IN MAINLAND CHINA			
Branches	Address	Telephone	Facsimile
BEIJING BRANCH	No.4, Building 28, Xuanwumen West Street, Beijing Postcode: 100053	(010) 63603664	(010) 63603656
TIANJIN BRANCH	Plus 1 No.19, Nanjing Road, Hexi District, Tianjin Postcode: 300203	(022) 23401616	(022) 23400503
HEBEI BRANCH	No. 40, Ziqiang Road, Shijiazhuang Postcode: 050000	(0311) 7888866	(0311) 8601010
SHANXI BRANCH	No. 126, Yingze Street, Taiyuan Postcode: 030001	(0351) 4957800	(0351) 4957871
INNER MONGOLIA BRANCH	No. 45, South Xincheng Street, Huhhot Postcode: 010010	(0471) 6200303	(0471) 6200257
LIAONING BRANCH	No. 176, Zhongshan Road, Heping District, Shenyang Postcode: 110002	(024) 22787600	(024) 22856915
DALIAN BRANCH	No. 1, Jiefang Street, Zhongshan District, Dalian Postcode: 116001	(0411) 82818818	(0411) 82804560
JILIN BRANCH	No. 810, Xi'an Road, Changchun Postcode: 130061	(0431) 8573030	(0431) 8988748
HEILONGJIANG BRANCH	No. 67, Hongjun Street, Nangang District, Harbin Postcode: 150001	(0451) 53619788	(0451) 53625552
SHANGHAI BRANCH	No.900, Lujiazui Ring Road, Shanghai Postcode: 200120	(021) 58880000	(021) 58781818
JIANGSU BRANCH	No. 188, Hongwu Road, Nanjing Postcode: 210002	(025) 84200545	(025) 84209316
SUZHOU BRANCH	No. 18, Suhua Road, Suzhou Postcode: 215021	(0512) 62788786	(0512) 62788019

BRANCHES AND SUBSIDIARIES

Branches	Address	Telephone	Facsimile
ZHEJIANG BRANCH	No. 288, Tiyuchang Road, Hangzhou Postcode: 310003	(0571) 85313000	(0571) 85313001
NINGBO BRANCH	No. 31, Guangji Street, Ningbo Postcode: 315010	(0574) 87313888	(0574) 87325019
ANHUI BRANCH	No. 373, Meiling Road, Hefei Postcode: 230001	(0551) 2874100	(0551) 2872014
FUJIAN BRANCH	No.142, Guping Road, Fuzhou Postcode: 350003	(0591) 87811098	(0591) 87856865
XIAMEN BRANCH	No. 98, Lujiang Road, Xiamen Postcode: 361003	(0592) 2158888	(0592) 2158862
JIANGXI BRANCH	No. 366, Bayi Street, Nanchang Postcode: 330006	(0791) 6848200	(0791) 6848318
SHANDONG BRANCH	No. 178, Luoyuan Street, Jinan Postcode: 250012	(0531) 86918888	(0531) 86169108
QINGDAO BRANCH	No. 71, Guizhou Road, Qingdao Postcode: 266002	(0532) 82651888	(0532) 82670157
HENAN BRANCH	No.80, Huayuan Road, Zhengzhou Postcode: 450003	(0371) 5556699	(0371) 5556688
HUBEI BRANCH	No. 709, Jianshe Street, Wuhan Postcode: 430015	(027) 65775888	(027) 65775881
THREE GORGES BRANCH	No. 122, Xiling First Road, Yichang, Hubei Postcode: 443000	(0717) 6736888	(0717) 6738137
HUNAN BRANCH	Yin'gang Plaza, No. 2, Baisha Road, Changsha Postcode: 410005	(0731) 4419191	(0731) 4419141
GUANGDONG BRANCH	No. 509, Dongfeng Middle Road, Guangzhou Postcode: 510045	(020) 83018888	(020) 83013950

BRANCHES AND SUBSIDIARIES

Branches	Address	Telephone	Facsimile
SHENZHEN BRANCH	East Section, Finance Centre, South Hongling Road, Shenzhen Postcode: 518010	(0755) 82488189	(0755) 82246144
GUANGXI BRANCH	No. 92, Minzu Road, Nanning Postcode: 530022	(0771) 5513110	(0771) 5513012
HAINAN BRANCH	CCB Plaza, Guomao Avenue, Haikou Postcode: 570125	(0898) 68587488	(0898) 68587569
CHONGQING BRANCH	No. 123, Minzu Road, Yuzhong District, Chongqing Postcode: 400010	(023) 63771855	(023) 63771835
SICHUAN BRANCH	Sichuan CCB Plaza, No. 86, Tidu Street, Chengdu Postcode: 610016	(028) 86767161	(028) 86767187
GUIZHOU BRANCH	No. 113, Ruijin North Road, Guiyang Postcode: 550003	(0851) 5976660	(0851) 6505883
YUNNAN BRANCH	CCB Plaza, Jinbi Road, Kunming Postcode: 650021	(0871) 3060997	(0871) 3060333
TIBET BRANCH	No. 32, Beijing Middle Road, Lhasa Postcode: 850001	(0891) 6838792	(0891) 6836818
SHAANXI BRANCH	No. 38, South Guangji Street, Xi'an Postcode: 710002	(029) 87606009	(029) 87617514
GANSU BRANCH	No. 59, Qin'an Road, Lanzhou Postcode: 730030	(0931) 4891555	(0931) 4891862
QINGHAI BRANCH	No. 59, West Street, Xining Postcode: 810000	(0971) 8261181	(0971) 8261225
NINGXIA BRANCH	No. 98, Nanxun West Road, Yinchuan Postcode: 750001	(0951) 4102918	(0951) 4106165
XINJIANG BRANCH	No. 36, Minzhu Road, Urumqi Postcode: 830002	(0991) 2848666	(0991) 2819160

BRANCHES AND SUBSIDIARIES

OVERSEAS BRANCHES AND REPRESENTATIVE OFFICES

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SUBSIDIARIES

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SINO-GERMAN BAUSPARKASSE CO. LTD.	27th Floor, Plus 1 No. 19, Nanjing Road, Hexi District, Tianjin 300203 Telephone: (022) 23126699 Facsimile: (022) 23122828 Website: www.sgb.cn
CCB PRINCIPAL ASSET MANAGEMENT CO., LTD.	No. 12C, Fuxing Road, Haidian District, Beijing 100038 Telephone: (010) 63975933, 63975936 Facsimile: (010) 63975939 Website: www.ccbfund.cn

CORPORATE INFORMATION

Legal name in Chinese:	中國建設銀行股份有限公司
Legal name in English:	China Construction Bank Corporation
Registered address:	No. 25 Finance Street, Xicheng District, Beijing, China
Postcode:	100032
Principal place of business in Hong Kong:	44–45/F, Tower One, Lippo Centre, 89 Queensway, Admiralty, Hong Kong
Website:	www.ccb.cn
Legal representative:	Guo Shuqing
Authorised representatives:	Chang Zhenming Zhao Lin
Secretary to the board:	Xuan Changneng
Company secretary:	Ha Yiu Fai (LLB, LLM, FCS, FCIS)
Qualified accountant:	Yuen Yiu Leung (MBA, FCMA, FCCA, FCPA, ACA)
Independent auditors:	KPMG
Compliance advisors:	China International Capital Corporation (Hong Kong) Limited Morgan Stanley Dean Witter Asia Limited
Legal advisor as to Hong Kong law:	Freshfields Bruckhaus Deringer
Listing venue of H shares:	The Stock Exchange of Hong Kong Limited
H share registrar:	Computershare Hong Kong Investor Services Limited Rooms 1712–16, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong