中銀香港(控股)有限公司
BOC HONG KONG (HOLDINGS) LIMITED

(Incorporated in Hong Kong with limited liability)

(the "Company", Stock Code: 2388)

2016 ANNUAL RESULTS ANNOUNCEMENT

The Board of Directors of the Company (the "Board") is pleased to announce the audited results of the Company and its subsidiaries for the year ended 31 December 2016. This announcement, containing the full text of the 2016 Annual Report of the Company, complies with the relevant requirements of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited in relation to information to accompany preliminary announcements of annual results. Printed version of the Company's 2016 Annual Report will be delivered to the Company's shareholders who have chosen to receive printed version and will also be available for viewing on the websites of Hong Kong Exchanges and Clearing Limited at www.hkexnews.hk and of the Company at www.bochk.com in mid April 2017.

Financial Highlights

	2016	2015
For the year	**HK$'m**	HK$'m
Net operating income before impairment allowances[1]	**41,754**	40,181
Operating profit[1]	**28,963**	27,815
Profit before taxation[1]	**29,452**	28,575
Profit for the year[2]	**56,323**	27,681
Profit attributable to the equity holders of the Company[2]	**55,503**	26,982
Per share	**HK$**	HK$
Basic earnings per share[2]	**5.2496**	2.5520
Dividend per share	**1.8800**	1.2240
At year-end	**HK$'m**	HK$'m
Total assets	**2,327,781**	2,382,815
Issued and fully paid up share capital	**52,864**	52,864
Capital and reserves attributable to the equity holders of the Company	**224,653**	194,750
Financial ratios	**%**	%
Return on average total assets[3]	**2.38**	1.19
Return on average shareholders' equity[4]	**26.47**	14.45
Cost to income ratio[1]	**29.25**	28.90
Loan to deposit ratio[5]	**64.55**	63.37
Average value of liquidity coverage ratio[6]		
First quarter	**112.92**	101.90
Second quarter	**109.70**	109.89
Third quarter	**118.69**	104.00
Fourth quarter	**107.02**	106.52
Total capital ratio[7]	**22.35**	17.86

1. The financial information is from continuing operations and the comparative information has been restated accordingly.
2. The financial information is from continuing operations and discontinued operations.
3. Return on average total assets $= \dfrac{\text{Profit for the year}}{\text{Daily average balance of total assets}}$
4. Return on average shareholders' equity

   $= \dfrac{\text{Profit attributable to the equity holders of the Company}}{\text{Average of the beginning and ending balance of capital and reserves attributable to the equity holders of the Company}}$
5. Loan to deposit ratio is calculated as at year end. Loan represents gross advances to customers. Deposit represents deposits from customers including structured deposits reported as "Financial liabilities at fair value through profit or loss". The ratio excludes assets held for sale and liabilities associated with assets held for sale.
6. The average value of liquidity coverage ratio is computed on the consolidated basis which comprises the positions of BOCHK and certain subsidiaries specified by the HKMA in accordance with the Banking (Liquidity) Rules.
7. Total capital ratio is computed on the consolidated basis for regulatory purposes that comprises the positions of BOCHK and certain subsidiaries specified by the HKMA in accordance with the Banking (Capital) Rules.
8. The Group has applied the merger accounting method in the preparation of financial statements for the combination with entity under common control in 2016. The comparative information for the year 2015 has been restated accordingly.

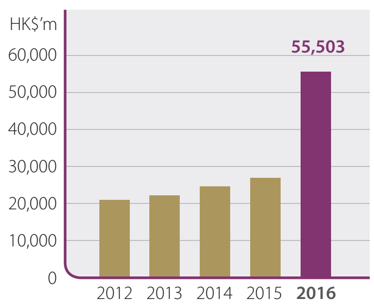
Five-Year Financial Summary

The financial information of the Group for the last five years commencing from 1 January 2012 is summarised below:

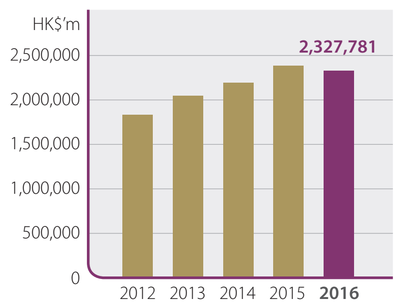
	2016	2015	2014	2013	2012
For the year	**HK$'m**	HK$'m	HK$'m	HK$'m	HK$'m
Net operating income before impairment allowances[1]	**41,754**	40,181	36,794	33,545	29,644
Operating profit[1]	**28,963**	27,815	26,261	23,571	20,077
Profit before taxation[1]	**29,452**	28,575	26,612	23,797	21,933
Profit for the year[2]	**56,323**	27,681	25,105	23,075	21,547
Profit attributable to the equity holders of the Company[2]	**55,503**	26,982	24,577	22,252	20,930
Per share	**HK$**	HK$	HK$	HK$	HK$
Basic earnings per share[2]	**5.2496**	2.5520	2.3246	2.1046	1.9796
At year-end	**HK$'m**	HK$'m	HK$'m	HK$'m	HK$'m
Advances and other accounts[3]	**992,137**	928,871	1,014,129	924,943	819,739
Total assets	**2,327,781**	2,382,815	2,189,367	2,046,936	1,830,763
Daily average balance of total assets	**2,369,100**	2,327,436	2,112,622	1,890,403	1,734,388
Deposits from customers[3,4]	**1,507,501**	1,418,058	1,483,224	1,327,980	1,229,131
Total liabilities	**2,097,221**	2,182,650	2,007,895	1,883,928	1,675,689
Issued and fully paid up share capital	**52,864**	52,864	52,864	52,864	52,864
Capital and reserves attributable to the equity holders of the Company	**224,653**	194,750	176,714	158,813	150,969
Financial ratios	**%**	%	%	%	%
Return on average total assets	**2.38**	1.19	1.19	1.22	1.24
Cost to income ratio[1]	**29.25**	28.90	28.21	28.76	30.92
Loan to deposit ratio[3]	**64.55**	63.37	64.79	64.63	63.32

1. The financial information is from continuing operations and the comparative information has been restated accordingly.
2. The financial information is from continuing operations and discontinued operations.
3. The financial information for the year 2016 and 2015 excludes assets held for sale and liabilities associated with assets held for sale.
4. Deposits from customers include structured deposits reported as "Financial liabilities at fair value through profit or loss".
5. The Group has applied the merger accounting method in the preparation of financial statements for the combination with entity under common control in 2016. The comparative information for the year 2015 has been restated accordingly. However, the financial information prior to year 2015 had not been restated as the difference before and after restatement is insignificant.

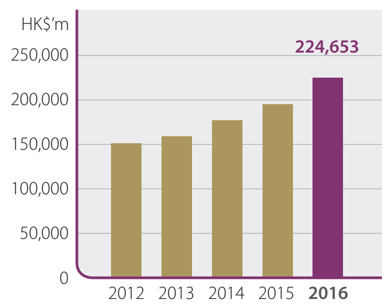
Profit attributable to the equity holders of the Company



Total assets



Capital and reserves attributable to the equity holders of the Company



Chairman's Statement

TIAN Guoli
Chairman

In 2016, we witnessed another year of sustained low growth in the global economies, characterised by depressed international investment and trade. The low growth trajectory of the developed countries continued, as did the moderating growth trend in developing countries. In global politics and the world's economies, frequent Black Swan events increased volatility substantially across financial markets. At home, the Chinese government began tackling the challenges of inadequate internal growth drivers and accumulated financial risks by introducing measures such as supply-side reform to encourage quality of growth and efficiency. These efforts have met with some initial success. During the year, the growth of the Chinese economy fell within a reasonable range, and its long-term fundamentals remained positive.

As an open economy, Hong Kong had to contend with many adverse externalities that caused weak economic performance. On the bright side, a robust labour market continued to support the local economy. However, abundant liquidity in the Mainland of China reduced the attractiveness of offshore borrowing by Chinese enterprises in Hong Kong. To a certain degree, this also hampered financing activities in Hong Kong. In the local stock market, investment sentiment stabilised somewhat following the massive correction in the early months of the year. Competition among banks was intense, and asset quality in the banking sector trended lower.

In spite of such a complicated operating environment, BOCHK was able to rise to these challenges. In line with our parent bank's strategic goal of "Serving Society and Delivering Excellence", we continued with the steady implementation of the Group's new transformation plan as set out by the Board of Directors.

During the year, BOCHK successfully disposed its shares in NCB, completed the acquisition of Bank of China (Malaysia) Berhad and officially opened the BOCHK Brunei Branch. All of these transactions represent a promising start in our strategy to transform BOCHK from a municipal bank into a regional bank. Additionally in early 2017, we successfully acquired Bank of China (Thai) Public Company Limited and entered into Asset Purchase Agreements with BOC in relation to the acquisition[1] of the Indonesia Business and the Cambodia Business, respectively. In March 2017, we completed the disposal of our interests in Chiyu Banking Corporation Limited. At the same time, we remained committed to providing quality financial products and services for corporate customers based in the Mainland of China, Hong Kong and Southeast Asia, as well as for multinational corporations. We also strengthened collaboration with

1 For further information on the acquisitions, please refer to the announcement made by the Group on 28 February 2017.

our Southeast Asia operations, which achieved some early satisfactory results. Capitalising on the significant opportunities arising from the national Belt and Road Initiative and from Chinese enterprises going global, we met the diverse demands for financing by these enterprises by offering merger and acquisition loans, trade finance, syndicated loans, settlement and currency exchange. I am also pleased to note that for 12 consecutive years, BOCHK succeeded in keeping its top ranking as an arranger in the Hong Kong-Macau syndicated loan market. In addition to this, we continued our close collaboration with our parent bank, BOC, to develop our business further in the Free Trade Zones of the Mainland of China. We also promoted product innovation while leveraging BOC Group's global network and diversified platforms with the aim of providing the best cross-border banking services in the market.

In 2016, BOCHK continued to capitalise on its RMB franchise and cement further its leading position in the local RMB market. As the sole RMB clearing bank in Hong Kong, BOCHK has been enhancing its clearing service capabilities and, in July 2016, received permission from the People's Bank of China to participate in China's Cross-border Interbank Settlement System ("CIPS"). This made us the first offshore bank to join CIPS as a direct participant and the only clearing bank to offer clearing services through both CIPS and the China National Advanced Payments System (CNAPS), further expanding Hong Kong's coverage in RMB clearing. In another important development, in October 2016, Renminbi was formally included in the Special Drawing Rights (SDR) basket of the International Monetary fund. Taking advantage of this opportunity, BOCHK was able to expand its client base into the central bank and sovereign institution segment. After the official launch of the Shenzhen-Hong Kong Stock Connect programme in December 2016, BOCHK obtained all the associated business qualifications to become the sole Settlement Bank for Northbound Trading and a provider of cross-border fund settlement for Southbound Trading. We continued to serve as the designated bank of the China Securities Depository and Clearing Corporation Limited (CSDCC) for settlement and currency exchange services. As global usage of the RMB continues for transaction, payment, trade finance, investment and central reserves, this will open up even greater prospects for the offshore RMB business. Accordingly, the Group will continue to adhere to its customer-centric principles and strive to become customers' first choice in offshore RMB services.

In 2016, BOCHK continued to deepen its local market penetration. Our branch network transformation strategy along with our existing competitive advantages enabled us to produce successful results in all major business areas. As part of our branch network transformation project, we optimised our customer management flow for SME customers, which led to a significant enhancement in both service efficiency and the customer experience. In our Wealth Management business, we raised our brand image, which helped us in achieving faster growth in the number of mid-to-high end customers and cross-border customers acquired, as well as in the total value of assets under management. We also continued to maintain our strong competitive edge in our eight key business platforms, namely, credit cards, private banking, life insurance, asset management, cash management, custody, trust, and securities and futures, all of which showed healthy development in the period. Good progress was made in the development and deployment of e-finance and our Big-data platform, which went into operation once the relevant infrastructure was constructed. We launched new services such as Apple Pay, Small-value Transfer, i-Service, and Instant Loan during the year. We also led the market in adopting blockchain technology in our mortgage valuation service, which helped to increase operating efficiency and served as a model of how to turn innovative ideas into reality. These efforts will not only benefit local FinTech development but also help elevate BOCHK's market position and brand recognition.

For our achievements during the year, BOCHK was named the Strongest Bank in Asia Pacific and Hong Kong and received the Best Retail Bank in Hong Kong and Wealth Management Business of the Year by *The Asian Banker*. Additionally, BOCHK received the Best Consumer Digital Bank in Hong Kong award by *Global Finance* and Listed Company Award of Excellence (Blue Chip) by *the Hong Kong Economic Journal*. For the ninth year in a row, BOCHK won the Best SME's Partner Award from the Hong Kong General Chamber of Small and Medium Business.

In 2016, BOCHK outpaced the market in key business areas such as loan growth, while increasing income and optimising the asset-liability structure. Throughout the year, we maintained our high standards of risk management, compliance and control, while key operating indicators such as capital adequacy ratios, liquidity coverage and asset quality all maintained at healthy levels. In short, this set of full year results was encouraging and achieved a fine balance between risk and return.

I am pleased to report that the Group delivered another year of record profits in 2016. During the year, the Group achieved strong growth in profit attributable to the equity holders, which grew by 105.7% year-on-year to HK$55,503 million. Earnings per share were HK$5.2496. Adjusted profit[2] increased by 6.8%, ahead of our major peers. Underpinned by these favourable results, the Board has recommended a final dividend of HK$0.625 per share. Together with the interim dividend of HK$0.545 per share, the full year dividend will be HK$1.170 per share. On a normal basis, the Company's total dividend payout as a percentage of profit attributable to the equity holders will be 48.4%. The realised gains of HK$29,956 million from the sale of our equity stake in NCB substantially increased the capital ratios of the Group. Taking into account various factors and the Board's view that the long-term development of the Group should be balanced with the interests of shareholders, the Company paid a special dividend of HK$0.710 per share after the 2016 interim results to reward pubic shareholders for their long-standing support of BOCHK over the years.

On 6 June 2016, Mr SHAN Weijian retired as an Independent Non-executive Director and ceased to be the chairman of the Audit Committee and a member of Remuneration Committee of the Company. Dr CHOI Koon Shum was appointed as an Independent Non-executive Director of the Company. On behalf of the Board, I would like to take this opportunity to express our great appreciation to Mr SHAN for his valuable contributions to the Company during his tenure of service, and welcome Dr CHOI to the Board. I believe Dr CHOI will bring new thinking to the Group with his extensive experience in the food industry, real estate development and international trade as well as technology and finance-related businesses. On 26 October 2016, due to a change in work arrangements, Mr CHAN Chun Ying resigned as the Board Secretary and Company Secretary of the Company and Bank of China (Hong Kong) Limited; he was succeeded by Mr LUO Nan. On behalf of the Board, I would like to thank Mr CHAN for his contributions to the Group during his tenure and to welcome Mr LUO to assume his position.

The year 2016 not only marked a successful new chapter in BOCHK's strategic transformation, but also another year of record results for us. This would not have been possible without the wisdom and guidance of the Board, the enthusiasm of our entire staff, the trust and loyalty

2 Without taking into consideration factors such as profit from discontinued operations and gain from disposal of certain equity instruments.

of our customers and the long-standing support of our shareholders, to whom I express my sincere gratitude.

If I may provide my perspective on what lies ahead in 2017, the banking industry will continue to face a mix of challenges and opportunities. Global politics and the world economy will remain full of complexity, uncertainty and cumulative financial risks. "De-globalisation" and reverse movements in liquidity are likely to cause a negative impact, which cannot be ignored. As a result, the world's major economies will find it increasingly difficult to align their monetary and fiscal policies. With the lack of clarity on the movement of US interest rates, the tightening of the Mainland's management of capital outflow, and the pre-emptive expansion of Chinese banking peers into the overseas market, competition in the banking industry looks set to intensify, presenting more challenges for business development and risk management. As China continues driving the Belt and Road Initiative forward, an increasing number of Mainland enterprises are eyeing globalisation opportunities, particularly in the markets of Southeast Asia. In its role as an international financial centre, Hong Kong can act effectively as a super-connector between China and the world by leveraging its robust legal system, highly efficient financial infrastructure and international talent pool. With the introduction of a series of market friendly policies by the Hong Kong SAR Government, including a preferential taxation arrangement and other government initiatives, setting up treasury centres in Hong Kong will become more attractive for multinational and Chinese corporations. This will help to generate enormous demand for banking and financial services, as well as other professional services. Furthermore, there has been growing demand for overseas asset allocation by Mainland enterprises and individuals, which will translate into potential business opportunities for a diverse range of banking services.

The momentum created by the Belt and Road Initiative, together with the growing integration of Guangdong Province, Hong Kong and Macau, should allow BOCHK to accelerate its regional development strategy by leveraging BOC Group's advantages of scale in both its overseas and domestic operations. This will involve focusing more on cross-border business, engaging with the local market and further developing our eight key business areas. In addition, we will continue to drive innovation and enhance our competitiveness in FinTech. In a challenging operating environment of increasing capital requirements and more rigorous regulation, it will also be critical for us to continue strengthening our asset-and-liability management, carefully monitoring our operating expenses and internal controls, and optimising our capital structure in order to ensure sustainable growth in the future.

Finally, I would like to note that the year 2017 marks the BOC's centenary of service to Hong Kong. During this centennial anniversary, we will continue to pursue opportunities for our business development and, as a socially-responsible corporate citizen, to contribute towards long-term prosperity and stability of Hong Kong. For the Group as a whole, this centennial year also represents a new chapter in our development. This is why we and everyone on our staff are pledged to continue pursuing excellence and to build on our solid foundation for the next 100 years for the benefit of shareholder value maximisation.

TIAN Guoli
Chairman
Hong Kong, 31 March 2017

Chief Executive's Report

YUE Yi
Vice Chairman & Chief Executive

In 2016, the global economy continued its mild growth pace while economic development on the Mainland reached a "new normal" and Hong Kong's economy slowed to an almost five-year low. In this challenging operating environment, we diligently implemented the Group's business strategy and executed the decisions of our Board. Taking advantage of market opportunities, we proactively explored new markets and introduced reforms and innovation. As a result, we attained another year of record results and elevated our brand and market position. We were named the Strongest Bank in Asia Pacific and Hong Kong for the third consecutive year and the Best Retail Bank in Hong Kong for the second consecutive year by *The Asian Banker*. We also received awards in many other business areas.

The Group's profitability continued to rise in 2016. Profit attributable to the equity holders grew by 105.7% year-on-year to HK$55,503 million, with adjusted profit[1] increasing by 6.8% to HK$23,712 million. Non-interest income rose 8.8% from 2015, bringing its share of net operating income before impairment allowances up by 1.76 percentage points. As at 31 December 2016, total assets amounted to HK$2,327,781 million, edging down 2.3% compared with the end of 2015 and basically filling the gap in total assets from the disposal of NCB. Return on average total assets ("ROA") and return on average shareholders' equity ("ROE") stood at 2.38% and 26.47%, respectively. The Group maintained a strong capital base, with a total capital ratio of 22.35% and Tier 1 capital ratio of 17.69%, up 4.49 percentage points and 4.80 percentage points respectively. Our liquidity position remained sound as we adhered to the regulatory requirements governing the liquidity coverage ratio ("LCR"). We also took proactive measures to optimise our asset and liability structure, with net interest margin rising from 1.29% in the first half of 2016 to 1.35% in the second half. Our asset quality improved continuously, with the classified or impaired loan ratio of 0.20%, down 0.03 percentage points compared with the end of 2015 and below the market average.

The Group grasped market opportunities and achieved sustainable and healthy business development in 2016. We endeavoured to support Belt and Road projects and Mainland enterprises going global. We also contributed to support the development of small- and medium-sized enterprises ("SMEs") and Hong Kong's real economy, while upgrading our services to government and public sector entities. In addition, we pushed forward the transformation

1 Without taking into consideration factors such as profit from discontinued operations and gain from disposal of certain equity instruments.

of our personal banking model and pursued business innovation. The development of the conventional deposit and loan business and agency business advanced in tandem. We also strengthened our cross-border services to meet the rising demand for overseas asset deployment by Mainland customers. This has enabled us to acquire more new customers. We expanded our treasury business by responding swiftly to market trends and introducing new financial products related to trading and investment. We also became the only overseas bank in the benchmarking of the Shanghai Gold price on the Shanghai Gold Exchange.

In pursuit of business diversification, we enhanced our eight major business platforms, namely credit cards, private banking, life insurance, asset management, cash management, custody, trust as well as securities and futures. To solidify our foundation for the sustainable development of our corporate banking business, we worked towards establishing a global transaction banking platform, explored collaborative business model of commercial and investment banking, and transformed our business under an asset- and capital-light model.

We reinforced our strength as a clearing bank and improved our core competitiveness in the RMB business. As the only clearing bank with both the China International Payment System ("CIPS") and the China National Automatic Payment System ("CNAPS") as our clearing channels, we continued to lead outstandingly in clearing volume among offshore markets. We obtained all business qualifications for Shenzhen-Hong Kong Stock Connect, following the earlier launch of Shanghai-Hong Kong Stock Connect. These included our appointment as the sole Settlement Bank for Northbound Trading by the Hong Kong Securities Clearing Company Limited. We also achieved rapid growth in the central bank customer segment and pursued new business opportunities related to the inclusion of RMB in the Special Drawing Rights ("SDR") basket of currencies.

As at the end of 2016, the Group had HK$1,507,501 million in customer deposit balances and HK$973,071 million in customer loan balances, up 9.8% and 11.7% year-on-year respectively, both growing faster than the market average. In addition, we made good progress in business related to the cross-border capital pool. We achieved a first-place ranking for the twelfth consecutive year as lead arrangers for syndicated loans in the Hong Kong and Macau region, and for the sixth consecutive year maintained the largest market share in the initial public offering ("IPO") receiving bank business. Moreover, our market share for new mortgage loans reached a four-year high.

We remained committed to promoting sustainable development through innovation and transformation as well as regional development. We made solid progress in our key business areas and strengthened our foundation for further development. First, we made substantial progress in our transformation from a local bank into a regional bank through asset restructuring. In 2016, we completed the transfer of NCB shares, the largest bank acquisition in Asia (excluding Japan), and recorded a profit of HK$30 billion, and also completed the acquisitions of Bank of China (Malaysia) Berhad. BOCHK's first overseas institution was opened in Brunei, completing BOC's financial service coverage to all 10 ASEAN nations. In the first quarter of 2017, we completed the acquisitions of Bank of China (Thai) Public Company Limited, and the disposal of all of our 70.49% interest in Chiyu. We entered into Acquisition Agreements with our parent bank in relation to the acquisitions of the Indonesia business and Cambodia business.

Second, we launched a branch network transformation project which expanded our service coverage to a comprehensive range from a retail focus. To fully capitalise on the Group's most extensive branch network in Hong Kong, we launched a full scale transformation of our branches, spurred on by the success of our pilot run. We upgraded our service capabilities to better serve SMEs and mid- and high-end personal customers with an integrated platform for a better customer experience.

Third, we stepped up our efforts in innovation to promote the development of financial technology ("FinTech") and mobile finance. We pioneered a number of Internet finance products, including a blockchain technology application for property valuation, our iService 24-hour video banking service, finger vein authentication, an interactive robot to provide customer-centric assistance, a Smart Investment Contest and QR-code based payments. Through all of these initiatives, we raised the intelligent service levels of our branches to give us a new competitive advantage in customer service. As a result, our customer base expanded notably in terms of Personal Internet Banking, Mobile Banking and Corporate Internet Banking, while our mobile payments, WeChat banking and other new service channels have become more appealing to young customers.

Fourth, as a domestic systemically important bank, we strictly adhered to the laws and guidelines set out by regulatory institutions and requirements of the Board and took the initiative to prevent various risks. We also improved our risk governance system and management to support the Group's sustainable and healthy development. We promoted a proactive risk management philosophy of planning ahead and managing more professionally and proactively. In addition, we drove business innovation with appropriate risk controls to accommodate relevant needs. Internal control and compliance management were also strengthened to prevent and tackle internal and external fraud. Additionally, we refined the Group's anti-money laundering measures and procedures for more effective control. We optimised our IT risk management framework and set up an intelligent cyber-security platform to contain these risks. We also improved our emergency response capability and reputational risk management.

For 2017, the international political and economic environment will remain complicated. The trend of subdued economic growth will continue globally amid weak trade performance, low interest rates and high risk. Rising protectionism and anti-globalist sentiments may cause greater uncertainty. All these, together with the competitive challenges from FinTech development, will make the operation and development of banks more difficult. Nevertheless, we also see many favourable factors and great opportunities. Although there will be downward pressure on the Hong Kong economy, it will be cushioned by a largely stable job market, sound public finances and ample liquidity. The banking industry will benefit from the further development of the major national strategies such as the Belt and Road Initiative, and Hong Kong's role as a super-connector. The RMB's inclusion into the SDR currency basket and its rise as a reserve and investment currency will also create new business opportunities for banks. What's more, we believe that continuous support from the Mainland of China will help Hong Kong further enhance its position and role in the economic development and opening-up of the Mainland. Hong Kong, in its role as an important international financial centre and with its unique One Country, Two Systems advantage, will continue to attract more businesses from the Mainland and overseas. BOCHK will also enjoy unprecedented opportunities with the support of its parent bank in consolidating BOC Group's Southeast Asia institutions and driving regional development.

The year 2017 marks the 20th anniversary of the return of Hong Kong to the motherland and the BOC's centenary of service to Hong Kong. On this special occasion, all sectors in society will pay greater attention to the Group, and our employees look forward to our future development with great anticipation. In the year ahead, the Group will fully implement various reform measures to increase efficiency and profits. We are confident in our prospects and have already developed and deployed a wide range of business strategies and measures. We will continue to develop our local business while exploring opportunities in Southeast Asian markets, particularly for our corporate banking business. We will also leverage our advantages to expand our cross-border business, while stepping up our regional expansion in Southeast Asia. In pursuit of business diversification, we will increase the development of our eight key business platforms. In addition, we will raise our professional standards and sharpen our competitive edge in the financial markets. We will remain focused on solidifying our deposit business, prudent management of our assets and liabilities as well as disciplined cost control. Our organisational structure and business processes will be optimised to improve the customer experience. In view of the potential of Internet finance to improve our competitiveness and productivity, we will continue to accelerate technological innovation.

We will strengthen our risk management and internal control to ensure compliance with various regulatory requirements. We will promote a good corporate culture and team building at all levels of the Group. As a socially responsible organisation, we aim to elevate our market influence and brand image, while contributing to Hong Kong's economic development and its long-term prosperity and stability, as well as improving the livelihood of the people.

On a final note, I would like to take this opportunity to express my heartfelt thanks to our customers, shareholders and friends for their generous support, as well as to the Board of Directors for their wise guidance, and to all of my colleagues for their diligence and contributions. What's past is prologue, and the new century is ushering in a new journey. We firmly believe that we are well positioned to create greater value for our stakeholders, given the Group's solid foundation and brand advantage, as well as our resolute and concerted efforts.

YUE Yi
Vice Chairman & Chief Executive
Hong Kong, 31 March 2017

FinTech Innovation

Management's Discussion and Analysis

As a result of the disposal of NCB and proposed disposal of Chiyu, the Group reported the financial results and positions of NCB and Chiyu in 2016 as discontinued operations, assets held for sale and liabilities associated with assets held for sale in the consolidated financial statements. The comparative amounts of consolidated income statement have been restated as if the discontinued operations had been discontinued at the beginning of year 2015. To facilitate a year-on-year comparison, comparative amounts of the consolidated balance sheet as well as certain financial ratios in this Management's Discussion and Analysis have been restated to enable analysis on a comparable basis.

Following the completion of the share acquisition of Bank of China (Malaysia) Berhad ("BOC Malaysia") on 17 October 2016, the Group has applied the merger accounting method in the preparation of financial statements for the combination with entity under common control. The comparative information for year 2015 has been restated accordingly.

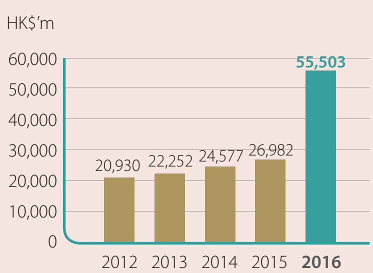
The above transactions are collectively referred as the "disposals and acquisition" in this Management's Discussion and Analysis.

Financial Performance and Conditions at a Glance

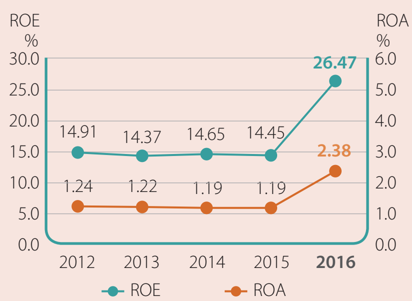
The following table is a summary of the Group's key financial results for the year 2016 in comparison with the previous four years. The average value of liquidity coverage ratio is reported on a quarterly basis.

Key Performance Trends

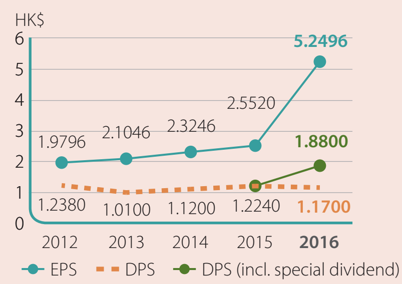
Profit Attributable to the Equity Holders



Return on Average Shareholders' Equity ("ROE") and Return on Average Total Assets ("ROA")



Earnings Per Share ("EPS") and Dividend Per Share ("DPS")



Profit attributable to the equity holders achieved a new high

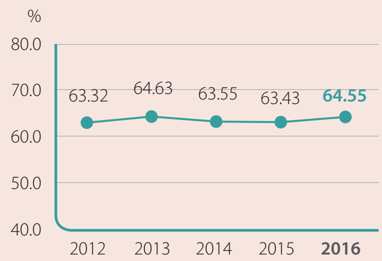
- Profit attributable to the equity holders increased by 105.7% year-on-year to HK$55,503 million.

Solid returns to shareholders

- ROE was 26.47%. ROE on continuing operations[1] was 12.23%.
- ROA was 2.38%. ROA on continuing operations[2] was 1.13%.
- EPS was HK$5.2496. Excluding the gain from the disposal of NCB, EPS would have been HK$2.4163. Dividend per share was HK$1.88, including the special dividend of HK$0.71 per share resulting from the gain on the disposal of all the issued shares of NCB.

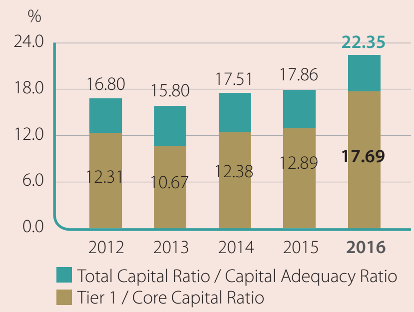
Financial Position

Loan to Deposit Ratio



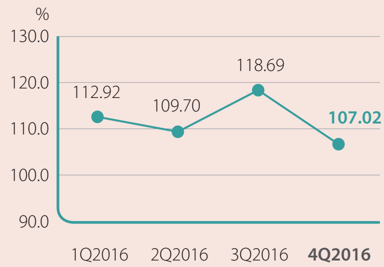
as at 31 December

Capital Ratio



as at 31 December

Average value of Liquidity Coverage Ratio



Loan to deposit ratio at a healthy level

- Advances to customers and deposits from customers grew by 11.7% and 9.8% respectively from the end of 2015. The loan to deposit ratio was 64.55%, up 1.12 percentage points from 63.43% at the end of 2015.

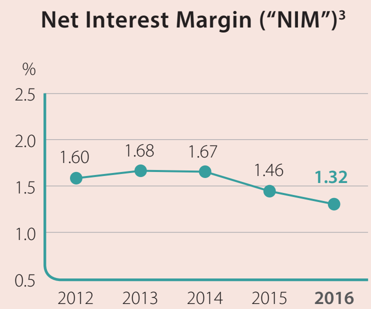
Enhanced capital position to support business growth

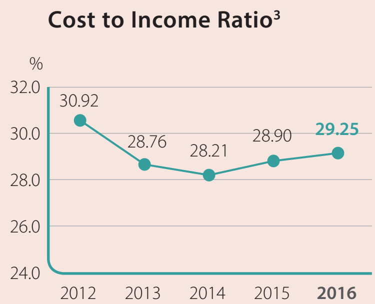
- The total capital ratio was 22.35% while the Tier 1 capital ratio was 17.69%, up 4.49 and 4.80 percentage points from that at the end of 2015.

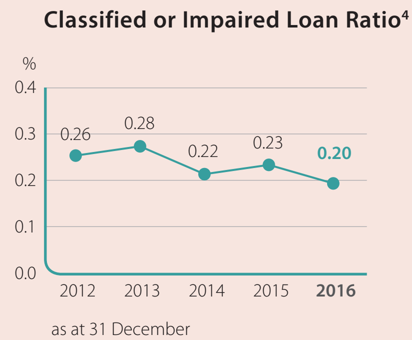
Sound liquidity position

- Average value of liquidity coverage ratio was well above the regulatory requirement throughout the four quarters of 2016.

Key Operating Ratios







Narrowing NIM with expanded asset size

- NIM was 1.32%, down 14 basis points year-on-year. The decrease was mainly due to the decrease in the average interest spread of RMB assets, caused by the drop in RMB market interest rates and the increase of RMB funds from the clearing bank business. The decrease in net interest margin was also due to the increase in short-term debt securities investments. NIM for the second half of 2016 improved half-on-half, up 6 basis points, which was attributable to lower deposit costs, an improved deposit mix and increased advances to customers.

Cautious cost control with better operational efficiency

- The cost to income ratio was 29.25%, up only 0.35 percentage point year-on-year, cost efficiency at a relatively good level in the industry.

Asset quality remained benign with classified or impaired loan ratio below market average

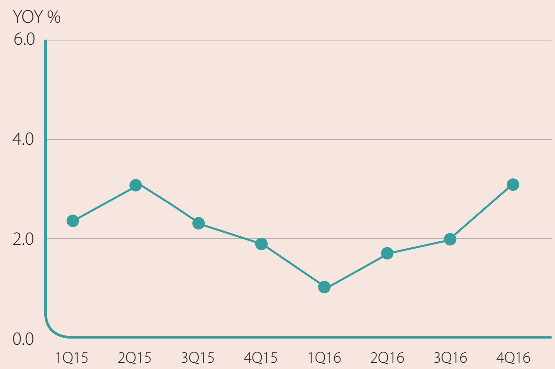
- The classified or impaired loan ratio was 0.20%, well below the market average.

1. ROE on continuing operations is calculated by dividing profit attributable to the equity holders from continuing operations by the average of the beginning and ending balance of capital and reserves attributable to the equity holders that excludes the impact of profit attributable to the equity holders from discontinued operations and special dividend paid.
2. ROA on continuing operations is calculated by dividing profit for the year from continuing operations by daily average balance of total assets excluding those of discontinued operations.
3. The financial information for the year 2016 is from continuing operations, and the comparative information has been restated accordingly. The Group has applied the merger accounting method in the preparation of financial statements for the combination with entity under common control in 2016. The comparative information for the year 2015 has been restated accordingly. However, the financial information prior to 2015 had not been restated as the difference before and after restatement is insignificant.
4. Classified or impaired loans represent advances which are either classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

Economic Background and Operating Environment

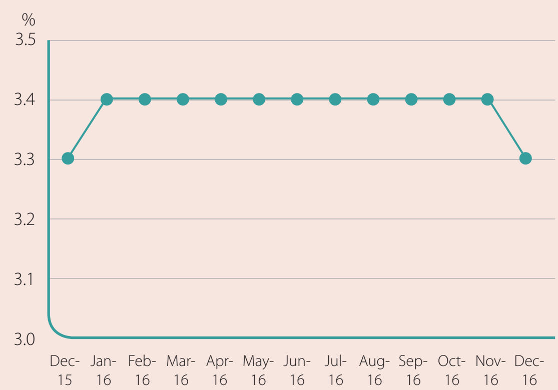
In 2016, global economic growth continued to be at a low level. In the US, the economy maintained a moderate growth trend in an improving employment market and with rising inflation. The US Federal Reserve raised the federal funds target rate in December, which was the second time in twelve months. In Europe, the Eurozone economy remained stable owing to the European Central Bank's ultra-loose monetary stance and despite fears that the Brexit referendum in June would significantly affect economic fundamentals. In ASEAN, the economy remained on track and outperformed global growth, supported by growing private and public consumption, robust infrastructure development and accommodative fiscal policy. In the Mainland of China, with accelerated restructuring and upgrading of traditional industries, as well as structural reform, economic growth remained stable despite headwinds from lacklustre international trade and weak private fixed asset investment.

Hong Kong Real GDP Growth Rate



Source: HKSAR Census and Statistics Department

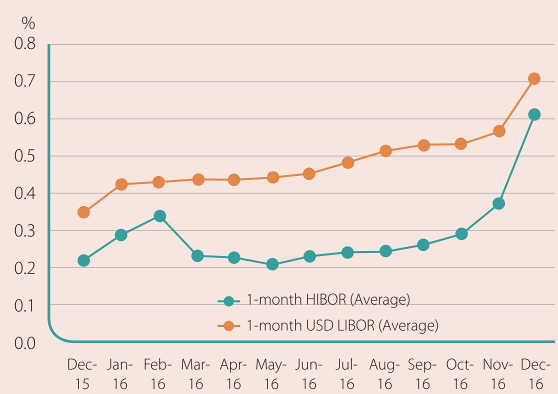
Hong Kong Unemployment Rate



Source: HKSAR Census and Statistics Department

In Hong Kong, the real GDP growth in 2016 was only 1.9% over the previous year. Sluggish international trade amid weakened global economic growth, and the structural adjustments in inbound tourism and retail sales hindered economic growth. The real GDP growth in the first quarter slowed to 1.0% over a year earlier. It gradually stablised and improved to 3.1% increase in the fourth quarter.

HIBOR and USD LIBOR



Source: Bloomberg

In 2016, there was abundant liquidity in the Hong Kong banking sector overall, and market interest rates continued at relatively low levels but there was increased volatility compared with 2015. In anticipation of a US interest rate hike, the average 1-month HIBOR and 1-month LIBOR rose from 0.23% and 0.20% respectively in 2015 to 0.30% and 0.50% respectively in 2016.

Management's Discussion and Analysis

In 2016, the Hong Kong stock market came under pressure at the beginning of the year, but resumed momentum during the second and third quarters, supported by factors including the smaller-than-expected contagion effect of Brexit, delay in US interest rate hikes and the approval of Shenzhen-Hong Kong Stock Connect implementation plan. The Hang Seng Index again experienced correction towards the end of the year, amid market concerns over imminent US interest rate hikes, finishing the year almost flat from the end of 2015. Transaction volumes decreased significantly from the high level in 2015.

During the year, local private domestic property price illustrated a V-shaped rebound, prompting the Government to raise the stamp duty in November 2016 as a corrective measure. The overall level of transaction activity in the local residential property market, in terms of the number of agreements for sale and purchase of residential building units, was lower than in 2015.

In 2016, the Mainland of China continued to introduce a number of initiatives to promote capital account convertibility and the internationalisation of the RMB. These included the relaxation of policies on Free Trade Zones ("FTZs"), allowing foreign entities to issue Panda bonds and participate in the Mainland's interbank bond market as well as the interbank foreign exchange market, and allowing overseas banks to join China's Cross-border Interbank Payment System ("CIPS"). RMB's inclusion in the Special Drawing Rights ("SDR") basket of currencies in October 2016 facilitated and encouraged offshore governments, central banks and institutions to invest in RMB assets. All of these initiatives encouraged the healthy development of the offshore RMB market and opened up new business opportunities to banks.

Banks in Hong Kong operated in a highly challenging environment in 2016. The global economic slowdown, destocking in the Mainland and increasing finance costs for Mainland corporates in Hong Kong continued to hinder loan demand. As low interest rates prevailed and market competition intensified, banks' profitability remained under pressure. Furthermore, the contraction of the local RMB funding pool intensified competition for offshore RMB deposits in Hong Kong and hence created upward pressure on deposit costs. Nevertheless, banks also had new opportunities to expand their business from the implementation of China's important strategies, such as the Belt and Road Initiative, Going Global Strategy and the inclusion of the RMB into the SDR basket.

Outlook for 2017

Heading into 2017, the overall operating environment for banks in Hong Kong will remain challenging. The trend of subdued economic growth will continue globally amid elevated political, economic and financial uncertainties. In the US, the labour market continues to improve and economic activities resume at a moderate pace. These, coupled with the support of low oil prices and accommodative monetary policy, economic growth is expected to improve somewhat. In some of the Eurozone member states, the prospect of elections in 2017 is creating new uncertainties. In the Mainland of China, the economic restructuring will continue to exert downward pressure on industrial production and investment, although economic growth is expected to continue at a steady rate supported by a proactive fiscal policy and stable monetary policy. In Hong Kong, the subdued global environment will probably maintain growth at a low level. External trade is unlikely to improve in the short-term amid the uncertainties arising from the strong US dollar, protective new trade policies that the US might initiate, the outcome of the Brexit trade negotiations, and the continuous restructuring and relocation of manufacturing in the Mainland. Further development of the RMB business in Hong Kong will require additional impetus across all channels amid the downward pressure on RMB exchange rates and the narrowing of onshore and offshore RMB interest rate differentials.

On a more positive note, domestic demand in Hong Kong, including private consumption and investment, is likely to be supported by a resilient labour market, the low interest rate environment, some consolidation in the property market and the benefits that accrue from the Mainland's financial reforms. What's more, the Mainland's important strategies, such as the Belt and Road Initiative and Going Global Strategy, and the deepening of RMB internationalisation will help to propel the growth of the offshore RMB market. In addition, growth trends are expected to be divergent in ASEAN member countries. However, as a key region for the Belt and Road Initiative and a market with significant potential, the ASEAN economy will see ample opportunities, including those from a number of new infrastructure projects, rising demand for financial services and a broader use of RMB in the region, and provide more business opportunities for banks in Hong Kong.

Consolidated financial review

The comparative information for the year 2015 has been restated as a result of the Group's disposals and acquisition.

Financial Highlights

HK$'m, except percentages	2016	(Restated) 2015	Change (%)
CONTINUING OPERATIONS			
Net operating income before impairment allowances	**41,754**	40,181	3.9
Operating expenses	**(12,213)**	(11,611)	5.2
Operating profit before impairment allowances	**29,541**	28,570	3.4
Operating profit after impairment allowances	**28,963**	27,815	4.1
Profit before taxation	**29,452**	28,575	3.1
Profit attributable to the equity holders of the Company	**55,503**	26,982	105.7

In 2016, the Group's profit attributable to the equity holders increased to HK$55,503 million, up 105.7% year-on-year, a new high since its listing. The Group proactively implemented Bank of China Group's strategies and captured market opportunities. It actively explored business opportunities in the ASEAN and expedited the development of business transformation and technological innovation, and continued to refine its business structure to become more customer-centric. It optimised its distribution channels and Internet finance capabilities in order to enhance its overall service capabilities. The Group also reinforced its strong franchise in RMB clearing business and stepped up its efforts in building key business platforms. It leveraged its competitive edge to achieve satisfactory performance in its core business areas. Key financial indicators remained at solid levels.

During the year, the Group's regional development plans gathered pace with synergies beginning to emerge. It successfully completed the sale of NCB and steadily pushed forward its proposed sale of shares in Chiyu. Meanwhile, it restructured its business in the ASEAN region in an orderly manner and completed the share acquisition of Bank of China (Malaysia) Berhad and Bank of China (Thai) Public Company Limited ("BOC Thailand") on 17 October 2016 and 9 January 2017 respectively. On 20 December 2016, BOCHK's first overseas institution in Brunei Darussalam ("Brunei") – the Brunei Branch formally commenced business, further optimising its business network.

The Group further improved its risk management, internal controls and compliance to safeguard its healthy and sustainable development. During the year, it further optimised its asset and liability structure. Total deposits and loans grew rapidly and ahead of the market with a higher market share. The proportion of current and savings deposits continued to rise, with asset quality outperforming the market.

Profits of 2016 and 2015 included factors such as profit from discontinued operations and gain from disposal of certain equity instruments. Without taking into consideration these factors, the Group's profit attributable to the equity holders in 2016 increased by 6.8% from 2015.

Profit attributable to the equity holders from continuing operations increased by HK$444 million, or 1.9%, year-on-year to HK$24,201 million, which was attributable to the higher net operating income before impairment allowances. The increase in net operating income was driven by the strong growth in net trading gain of the banking business, mainly contributed by the net gain from foreign exchange swap contracts in 2016. Net interest income was higher due to the expansion in average interest-earning assets, but the increase was partially offset by the lower net interest margin. Also contributing to the increase in net operating income was the improved performance of the Group's insurance segment. The increase was, however, partially offset by the decline in net fee and commission income. Meanwhile, operating expenses rose, reflecting the Group's efforts to strengthen resource allocation and continuous investment in human resources and infrastructure enhancements to support its long-term growth. The net charge of loan impairment allowances dropped, due to the lower net charge of individually assessed impairment allowances. As a result, profit increased year-on-year.

Second Half Performance

As compared with the first half of 2016, net operating income before impairment allowances of continuing operations increased by HK$888 million, or 4.3% half-on-half. This growth in net operating income was attributable to higher net interest income from the rebound in net interest margin and the expansion in average interest-earning assets. Net operating income of the Group's insurance segment also rose. The increase was partially offset by the decline in net fee and commission income. Operating expenses increased by HK$765 million, or 13.4%, while the net charge of loan impairment allowances decreased by HK$479 million, or 89.7%. As a result, profit rose by HK$715 million, or 6.1%, on a half-on-half basis, to HK$12,458 million.

Income Statement Analysis

The following income statement analysis is based on the Group's continuing operations, and the comparative information has been restated as a result of the Group's disposals and acquisition.

Net Interest Income and Net Interest Margin

HK$'m, except percentages	2016	(Restated) 2015	Change (%)
Interest income	**35,890**	37,492	(4.3)
Interest expense	**(10,462)**	(12,316)	(15.1)
Net interest income	**25,428**	25,176	1.0
Average interest-earning assets	**1,918,837**	1,729,850	10.9
Net interest spread	**1.22%**	1.36%	
Net interest margin*	**1.32%**	1.46%	

* Net interest margin is calculated by dividing net interest income by average interest-earning assets.

The Group's net interest income increased by HK$252 million, or 1.0%, year-on-year. The increase was attributable to the growth in average interest-earning assets, partially offset by the lower net interest margin.

Average interest-earning assets expanded by HK$188,987 million, or 10.9%. The increase in the average balances of deposits from customers as well as deposits from banks led to the increase in the average balances of both advances to customers and debt securities investments.

Net interest margin was 1.32%, down 14 basis points. In view of the challenging operating environment, the Group continued to manage its deposit pricing and deposit mix and at the same time grew its loan portfolio, which led to the positive impact to net interest margin. However, the lower average interest spread of the RMB business, which was caused by the drop in RMB market interest rates and the increase of RMB funds from the clearing bank business, offset the positive impact described above. The narrowing of net interest margin was also due to the increase in lower-yielding short-term debt securities investments.

The table below summarises the average balances and average interest rates of individual categories of assets and liabilities:

	2016		(Restated) 2015	
ASSETS	Average balance HK$'m	Average yield %	Average balance HK$'m	Average yield %
Balances and placements with banks and other financial institutions	**325,274**	**1.37**	346,278	2.36
Debt securities investments	**632,911**	**1.62**	547,447	1.93
Advances to customers	**938,700**	**2.23**	821,139	2.26
Other interest-earning assets	**21,952**	**0.89**	14,986	1.40
Total interest-earning assets	**1,918,837**	**1.87**	1,729,850	2.17
Non interest-earning assets[1]	**450,263**	**–**	597,586	–
Total assets	**2,369,100**	**1.51**	2,327,436	1.61

LIABILITIES	Average balance HK$'m	Average rate %	Average balance HK$'m	Average rate %
Deposits and balances from banks and other financial institutions	**227,237**	**0.75**	209,497	0.91
Current, savings and time deposits	**1,331,609**	**0.57**	1,244,154	0.75
Subordinated liabilities	**19,435**	**3.05**	19,560	2.25
Other interest-bearing liabilities	**35,917**	**1.51**	38,724	1.76
Total interest-bearing liabilities	**1,614,198**	**0.65**	1,511,935	0.81
Shareholders' funds[2] and other non interest-bearing deposits and liabilities[1]	**754,902**	**–**	815,501	–
Total liabilities	**2,369,100**	**0.44**	2,327,436	0.53

1. Including assets held for sale and liabilities associated with assets held for sale respectively.
2. Shareholders' funds represent capital and reserves attributable to the equity holders of the Company.

Second Half Performance

Compared with the first half of the year, net interest income increased by HK$1,580 million, or 13.3%, to HK$13,504 million, due to the growth in average interest-earning assets and the rebound in net interest margin. Average interest-earning assets were up HK$122,001 million, or 6.6%, which was supported by the increase in deposits from customers. Net interest margin was 1.35%, a rise of 6 basis points half-on-half. The widening of net interest margin was attributable to lower deposit costs through effective pricing control, an improved deposit mix and increased advances to customers. The increase was partially offset by the increase in lower-yielding short-term debt securities investments.

Net Fee and Commission Income

HK$'m, except percentages	2016	(Restated) 2015	Change (%)
Credit card business	**3,702**	3,726	(0.6)
Loan commissions	**3,500**	3,239	8.1
Securities brokerage	**1,954**	3,255	(40.0)
Insurance	**1,630**	1,467	11.1
Funds distribution	**735**	901	(18.4)
Bills commissions	**631**	561	12.5
Payment services	**593**	561	5.7
Trust and custody services	**470**	473	(0.6)
Currency exchange	**336**	302	11.3
Safe deposit box	**277**	248	11.7
Others	**944**	839	12.5
Fee and commission income	**14,772**	15,572	(5.1)
Fee and commission expense	**(4,231)**	(4,299)	(1.6)
Net fee and commission income	**10,541**	11,273	(6.5)

Net fee and commission income decreased by HK$732 million, or 6.5%, to HK$10,541 million in 2016. The decrease was mainly attributable to the stock market turnover in 2016 amid the weakened investment sentiment, which resulted in the decline of 40.0% and 18.4% respectively in fee and commission income from securities brokerage and funds distribution from 2015. However, income from other businesses recorded satisfactory growth year-on-year as the Group leveraged its diversified business platforms to record healthy growth in a number of areas. Loan commissions rose by 8.1%, due to the growth of commission income from corporate loans. During the year, the Group captured opportunities from the Belt and Road Initiative and in the Southeast Asia, actively explored financing needs of Mainland corporates seeking global expansion and also cultivated the Hong Kong market. These resulted in satisfactory growth in new loan drawdowns and loan commissions. With the rise in business volumes, income from insurance and bills commissions increased by 11.1% and 12.5% respectively. Income from currency exchange rose 11.3%, driven by the higher demand for foreign currency banknotes. Commission income from payment services and safe deposit box also recorded healthy growth.

Second Half Performance

Compared with the first half of 2016, net fee and commission income dropped by HK$671 million, or 12.0%, in the second half. On one hand, the Group was able to achieve strong growth of 29.1% in commission income from securities brokerage. Income from funds distribution, trust and custody services along with payment services also grew. On the other hand, loan commissions dropped from the high level in the first half, as did bills commissions. Fee and commission expense rose, which was mainly attributable to higher insurance and securities brokerage related expenses.

Net Trading Gain

HK$'m, except percentages	2016	(Restated) 2015	Change (%)
Foreign exchange and foreign exchange products	**3,618**	2,051	76.4
Interest rate instruments and items under fair value hedge	**867**	295	193.9
Equity and credit derivative instruments	**88**	194	(54.6)
Commodities	**32**	57	(43.9)
Net trading gain	**4,605**	2,597	77.3

Net trading gain increased by HK$2,008 million, or 77.3% year-on-year, to HK$4,605 million. Net trading gain from foreign exchange and foreign exchange products increased by HK$1,567 million, primarily due to the net gain from foreign exchange swap contracts*, as well as the increase in currency exchange income from customer transactions. Net trading gain from interest rate instruments and items under fair value hedge increased by HK$572 million, which was mainly attributable to the mark-to-market changes of certain debt securities and interest rate instruments, caused by interest rate movements. The decrease in net trading gain from equity and credit derivative instruments was mainly due to the decreased income from equity-linked products. The decrease in net trading gain from commodities was mainly due to the lower gain in bullion transactions.

Second Half Performance

Compared with the first half of 2016, net trading gain decreased slightly by HK$25 million, or 1.1%. The decrease was mainly attributable to the mark-to-market changes of certain debt securities.

* Foreign exchange swap contracts are normally used for the Group's liquidity management and funding activities. In foreign exchange swap contracts, the Group exchanges one currency (original currency) for another (swapped currency) at the spot exchange rate (spot transaction) and commits to reverse the spot transaction by exchanging the same currency pair at a future maturity date at a predetermined rate (forward transaction). In this way, surplus funds in the original currency are swapped into another currency for liquidity and funding purposes with minimal foreign exchange risk. The exchange difference between the spot and forward contracts is recognised as a foreign exchange gain or loss (as included in "net trading gain"), while the corresponding interest differential between the surplus funds in the original currency and swapped currency is reflected in net interest income.

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

HK$'m, except percentages	2016	(Restated) 2015	Change (%)
Net gain/(loss) on financial instruments designated at fair value through profit or loss	**101**	(751)	N/A

The Group recorded a net gain of HK$101 million on financial instruments designated at FVTPL in 2016, compared with a net loss of HK$751 million in 2015. The change was mainly attributable to the mark-to-market gains of debt securities and bond fund investments of BOC Life in 2016, as opposed to the mark-to-market losses in 2015, with the former being caused by market interest rates movements. The changes in market value of its debt securities portfolio were offset by the corresponding changes in policy reserves, as reflected in the changes in net insurance benefits and claims attributable to the movement of market interest rates.

Second Half Performance

A net loss of HK$933 million was recorded in the second half of the year, as opposed to a net gain of HK$1,034 million in the first half. The change was mainly attributable to the mark-to-market loss of debt securities investments of BOC Life, compared with the mark-to-market gain in the first half.

Operating Expenses

HK$'m, except percentages	2016	(Restated) 2015	Change (%)
Staff costs	**6,787**	6,420	5.7
Premises and equipment expenses (excluding depreciation)	**1,557**	1,412	10.3
Depreciation on owned fixed assets	**1,788**	1,713	4.4
Other operating expenses	**2,081**	2,066	0.7
Total operating expenses	**12,213**	11,611	5.2

	At 31 December 2016	(Restated) At 31 December 2015	Change (%)
Staff headcount measured in full-time equivalents	**12,154**	12,236	(0.7)

Total operating expenses increased by HK$602 million, or 5.2%, from 2015, as a result of the Group's ongoing investment in human resources and projects, including enhancements in business systems and platforms as well as Internet finance services, to support long-term business growth. The Group remained focused on disciplined cost control, however, and the cost to income ratio was below the industry average at 29.25%.

Staff costs increased by 5.7% year-on-year, mainly due to higher salaries following the annual salary increment.

Premises and equipment expenses were up 10.3%, reflecting higher rental costs and IT-related expenses associated with the Group's strategic initiatives.

Depreciation on owned fixed assets rose by 4.4%, largely due to a larger depreciation charge on premises following the upward property revaluation in Hong Kong in 2015 and on IT infrastructure.

Second Half Performance

Compared with the first half of 2016, operating expenses rose by HK$765 million, or 13.4%, in the second half of the year. The increase was due to higher staff costs and IT-related expenses, as well as an increase in advertising and business promotional expenses.

Net Charge of Loan Impairment Allowances

HK$'m, except percentages	2016	(Restated) 2015	Change (%)
Net (charge)/reversal of allowances before recoveries			
– individually assessed	**(31)**	(412)	(92.5)
– collectively assessed	**(694)**	(537)	29.2
Recoveries	**136**	143	(4.9)
Net charge of loan impairment allowances	**(589)**	(806)	(26.9)

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

	At 31 December 2016	(Restated) At 31 December 2015
Loan impairment allowances		
– individually assessed	**0.05%**	0.06%
– collectively assessed	**0.27%**	0.27%
Total loan impairment allowances	**0.32%**	0.33%

The net charge of loan impairment allowances was HK$589 million in 2016, a decrease of HK$217 million from 2015. Net charge of individually assessed impairment allowances fell by 92.5%, mainly caused by the reversal of impairment allowances for a few corporate advances. Net charge of collectively assessed impairment allowances amounted to HK$694 million, up 29.2%, mainly attributable to the higher growth rate of advances to customers in 2016.

Total loan impairment allowances as a percentage of gross advances to customers was 0.32%, which was relatively unchanged from 2015.

Second Half Performance
Net charge of loan impairment allowances decreased by HK$479 million, or 89.7%, from the first half of the year. The decrease was due to the net reversal of individually assessed impairment allowances in the second half of the year as opposed to the net charge in the first half. Meanwhile, there was a lower net charge of collectively assessed impairment allowances owing to lower loan growth in the second half of the year.

Balance Sheet Analysis

The comparative information at 31 December 2015 has been realigned to enable analysis on a comparable basis.

Asset Deployment

HK$'m, except percentages	At 31 December 2016 Amount	At 31 December 2016 % of total	(Restated) At 31 December 2015 Amount	(Restated) At 31 December 2015 % of total	Change (%)
Cash and balances with banks and other financial institutions	**229,073**	**9.9**	225,985	9.5	1.4
Placements with banks and other financial institutions maturing between one and twelve months	**70,392**	**3.0**	62,661	2.6	12.3
Hong Kong SAR Government certificates of indebtedness	**123,390**	**5.3**	101,950	4.3	21.0
Securities investments[1]	**659,523**	**28.3**	564,075	23.7	16.9
Advances and other accounts	**992,137**	**42.6**	901,082	37.8	10.1
Fixed assets and investment properties	**63,959**	**2.8**	63,998	2.7	(0.1)
Other assets[2]	**136,014**	**5.8**	109,350	4.6	24.4
Assets held for sale	**53,293**	**2.3**	353,714	14.8	(84.9)
Total assets	**2,327,781**	**100.0**	2,382,815	100.0	(2.3)

1. Securities investments comprise investment in securities and financial assets at fair value through profit or loss.
2. Interests in associates and a joint venture, deferred tax assets and derivative financial instruments are included in other assets.

As at 31 December 2016, total assets of the Group amounted to HK$2,327,781 million, a decrease of HK$55,034 million, or 2.3%, from the end of 2015. The decrease in total assets was attributable to the decrease in assets held for sale following the Group's disposal of NCB in 2016. The Group continued to enhance its management of assets and liabilities and successfully expanded its businesses amid challenges in the operating environment.

Key changes in the Group's total assets include the following:

- Securities investments increased by HK$95,448 million, or 16.9%, with increases mainly in government-related and high-quality banks and financial institutions bonds.
- Advances and other accounts rose by HK$91,055 million, or 10.1%, with the growth in advances to customers by HK$101,945 million, or 11.7%.
- Other assets grew by HK$26,664 million, or 24.4%, mainly due to the increases in derivative financial instruments, and accounts receivable and prepayments.
- Assets held for sale decreased by HK$300,421 million, or 84.9% as the Group completed the disposal of NCB on 30 May 2016. As a result of the Group's proposed disposal of Chiyu, assets of Chiyu as at 31 December 2016 are presented separately as assets held for sale.

Advances to Customers

HK$'m, except percentages	At 31 December 2016 Amount	At 31 December 2016 % of total	(Restated) At 31 December 2015 Amount	(Restated) At 31 December 2015 % of total	Change (%)
Loans for use in Hong Kong	**663,415**	**68.2**	550,713	63.2	20.5
Industrial, commercial and financial	**374,891**	**38.5**	284,241	32.6	31.9
Individuals	**288,524**	**29.7**	266,472	30.6	8.3
Trade finance	**72,121**	**7.4**	78,593	9.0	(8.2)
Loans for use outside Hong Kong	**237,535**	**24.4**	241,820	27.8	(1.8)
Total advances to customers	**973,071**	**100.0**	871,126	100.0	11.7

In 2016, the Group succeeded in capturing opportunities arising from national strategies and growth opportunities in the ASEAN region. It continued to leverage its strong customer base and strengthened collaboration with BOC to reinforce financial services offered to corporates, in particular, for Mainland enterprises going global and leading corporates in the ASEAN region. The Group remained the top mandated arranger in the Hong Kong-Macau syndicated loan market for the twelfth consecutive year. It also strongly supported leading corporates and SMEs in the local market. The Group adhered to a prudent credit strategy and focused on customer selection to achieve quality growth. Advances to customers grew by HK$101,945 million, or 11.7%, to HK$973,071 million in 2016.

Loans for use in Hong Kong grew by HK$112,702 million or 20.5%.

- Lending to the industrial, commercial and financial sectors increased by HK$90,650 million, or 31.9%, representing a broad-based growth in various industry sectors including property development, transport and transport equipment, wholesale and retail trade, manufacturing, information technology and recreational activities.

- Lending to individuals increased by HK$22,052 million, or 8.3%. Residential mortgage loans (excluding those under government-sponsored home purchasing schemes) grew by 5.4% while other individual loans increased by 29.0%.

Trade finance decreased by HK$6,472 million, or 8.2%, while loans for use outside Hong Kong decreased by HK$4,285 million, or 1.8%.

Loan Quality

HK$'m, except percentages	At 31 December 2016	(Restated) At 31 December 2015
Advances to customers	**973,071**	871,126
Classified or impaired loan ratio	**0.20%**	0.23%
Total impairment allowances	**3,124**	2,906
Total impairment allowances as a percentage of advances to customers	**0.32%**	0.33%
Residential mortgage loans[1] – delinquency and rescheduled loan ratio[2]	**0.02%**	0.02%
Card advances – delinquency ratio[2]	**0.24%**	0.20%

	2016	2015
Card advances – charge-off ratio[3]	**1.51%**	1.39%

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

The Group maintained benign asset quality during the year. The classified or impaired loan ratio was 0.20% as at 31 December 2016. Classified or impaired advances to customers decreased by HK$39 million, or 2.0%, to HK$1,955 million.

The credit quality of the Group's residential mortgage loans and card advances remained sound. The combined delinquency and rescheduled loan ratio of residential mortgage loans was 0.02% at the end of 2016. The charge-off ratio of card advances was 1.51%.

Deposits from Customers*

HK$'m, except percentages	At 31 December 2016 Amount	At 31 December 2016 % of total	(Restated) At 31 December 2015 Amount	(Restated) At 31 December 2015 % of total	Change (%)
Demand deposits and current accounts	**172,427**	**11.5**	130,958	9.5	31.7
Savings deposits	**796,571**	**52.8**	701,304	51.1	13.6
Time, call and notice deposits	**535,078**	**35.5**	538,478	39.2	(0.6)
	1,504,076	**99.8**	1,370,740	99.8	9.7
Structured deposits	**3,425**	**0.2**	2,571	0.2	33.2
Total Deposits from customers	**1,507,501**	**100.0**	1,373,311	100.0	9.8

* Including structured deposits

In 2016, the Group implemented a number of deposit strategies and flexibly responded to market changes, achieving good progress in deposit taking, improvement in deposit mix and lowering of deposit costs. The measures included expansion of wealth management business for the mid- to high-end customer segment, development of payroll account services, expansion of central bank and supranational clients, and development of receiving bank business for IPOs. Consequently, total deposits from customers rose by HK$134,190 million, or 9.8%, to HK$1,507,501 million at the end of 2016. The proportion of current and savings deposits increased to 64.3%, up 3.7 percentage points from the end of 2015. Time, call and notice deposits fell by 0.6%. Savings deposits increased by 13.6% while demand deposits and current accounts grew strongly by 31.7%.

Capital and Reserves Attributable to the Equity Holders of the Company

HK$'m, except percentages	At 31 December 2016	(Restated) At 31 December 2015	Change (%)
Share capital	**52,864**	52,864	–
Premises revaluation reserve	**35,608**	40,278	(11.6)
Reserve for fair value changes of available-for-sale securities	**(592)**	294	N/A
Regulatory reserve	**9,227**	10,928	(15.6)
Translation reserve	**(722)**	(346)	108.7
Merger reserve	**–**	1,789	(100.0)
Retained earnings	**128,268**	88,943	44.2
Reserves	**171,789**	141,886	21.1
Capital and reserves attributable to the equity holders of the Company	**224,653**	194,750	15.4

Capital and reserves attributable to the equity holders of the Company amounted to HK$224,653 million as at 31 December 2016, an increase of HK$29,903 million, or 15.4%, from the end of 2015. Retained earnings rose by 44.2%, mainly reflecting the profit for 2016 after the appropriation of dividends. The premises revaluation reserve decreased by 11.6%, which was attributable to the corresponding amount released to retained earnings upon disposal of discontinued operations and the decline in the valuation of premises in 2016. Reserve for fair value changes of available-for-sale securities turned from a surplus into a deficit, mainly reflecting market interest rate movements. The regulatory reserve fell by 15.6%, as the growth in advances to customers was more than offset by the corresponding regulatory reserve released to retained earnings upon the disposal of discontinued operations. Merger reserve was arising on the Group's application of merger accounting method in relation to the combination with BOC Malaysia.

Capital Ratio and Liquidity Coverage Ratio

HK$'m, except percentages	At 31 December 2016	At 31 December 2015
Consolidated capital after deductions		
Common Equity Tier 1 capital	**158,828**	121,089
Additional Tier 1 capital	**458**	561
Tier 1 capital	**159,286**	121,650
Tier 2 capital	**41,926**	46,886
Total capital	**201,212**	168,536
Total risk-weighted assets	**900,288**	943,802
Common Equity Tier 1 capital ratio	**17.64%**	12.83%
Tier 1 capital ratio	**17.69%**	12.89%
Total capital ratio	**22.35%**	17.86%

	2016	2015
Average value of liquidity coverage ratio		
First quarter	**112.92%**	101.90%
Second quarter	**109.70%**	109.89%
Third quarter	**118.69%**	104.00%
Fourth quarter	**107.02%**	106.52%

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

The Banking (Capital) (Amendment) Rules 2014 came into effect on 1 January 2015 as a means of implementing the Basel III capital buffer requirements arising from the operation of the Capital Conservation Buffer ("CCB") and Countercyclical Capital Buffer ("CCyB"), as well as the Higher Loss Absorbency ("HLA") requirement for domestic systemically important authorised institutions ("D-SIBs") that came into effect on 1 January 2016. The CCB is designed to ensure that banks build up capital outside periods of stress, which can be drawn down when losses are incurred. The CCyB is set on a individual country basis and is built up during periods of excessive credit growth for absorbing future losses, and the HLA is an additional capital requirement for D-SIBs. These three requirements are expressed as a percentage of the Common Equity Tier 1 ("CET1") capital to the risk-weighted assets ("RWAs") of an authorised institution ("AI") and under the phase-in arrangements from 2016 to 2019. The CCB begins with a rate of 0.625% of RWAs in 2016 and will increase each subsequent year by an additional 0.625% to reach its final of 2.5% of RWAs on 1 January 2019. On 27 January 2015 and 14 January 2016, the HKMA announced a CCyB for Hong Kong of 0.625% and 1.25% of RWAs from 1 January 2016 and 1 January 2017 respectively, equivalent to 2.5% once fully implementation of Basel III. On 16 March 2015 and 31 December 2015, the HKMA announced the designation of BOCHK as one of the D-SIBs in Hong Kong, requiring BOCHK to establish 0.375% and 0.75% of RWAs for HLA from 1 January 2016 and 1 January 2017 respectively, equivalent to 1.5% on full implementation of Basel III.

The Group's capital level was significantly enhanced by the gain from the disposal of NCB. With the phase-in arrangements of the Basel III capital buffer requirements that came into effect from 2016, the Group responded to this higher regulatory requirement by opting to comply with the 2019 Basel III capital buffer requirements in one go during the course of formulating its internal capital management targets. In addition to this regulatory requirement, the Group took into consideration its strategic initiatives and risk appetite as well as its short- and long-term capital requirement, with the support of capital replenishment solutions, to ensure the long-term stability of its capital level. The Group attached a high degree of importance to the need for capital accumulation and focused on internal growth to ensure its sustainable business development. To meet these requirements, the Group continued to refine its measures to monitor changes in the risk-weights of its assets. At the same time, the Group made use of stringent and forward-looking stress testing to assess the demand and supply of capital under different stress scenarios, examine management targets for capital adequacy and formulate a capital adjustment solution to ensure the Group's ability to comply with the capital requirement under stress conditions.

During the year, the Group complied with all capital requirements of the HKMA. At 31 December 2016, the CET1 capital ratio was 17.64% and Tier 1 capital ratio was 17.69%, up 4.81 and 4.80 percentage points respectively from the end of 2015. Profits net of dividends for the year 2016 drove up CET1 capital and Tier 1 capital by 31.2% and 30.9% respectively. Total RWAs were down 4.6%, as the increase in credit RWAs due to the growth in advances to customers in 2016 was more than offset by the reduction in RWAs following the disposal of NCB. The total capital ratio was 22.35%.

The average value of the liquidity coverage ratio ("LCR") is calculated based on the arithmetic mean of the LCR as at the end of each working day in the quarter and the calculation methodology and instructions set out in the HKMA return of liquidity position. The LCR is computed on a consolidated basis, which comprises the positions of BOCHK and certain subsidiaries specified by the HKMA in accordance with the Banking (Liquidity) Rules.

The Group's liquidity position stayed at a solid level in 2016. The average value of LCR for all four quarters of 2016 are as above, which were higher than the regulatory minimum.

Business Review

2016 Business Highlights

Personal Banking

- Completed implementation of the branch transformation project, with upgrade of the branch network and optimisation of business workflows, to provide a more comprehensive range of services for both personal and corporate customers in Hong Kong. Operating efficiency was significantly enhanced, and a number of businesses achieved satisfactory growth.
- Built an omni-channel banking service and launched a series of new functions, including the 24-hour video banking iService.
- Committed to the development of the cross-border business to meet the increasing demand for overseas asset deployment by Mainland customers. Continuously refined the customer mix and introduced a new service model for the wealth management business, which successfully expanded the mid- to high-end customer segment in Hong Kong and Mainland of China.
- Named Best Retail Bank in Hong Kong for two consecutive years; awarded Wealth Management Business of the Year 2016 by *The Asian Banker*.

Corporate Banking

- Succeeded in capturing opportunities from major national strategic initiatives, including the Belt and Road. Provided a comprehensive range of financial services in support of Mainland enterprises' overseas expansion. Completed financing projects for a number of cross-border merger and acquisition ("M&A") transactions and major projects for leading local enterprises in the ASEAN region.
- Leveraged the synergy arising from collaboration within the Group and its platform for cross-border business development in FTZs and enhanced market influence.
- Cultivated the local market by expanding its customer base in the commercial sector and institutional business. Continued to establish business relationships with overseas central banks and financial institutions and, in a major breakthrough for the Group, a relationship with a large overseas sovereign wealth fund.
- Through the branch transformation project integrating commercial centres and branches, the Group reinforced its service and sales capabilities for local SME customers.
- Arranged a number of significant syndicated loans and remained the top mandated arranger in the Hong Kong-Macau syndicated loan market for the twelfth consecutive year.
- Acted as the receiving bank for a number of major IPOs in Hong Kong, including one of the year's largest IPOs, which consolidated its leading position in the market.
- Named the Best Transaction Bank in Hong Kong for 2016 by *The Asian Banker*; a trade finance project received the Best Corporate Trade Finance Deal in Hong Kong for 2016. Received the Best SME's Partner Award for the ninth year in a row.

Treasury

- Focused on customer needs and captured market opportunities with introduction of innovative time-to-market products.
- Expanded treasury products and services to markets in the ASEAN region and along the Belt and Road to drive further growth of ASEAN entities' treasury business.
- Achieved encouraging growth in the bond underwriting business. Assisted in the underwriting of the first Silver Bond issued by the HKSAR Government and the first Chinese Green Covered Bond issued by BOC's London Branch.
- Strategically increased investments in high-quality bonds to enhance returns, while remaining alert to risk.
- Received the Hong Kong Domestic Foreign Exchange Bank of the Year award by *Asian Banking and Finance* for the second consecutive year.

RMB Business in Hong Kong

- Maintained its status as the clearing bank and Primary Liquidity Provider for offshore RMB business in Hong Kong.
- Obtained all business qualifications for Shenzhen-Hong Kong Stock Connect.
- Joined CIPS – the first overseas bank to join this system as a direct participant and became the only clearing bank with both CIPS and CNAPS as its clearing channels.
- Reinforced its leading position in the Hong Kong RMB insurance market.

ASEAN Business

- Completed the acquisition of the share capital of BOC Malaysia and BOC Thailand on 17 October 2016 and 9 January 2017 respectively.
- Brunei Branch commenced operation on 20 December 2016, becoming the first Chinese financial institution to establish a presence in the country.
- Adopted a matrix management structure for its ASEAN entities, met regulatory requirements and established a control mechanism. Set up a business supervisory committee and a business integration team to provide various support resources.
- Provided support to enterprises going global and made inroads with enterprises in regional mainstream businesses, achieving rapid growth in financing scale and business cooperation.
- Collaborated in marketing activities and assisted in the business development of its ASEAN entities, with significant progress made on major financing projects.
- Received My Favourite "Belt and Road" Banking Service Award from *Sky Post*.

Eight key business platforms

- Credit card business maintained its market leadership in the UnionPay card business.
- Private Banking business continued to optimise products and its service platform, achieved encouraging growth in both the number of clients and assets under management.
- BOC Life continued to enhance product and service innovation, launched featured products and diversified its distribution channels. Received Insurance Company of the Year – Outstanding Performance and Saving Plan – Excellence awards in the 2016 Financial Institution Awards by *Bloomberg Businessweek*.
- BOCHK AM continued to enrich its product range and explored new business opportunities, with assets under management growing significantly by 1.7 times. Three funds issued under the BOCHK All Weather Creation Series received awards in the CAMAHK – Bloomberg Offshore China Fund Awards 2016.
- Cash management business continued with product innovation and feature enhancements, pioneered the launch of payment by e-Cheque services to enhance its competitive edge. Won the Achievement Award for the Best Cash Management Bank in Hong Kong by *The Asian Banker* for the fourth consecutive year.
- Custody business diversified its client mix and enlarged its client base, with rapid growth in assets under custody. Won the Best Custody Specialist – China award from *The Asset* magazine.
- BOCI-Prudential Trustee enhanced its sales, referrals and cross-selling capabilities; the My Choice MPF Scheme received a number of industry awards.
- Po Sang Securities and Futures made steady progress and continued to widen its product range.

Technology and operations

- Launched a series of FinTech products and services, including several innovative applications that were first to market, enhancing operating efficiency and the customer experience. The total number of customers using e-channels increased notably. Also set up a Smart Flagship Branch with new technology applications.
- Established the BOCHK-ASTRI FinTech Collaboration Centre to develop new financial technologies for the banking sector.
- Received Technology Innovation Awards – Best Mobile Social Media Engagement Project by *The Asian Banker* and awarded The Best Consumer Digital Bank in Hong Kong by *Global Finance* magazine.

Business Segment Performance

Profit before Taxation by Business Segments

HK$'m, except percentages	2016	% of total	2015	(Restated) % of total	Change (%)
CONTINUING OPERATIONS					
Personal Banking	**7,538**	25.6	9,070	31.7	(16.9)
Corporate Banking	**12,614**	42.8	10,752	37.6	17.3
Treasury	**8,552**	29.0	7,846	27.5	9.0
Insurance	**1,230**	4.2	932	3.3	32.0
Others	**(482)**	(1.6)	(25)	(0.1)	N/A
Total profit before taxation	**29,452**	100.0	28,575	100.0	3.1

Note: For additional segmental information, see Note 47 to the Financial Statements.

Personal Banking

Financial Results

Personal Banking's profit before taxation was HK$7,538 million in 2016, a decrease of HK$1,532 million, or 16.9%, year-on-year. The decrease was mainly caused by the drop in net fee and commission income, as a result of the decrease in income from securities brokerage and funds distribution.

Net interest income increased by 6.4%. This was mainly driven by the increase in the average balance of deposits and loans. Net fee and commission income decreased by 15.1%. The decrease was mainly attributable to the exceptionally high stock market turnover in 2015, and the weakening investment sentiment in 2016 which resulted in the sharp decline of income from securities brokerage and funds distribution from the high level in 2015. Fee and commission income from insurance and safe deposit box grew healthily. Net gain on other financial assets dropped year-on-year as the Group captured market opportunities to dispose of certain equity instruments and realised a net gain in 2015.

Business Operations

Implementation of the branch transformation project and omni-channel

In 2016, the Group completed its branch transformation project to transform its single brand retail branches into multi brand branches for serving personal and corporate customers. This project enabled the Group to continuously improve its customer mix, increase two-way referrals and provide better service to SME customers. Consequently, encouraging results were achieved in operating efficiency across various business areas, including satisfactory growth in deposits from customers, remittance, merchant acquiring services and commercial cards. As part of its initiative to build an omni-channel banking service, the Group launched its 24-hour video banking iService to address customers' banking needs beyond the opening hours of branches, and expanded the number of coverage points in its automated banking network.

New service model for cross-border services and new management model for ASEAN

With better planning and a new management model in place, the Group was better able to serve cross-border customers from the Mainland during the year. At the same time, the Group deepened its collaboration with various BOC entities, stepped up staff training, offered referral incentives, and launched a series of promotional campaigns in order to acquire new cross-border customers. Meanwhile, with good progress made in respect of the regional transformation, the Group also developed a new management structure and established a matrix-style management mechanism for cross-region services and referrals to help accelerate business expansion in the ASEAN region. It fully leveraged its expertise by introducing its products and services to ASEAN entities to broaden their product offerings and strengthen cross-region sales support.

Recognised wealth management services

During the year, the Group deepened relationships with existing wealth management customers and made a concerted effort to acquire new customers in the mid- to high-end market. It also introduced a new service model for top-tier Wealth Management customers by providing customised products and streamlined services. This was accompanied by a series of marketing programmes designed to raise the Group's image in wealth management and by the optimisation of its team of relationship managers. As a result, the Group recorded satisfactory growth in the total number of Wealth Management customers as well as their total relationship balances. In recognition of its outstanding performance in retail banking, BOCHK received the Best Retail Bank in Hong Kong award for the second consecutive year and the Wealth Management Business of the Year 2016 award, both from *The Asian Banker*.

The Group's Private Banking business continued to provide customer-centric financial solutions that cater for the personal, family and business needs of its high net-worth customers. In 2016, the Group further upgraded the private banking team, optimised business workflows and expanded its product and service offerings on its enhanced open platform. In addition to serving the local market, the Group looked for opportunities to expand its customer base through closer cooperation with different units of the Group and BOC's Mainland and overseas entities, including a series of customer events in Hong Kong, the Mainland of China and Southeast Asia, to establish stronger customer relationships and raised awareness of its brand. As a result, the Group achieved encouraging growth in both the number of Private Banking clients and their assets under management.

Improvements in the residential mortgage and other retail loan services

The local residential property market was relatively quiet in the first half of 2016 with the slowdown in transaction volume. To acquire new business, the Group focused on enhancing the service capabilities of its front-line staff and optimising the sales team for the launch of the branch transformation project. The Group also expanded its mortgage service into the luxury property market, acquired customers in the mid- to high-end market and shortened the credit assessment approval process. Additionally, the Group launched blockchain technology application for property valuation and completed the first case with its surveyor partner. Furthermore, the Group continued to refine the personal lending business model by expanding eligible collateral types for secured lending business, and enhanced the servicing flow.

A wider range of investment and insurance products

Heightened volatility in the global financial market and a generally weak global recovery dampened market sentiments, resulting in a notable year-on-year decline in stock market transactions. Correspondingly, the Group's investment business was adversely affected with lower commission income from securities brokerage and funds distribution. In line with the launch of Shenzhen-Hong Kong Stock Connect, the Group provided customers with a comprehensive range of China A shares trading services for investing in Hong Kong and China. Also during the period, the Group succeeded in acquiring new securities customers through a new promotional campaign.

With regard to the bancassurance business, the Group always strived for excellence by offering a wider range of products, enhancing cross-selling activities and providing customised services to meet customers' needs at different life stages with the aim of penetrating the high-end customer segment and Mainland customers. With the completion of the branch transformation project, the Group strategically extended the scope of insurance services to company customers to meet their protection needs and to make insurance services as one of their key financial solutions.

Continuous enhancement in credit card service

The Group's credit cardholders' spending in 2016 registered a lower volume from 2015, mainly due to the contraction in total retail sales in Hong Kong. Nonetheless, the Group recorded a growth in the volume of merchant acquiring business over the previous year, supported by a number of new major merchants acquired in Hong Kong during the year. It also maintained its leadership in the UnionPay merchant acquiring and card issuing business in Hong Kong. In 2016, the Group focused on acquiring mid- to high-end personal customers and high-quality corporate customers, with satisfactory growth recorded in each segment. The business integration achieved through the branch transformation project allowed for closer collaboration within different business units and increased cross-selling and credit card promotions. The Group also introduced a number of new credit cards and launched targeted promotional programmes to bolster cardholder spending on daily necessities, online shopping and overseas purchases. In keeping with its commitment to develop e-Channels and mobile payment solutions to cater for the different financial needs and lifestyles of customers, the Group launched Apple Pay as a fast, convenient and secure payment for its credit cardholders.

Corporate Banking

Financial Results

Corporate Banking's profit before taxation was HK$12,614 million, a growth of HK$1,862 million, or 17.3%, year-on-year. The growth was mainly driven by the increase in net interest income and net fee and commission income.

Net interest income increased by 16.3%, mainly driven by the increase in the average balance of loans, together with the increase in the average balance of deposits and the improvement in deposit spread. Net fee and commission income grew by 8.2%, led by the increase in loan commissions. Operating expenses were up 10.1%, mainly due to the increase in staff costs and rental expenses. Net charge of impairment allowances decreased by 64.5%, mainly caused by the reversal of individually assessed impairment allowances for a few corporate advances.

Business Operations

Cross-border business and expansion in ASEAN

In 2016, the Group captured the opportunities arising out of major national strategic initiatives and expanded its customer base. Business development along the Belt and Road and in the ASEAN region paved the way for the transformation of BOCHK into a regional bank. The Group also strengthened its collaboration with BOC's branches and provided leading Mainland enterprises with funding solutions in support of their development along the Belt and Road and in ASEAN where it assisted non-Chinese and leading local enterprises on several major projects. Moreover, the Group coordinated with BOC entities in ASEAN to enable them to increase their competitive edge and market influence in the region. At the same time, the Group focused on product and service innovations to better meet the needs of customers and successfully broadened its customer base by exploring both upstream and downstream companies in the supply chain of existing customers as well as new customers from emerging industries.

In collaboration with BOC entities in the Mainland and overseas, the Group completed financing projects for a number of cross-border M&A transactions in support of Mainland enterprises' overseas expansions, making successful inroads in the business development of merger financing. Business development in Free Trade Zones in Shanghai, Tianjin, Fujian and Guangdong and further cooperation among BOC's Guangdong, Hong Kong and Macau operations added to BOC Group's market influence in these areas. Acting as BOC's Asia-Pacific Syndicated Loan Centre, the Group worked closely with BOC's overseas branches on a number of significant syndicated loans. The Group remained the top mandated arranger in the Hong Kong-Macau syndicated loan market for a twelfth consecutive year.

A growing base of commercial customers

In 2016, the Group further expanded its customer base of leading enterprises. In the local market, it strengthened its relationships with trade associations, family-owned businesses and second- and third-tier listed companies. Based on BOC Group's global network coverage, the Group was able to take advantage of business opportunities with leading overseas enterprises and, through closer collaboration with BOC, acquire cross-border businesses in the ASEAN region. Through its branch transformation project integrating commercial centres and branches, the Group reinforced its service and sales capabilities for local SME customers. In recognition of its long-standing support of SMEs in Hong Kong, BOCHK received the Best SME's Partner Award from the Hong Kong General Chamber of Small and Medium Business for the ninth year in a row.

Working with institutional businesses

During the year, the Group continued to form new relationships with overseas central banks and corresponding banks. In collaboration with BOC, the Group also established business relationships with overseas regional development banks and, in a major breakthrough for the Group, a relationship with a large overseas sovereign wealth fund. In Hong Kong, the Group expanded cooperation with government and public sector entities by offering differentiated services and business solutions. Moreover, it acted as the receiving bank for a number of major IPOs in Hong Kong, including one of the year's largest, which consolidated its leading position in the market.

Product innovation in transaction banking

The Group reinforced its competitive advantage in the trade finance and cash management business through continuous product innovation and feature enhancements. During the year, the Group launched a USD Trade Finance Incentive programme and the new concept of Trade Buffet programme, both of which have strong customer potential. It also pioneered the launch of ePresentation under Letter of Credit, further increasing its competitive edge in trade finance. Additionally, the Group continued to enhance its service capabilities in cross-border cash management and assisted a number of large corporate clients in maximising their cash liquidity through onshore and offshore two-way cash sweeping. Following its pioneer launch of payment by e-Cheque services, the Group introduced solutions that support corporates issuing e-Cheques via ERP Integration and Corporate File Transfer Service. It also introduced 29 non-major currencies as supporting currencies for its remittance service to cover majority of countries along the Belt and Road. In recognition of its outstanding transaction banking services, BOCHK was named Best Cash Management Bank in Hong Kong for the fourth consecutive year and the Best Transaction Bank in Hong Kong for 2016 by *The Asian Banker*. A trade finance project undertaken by BOCHK was also named the Best Corporate Trade Finance Deal in Hong Kong for 2016. In addition to these accolades, BOCHK was named Hong Kong Domestic Cash Management Bank of the Year for the third consecutive year by *Asian Banking and Finance*.

New client segments for custody services

In 2016, the large number of M&A and corporate activities in the market created robust demand for escrow deals. Of the investor segments, segregated mandates and proprietary accounts generally fared better than funds. Although other client segments were affected to various degrees by market volatility and subdued turnover volumes, active portfolio building by new clients enabled the Group to capture business opportunities. During the year, it made solid progress in the Qualified Domestic Institutional Investors ("QDII") business, as a result of active market sentiment and the increasing demand from Mainland institutions for QDII products. Business relationships were also established with new client segments from the Mainland of China, Hong Kong and overseas. Moreover, the Group collaborated more closely with BOC and its overseas entities to enhance service in areas such as the Mainland-Hong Kong Mutual Recognition of Funds scheme which was well received by its partners. In recognition of its outstanding custody services, the Group won the Best Custody Specialist – China award from *The Asset magazine*. At the end of 2016, excluding the RMB fiduciary accounts for participating banks, total assets under the Group's custody were valued at HK$856.0 billion.

Proactive measures to contain risk

In 2016, the Group continued to adhere to a prudent credit strategy and made further refinements to its Know Your Customers and risk management policies. In view of the uncertain economic environment, the Group carried out close credit monitoring on a more frequent and proactive basis. This included monitoring the credit positions of customers in vulnerable industries and countries that could be negatively affected by uncertainties in the global economic environment. More pre-lending monitoring measures were adopted, including the continuous optimisation of the industry mix and closer management of the clustering limit to meet the more stringent regulatory requirements. Additionally, the Group remained alert to emerging risks in the Mainland market and closely monitored customers in segments under threat of overcapacity. It also established a trigger point to review and manage the concentration risk of Mainland exposures. With regard to the Belt and Road Initiative, Mainland enterprises going global and the acquisition of BOC's assets in ASEAN, the Group adopted underwriting standards and credit risk management to monitor the risks associated with the local political and economic environment, tax issues and legal risks. The Group has also been raising related underwriting standards in its credit policies and procedures so that it has more efficient and sound risk control measures governing the Group's business development in new markets.

Treasury

Financial Results

Treasury's profit before taxation was HK$8,552 million, an increase of HK$706 million, or 9.0%, from the previous year. The growth was driven by the increase in net trading gain.

Net interest income decreased by 27.0%, mainly due to the decline in the average yield of debt securities investments, coupled with the decrease in the average balance of RMB balances and placements with banks and the decline in the average yield of related assets caused by the drop in market interest rates. The decrease was, however, partially offset by the higher average balance of debt securities investments. Net trading gain was up strongly, primarily due to the net gain from foreign exchange swap contracts, the increase in currency exchange income from customer transactions as well as the mark-to-market changes of certain debt securities and interest rate instruments.

Business Operations

Acclaim for the Group's treasury business

In response to the complex economic environment and volatile global financial markets, the Group broadened its product and service offerings to meet the diverse needs of customers. It also focused on increasing customer transactions and advancing its strategy of diversification in trading currencies, trading mix, customer segments and business model. As a result, foreign exchange trading volume and related revenue for customer transactions grew satisfactorily during the year. In the banknotes business, it developed relationships with central banks and financial institutions, particularly in countries in the ASEAN region and along the Belt and Road. During the review period, the Group underwrote the first Silver Bond issued by the HKSAR Government and the first Chinese Green Covered Bond issued by BOC's London Branch. In recognition of its outstanding performance in the treasury business, BOCHK received the Hong Kong Domestic Foreign Exchange Bank of the Year award by *Asian Banking and Finance* for the second consecutive year. BOCHK also won the Excellence Brand of Foreign Exchange award in The Hong Kong Leaders' Choice Award 2016 organised by Metro Finance, and received the Outstanding Treasury Business – Dim Sum Bond Market Maker, the Outstanding Retail Banking – Diversified Investment Business, and the Outstanding Treasury Product – (Foreign Exchange) Derivative Trading at the RMB Business Outstanding Awards 2016, organised by Metro Finance, Metro Finance Digital and Hong Kong *Wen Wei Po*.

Business expansion in ASEAN

In line with its ASEAN development strategy, the Group set up mechanisms for closer cooperation with BOC Malaysia, BOC Thailand and BOC's entities in the ASEAN region to promote further growth in their treasury businesses and provide support for their funding needs. Along with the opportunities arising from the internationalisation of the RMB and the Belt and Road Initiative, the Group publicised its treasury products and services by consolidating its relationships with central banks, sovereign wealth funds and financial institutions in several overseas markets and the Mainland of China.

Further enhancement in BOCHK's strong franchise as the RMB clearing Bank

The Group continued to ensure the stable development and continuous improvement of its RMB clearing services in Hong Kong and overseas in 2016. During the year, BOCHK obtained approval from the PBOC to join the CIPS and became the first offshore bank to join the system as a direct participant, and the only clearing bank with both CIPS and China National Automatic Payment System ("CNAPS") as its clearing channels. This not only enhanced the Group's clearing capabilities but also expanded its coverage of Hong Kong's RMB clearing network, making it easier to use RMB in both cross-border payments and overseas settlements, while reinforcing Hong Kong's position as the major offshore RMB centre. In addition, the Group continued to function as an active Primary Liquidity Provider with RMB liquidity to stabilise the market. BOCHK also obtained all qualifications for Shenzhen-Hong Kong Stock Connect, including that of sole Settlement Bank for Northbound Trading and the provision of cross-border fund settlement services for Southbound Trading.

A proactive but risk aware investment strategy

The Group continued to be prudent in managing its banking book investments. It closely monitored changes in the market and sought investment opportunities to enhance returns while remaining attuned to risk. During the year, the Group adjusted its investment portfolio in response to changes in interest rates and increased its investments in high-quality bonds.

Insurance

Financial Results

Profit before taxation in the Group's Insurance segment was HK$1,230 million in 2016, up 32.0% year-on-year. The growth was mainly attributable to the improved performance of its bond fund investments which recorded a net trading gain in 2016 versus a net trading loss in 2015. Net gain on other financial assets increased strongly as the Group recorded a higher gain from the disposal of certain debt securities investments in 2016. The growth was partially offset by the decrease in reinsurance income due to the decline in new RMB businesses amid the slowdown of the RMB insurance market. Net insurance premium income dropped by 14.5% as the Group adjusted its product mix by reducing its single premium business and enlarging its regular premium business in order to ensure a stable stream of renewal premium income for continuous growth.

Business Operations

Product innovation and distribution channel diversification

In 2016, the Group continued to broaden its product offerings and optimise features through its insurance arm in order to provide customers with a more comprehensive product selection. New products launched during the year included the MaxiWealth ULife Insurance Plan for customers who want flexibility in financial planning and whole life protection, the UltraReach Insurance Plan for customers with insurance and savings needs, and Cancer Rider to supplement additional benefits. Other products introduced in 2016 were the GoSports Accident Insurance Plan, Target 5 Years Plus Insurance Plan and SmartUp Wholelife Insurance Plan. To secure new business from non-bank sources, the Group diversified its distribution channels by expanding the tied agency channel, broker channel, telemarketing and e-channels. The Group also reinforced its high-net-worth customer business by strengthening collaboration within the Group and enhancing cross-selling opportunities. Additionally, it set up a new Customer Service Centre and supporting team to provide a better experience for cross-border customers.

Leadership in RMB insurance products and strengthening market recognition

The Group maintained its leading position in the Hong Kong RMB insurance market during the year through a diversified and comprehensive range of products. It also launched a variety of promotions, including programmes for an enhanced returns policy and premium discounts, as well as acting as the title sponsor for an RMB currency exchange rates programme on a TV news channel, reinforcing its image as a provider of RMB insurance. In recognition of its performance in the insurance sector, BOC Life was named Insurance Company of the Year – Outstanding Performance and Saving Plan – Excellence awards in the 2016 Financial Institution Awards by *Bloomberg Businessweek*. It also received the Best Life Insurance Award in the 2016 Metro Awards for Banking and Finance Corporation by *Metro Daily* and *Metro Prosperity*. In the RMB Business Outstanding Awards – Outstanding Insurance Business organised by Metro Finance, Metro Finance Digital and Hong Kong *Wen Wei Po*, BOC Life won all the awards for a fifth consecutive year. In addition, BOC Life took four awards in the insurance sector of *Benchmark*'s 2016 Wealth Management Awards, including the Customer Insight Award – Best-in-Class and Innovation Award – Best-in-Class.

Eight Key Business Platforms

In pursuit of business diversification, the Group enhanced its eight key business platforms with satisfactory performance. Business operations of credit cards, private banking, cash management, custody and life insurance have been discussed under Personal Banking, Corporate Banking and Insurance segment respectively. Business operations of asset management, trust as well as securities and futures are discussed below.

A greater choice of asset management products

BOCHK Asset Management Limited ("BOCHK AM") enriched its product range in 2016 as part of its ongoing business development. The BOCHK All Weather China High Yield Bond Fund, as a northbound fund under the Mainland-Hong Kong Mutual Recognition of Funds scheme, was launched for distribution in the Mainland. A new retail fund, the BOCHK All Weather Asian Bond Fund, was launched, which aims to achieve medium- to long-term income growth and capital appreciation through investment in Asian bonds. Both of these funds were well received by customers. BOCHK AM also expanded its distribution channels to enhance sales capabilities to retail and high-end customers. In addition, new business opportunities were explored through collaboration with BOC's overseas branches and participation in the Group's ASEAN expansion. As a result of BOCHK AM's progress in new businesses, the assets under management at the end of 2016 grew by 1.7 times from the end of 2015. In recognition of its outstanding performance, BOCHK AM won the Outstanding Achiever – High Yield Fixed Income and Best-In-Class, Manager of the Year Award – High Yield Fixed Income in the Fund of the Year Awards 2016 by *Benchmark*. BOCHK AM also won the Best for Retail Focused Investment Solutions – Hong Kong in the 2016 Wealth & Money Management Awards by *Wealth & Finance International*. In addition, three funds issued under the BOCHK All Weather Creation Series received three awards in the CAMAHK – Bloomberg Offshore China Fund Awards 2016. Also, in the Best of the Best Awards announced by *Asia Asset Management* in January 2017, BOCHK AM was named the Best China Fund House and the Best RMB Manager in Hong Kong, as well as the Best Offshore RMB Bond Performance (5 years).

Development of the trustee services business

The Group provides trustee, provident fund, retirement fund and unit trust administration services through its subsidiary company, BOCI-Prudential Trustee Limited ("BOCI-Prudential Trustee"). During the year, BOCI-Prudential Trustee improved its sales, referrals and cross-selling capabilities by collaborating with various units of the Group. It also made a number of functional enhancements to its online MPF administration platform and mobile application for an enhanced customer experience. Moreover, the launch of a Hotline Referral Service saw encouraging results in converting service calls into MPF account consolidation opportunities and creating MPF transfer-in of assets. In recognition of its performance in trustee services, BOCI-Prudential Trustee was awarded the Excellent Brand of MPF Online Platform in The Hong Kong Leaders' Choice Brand Award 2016 organised by Metro Finance. It was also named Best of MPF App Service Provider in the e-Brand Awards 2016 organised by *e-zone* magazine of *Hong Kong Economic Times*. Additionally, a number of industry awards went to BOCI-Prudential Trustee's My Choice MPF Scheme.

Expansion of securities and futures brokerage services

The Group engages in the provision of brokerage services for futures and options trading through its subsidiary company, Po Sang Securities and Futures Limited ("Po Sang Securities and Futures"). During the year, Po Sang Securities and Futures broadened the range of products it offers to include trading services for Sector Index Futures Contracts, RMB Currency Futures Contracts and those under Shenzhen-Hong Kong Stock Connect. It also upgraded its trading system and strengthened its brand image through the launch of a number of promotional campaigns.

Disposal of Nanyang Commercial Bank, Limited

On 18 December 2015, the Group entered into a Sale and Purchase Agreement with Cinda Financial Holdings Co., Limited ("Cinda Financial") and jointly made an announcement with BOC in relation to the Group's disposal of all the issued shares of NCB.

The total consideration for the disposal is HK$68 billion, which was determined with reference to various factors, including (i) the net asset value of NCB and the price-to-book multiples achieved in similar transactions in the Hong Kong banking sector; (ii) scarcity value of banking licences in Hong Kong and China; (iii) future development prospects of NCB and NCB (China); and (iv) potential synergies between NCB and China Cinda Asset Management Co., Ltd. and its subsidiaries.

The disposal was completed on 30 May 2016 (the "Completion Date") in accordance with the terms and conditions of the Sale and Purchase Agreement. Upon completion, NCB ceased to be a subsidiary of both BOC and the Group. BOCHK, NCB and Cinda Financial entered into a Transitional Services Agreement on the Completion Date, pursuant to which BOCHK provides certain transitional support services to NCB and NCB (China) at service charges mutually agreed upon by the parties for an initial term of three years from the Completion Date (which may be extended for a further 12-month period at the election of NCB and further extended if and as mutually agreed by the parties) to facilitate the transition.

For further information on the disposal, please refer to the joint announcements made by BOC and the Group on 18 December 2015 and 27 May 2016.

The operating results of NCB, which are reported as discontinued operations, for the period up to the date of the disposal and the year of 2015 and the gain on disposal of NCB were as follows:

HK$'m	**2016**	2015
Profit of discontinued operations	**961**	2,827
Gain on disposal of discontinued operations	**29,956**	–

Disposal of Chiyu Banking Corporation Limited

On 22 December 2016, the Group entered into a Sale and Purchase Agreement with Xiamen International Investment Limited ("XIL") and the Committee of Jimei Schools ("CB") and jointly made an announcement with BOC in relation to the Group's disposal of a total of 2,114,773 ordinary shares of Chiyu (representing approximately 70.49%) of the total issued shares of Chiyu (the "Disposal") by BOCHK.

The total consideration for the Disposal is HK$7.685 billion, of which (i) XIL has agreed to purchase, or procure the purchase through its three wholly-owned subsidiaries of, 1,929,373 ordinary shares of Chiyu (representing approximately 64.31% of the total issued shares of Chiyu); and (ii) CB has agreed to purchase, or procure the purchase through Chip Bee Private Institution of, 185,400 ordinary shares of Chiyu (representing approximately 6.18% of the total issued shares of Chiyu). Chip Bee Private Institution is an existing registered shareholder of Chiyu prior to the Disposal holding 416,407 ordinary shares of Chiyu (representing approximately 13.88% of the total issued shares of Chiyu).

The Disposal was completed on 27 March 2017 (the "Completion Date") in accordance with the terms and conditions of the Sale and Purchase Agreement. Upon completion, Chiyu ceased to be a subsidiary of both BOC and the Group. BOCHK, Chiyu and XIL entered into a Transitional Services Agreement on 22 December 2016, which takes effect from the Completion Date, pursuant to which BOCHK provides certain transitional support, information technology and other assistance to Chiyu at service charges mutually agreed for a term of four years from the Completion Date (with an option for Chiyu to extend this term for two consecutive periods of one year each) to facilitate the transition.

For further information on the Disposal, please refer to the joint announcements made by BOC and the Group on 22 December 2016 and 24 March 2017.

ASEAN strategy: transforming into a regional bank

The Group made significant progress in developing its ASEAN business during the year. On 30 June 2016, BOCHK entered into Share Purchase Agreements with BOC in relation to the acquisitions of the entire issued share capital of BOC Thailand and the entire issued share capital of BOC Malaysia, respectively, as part of the restructuring exercise of the BOC Group in the ASEAN region. The share acquisition of BOC Malaysia and BOC Thailand was subsequently completed on 17 October 2016 and 9 January 2017 respectively. On 20 December 2016, the Group's Brunei Branch celebrated its grand opening which made it the first Chinese financial institution to establish a presence in the country.

On 28 February 2017, BOCHK entered into Asset Purchase Agreements with BOC in relation to the acquisition of the Indonesia Business and the Cambodia Business, respectively. The completion of each proposed acquisition is subject to the satisfaction of the conditions precedent stated in the respective Asset Purchase Agreement. Upon completion, all the assets and liabilities arising in connection with the Indonesia Business and Cambodia Business will be transferred to and assumed by BOCHK. For further information on the acquisitions, please refer to the announcement made by the Group on 28 February 2017.

ASEAN is a high growth market that has been one of the core regions for the BOC Group's overseas business development over the years. ASEAN is also a key region for both the Belt and Road Initiative and RMB internationalisation. The acquisition of certain ASEAN assets from BOC signified the start of the transformation of BOCHK from a local bank into a regional bank, in line with the Group's integration strategy for BOC Group's domestic and overseas operations. With the acquisition of BOC Thailand, BOC Malaysia, BOC Jakarta Branch and BOC Phnom Penh Branch as well as the establishment of the Brunei Branch, together with its competitive advantages in services, products and resources, the Group is in an excellent position as the largest offshore RMB clearing bank to further develop its business in the region. To achieve this objective, the Group will adopt a matrix management structure. It has also set up a business supervisory committee and a business integration team to coordinate and manage the integration work, ensuring a smooth transition of business operations and management of the ASEAN institutions.

Technology and Operations

In 2016, in view of the complex operating environment and market trend, the Group remained committed to the strategy of innovative development. It captured market opportunities with latest trend in innovation and technology, and proactively pushed forward its business development, achieving new breakthroughs in a number of areas. Innovation and technology became the new growth driver for business development.

The Group continued to strengthen its information technology and business operation infrastructure in order to support its business growth and increase operational efficiency during the year. New initiatives in 2016 included the launch of a series of FinTech products and services that integrate Internet technology with traditional banking to provide better customer experience and support for the growth of the Personal Banking, SME and Corporate Banking businesses. Most of these products and services are leveraged on the mobile platform, including e-Cheque Services, P2P Small Value Transfers, BOC Loan mobile app, QR code payment pilot and Apple Pay and some of these were new to the market.

In 2016, the Group established a Big Data platform in order to improve its information management and target marketing capabilities, and brought in blockchain technology application to expedite property valuations. It also set up a Smart Flagship Branch with new technology applications such as the use of finger-vein to authenticate customer identity, an interactive robot (named RoBOC) to interact with customers, and an online appointment and smart queuing service. Also introduced was the new BOCHK iService, a 24-hour video banking service that addresses customers' banking needs beyond the opening hours of branches. All of these innovations helped to raise the Group's overall service capabilities and increased the total number of customers using e-channels such as Internet and Mobile Banking services from the end of 2015.

As part of its commitment to FinTech in Hong Kong, the Group signed a Memorandum of Understanding with the Hong Kong Applied Science and Technology Research Institute ("ASTRI") to establish the BOCHK-ASTRI FinTech Collaboration Centre. Under this agreement, both parties will develop new financial technologies for the banking sector and promote FinTech in Hong Kong. One of the projects jointly launched was the use of Artificial Intelligence stock trading model in the Smart Investment Contest, enabling the contestants to experience the use of FinTech in investment services.

In recognition of the Group's innovations in technology, BOCHK received a number of local and international awards, including the Technology Innovation Awards – Best Mobile Social Media Engagement Project award by *The Asian Banker* and The Best Consumer Digital Bank in Hong Kong by *Global Finance* magazine. BOCHK also received the Digital Banking Initiative of the Year – Hong Kong, Mobile Banking Initiative of the Year – Hong Kong, and Social Media Initiative of the Year – Hong Kong in the Retail Banking Awards 2016 by *Asian Banking and Finance*.

Business Focus for 2017

The year 2017 will be one of both opportunities and challenges for banks in Hong Kong. The international political and economic environment will be complex and fast-changing. The trend of subdued economic growth will continue globally. This, coupled with intensifying market competitions and challenges from FinTech development, will make the operation and development of banks more difficult. Nevertheless, major national strategic initiatives, RMB's inclusion in the SDR basket of currencies and ASEAN economic development will provide banks with more room for growth. The Group will respond swiftly to changes in the market, capture business opportunities and implement BOC's strategic goal of Serving Society, Delivering Excellence. It will strengthen resources allocation and accelerate business transformation and innovation to achieve sustainable development in all areas.

The Group will continue to develop its local business while exploring opportunities in Southeast Asian markets, particularly for its corporate banking business. Leveraging opportunities from the Belt and Road Initiative, ASEAN business development as well as the regional integration of Guangdong, Hong Kong and Macau, it will deepen collaboration with BOC's entities in the Mainland and overseas to acquire customers among large corporates, enterprises going global and financial institutions. In Hong Kong, the Group will strengthen business cooperation with local commercial, government and financial institution sectors. It will establish an integrated business model to serve customers more comprehensively and efficiently.

The Group will capitalise on its strong franchise and expand cross-border business. Its corporate banking, personal banking and financial market businesses will focus on cross-border services and exert its strong supporting role in Bank of China Group's cross-border business. It will deepen collaboration with BOC's entities in the Mainland and overseas to uplift the overall contribution of cross-border business.

The Group will step up its regional expansion, including the combination and consolidation of its ASEAN entities. Aiming at a smooth transition of business operations and becoming a mainstream bank in the local area, it will adopt an integrated management model and reinforce its support to ASEAN entities. It will also refine the risk management system of ASEAN entities to meet the Group's and local regulatory requirements.

In pursuit of business diversification, the Group will expedite the development of its eight key business platforms, including credit cards, private banking, life insurance, asset management, cash management, custody, trust as well as securities and futures. It will fully leverage the competitive advantages of each business platform to enlarge customer base and meet their changing demand with an enriched product portfolio.

The Group will elevate its professional standards and competitive edge in the financial markets. It will take advantage of market changes to increase trading and investment profitability. It will seize opportunities from RMB's inclusion in the SDR basket of currencies and expand its institutional business. In addition, it will develop a diversified business platform and establish a collaborative business model of commercial and investment banking.

The Group will remain focused on solidifying its deposit business, prudent management of its assets and liabilities as well as disciplined cost control. It will continue to optimise its asset and liability structure, adopt a flexible strategy to expand its deposit base and refine its management of deposit costs. It will better allocate resources with enhanced cost control.

The Group will optimise its business processes for a better customer experience. It will remain customer-centric, improve service model and business processes to increase customer satisfaction. It will deepen the branch transformation and enhance the efficacy of distribution channels, which can contribute to the operational efficiency and overall service capabilities of its branch network.

In view of the potential of Internet finance to improve its competitiveness and productivity, the Group will continue to accelerate technological innovation. It will step up its efforts in technological innovation to drive faster business growth. Together with branch transformation, it will raise the intelligent service levels of its branches to upgrade production efficiency and service capabilities. In line with its strategy in the Southeast Asia, the Group will plan the integration of overseas systems with its own and the application framework to improve the overall operational capabilities. At the same time, the Group will consolidate its intelligent infrastructure for safe and efficient business operation.

The Group will strengthen its risk management and internal control to ensure compliance with various regulatory requirements. It will continue to enhance overall risk management to safeguard the sustainable and healthy development. It will refine its credit approval management and risk management in the Southeast Asia to maintain solid asset quality and control credit costs. It will also strengthen compliance control and upgrade its anti-money laundering measures.

Credit Ratings

As at 31 December 2016	Long-term	Short-term
Standard & Poor's	A+	A-1
Moody's	Aa3	P-1
Fitch	A	F1

RISK MANAGEMENT

Banking Group

Overview

The Group believes that sound risk management is crucial to the success of any organisation. In its daily operation, the Group attaches a high degree of importance to risk management and emphasises that a balance must be struck between risk control and business development. The principal types of risk inherent in the Group's businesses are credit risk, interest rate risk, market risk, liquidity risk, operational risk, reputation risk, legal and compliance risk, and strategic risk. The Group's risk management objective is to enhance shareholder value by maintaining risk exposures within acceptable limits. The Group has a defined risk appetite statement approved by the Board, which is an expression of the types and level of risk that the Group is willing to take in a controllable way in order to achieve its business goals and to meet the expectations of its stakeholders. For details of the Group's risk management governance structure, please refer to Note 4 to the Financial Statements.

Credit risk management

Credit risk is the risk of loss that a customer or counterparty is unable to or unwilling to meet its contractual obligations. Credit risk exists in the trading book and banking book, as well as from on- and off-balance sheet transactions of the Group. It arises principally from lending, trade finance and treasury businesses. For details of the Group's Credit Risk Management, please refer to Note 4.1 to the Financial Statements.

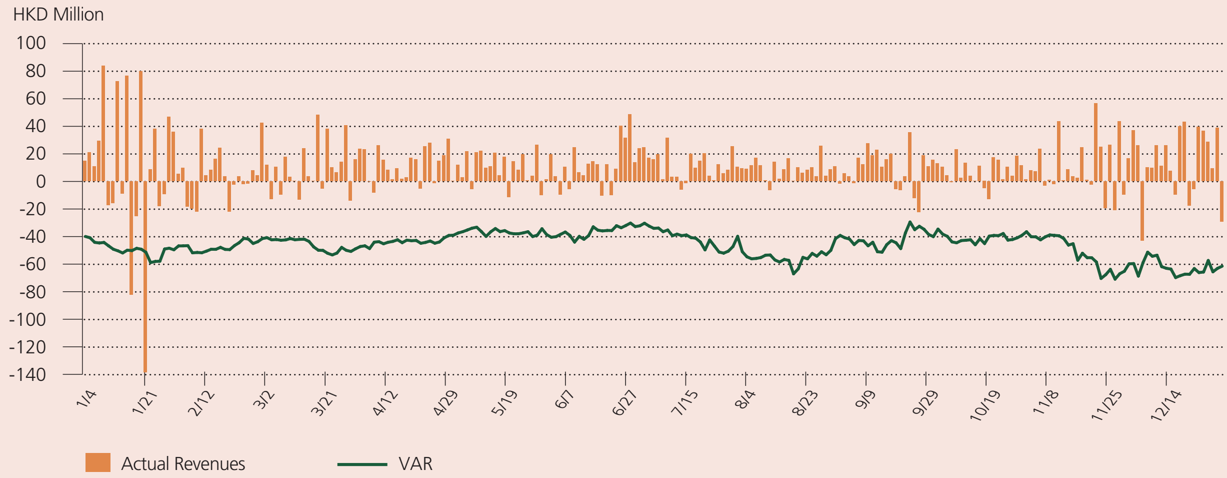
Market risk management

Market risk refers to the risk of loss arising from movements in the value of foreign exchange, interest rate, equity and commodity positions held by the Group due to the volatility of financial market price (foreign exchange rate, interest rate, equity price, commodity price). The Group adopts a moderate market risk appetite to achieve a balance between risk and return. For details of the Group's Market Risk Management, please refer to Note 4.2 to the Financial Statements.

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

The Group adopts back-testing to measure the accuracy of VAR model results. The back-testing compares the calculated VAR figure of market risk positions of each business day with the actual and hypothetical revenues arising from those positions on the next business day. Generally speaking, the number of back-testing exceptions in a rolling 12-month period will not exceed four times, given a 99% confidence level. The graph below shows the back-testing result of the VAR against actual revenues of the Group.

Daily Back-testing in 2016



There were two actual losses exceeding the VAR for the Group in 2016 as shown in the back-testing results.

Interest rate risk management

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

Liquidity risk management

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

Operational risk management

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

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

The Group has put in place an effective internal control process which requires the establishment of policies and control procedures for all the key activities. The Group adheres to the fundamental principle of proper segregation of duties and authorisation. The Group adopts various operational risk management tools or methodologies such as key risk indicators, self-assessment, operational risk events reporting and review to identify, assess, monitor and control the risks inherent in business activities and products, as well as purchase of insurance to mitigate unforeseeable operational risks. Business continuity plans are established to support business operations in the event of an emergency or disaster. Adequate backup facilities are maintained and periodic drills are conducted.

Reputation risk management

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

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

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

Legal and compliance risk management

Legal risk is the risk that unenforceable contracts, lawsuits or adverse judgments may disrupt or otherwise negatively affect the operations or financial conditions of the Group. Compliance risk is the risk of legal or regulatory sanctions, financial losses or losses in reputation the Group may suffer as a result of its failure to comply with applicable laws and regulations. Legal and compliance risks are managed by the LCO, which reports directly to the CRO. As part of the Group's corporate governance framework, the policy for the management of legal and compliance risks is approved by the RC as delegated by the Board.

Strategic risk management

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

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

Capital management

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

To comply with the HKMA's requirements as stated in the Supervisory Policy Manual "Supervisory Review Process", the Group adopts the internal capital adequacy assessment process ("ICAAP") and reviews it annually. Based on the HKMA's guidelines on Pillar II, ICAAP has been initiated to assess the extra capital needed to cover the material risks not captured or not adequately captured under Pillar I, and therefore minimum Common Equity Tier 1 capital ratio, minimum Tier 1 capital ratio and minimum Total capital ratio are determined. Meanwhile, operating ranges for the aforementioned capital ratios have also been established which enable the flexibility for future business growth and efficiency of capital utilisation.

Stress testing

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

BOC Life

BOC Life's principal business is the underwriting of long-term insurance business in life and annuity (Class A), linked long term business (Class C), permanent health (Class D), retirement scheme management category I (Class G) and retirement scheme management category III (Class I) in Hong Kong. Major types of risk arising from BOC Life's insurance business are insurance risk, interest rate risk, liquidity risk, credit risk, equity price risk and currency risk. BOC Life closely monitors these risks and reports to its Risk Management Committee on a regular basis. The key risks of its insurance business and related risk control process are as follows:

Insurance risk management

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

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

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

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

Interest rate risk management

An increase in interest rates may result in the depreciation of the value of BOC Life's investment assets. It might induce customers to surrender their insurance policies/contracts. A decrease in interest rates may result in an increase in insurance liability and an inability to adequately match guarantees or lower returns leading to customer dissatisfaction. BOC Life manages the matching of assets and liabilities of its portfolios within an asset liability management framework that has been developed to achieve investment returns that match its obligations under insurance contracts; and to manage the adverse impact due to interest rate movement.

Liquidity risk management

Liquidity risk is the risk of not being able to meet obligations as they fall due without incurring unacceptable loss. BOC Life's asset and liability management framework includes cash flow management to preserve liquidity to match policy payout from time to time.

Credit risk management

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

- Default risk associated with bonds, notes and counterparties
- Credit spread widening as a result of credit migration (downgrade)
- Reinsurers' share of insurance unpaid liabilities
- Amounts due from reinsurers in respect of claims already paid
- Amounts due from insurance contract holders
- Amounts due from insurance intermediaries

BOC Life manages credit risk by placing limits on its exposure to each investment counterparty and issuer. Such limits are subject to review by the Management at least once a year.

In order to enhance its credit risk management, BOC Life has strengthened its communication with the Group while closely monitoring and updating internal controls to ensure consistency with the Group's credit risk management and investment strategy.

Equity price risk management

Equity price risk refers to the risk of loss due to volatility of market price in listed equity securities and equity funds. BOC Life's asset and liability framework includes managing the adverse impact due to equity price movement through stress test and exposure limit.

Currency risk management

Currency risk refers to the risk of loss due to volatility of exchange rate. BOC Life's asset and liability framework includes managing the adverse impact due to exchange rate movement through stress test, exposure limit and risk limit.

Customer Centrism

Corporate Information

Board of Directors

Chairman
TIAN Guoli#

Vice Chairmen
CHEN Siqing#
YUE Yi

Directors
REN Deqi#
GAO Yingxin#
XU Luode#
LI Jiuzhong
CHENG Eva*
CHOI Koon Shum* (appointment effective from the immediate conclusion of the annual general meeting held on 6 June 2016)
KOH Beng Seng*
TUNG Savio Wai-Hok*
SHAN Weijian* (retirement effective from the immediate conclusion of the annual general meeting held on 6 June 2016)

Non-executive Directors
* Independent Non-executive Directors

Senior Management

Chief Executive
YUE Yi

Chief Risk Officer
LI Jiuzhong

Deputy Chief Executives
LIN Jingzhen
YUAN Shu

Chief Operating Officer
ZHONG Xiangqun

Chief Financial Officer
SUI Yang

Deputy Chief Executive
KUNG YEUNG Ann Yun Chi

Company Secretary

LUO Nan (appointment effective from 26 October 2016)
CHAN Chun Ying (resignation effective from 26 October 2016)

Registered Office

24th Floor
Bank of China Tower
1 Garden Road
Hong Kong

Auditor

Ernst & Young

Share Registrar

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

ADR Depositary Bank

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

Website

www.bochk.com

DIRECTORS

Mr TIAN Guoli
Chairman

Aged 56, is the Chairman of the Board of Directors and the Chairman of the Nomination Committee of the Company and BOCHK. He is the Chairman and Executive Director of BOC since May 2013 and also a Director of BOC (BVI) and BOCHKG. Prior to joining BOC in April 2013, Mr TIAN served as Vice Chairman of the Board of Directors and General Manager of China CITIC Group from December 2010 to April 2013. During this period, he served as Chairman of the Board of Directors and Non-executive Director of China CITIC Bank. From April 1999 to December 2010, Mr TIAN successively served as Vice President and President of China Cinda Asset Management Company, and Chairman of the Board of Directors of China Cinda Asset Management Corporation Limited. From July 1983 to April 1999, Mr TIAN held various positions in China Construction Bank ("CCB"), including General Manager of sub-branch, Deputy Branch General Manager, Department General Manager of CCB Head Office and Assistant Executive President of CCB Head Office. Mr TIAN graduated from Hubei Institute of Finance and Economics in 1983 and was awarded a Bachelor's Degree in Economics.

Mr CHEN Siqing
Vice Chairman

Aged 56, is the Vice Chairman of the Board of Directors and member of each of the Remuneration Committee and the Nomination Committee of the Company and BOCHK. He is the Vice Chairman and Executive Director of BOC since April 2014 and President of BOC since February 2014. He is also a Director of BOC (BVI) and BOCHKG. Mr CHEN joined BOC in 1990 and worked in the Hunan Branch before he was seconded to the Hong Kong Branch of China and South Sea Bank Ltd. as Assistant General Manager. Mr CHEN held various positions in BOC from June 2000 to May 2008, including Assistant General Manager, Vice General Manager of the Fujian Branch, General Manager of the Risk Management Department of BOC and General Manager of the Guangdong Branch. He served as Executive Vice President of BOC from June 2008 to February 2014 and Chairman of the Board of Directors of China Culture Industrial Investment Fund Co., Ltd. from December 2010 to April 2015. Mr CHEN has been serving as the Chairman of the Board of Directors of BOC Aviation Limited (formerly known as BOC Aviation Private Limited) since December 2011 which has been listed on Hong Kong Stock Exchange on 1 June 2016. Mr CHEN graduated from Hubei Institute of Finance and Economics in 1982 and obtained an MBA from Murdoch University, Australia in 1999. He is a Certified Public Accountant.

Mr YUE Yi

Vice Chairman, Executive Director and Chief Executive

Aged 60, is the Vice Chairman, Executive Director and the Chief Executive with overall responsibility for the business and operations of BOCHK and a member of the Strategy and Budget Committee of the Company and BOCHK. He has been appointed as Chairman of BOCHK Charitable Foundation and BOC Life with effect from 6 March 2015. On 6 March 2015, he has been appointed as the designated representative of BOCHK to Hong Kong Association of Banks where he serves as the presiding Chairman in 2017, member of each of Banking Advisory Committee and Bank Notes Issue Advisory Committee, director of Hong Kong Interbank Clearing Limited, HKICL Services Limited and Hong Kong Note Printing Limited as well as council member of Treasury Markets Association. On 7 March 2015, he has been appointed as Vice Chairman of Board of Trustee and Chairman of Investment Subcommittee respectively of Ho Leung Ho Lee Foundation. Mr YUE was the Honorary President of Hong Kong Chinese Enterprises Association ("HKCEA") from 22 June 2015 to 7 April 2016 and has been appointed as President of HKCEA and Chairman of The Hong Kong Chinese Enterprises Charitable Foundation Limited since 7 April 2016, member of Exchange Fund Advisory Committee since 15 July 2015, Vice President of Hong Kong Institute of Bankers since 4 August 2015, special advisor of Maritime Silk Road Society since 16 December 2015, Honorary member of Hong Kong-Japan Business Co-operation Committee since 11 January 2016, member of General Committee of Hong Kong General Chamber of Commerce since 10 May 2016, Chairman of Chinese Banking Association of Hong Kong Company Limited since 20 June 2016, Honorary President of Chinese Bankers Club, Hong Kong since 3 October 2016, member of Advisory Committee of China (Guangdong) Pilot Free Trade Zone Qianhai and Shekou Area of Shenzhen and Qianhai Shenzhen-Hong Kong Modern Service Industry Cooperation Zone since 26 November 2016, council member of Hong Kong Trade Development Council and member of Currency Board Sub-Committee of Exchange Fund Advisory Committee since 1 January 2017 as well as member of HKSAR Economic Development Commission since 17 January 2017. He was the Chairman of Chiyu, NCB and NCB (China), Executive Vice President of BOC from August 2010 to March 2015, Chairman of Bank of China (UK) Limited from September 2010 to October 2015, Chairman of BOCI from November 2011 to August 2015, Chairman of Bohai Industrial Investment Fund Management Co., Ltd. from March 2012 to mid-2015, and Chairman of Bank of China (Luxembourg) S.A. from January 2014 to August 2015. Mr YUE joined BOC in 1980 and has been working in the Beijing Branch, Seoul Branch and the Head Office of BOC. He served as the Vice President of BOC Beijing Branch from January 1993 to January 2000, as General Manager of Seoul Branch from January 2000 to October 2003, as Deputy General Manager/General Manager of the Retail Banking Department from October 2003 to February 2005, as General Manager of the Personal Banking Department from February 2005 to March 2008, as member of the Group Executive Committee, Vice Chairman of Personal Banking Committee, Global Head of Personal Banking Business from March 2008 to March 2009, as member of the Group Executive Committee, Vice Chairman of Financial Markets Committee, Global Head of Financial Markets Business from March 2009 to October 2010. Mr YUE is a master degree holder and he received his Master's Degree in Finance from Wuhan University in 1999.

Mr REN Deqi

Non-executive Director

Aged 53, is a Non-executive Director, Chairman of the Strategy and Budget Committee and member of the Risk Committee of the Company and BOCHK. He has been serving as the Executive Director of BOC since 8 December 2016 and the Executive Vice President of BOC since July 2014. Prior to joining BOC in May 2014, Mr REN worked in CCB for many years and held various positions. From October 2013 to May 2014, he served as General Manager of Risk Management Department of CCB. From August 2003 to October 2013, he successively served as Deputy General Manager of Credit Approval Department, General Manager of Risk Control Department, General Manager of Credit Management Department, and General Manager of the Hubei Branch of CCB. Mr REN received a Master's Degree in Engineering from Tsinghua University in 1988.

Mr GAO Yingxin

Non-executive Director

Aged 54, is a Non-executive Director, member of each of the Risk Committee and the Strategy and Budget Committee of the Company and BOCHK. Prior to his re-designation as a Non-executive Director in March 2015, he was Deputy Chief Executive (Corporate Banking) of the Company and BOCHK from February 2005 to March 2015 and Executive Director of the Company and BOCHK from May 2007 to March 2015. Mr GAO has been serving as the Executive Director of BOC since 8 December 2016 and the Executive Vice President since 6 May 2015, Chairman of the board of directors of China Cultural Industrial Investment Fund Co., Ltd. in May 2015, Chairman of BOCI and Chairman of Bank of China (Luxembourg) S.A. in August 2015, and Chairman of Bank of China (UK) Limited in October 2015. He was the Chairman of NCB, Vice Chairman of NCB (China) and Director of BOCG Insurance and resigned all the positions in March 2015. Before joining BOCHK, he was President and Chief Operating Officer of BOCI. Mr GAO joined BOC Group in 1986 where he began working on financing projects for various industries at BOC's Head Office in Beijing. In 1999, he became General Manager of Corporate Banking at BOC Head Office where he was responsible for managing and building BOC Group's customer relationships with and global financing for multinational corporations and premium domestic clients in the Mainland of China. He was also in charge of BOC's major financing projects. From 1995 to 1996, he worked for the Finance Department of Northern Telecom (Nortel) Head Office in Canada. Mr GAO graduated from the East China University of Science and Technology with a Master's Degree in Engineering in 1986.

Board of Directors and Senior Management

Mr XU Luode

Non-executive Director

Aged 54, is a Non-executive Director, member of each of the Remuneration Committee and the Strategy and Budget Committee of the Company and BOCHK. He is the Executive Vice President of BOC since June 2015. Prior to joining BOC in April 2015, Mr XU served as Chairman of Shanghai Gold Exchange from August 2013 to April 2015. From August 2007 to August 2013, he served as the Vice Chairman of the Board of Directors and President of China UnionPay Company Limited ("China UnionPay"). Mr XU worked in The People's Bank of China ("PBOC") for many years. He served as Director General of the Payment and Settlement Department of PBOC from October 2003 to August 2007, and served as the Deputy General Director of the General Executive Office of PBOC from March 1999 to October 2003. He has been serving as Chairman of BOCCC since June 2015, Chairman of BOC Consumer Finance Co., Limited and Director of China UnionPay since July 2015. Mr XU received a Bachelor's Degree in Economics from Hunan College of Finance and Economics in 1983.

Mr LI Jiuzhong

Executive Director

Aged 54, is an Executive Director of the Company and BOCHK. He has been the Chief Risk Officer of the Group since March 2010. He is in charge of the Group's overall risk management function, overseeing the BOCHK's Risk Management Department, Legal & Compliance and Operational Risk Management Department, and Financial Crime Compliance Department. He is also a Director of BOCCC and BOC Life. He was a Director of NCB and NCB (China). Mr LI has over 30 years' experience in the banking industry. Mr LI joined BOC in 1983 and, since then, he has assumed various positions at BOC Head Office and overseas branch. He served as Assistant General Manager and became Deputy General Manager of BOC London Branch from 1996 to 2002, Deputy General Manager of Corporate Banking Department of BOC Head Office from 2002 to 2004, and also General Manager of Corporate Banking Department, Risk Management Department, and Global Markets Department of BOC Head Office from 2004 to 2009. Mr LI graduated from Northeast Petroleum University in 1983 with a Bachelor's Degree in Science in Oilfield Development and Management and obtained a Master's Degree in Science in International Banking and Financial Studies from Heriot-Watt University (UK) in 1993.

Mdm CHENG Eva

Independent Non-executive Director

Aged 56, is an Independent Non-executive Director and member of each of the Audit Committee and the Strategy and Budget Committee of the Company and BOCHK. She was the former Secretary for Transport and Housing of the Government of the HKSAR. She joined the government's Administrative Service in August 1983 and was posted to various bureaux and departments, including serving as the Permanent Secretary for Economic Development and Labour (Economic Development) and Commissioner for Tourism. She retired from the Government of the HKSAR on 30 June 2012. Mdm CHENG holds a Bachelor's Degree in Social Sciences from University of Hong Kong.

Dr CHOI Koon Shum

Independent Non-executive Director

(appointment effective from 6 June 2016)

Aged 59, is an Independent Non-executive Director and member of each of the Audit Committee, the Nomination Committee and the Remuneration Committee of the Company and BOCHK. Dr CHOI is the Chairman of Sunwah Group, Sunwah International Limited (listed in Toronto), Sunwah Kingsway Capital Holdings Limited (listed in Hong Kong) and Vietnam VinaCapital. He is also an Independent Non-executive Director of Hui Xian Asset Management Limited, the Manager of Hui Xian Real Estate Investment Trust (listed in Hong Kong). Dr CHOI has extensive experience in food industry, real estate development, international trade as well as technology and finance related business.

Dr CHOI is a member of the National Committee of the Chinese People's Political Consultative Conference ("CPPCC") of the People's Republic of China, Deputy Director of the Committee for Education, Science, Culture, Health and Sports of the CPPCC. He also holds a number of public positions including Chairman of the Chinese General Chamber of Commerce in Hong Kong, Standing Committee Member of the All-China Federation of Industry and Commerce, Economic Advisor to the President of the Chinese Academy of Sciences, Founding Patron and Senior Advisor to the President of the Academy of Sciences of Hong Kong, Executive Director of the China Overseas Friendship Association, Hong Kong China's Representative of Asia Pacific Economic Co-operation (APEC) Business Advisory Council, Council Member of the Economic Development Commission of Hong Kong Special Administrative Region and Council Member of the Hong Kong Trade Development Council, Founding Chairman of the Hong Kong-Vietnam Chamber of Commerce, Founding Chairman of the Hong Kong-Korea Business Council, Honorary Ambassador of Foreign Investment Promotion for the Republic of Korea, Chairman of the China-India Software Association, Chairman of the China Hong Kong Israel Technology Cooperation and Promotion Center and Chairman of the US-China Center for Research on Educational Excellence of the Michigan State University. Dr CHOI is a Court or Council Member of a number of universities including the Fudan University, the Nanjing University, United College of the Chinese University of Hong Kong, the Hong Kong University of Science and Technology and the Hong Kong Polytechnic University.

Mr KOH Beng Seng

Independent Non-executive Director

Aged 66, is an Independent Non-executive Director, Chairman of the Risk Committee and member of each of the Audit Committee, the Remuneration Committee and the Nomination Committee of the Company and BOCHK. Mr KOH is currently the Chief Executive Officer of Octagon Advisors Pte Ltd, a business and management consulting company based in Singapore. He is also the Non-executive Chairman of Great Eastern Holdings Limited, Independent Non-executive Director of Singapore Technologies Engineering Ltd and United Engineers Limited, all listed in Singapore. Mr KOH is also a Director of Hon Sui Sen Endowment CLG Limited. He was formerly a Director of Sing Han International Financial Services Limited. Mr KOH was Deputy President of United Overseas Bank ("UOB") and a member of UOB's Executive Committee from 2000 to 2004. During this period, he was in charge of UOB's operations, delivery channels, information technology, corporate services, risk management and compliance functions and played a key role in driving the successful integration of Overseas Union Bank and UOB in 2001. Prior to that, Mr KOH has spent over 24 years at the Monetary Authority of Singapore where he made significant contributions to the development and supervision of the Singapore financial sector in his capacity as Deputy Managing Director, Banking & Financial Institutions Group. He has also served as a Director of Chartered Semiconductor Manufacturing and as a part-time adviser to the International Monetary Fund. Mr KOH holds a Bachelor's Degree in Commerce from Nanyang University in Singapore and a Master's Degree in Business Administration from Columbia University in the United States.

Mr TUNG Savio Wai-Hok

Independent Non-executive Director

Aged 65, is an Independent Non-executive Director, Chairman of the Audit Committee and the Remuneration Committee, member of each of the Nomination Committee, the Risk Committee and the Strategy and Budget Committee of the Company and BOCHK. Mr TUNG is currently the Chairman of Investcorp Technology Partners and Senior Advisor of Investcorp, he was the Chief Investment Officer and one of the founding partners of Investcorp. Mr TUNG was appointed a Director, a member of the Compensation Committee and the Cybersecurity Committee of Tech Data Corporation, a company listed on NASDAQ. Before joining Investcorp in 1984, he worked for Chase Manhattan Bank for about 11 years, holding various positions in its front, middle and back offices and served in its offices in New York, Bahrain, Abu Dhabi and London. Mr TUNG has served on the boards of many of Investcorp portfolio companies, including Club Car, Circle K, Saks Fifth Avenue, Simmons Mattresses, Star Market, and Stratus Computer. He is also a board member and treasurer of the Aaron Diamond AIDS Research Center, an affiliate of Rockefeller University. Mr TUNG holds a BSc in Chemical Engineering from Columbia University of New York, where he is also a trustee emeritus and a member of the Columbia University Medical Center Board of Visitors.

SENIOR MANAGEMENT

Mr LIN Jingzhen
Deputy Chief Executive

Aged 51, is the Deputy Chief Executive of the Group, overseeing Global Corporate Banking Department, Commercial Banking Department, Transaction Banking Department, Institutional Business Department and Southeast Asia Business. He was the Vice Chairman of NCB (China). Prior to joining the Group, Mr LIN served as General Manager of Corporate Banking Department of BOC in charge of the corporate banking business, covering product development, relationship management with premium customers, and major project financing etc. Joining BOC in 1987, Mr LIN has extensive experience in corporate banking business and held various positions in Hong Kong Branch, Xiamen Branch, Fujian Branch and the Head Office of BOC. Mr LIN graduated from Xiamen University with a Bachelor's Degree in Finance and a Master's Degree in Business Administration.

Mr YUAN Shu
Deputy Chief Executive

Aged 54, is the Deputy Chief Executive of the Group in charge of the financial market business, including Global Markets, Investment Management, Global Transaction Banking, Asset Management and other capital market-related businesses. He is also a Director of BOC Life, a Director and Chairman of BOCI-Prudential Trustee, BOC Group Trustee Company Limited and Po Sang Securities and Futures Limited. Mr YUAN has over 30 years of experience in the industry with solid professional expertise and management experience. He has held different positions in the financial market businesses at Head Office and in various overseas branches of BOC. Mr YUAN joined the Trading Department of BOC in 1983 then held positions in the Paris and Tokyo branches, as well as the Trading Department and Global Financial Markets Department of BOC Head Office. Mr YUAN was Director (Trading) of the Global Financial Markets Department in 2006 and was promoted to General Manager (Trading) of the Financial Markets Unit in 2010. Prior to joining the Group as Deputy Chief Executive (Financial Markets), he served as the General Manager of the Hong Kong Branch, BOC, from December 2014. Mr YUAN graduated from Renmin University of China majoring in International Finance.

Board of Directors and Senior Management

Mr ZHONG Xiangqun

Chief Operating Officer

Aged 47, is the Chief Operating Officer of the Group, overseeing the Bank-wide Operation Department, Information Technology Department, E-Finance Centre and Corporate Services Department. He is also a Director of BOCCC. Prior to joining the Group, Mr ZHONG served as General Manager of E-Finance Department of BOC in charge of the development of e-finance business, covering mobile payment, e-business, e-financing and big data application. Joining BOC in 1994, Mr ZHONG has held management positions in Information Technology Department, Personal Banking Unit, Card Centre and Innovation & Development Department, etc. He was a Director of China UnionPay and a Member of China Financial Standardization Technical Committee. Mr ZHONG has solid expertise in information technology and cyber security as well as practical business experience. Mr ZHONG graduated from Peking University with a Bachelor's Degree in Information Science specialised in Software and a Master's Degree in Applied Mathematics.

Mdm SUI Yang

Chief Financial Officer

Aged 43, is the Chief Financial Officer of the Group, overseeing Financial Management Department and General Accounting and Accounting Policy Department. Mdm SUI is the Chairman of BOCHK Asset Management Limited. She was also a Director of NCB. Prior to joining the Group in August 2014, Mdm SUI served as Deputy General Manager of Financial Management Department of BOC. She joined BOC in April 1997 and assumed various positions in Finance & Accounting Department of BOC including Deputy General Manager of Management Information System ("MIS") Centre of BOC from September 2008 to March 2011, Assistant General Manager of MIS Centre of BOC from March 2007 to September 2008 and Assistant General Manager of MIS Centre and Finance & Accounting Department of BOC from August 2006 to March 2007. Mdm SUI possesses extensive knowledge and experience in financial management. She obtained a Master's Degree and a Bachelor's Degree in Economics from the Central University of Finance & Economics (formerly the Central Institute of Finance and Banking). Mdm SUI is a member of the Chinese Institute of Certified Public Accountants.

Mrs KUNG YEUNG Ann Yun Chi

Deputy Chief Executive

Aged 54, is the Deputy Chief Executive of the Group in charge of Personal Banking and Wealth Management Department, Personal Banking Risk and Integrated Management Department, Channel Management Department, Private Banking, BOCCC and BOC Life. She is also the Vice Chairman of BOCCC and a Director of BOC Life. Mrs KUNG joined BOCHK in August 2007 as Head of Channel Management. She was appointed as the Head of Personal Banking in April 2011, and was promoted to her current role in March 2015. Prior to joining the Group, Mrs KUNG was the General Manager of Branch and Direct Banking of Standard Chartered Bank (Hong Kong) Limited and had held various senior positions covering banking products, customer segments, wealth management and marketing within the organisation. With over 25 years of experience in the industry, Mrs KUNG possesses extensive knowledge in personal banking and a strong background in financial services. Mrs KUNG graduated from the University of Southern California in the United States of America where she obtained her Bachelor of Science Degree in Business Administration with a concentration in Accounting.

Report of the Directors

The Directors are pleased to present their report together with the audited consolidated financial statements of the Group for the year ended 31 December 2016.

Principal Activities

The principal activities of the Group are the provision of banking and related financial services. An analysis of the Group's performance for the year by business segments is set out in Note 47 to the Financial Statements.

Business Review

For business review of the Group for the year, please refer to "Chairman's Statement", "Chief Executive's Report", "Management's Discussion and Analysis", "Corporate Governance" and "Corporate Social Responsibility" sections.

Results and Appropriations

The results of the Group for the year are set out in the consolidated income statement on pages 125 to 126.

The Board has recommended a final dividend of HK$0.625 per share, amounting to approximately HK$6,608 million, subject to the approval of shareholders at the forthcoming annual general meeting to be held on Wednesday, 28 June 2017. If approved, the final dividend will be paid on Friday, 14 July 2017 to shareholders whose names appear on the Register of Members of the Company on Friday, 7 July 2017. Together with the interim dividend of HK$0.545 per share and the special dividend of HK$0.710 per share declared in August 2016, the total dividend payout for 2016 would be HK$1.880 per share.

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

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to attend and vote at the Annual General Meeting of the Company, from Thursday, 22 June 2017 to Wednesday, 28 June 2017 (both days inclusive), during which period no transfer of shares will be registered. In order to attend and vote at the Annual General Meeting of the Company, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, not later than 4:30 p.m. on Wednesday, 21 June 2017. The Annual General Meeting of the Company will be held at 2:00 p.m. on Wednesday, 28 June 2017.

Closure of Register of Members for Entitlement to Final Dividend

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to the proposed final dividend, from Tuesday, 4 July 2017 to Friday, 7 July 2017 (both days inclusive), during which period no transfer of shares will be registered. In order to qualify for the proposed final dividend, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, not later than 4:30 p.m. on Monday, 3 July 2017. Shares of the Company will be traded ex-dividend as from Friday, 30 June 2017.

Donations

Charitable and other donations made by the Group during the year amounted to approximately HK$9 million.

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

Shares Issued

Details of the Company's issued shares are set out in Note 41 to the Financial Statements.

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

Distributable Reserves

Distributable reserves of the Company as at 31 December 2016, calculated under Part 6 of the Hong Kong Companies Ordinance, amounted to approximately HK$7,201 million.

Five-year Financial Summary

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

Directors

The list of Directors of the Company is set out on page 54. The biographical details of the Directors and senior management are set out on pages 55 to 63. The term of office for each Non-executive Director is approximately three years.

Dr CHOI Koon Shum was appointed as Independent Non-executive Director with effect from the conclusion of the annual general meeting held on 6 June 2016 and Mr SHAN Weijian retired as Independent Non-executive Director with effect from the conclusion of the annual general meeting held on 6 June 2016. The Board would like to express its great appreciation to Mr SHAN for his valuable contributions during his tenure of office.

In accordance with Article 98 of the Articles of Association and pursuant to Code A.4.2 of the Corporate Governance Code, the terms of office of Mr TIAN Guoli, Mr CHEN Siqing, Mr LI Jiuzhong and Mdm CHENG Eva will expire at the forthcoming annual general meeting. All the retiring Directors being eligible, will offer themselves for re-election at the forthcoming annual general meeting. Further, pursuant to Article 102 of the Articles of Association, any Director appointed by the Board during the year shall hold office only until the next following annual general meeting, and shall then be eligible for re-election at such meeting. Accordingly, the term of office of Dr CHOI Koon Shum, who had been appointed on 6 June 2016, will expire at the forthcoming annual general meeting and, being eligible, will offer himself for re-election.

Save for the list of Directors of the Company as set out on page 54, other directors of the Company's subsidiaries during the year ended 31 December 2016 are as follows:

YUAN Shu	ZHONG Xiangqun	SUI Yang	KUNG YEUNG Ann Yun Chi
CHAI Woon Chew	CHAN Chi Fai	CHAN Hing Wah	CHAN Ka Pui
CHAN Lap Bong	CHAN Siu Ping Chordio	CHAN Yiu Fai	CHEN Zhong Xin
CHENG Po Kee	CHEUNG Wai Hing	CHEUNG Wing Shing Vincent	CHEW Lee Lin
CHU Wing Yiu	DATUK TER Leong Yap	DU Qiang	FU Kim
FUNG Pui Cheung	GUAN Xuefei	GWEE Siew Ping	HU Haozhong
HUANG Ling	KAN Wai Mun Carmen	KWONG Shu Ming	LAU Hon Chuen
LAU Tim	LEE Hoi Yin, Stephen	LEUNG Yuen Hong	LIU Hui Jun
LIU Min	LIU Yalin	LO Kin Wing Terry	LO Ping Wa
LO Wai Man Mary	MOK Chung Man	Neil Anthony TORPEY	NG Leung Sing
QIU Hengchang	SHEN Hua	SHING Sze Yee	SHUM Wai Chun
SO Pui Sheung	SO Shing Shun	SUN Dawei	SZE Ying Tat
TAN Wan Chye	TANG Fong Chai Francis	TSANG Kam Yin Wendy	TSE Siu Ling
WANG Hongwei	WANG Jian	WANG Tong	WANG Yunchao
WONG Chek Ming	WONG Chun Keung	WONG Kine Yuen	WONG Man Chiu
WONG Man Yee	WONG Siu Man	WOO Chia Wei	YANG Ruhai
YIP Man Kai	YU Kwok Chun	ZENG Xiaoping	ZHANG Qingsong
ZHANG Zhao	CHAN Kam Lun*	CHOW Chak Chee*	CHUNG Chun Wa*
FUNG Kam Chung Astrid*	FUNG Yin Fan Kamill*	HO Ka Chuen Clement*	HUANG Hong*
KAI Chi On*	LAM Man Yi*	LIU Xin Qun*	LU Ying*
NG Chui Sheung*	TO Chi Wing*	ZHAO Chuntang*	XIAO Wei#
LIN Jingzhen#	CHAN Sai Ming#	CHANG Hsin Kang#	CHENG Zeyu#
CHOW Tak Man#	FANG Hongguang#	GONG Huazhang#	LAN Hong Tsung, David#
LEUNG Ka Chun#	NG Kwok Yuen#	WANG Jianqiang#	

* Resigned/retired during the year.

\# Directors of the subsidiaries that were disposed during the year.

Directors' Service Contracts

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

Directors' Interests in Transactions, Arrangements or Contracts

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

Directors' Interests in Competing Business

Mr TIAN Guoli, Mr CHEN Siqing, Mr REN Deqi and Mr GAO Yingxin are Executive Directors of BOC. Mr XU Luode is Executive Vice President of BOC.

BOC is a joint stock commercial bank with limited liability, established under the laws of the PRC, providing a full range of commercial banking and other financial services through its associates throughout the world. Certain of the Group's operations overlap with and/or are complementary to those of BOC and its associates. To the extent that BOC or its associates compete with the Group, the Directors believe that the Group's interests are adequately protected by good corporate governance practices and the involvement of the Independent Non-executive Directors.

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

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

Directors' Rights to Acquire Shares

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

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

As at 31 December 2016, the interests and short position of Directors, Chief Executive and their respective associates, in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 of the Listing Rules (the "Model Code") are set out below:

Associated corporation of the Company:

Bank of China Limited (H Shares)

Name of director	Number of shares/underlying shares held				Approximate % of the total issued H shares
	Personal interests	Family interests	Corporate interests	Total	
Choi Koon Shum	4,000,000	40,000[1]	1,120,000[2]	5,160,000	0.01%

Notes:

1. Such shares are held by the spouse of Dr Choi Koon Shum.
2. Dr Choi Koon Shum is deemed to be interested in the 1,120,000 shares held through Choi Koon Shum Education Foundation Limited by virtue of the SFO.

All the interests stated above represented long positions. Save as disclosed above, as at 31 December 2016, none of the Directors, Chief Executive or their respective associates had any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

Interest of Substantial Shareholders

The register maintained by the Company pursuant to section 336 of the SFO recorded that, as at 31 December 2016, the following parties had the following interests (as defined in the SFO) in the Company set opposite their respective names:

Name of Corporation	No. of shares held in the Company	Approximate % of total issued shares
Central Huijin	6,984,274,213	66.06%
BOC	6,984,274,213	66.06%
BOCHKG	6,984,175,056	66.06%
BOC (BVI)	6,984,175,056	66.06%

Notes:

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

All the interests stated above represented long positions. Apart from the disclosure above, according to the register maintained by the Company pursuant to section 336 of the SFO, BOCI Financial Products Limited had an interest in 143,522 shares which represented short positions. BOC and Central Huijin are deemed to be interested in such number of shares for the purpose of the SFO. Save as disclosed, no other interests or short positions were recorded in the register maintained by the Company under section 336 of the SFO as at 31 December 2016.

Management Contracts

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

Equity-linked Agreements

No equity-linked agreements were entered into by the Company during the year or subsisted at the end of the year.

Permitted Indemnity Provision

Pursuant to the Articles of Association, every Director shall be indemnified out of funds of the Company against all liabilities incurred by him/her to the extent permitted by the Hong Kong Companies Ordinance. The Company has maintained insurance for the benefit of Directors against liability which may lawfully be insured by the Company.

Purchase, Sale or Redemption of the Company's Shares

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

Major Customers

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

Connected Transactions

The Independent Non-executive Directors have reviewed the transactions which the Company disclosed in a public announcement on 10 December 2013 and confirmed that these transactions were:

(i) entered into in the ordinary and usual course of business of the Group;

(ii) conducted on normal commercial terms or better;

(iii) entered into according to the relevant agreements governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole; and

(iv) in each case where an annual cap had been set, that such cap was not exceeded.

In accordance with paragraphs 14A.56 and 14A.71(6)(b) of the Listing Rules, the Board of Directors engaged the auditor of the Company to report on the Group's continuing connected transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 (Revised) "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. The auditor has issued its unqualified letter containing its findings and conclusions in respect of the above continuing connected transactions. In accordance with paragraph 14A.57 of the Listing Rules, a copy of the auditor's letter has been provided by the Company to the Stock Exchange.

Budgetary Discipline and Reporting

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

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

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

Auditor

The financial statements for the year 2016 have been audited by Ernst & Young who will retire and offer themselves for re-appointment at the 2017 annual general meeting.

On behalf of the Board

TIAN Guoli
Chairman
Hong Kong, 31 March 2017

Corporate Governance

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

The Company has been in full compliance with all code provisions as set out in the Corporate Governance Code contained in Appendix 14 of the Listing Rules except for Code provision E.1.2. Due to other business arrangement, Mr TIAN Guoli, Chairman of the Board, was unable to attend the annual general meeting held on 6 June 2016 and delegated Mr YUE Yi, Vice Chairman and Chief Executive of the Company, to chair the meeting of the Company. The Company also complies with nearly all the recommended best practices set out in the Corporate Governance Code. In particular, the Company publishes quarterly financial and business reviews so that shareholders and investors can be better updated of the performance, financial positions and prospects of the Company on a timely basis. BOCHK, the Company's wholly-owned and principal operating subsidiary, is in full compliance with the guidelines as set out in the Supervisory Policy Manual module CG-1 entitled "Corporate Governance of Locally Incorporated Authorised Institutions" ("SPM CG-1") issued by the HKMA. To further enhance corporate governance standard, the Company will revamp its corporate governance system and strengthen relevant measures by referencing to market trend as well as guidelines and requirements issued by regulatory authorities. The Company will continue to maintain sound corporate governance standards and procedures to ensure the completeness, transparency and quality of our information disclosure.

Corporate Governance Policy

Policy Statement

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

Essential Principles

(1) Eminent Board

Authority	The Board is responsible for supervising the management of the business and affairs of the Group with due regard to maximising shareholder value and enhancing corporate governance standard of the Group. The Board is obliged to act honestly and in good faith and to make decisions objectively in the best interests of the Group and its shareholders as a whole.
Structure	The Company is led by a high caliber Board with strong representation of Independent Non-executive Directors. The Board has a well-balanced composition of Executive Directors, Non-executive Directors and Independent Non-executive Directors. Both the number and percentage of the Independent Non-executive Directors are well above the requirements set by relevant rules and regulations. All Directors are eminent individuals from diverse disciplines with extensive professional experience and are able to make objective judgement.
Roles of Chairman and Chief Executive	In order to promote balance of power, the roles of Chairman and Chief Executive are segregated. The Company may benefit from the segregation as the Chairman can focus on leading the Board and monitoring corporate governance and shareholder issues, while the Chief Executive leading the Management to perform the day-to-day operations and affairs of the Company.
Board Committees	The Board has established five standing Board Committees which are delegated with different responsibilities to assist the Board in performing its duties. They are Audit Committee, Nomination Committee, Remuneration Committee, Risk Committee, and Strategy and Budget Committee. Most of them are composed of a majority of Independent Non-executive Directors. Each of the Board Committees has a well-defined mandate with the roles and responsibilities delineated therein. The performance and effectiveness of these standing Board Committees are evaluated periodically with a view to making further enhancement. Other Board Committees like Independent Board Committee and Search Committee will be formed as and when required under the appropriate circumstances.

(2) Prudent Risk Management

The Board recognises the need for risk control and management being a vital component of the business of the Group. The Board formulates and oversees the risk management strategies, and the related framework and policies with the assistance of the Risk Committee and other relevant Board Committee(s). The Management performs the daily risk management responsibilities of the Group under the guidance of the Risk Committee.

(3) Fair Remuneration System

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

(4) Effective Disclosure Mechanism

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

(5) Upholding Shareholders' Rights

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

(6) Safeguarding Stakeholders' Interests

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

(7) Sustainable Corporate Social Responsibility

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

(8) Pursuit of "Good to Great"

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

Policy Goal

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

Corporate Governance Framework

Responsibilities of the Board and Management

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

- formulating the Group's mid and long-term strategy and monitoring the implementation thereof;
- reviewing and approving the annual business plans and financial budgets;
- approving the annual, interim and quarterly results;
- reviewing and monitoring the Group's risk management and internal control;
- ensuring good corporate governance of the Group and effective compliance; and
- monitoring the performance of the Management.

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

Roles of the Chairman and the Chief Executive

To avoid concentration of power in any single individual, the positions of the Chairman and the Chief Executive of the Company are held by two different individuals. Their roles are distinct, clearly established and stipulated in the Board's Mandate. In short, the Chairman is responsible for ensuring that the Board properly discharges its responsibilities and conforms to good corporate governance practices and procedures. In addition, as the Chairman of the Board, he is also responsible for ensuring that all Directors are properly briefed on all issues currently on hand, and that all Directors receive adequate, accurate and reliable information in a timely manner. The Chief Executive is responsible for providing leadership for the whole Management and implementing important policies and development strategies as adopted by the Board. Led by the Chief Executive, the Management Committee fulfils responsibilities including management of the Group's routine operation, implementation of business development strategies and realisation of the Group's long-term targets and strategies.

Board Committees

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

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

Corporate Governance

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

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

Board of Directors

Composition and Terms of Office of the Board

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

The Board currently has eleven members, comprising four Independent Non-executive Directors, five Non-executive Directors and two Executive Directors. Upon the immediate conclusion of the annual general meeting held on 6 June 2016, the following changes in Directors as well as Chairmen and members of Board Committees had taken effect: Mr SHAN Weijian retired as an Independent Non-executive Director and ceased to be the Chairman of the Audit Committee and a member of each of Nomination Committee and Remuneration Committee. Dr CHOI Koon Shum was appointed as an Independent Non-executive Director and a member of each of Audit Committee, Nomination Committee and Remuneration Committee. Mr TUNG Savio Wai-Hok was appointed as the Chairman of the Audit Committee. Save as disclosed above, there were no other changes to the composition of the Board and Board Committees during the year and up to the date of this Annual Report.

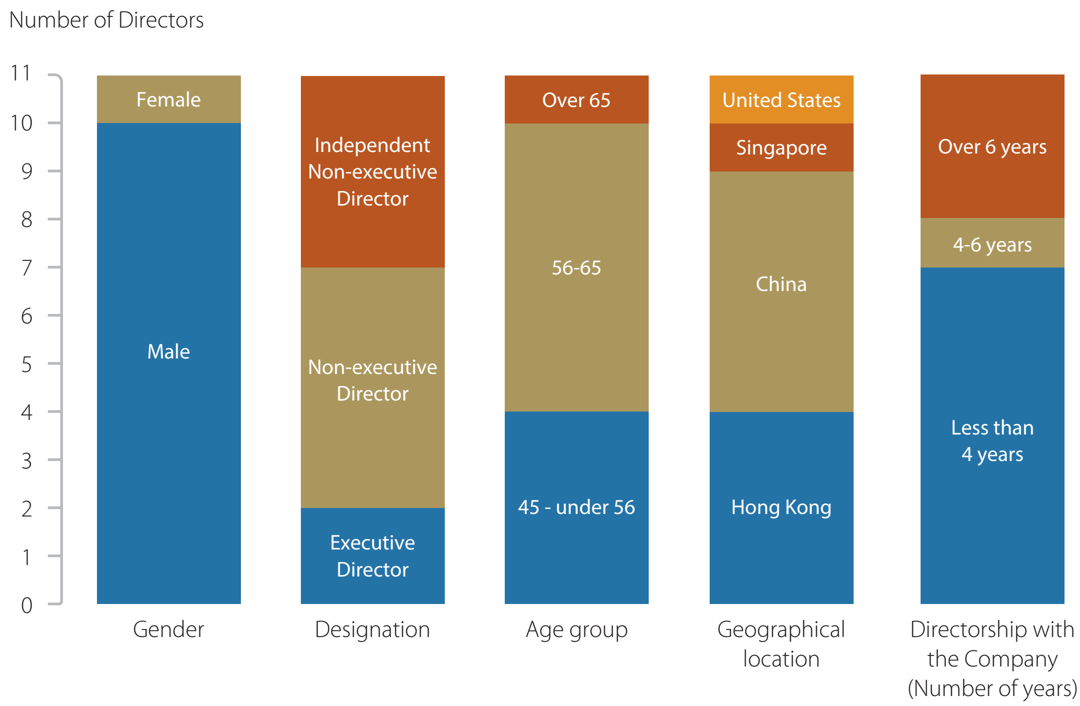
All the existing Non-executive Directors and Independent Non-executive Directors of the Company have been appointed for a fixed term of approximately 3 years, with formal letters of appointment setting out the key terms and conditions of their appointment. In accordance with Article 98 of the Articles of Association and pursuant to Code provision A.4.2 of the Corporate Governance Code, the terms of office of Mr TIAN Guoli, Mr CHEN Siqing, Mr LI Jiuzhong and Mdm CHENG Eva will expire at the forthcoming annual general meeting, and being eligible, offer themselves for re-election. Further, pursuant to the Articles of Association, any Director appointed by the Board during the year shall hold office only until the next following general meeting or the next following annual general meeting of the Company, and shall then be eligible for re-election at such meeting. Accordingly, the term of office of Dr CHOI Koon Shum, who was appointed on 6 June 2016, will expire at the forthcoming annual general meeting and, being eligible, offer himself for re-election. Further details regarding the proposed re-election of Directors are set out in the section headed "Report of the Directors". In addition, the Company has also established a written and formal process for the appointment of Independent Non-executive Directors to ensure that the appointment procedures are standardised, thorough and transparent.

Diversity and Independence of the Board Members

The Company recognises the importance and benefits of board diversity. In order to promote Board efficiency and standards of corporate governance, the guidance set out in the "Board Diversity Policy" adopted by the Company will be considered in identifying suitable and qualified candidates to be a Board member, which covers a number of aspects, including but not limited to gender, age, cultural and educational background, ethnicity, geographical location, professional experience, skills and knowledge, etc., in order to have an appropriate proportion in the Board composition from various aspects as aforementioned. At the same time, all Board appointments are made on merit, in the context of the skills and experience the Board as a whole required and the various perspectives of Board diversity elements as mentioned above shall also be adequately considered.

Under the current board membership, all Directors possess extensive experience in banking and management. In addition, over one-third of them are Independent Non-executive Directors, some of whom are experts in strategic development, financial and/or risk management. The Board has formulated the "Policy on Independence of Directors" which stipulates the criteria on independence of Independent Non-executive Directors. The Company has received from each of the Independent Non-executive Directors an annual confirmation of his/her independence by reference to the said independence policy. Based on the information available to the Company, it considers that all of the Independent Non-executive Directors are independent. Biographical details of the professional experience, skills and knowledge of the Directors are set out in the section headed "Board of Directors and Senior Management" and are available under the sub-section "Organisation" of the section headed "About Us" on the Company's website at www.bochk.com.

An analysis of the Board Composition during the year is set out below:



Mr TIAN Guoli, Mr CHEN Siqing, Mr REN Deqi and Mr GAO Yingxin are Executive Directors of BOC. Mr XU Luode is Executive Vice President of BOC. Mr YUE Yi was Executive Vice President of BOC (he resigned such position with effect from 6 March 2015). Save as disclosed above, there are no other relationships between the Board members, including financial, business, family or other material relationships.

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

Directors' Liability Insurance Policy

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

Directors' Training and Professional Development

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

The Company also provides regular updates to Board members on material changes to regulatory requirements applicable to the Directors and the Company on a timely basis; and arranges regular meetings with the Management to facilitate the understanding of the latest business development of the Company. In addition, Board members are encouraged to participate actively in continuous training programmes. The Company also arranges relevant professional training programmes for Board members at the Company's expense.

During the year, all Directors have participated in continuous professional development to develop and refresh their knowledge and skills in accordance with Code provision A.6.5 of the Corporate Governance Code contained in Appendix 14 to the Listing Rules. In 2016, the Company invited experts to deliver seminars to the Directors and senior management with regard to update on requirements under Basel Accord, sustainability for banks, funds transfer pricing, and the latest supervisory requirements and industrial trends on anti-money laundering. Each of the Directors received a series of training locally or overseas as he/she thought fit, hosted or attended briefings, meetings, seminars and conferences organised by the Company and other organisations. Relevant training included, among others:

– national policy outlook;
– developments of financial technology;
– risk management and internal controls;
– regulatory updates; and
– banking industry development trend, etc.

The Directors' records of annual training information have been entered in the register of directors' training records maintained and updated by the Company from time to time. The following summarises continuous professional development participated by all Directors of the Company during the year:

Directors Note	Corporate Governance	Regulatory updates	Banking industry development trend and global/national economy
Non-executive Directors			
Mr TIAN Guoli	✓	✓	✓
Mr CHEN Siqing	✓	✓	✓
Mr REN Deqi	✓	✓	✓
Mr GAO Yingxin	✓	✓	✓
Mr XU Luode	✓	✓	✓
Independent Non-executive Directors			
Mdm CHENG Eva	✓	✓	✓
Dr CHOI Koon Shum	✓	✓	✓
Mr KOH Beng Seng	✓	✓	✓
Mr TUNG Savio Wai-Hok	✓	✓	✓
Executive Directors			
Mr YUE Yi	✓	✓	✓
Mr LI Jiuzhong	✓	✓	✓

Note: The training records for those Directors who resigned or retired during the year have not been included herein. Please refer to the section headed "Composition and Terms of Office of the Board" under "Board of Directors" for details of changes in Directors during the year and up to the date of this Annual Report.

Directors' Attendance of the Meetings of the Board of Directors, Board Committees and General Meeting

Seven Board meetings were held during 2016 with an average attendance rate of 82%. Regular meeting schedule for the year was prepared and approved by the Board in the preceding year. Ad hoc Board meetings will be convened as appropriate. In general, formal notice of regular Board meetings shall be sent to all Directors at least 14 days before the date of the scheduled meetings and Board agenda and meeting materials are despatched to all Board members for review at least seven days prior to the scheduled meetings. Board agenda is approved by the Chairman following consultation with other Board members and the senior management. In addition, in order to facilitate open discussion with all Non-executive Directors and on their requests, the Chairman will meet with all Non-executive Directors (including Independent Non-executive Directors), in the absence of Executive Directors and the senior management, during the discussion session before each Board meeting. Relevant practice has been incorporated in the Working Rules of the Board.

Details of respective Directors' attendance at the Board meetings, Board committee meetings and annual general meeting in 2016 are set out as follows:

	Number of meetings attended/Number of meetings convened during directors' term of office						
		Board Committees					General Meeting
Directors Note	Board	Audit Committee	Nomination Committee	Remuneration Committee	Risk Committee	Strategy and Budget Committee	Annual General Meeting
Number of meetings held during the year	7	5	1	2	5	5	1
Non-executive Directors							
TIAN Guoli *(Chairman)*	3/7	–	1/1	–	–	–	0/1
CHEN Siqing *(Vice Chairman)*	4/7	–	1/1	2/2	–	–	1/1
REN Deqi	5/7	–	–	–	4/5	5/5	1/1
GAO Yingxin	5/7	–	–	–	4/5	3/5	0/1
XU Luode	7/7	–	–	1/2	–	4/5	1/1
Independent Non-executive Directors							
CHENG Eva	7/7	5/5	–	–	–	5/5	1/1
CHOI Koon Shum	4/4	3/3	–	1/1	–	–	–
KOH Beng Seng	7/7	5/5	1/1	2/2	5/5	–	1/1
TUNG Savio Wai-Hok	6/7	5/5	1/1	2/2	5/5	5/5	1/1
SHAN Weijian *(retired)*	1/3	2/2	1/1	1/1	–	–	0/1
Executive Directors							
YUE Yi *(Vice Chairman and Chief Executive)*	7/7	–	–	–	–	4/5	1/1
LI Jiuzhong	7/7	–	–	–	–	–	1/1
Average Attendance Rate	82%	100%	100%	92%	90%	87%	73%

Note: Please refer to the section headed "Composition and Terms of Office of the Board" under "Board of Directors" for details of changes in Directors during the year and up to the date of this Annual Report.

Apart from formal Board meetings and annual general meeting, the Company has set up a system of pre-communication meetings of the Independent Non-executive Directors, where major agenda items will be presented to the Independent Non-executive Directors before each Board meeting, and their comments will be timely conveyed to the Management for follow up action so as to streamline the resolution process of the Board meetings. Moreover, the Company arranges, on a regular basis, other casual events for the Board members and the senior management to facilitate their communication and interactions. For example, the Company organises working meals from time to time, Board members and senior management have been invited to join and share insights on the Company's business and strategic issues. Further, a board retreat has also been held during the year to enhance communication between the Board and the senior management.

Board Committees

Audit Committee

The Audit Committee comprised four members at the end of the year, all of which are Independent Non-executive Directors. Its composition, main duties and major works performed during the year are as follows:

Composition

Mr TUNG Savio Wai-Hok (Chairman)
Mdm CHENG Eva
Dr CHOI Koon Shum
Mr KOH Beng Seng

Main duties

- integrity of financial statements and financial reporting process
- monitoring of risk management and internal control systems
- effectiveness of internal audit function and performance appraisal of the General Manager of Group Audit
- appointment of external auditor and assessment of its qualification, independence and performance and, with authorisation of the Board, determination of its remuneration
- periodic review and annual audit of the Company's and the Group's financial statements, and financial and business review
- compliance with applicable accounting standards as well as legal and regulatory requirements on financial disclosures
- corporate governance framework of the Group and implementation thereof

Major works performed during the year (included the review and, where applicable, approval of)

- the Company's financial statements for the year ended 31 December 2015 and the annual results announcement that were recommended to the Board for approval
- the Company's interim financial statements for the six months ended 30 June 2016 and the interim results announcement that were recommended to the Board for approval
- the Company's announcements on quarterly financial and business review for the period ended 31 March 2016 and 30 September 2016 that were recommended to the Board for approval
- the audit reports and report on internal control recommendations submitted by external auditor, and the on-site examination reports issued by regulators
- the appointment of external auditor, the fees payable to external auditor for the annual audit, interim review and other non-audit services
- the Group's audit plan for next year and key areas identified
- the deployment of human resources and pay level of the Internal Audit, its budget for next year and review of the effectiveness of the internal audit function
- the 2015 performance appraisal and key performance indicators for the General Manager of Group Audit and the Group Audit for next year
- the annual review of the effectiveness of the Group's risk control and internal control systems

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

Nomination Committee

The Nomination Committee comprised five members at the end of the year, including two Non-executive Directors and three Independent Non-executive Directors. Its composition, main duties and major works performed during the year are as follows:

Composition

Mr TIAN Guoli[1] (Chairman)
Mr CHEN Siqing[1]
Dr CHOI Koon Shum[2]
Mr KOH Beng Seng[2]
Mr TUNG Savio Wai-Hok[2]

Main duties

- overall human resources strategy of the Group
- selection and nomination of Directors, Board Committee members and Senior Management
- structure, size and composition (including but not limited to gender, age, cultural and educational background, ethnicity, geographical location, professional experience, skills and knowledge, etc.) of the Board and Board Committees
- effectiveness of the Board and Board Committees
- training and continuous professional development of Directors and Senior Management
- code of conduct applicable to employees

Major works performed during the year (included the approval, review and proposal to the Board)

- consideration of the matters relating to the recruitment, adjustment and appointment of Directors and Senior Management
- consolidation of self-evaluation results of the Board and Board Committees, and putting forward recommendations to the Board to further enhance the functions and effectiveness of the Board and Board Committees
- annual review on the "Policy on Independence of Directors"

Notes:
1. Non-executive Director
2. Independent Non-executive Director

Remuneration Committee

The Remuneration Committee comprised five members at the end of the year, including two Non-executive Directors and three Independent Non-executive Directors. Its composition, main duties and major works performed during the year are as follows:

Composition

Mr TUNG Savio Wai-Hok[1] (Chairman)
Mr CHEN Siqing[2]
Mr XU Luode[2]
Dr CHOI Koon Shum[1]
Mr KOH Beng Seng[1]

Main duties

- remuneration strategy and incentive framework of the Group
- remuneration of Directors, Board Committee members, Senior Management and Key Personnel

Major tasks performed during the year (included the approval, review and proposal to the Board)

- formulation, review and amendment on the major human resources and remuneration policies
- performance appraisal result of the Executive Directors and Senior Management for year 2015
- proposal on staff bonus for year 2015 and salary adjustment for year 2016 for the Group, including the Senior Management
- remuneration relating to the appointment of Senior Management
- key performance indicators of the Group and the Senior Management for year 2017
- proposal on human resources budget of the Group for year 2017

Notes:
1. Independent Non-executive Director
2. Non-executive Director

Risk Committee

The Risk Committee comprised four members at the end of the year, including two Non-executive Directors and two Independent Non-executive Directors. Its composition, main duties and major accomplishments during the year are as follows:

Composition

Mr KOH Beng Seng[1] (Chairman)
Mr REN Deqi[2]
Mr GAO Yingxin[2]
Mr TUNG Savio Wai-Hok[1]

Main duties

- formulation of the risk appetite and risk management strategy of the Group and determination of the Group's risk profile
- identification, assessment and management of material risks faced by various business units of the Group
- review and assessment of the adequacy and effectiveness of the Group's risk management policies, systems and internal controls
- review and monitoring of the Group's capital management
- review and approval of the Group's target balance sheet
- review and monitoring of the Group's compliance with risk management policies, systems and internal controls, including the Group's compliance with prudential, legal and regulatory requirements governing the businesses of the Group
- review and approval of high-level risk-related policies of the Group
- review and approval of significant or high risk exposures or transactions
- review of key reports, including risk exposure reports, model development and validation reports, and credit risk model performance reports

Major works performed during the year

- review/approval of key risk management policies, including the "BOCHK Group Operating Principles", the "Risk Management Policy Statement of BOCHK Group", the "Capital Management Policy of BOCHK", the "BOCHK Group Financial Instruments Valuation Policy", the "Staff Code of Conduct", the "Technology Risk Management Policy", the "Policy for Validating Internal Rating Systems", the "Connected Transactions Management Policy", the "Sharing and Use of Credit Data Management Policy", the "Stress Test Policy of BOCHK" and stress test scenarios, and a range of risk management policies covering strategic risk, credit risk, market risk, liquidity risk, interest rate risk, operational risk, legal, compliance and reputation risk, etc.
- review of the risk adjustment method for group bonus funding mechanics and the approval of the results of risk adjustment of BOCHK Group for 2015
- review/approval of the Group's operating plans, including the Group's target balance sheets, the BOCHK's banking book investment plans and portfolio key risk indicators, as well as risk management limits
- review and monitoring of Basel Accord implementation, including review of model validation reports and model performance reports, and receiving the status reports of the allocation of risk-weighted assets
- review of various risk management reports
- review/approval of significant high risk exposures or transactions

Notes:
1. Independent Non-executive Director
2. Non-executive Director

Strategy and Budget Committee

The Strategy and Budget Committee comprised six members at the end of the year, including three Non-executive Directors, two Independent Non-executive Directors as well as the Chief Executive and Executive Director of the Company. Its composition, main duties and major works performed during the year are as follows:

Composition

Mr REN Deqi[1] (Chairman)
Mr YUE Yi[2]
Mr GAO Yingxin[1]
Mr XU Luode[1]
Mdm CHENG Eva[3]
Mr TUNG Savio Wai-Hok[3]

Main duties

- review the Group's medium to long-term strategic plan for Board approval
- monitor the Group's implementation of medium to long-term strategy, provide guidance on strategy direction for management
- review major investments, capital expenditure and strategic commitments of the Group, and make recommendations to the Board
- review and monitor the Group's regular/periodic (including annual) business plan
- review budget for Board approval and monitor performance against budgeted targets

Major works performed during the year

- reviewed the Group's acquisition of some ASEAN branches of BOC for Board approval, and discussed opportunities and strategies of Southeast Asia business development
- discussed development strategies of key business platforms, including private bank, transaction banking, trustee, insurance, etc., and approved capital injection to BOCHK Asset Management Limited
- reviewed IT three-year plan and BOC's Core Banking System Integration Project
- reviewed and monitored the implementation of the Group's financial budget and business plan for 2016, and also reviewed and endorsed the Group's financial budget and business plan submitted by the Management for the year 2017 and recommended the same to the Board
- discussed overseas expansion and asset allocation strategies of BOC Life

Notes:
1. Non-executive Director
2. Executive Director
3. Independent Non-executive Director

Ad Hoc Committee

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

Independent Board Committee

An Independent Board Committee was set up in June 2016 to review and approve the continuing connected transactions and the new caps between the Group on the one hand and BOC and its associates on the other hand, for the three years ending 31 December 2019.

The Committee comprised all the Independent Non-executive Directors and was chaired by Mr TUNG Savio Wai-Hok. The Committee has engaged Investec Capital Asia Limited as the independent financial adviser. On the basis of Investec Capital Asia Limited's advice and recommendations, the Committee has been satisfied that the continuing connected transactions are entered into in the ordinary and usual course of business of the Group, on normal commercial terms, and the continuing connected transactions and the annual caps imposed on such transactions for the three years ending 31 December 2019 are in the interests of the Company and its shareholders as a whole and are fair and reasonable so far as the independent shareholders are concerned. The Committee also recommends the proposed annual caps of the continuing connected transactions to the Board and the independent shareholders. As the annual caps for certain categories of continuing connected transactions represent more than 5% of the applicable percentage ratios as defined in the Listing Rules, such transactions are subject to the approval of the independent shareholders of the Company. For such purpose, an extraordinary general meeting is scheduled to be held immediately after the annual general meeting of the Company on 28 June 2017. Shareholders please refer to the circular issued by the Company dated 9 January 2017 and notice of the extraordinary general meeting to be issued by the Company in April 2017 for details on the continuing connected transactions and the extraordinary general meeting respectively. Shareholders can also view and download the aforesaid documents from the Company's website at www.bochk.com.

Directors' Securities Transactions

The Company has established and implemented the "Code for Securities Transactions by Directors" (the "Company's Code") to govern the Directors' dealings in securities transactions of the Company. Terms of the Company's Code are more stringent than the mandatory standards set out in the "Model Code for Securities Transactions by Directors of Listed Issuers" as contained in Appendix 10 of the Listing Rules. Apart from the securities of the Company, the Company's Code also applies to the Director's dealings in the securities of BOC and its subsidiary, BOC Aviation Limited, which have been listed on the Stock Exchange of Hong Kong since June 2006 and June 2016 respectively. Upon specific enquiry by the Company, all Directors confirmed that they had strictly complied with the provisions as set out in both the Company's Code and the said Model Code throughout the year 2016.

Directors' Remuneration

Pursuant to the "Policy on Directors' Remuneration" adopted by the Company, when recommending the remuneration of Directors, the Remuneration Committee should benchmark against companies of comparable business type or scale, and job nature and workload at both the Board and Board Committee levels (including frequency of meetings and nature of agenda items) in order to compensate Directors fairly. No individual Director is allowed to participate in the procedures for deciding his/her individual remuneration package. Information relating to the remuneration of each Director for 2016 is set out in Note 20 to the Financial Statements. The present scale of Director's fees, including additional fees for membership of Board Committees, is given below:

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

Note: For the year ended 31 December 2016, all Non-executive Directors (excluding Independent Non-executive Directors) have not received their Directors' fee as mentioned above and Executive Directors did not receive any additional fees for being Chairmen or members of the Board Committees.

The Remuneration Committee also has the delegated responsibility from the Board to determine the remuneration packages of the Executive Directors and Senior Management, including benefits in kind, pension rights and compensation payments (including any compensation payable for loss or termination of their office or appointment, early payout of deferred remuneration), as well as the performance-based remuneration. Moreover, it will recommend to the Board on their remuneration package upon joining, sign-on bonus and contract guaranteed bonus, etc.

Remuneration and Incentive Mechanism

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

The Remuneration and Incentive Policy of the Group is generally in line with the broad principles set out in the HKMA's "Guideline on a Sound Remuneration System" and applicable to the Company and all of its subsidiaries (including the branches and institutions in and out of Hong Kong).

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

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

  - "Senior Management": The senior executives designated by the Board who are responsible for oversight of the firm-wide strategy or material business lines, including Chief Executive, Deputy Chief Executives, Chief Financial Officer, Chief Risk Officer, Chief Operating Officer, Board Secretary and General Manager of Group Audit.

  - "Key Personnel": The employees whose individual business activities involve the assumption of material risk which may have significant impact on risk exposure, or whose individual responsibilities are directly and materially linked to the risk management, or those who have direct influence to the profit, including heads of material business lines, heads of major subsidiaries and overseas institutions, head of trading, as well as heads of risk control functions.

- **Determination of the Remuneration Policy**

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

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

1. *Performance Management Mechanism*

   To reflect the "performance-driven" corporate culture, the Group has put in place a performance management mechanism to formalise the performance management at the levels of the Group, units and individuals. The annual targets of the Group will be cascaded down under the framework of balanced scorecard whereby the performance of the "Senior Management" and different units (including business units, risk control units and other units) would be assessed from the perspectives of financial, customer, building blocks/key tasks, human capital, risk management and compliance. For individual staff at different levels, annual targets of the Group will be tied to their job requirements through the performance management mechanism. Performance of individuals will be appraised on their achievement against targets, their contribution towards performance of their units and fulfilment of risk management duties and compliance, etc. Not only is target accomplishment taken into account, but the risk exposure involved during the course of work could also be evaluated and managed, ensuring security and normal operation of the Group.

2. *Risk Adjustment of Remuneration*

   To put the principle of aligning performance and remuneration with risk into practice, based on "The Risk Adjustment Method", the key risk modifiers of BOCHK have been incorporated into the performance management mechanism of the Group. Credit risk, market risk, interest rate risk, liquidity risk, operational risk, legal risk, compliance risk and reputation risk form the framework of "The Risk Adjustment Method". The size of the variable remuneration pool of the Group is calculated according to the risk adjusted performance results approved by the Board and is subject to the Board's discretion. This method ensures the Group to fix the Group's variable remuneration pool after considering risk exposures and changes and to maintain effective risk management through the remuneration mechanism.

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

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

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

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

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

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

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

The vesting of the deferred variable remuneration is linked with the long term value creation of the Group. The vesting conditions are closely linked to the annual performance of the Group in the next 3 years and the individual behaviour of the staff concerned. When the Group's performance has met the threshold requirement, the deferred variable remuneration would be vested following the corresponding schedule. However, if a staff is found to have committed fraud, or any financial or non-financial factors used in performance measurement or variable pay determination are later proven to have been manifestly worse than originally understood in a particular year, or individual behaviour/management style pose negative impacts to the business unit and even the Group, including but not limited to improper or inadequate risk management, etc., the unvested portion of the deferred variable remuneration of the relevant staff would be forfeited.

- **Annual Review of Remuneration Policy**

  The Remuneration Policy of the Group is subject to annual review with reference to changes on external regulatory requirements, market conditions, organisational structure and risk management requirements, etc. Review conducted this year including: due to the disposals of NCB and Chiyu and the regional development strategy of the Group, the computation methods of "Group Bonus Funding Policy" was reviewed; due to regional development strategy and organisation structural changes, the scope of application of "Remuneration and Incentive Policy" and "Variable Pay Deferral Policy" and the identification criteria and position lists of "Senior Management", "Key Personnel" and etc. as delineated in the "Guideline on a Sound Remuneration System" were also reviewed.

- **External Remuneration Consultant**

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

- **Disclosure on Remuneration**

  The Group has fully complied with the guideline in Part 3 of the "Guideline on a Sound Remuneration System" issued by the HKMA to disclose information in relation to our remuneration and incentive mechanism.

External Auditor

Pursuant to the "Policy on External Auditor Management" adopted by the Board, the Audit Committee reviewed and monitored and was satisfied with the independence and objectivity of Ernst & Young, the Group's external auditor, and the effectiveness of its audit procedures, based on the principles and standards set out in the said Policy that were in line with international best practices. Upon the recommendation of the Audit Committee, the Board will propose that Ernst & Young be re-appointed as auditor of the Group at the Company's 2017 annual general meeting. Subject to shareholders' authorisation, the Board will authorise the Audit Committee to determine the remuneration of Ernst & Young. For 2016, the fee charged by Ernst & Young was HK$44 million, of which HK$28 million was for audit services and HK$16 million related to other services (mainly including tax-related and advisory services). For 2015, the fee paid by the Group to Ernst & Young was HK$43 million, of which HK$28 million was for audit services and HK$15 million related to other services (mainly including tax-related and advisory services). The Audit Committee was satisfied that the non-audit services in 2016 did not affect the independence of Ernst & Young.

Risk Management and Internal Control

The Board is responsible for evaluating and determining the nature and extent of the risks it is willing to take in achieving the Group's strategic objectives, and ensuring that the Group establishes and maintains appropriate and effective risk management and internal control systems. The Board oversees the Management in the design, implementation and monitoring of the risk management and internal control systems. According to the Board's scope of delegation, the Management is responsible for the day-to-day operations and risk management, and the Management needs to provide a confirmation to the Board on the effectiveness of these systems.

The risk management and internal control systems are designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable and not absolute assurance against material misstatement or loss; to manage the risk of system failure; and to assist in the achievement of the Group's objectives. In addition to safeguarding the Group's assets, it also ensures the maintenance of proper accounting records and compliance with relevant laws and regulations.

The Group conducts an annual review of the effectiveness of its risk management and internal control systems covering all material controls, including financial, operational and compliance controls as well as risk management. The review is conducted by reference to the guidelines and definitions given by the regulatory and professional bodies for the purpose of assessing five different internal control elements, namely, the control environment, risk assessment, control activities, information and communication, and monitoring. The assessment covers all the major internal controls and measures, including financial, operational and compliance controls as well as risk management functions. The review also considers the adequacy of resources, staff qualifications and experience and training of the Group's accounting, financial reporting and internal audit functions. The review is coordinated by the Group's internal audit which, after the Management and various business departments have performed their self-assessment and the Management has confirmed the effectiveness of the relevant systems, then carries out an independent examination and other post-assessment work on the review process and results. The results of the 2016 review, which have been reported to the Audit Committee and the Board, revealed that the Group's risk management and internal control systems were effective and adequate.

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

- a rational organisational structure with appropriate personnel is developed and whose responsibility, authority, and accountability are clearly delineated. The Group has formulated policies and procedures to ensure reasonable checks and balances for all the operating units, reasonable safeguard for the Group's assets and adherence to relevant laws and regulations and risk management in its operations;

- the Management draws up and continuously monitors the implementation of the Group's strategies, business plans and financial budgets. The accounting and management systems that are in place provide the basis for evaluating financial and operational performance;

- the Group has various risk management and human resources policies. There are specific units and personnel that are responsible for handling reputation, strategic, legal, compliance, credit, market, operational, liquidity and interest rate risks. There are also procedures and internal controls for the handling and dissemination of inside information. The Group has set up mechanisms to identify, evaluate and manage all the major risks, and has established corresponding internal control procedures as well as processes for resolving internal control defects. (The Group's risk management is given on pages 46 to 51);

- the Group has established an information technology governance structure that produces a range of reports on information systems and management, including information on the monitoring of various business units, financial information and operating performance. Such information facilitates the Management, business units and the regulatory bodies in assessing and monitoring the Group's operation and performance. Proper communication channels and reporting mechanisms are in place at various business units and levels to facilitate exchange of information;

- pursuant to a risk-based approach and in accordance with the internal audit plan approved by the Audit Committee, the Group's internal audit conducts independent reviews on such aspects as financial activities, various business areas, various kinds of risks, operations and activities. Reports are submitted directly to the Audit Committee. The Group's internal audit closely follows up on the items that require attention in a systematic way and reports to the Management and the Audit Committee in a timely manner; and

- the Audit Committee reviews the reports submitted by external auditor to the Group's Management in connection with the annual audit as well as the recommendations made by regulatory bodies on risk management and internal control. The Group's internal audit follows up on the same to ensure timely implementation of the recommendations, and also periodically reports the status of the implementation to the Management and the Audit Committee.

The Group is committed to upholding good corporate governance practices and the internal control system of all subsidiaries are reviewed regularly. During the year of 2016, continuous improvements on the organisation structure and segregation of duty, the risk management policy and procedure, and the enhancement of disclosure transparency have been undertaken by the Group. In response to internal and external changes in global economic condition, operating environment, regulatory requirement and business development, the Group has implemented a series of measures and undertaken an on-going review on the effectiveness of the internal control mechanism. In 2016, areas for improvement have been identified and appropriate measures have been implemented.

Communication with Shareholders

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

Mr YUE Yi (the Chairman of annual general meeting), Mr TUNG Savio Wai-Hok (the Chairman of the Remuneration Committee), Mr KOH Beng Seng (the Chairman of the Risk Committee), Mr REN Deqi (the Chairman of the Strategy and Budget Committee), and Ernst & Young, the auditor were present at the Company's 2016 annual general meeting held on 6 June 2016 at Grand Ballroom, The Lobby Floor, Grand Hyatt Hong Kong, 1 Harbour Road, Wan Chai, Hong Kong to respond to enquiries raised by shareholders. Mr TIAN Guoli, Mr GAO Yingxin and Mr SHAN Weijian (the former Chairman of Audit Committee) were unable to attend the meeting due to other business engagements. Save as disclosed above, all other Directors including Mr CHEN Siqing, Mr XU Luode, Mr LI Jiuzhong and Mdm CHENG Eva were also present at the meeting. Resolutions passed at the Company's 2016 annual general meeting included: adoption of the Company's 2015 financial statements, declaration of 2015 final dividend, re-election of Directors, re-appointment of auditor, the grant of general mandates to the Board to issue and buy back shares of the Company, relevant voting results are available under the sub-section "Stock Exchange Announcements" of the section headed "Investor Relations" on the Company's website at www.bochk.com.

As disclosed in the 2015 Annual Report of the Company, in view of the investors' concern regarding the potential dilution of the shareholder value arising from the exercise of power pursuant to the grant of a general mandate to issue shares to the Board, the Board has voluntarily reduced the general mandate to issue shares of up to 5% of the total number of shares in issue as compared to the 20% limit permitted under the Listing Rules in the event that the issue of shares is for cash and not related to any acquisition of assets for approval by the shareholders at the 2016 annual general meeting. The Board would also recommend the threshold of up to 5% of the total number of shares in issue (subject to adjustment in case of any subdivision and consolidation of shares after the passing of the relevant resolution) at the 2017 annual general meeting for approval by shareholders. Further, given its commitment to high standards of corporate governance, the Board also adopted certain internal policies for the exercise of the powers granted to the Board under the general mandates to issue shares solely for cash and buy back shares. The relevant policies are summarised as follows:

- the Board will not exercise the mandate at a discount that will result in significant dilution of shareholder value. In the exercise of such power to issue shares for cash, the Board will have regard to factors such as the Group's total capital ratio, and in particular, its Tier 1 capital, cost and benefit of raising Tier 2 capital, need for cash for the Group's business development, the principle that shareholders should be treated equally and the alternative of conducting a rights issue; and

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

All the resolutions proposed at the Company's 2017 annual general meeting will be voted on by poll. Accordingly, the Company will engage Computershare Hong Kong Investor Services Limited, the Company's Share Registrar, to act as the scrutineer for such purpose. The results of the poll voting will be posted on the Stock Exchange's website and the Company's website as soon as practicable following conclusion of the vote-counting for shareholders' information.

Besides, in order that shareholders can have a better understanding of the agenda items to be discussed at the 2017 annual general meeting and to encourage their active participation so that exchange of views and communication can be further enhanced, the Company has provided detailed information on the 2017 annual general meeting in a circular to shareholders which includes introduction to the proposed resolutions to be approved at the annual general meeting, information on the retiring Directors who are eligible for re-election, information on voting and other issues relating to the 2017 annual general meeting in the form of "Frequently Asked Questions".

Shareholders' Rights

Shareholders are entitled to convene an extraordinary general meeting, propose a resolution at an annual general meeting, and propose a person for election as a Director. Please see the detailed procedures as follows:

- **the way in which shareholders can convene an extraordinary general meeting:**

  Any shareholder(s) holding not less than 5% of total voting rights of all the shareholders who have a relevant right to vote may request the Board to convene an extraordinary general meeting. The request, duly signed by the shareholder(s) concerned, must clearly state the general nature of the business to be dealt with at the meeting and may include the text of the proposed resolution. Such request must be deposited at the registered office of the Company, 24th Floor, Bank of China Tower, 1 Garden Road, Hong Kong. The Company would take appropriate actions and make necessary arrangements in accordance with the requirements under sections 566 to 568 of the Hong Kong Companies Ordinance once a valid request is received.

- **the procedures for proposing a resolution at an annual general meeting:**

  The following shareholders are entitled to request the Company to give notice of a resolution that may properly be moved at an annual general meeting of the Company:

  (a) shareholders representing at least 2.5% of the total voting rights of all the shareholders who have a relevant right to vote; or

  (b) at least 50 shareholders who have a relevant right to vote.

  The request identifying the proposed resolution, duly signed by the shareholders concerned, must be deposited at the registered office of the Company, 24th Floor, Bank of China Tower, 1 Garden Road, Hong Kong not less than six weeks before the annual general meeting, or if later, the time at which notice is given of that meeting. The Company would take appropriate actions and make necessary arrangements in accordance with the requirements under sections 615 to 616 of the Hong Kong Companies Ordinance once valid documents are received.

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

  If a shareholder wishes to propose a person other than a retiring Director for election as a Director at a general meeting, the shareholder should lodge at the registered office of the Company (24th Floor, Bank of China Tower, 1 Garden Road, Hong Kong), (a) a notice in writing signed by such shareholder (other than the proposed person) duly qualified to attend and vote at the meeting of his/her intention to propose such person for election; (b) a notice signed by the proposed person indicating his/her willingness to be elected; and (c) a sum reasonably sufficient to meet the Company's expenses in giving effect thereto.

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

Further shareholder information is set out in the section headed "Investor Relations". Shareholders are welcome to send in any written enquiries to the Board for the attention of the Company Secretary either by post to the registered office of the Company at 24th Floor, Bank of China Tower, 1 Garden Road, Hong Kong or by way of email to investor_relations@bochk.com. The Company Secretary would direct the enquiries received to appropriate Board Member(s) or the Chairman of the Board Committee(s) who is in charge of the areas of concern referred therein for further handling. The Board, assisted by the Company Secretary, would make its best efforts to ensure that all such enquiries are addressed in a timely manner.

Disclosure of Information

The Company recognises the importance of timely and effective disclosure of information and formulates its policies, procedures and controlling measures on information disclosure (including inside information) in accordance with the requirements under applicable laws, regulations and regulatory requirements which includes the Securities and Futures Ordinance, Listing Rules and Hong Kong Monetary Authority Supervisory Policy Manual. The Information Disclosure Policy has been posted on the Company's website at www.bochk.com.

Directors' Responsibility Statement in relation to Financial Statements

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

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

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

Investor Relations

Investor Relations Policy and Guidelines

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

Investor Relations Programmes

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

The Company's investor relations strategies and programmes are formulated and overseen by the Investor Relations Committee, which is chaired by the Company's Chief Executive and comprises members of the senior management. The Investor Relations Division of the Board Secretariat, which reports directly to the Board, is responsible for the implementation of these strategies and acts as an intermediary between the Company and the investment community. Both the Board and the Committee evaluate the effectiveness of the investor relations programmes on a regular basis.

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

Information Disclosure Policy

Relevant laws in respect of information disclosure of Hong Kong listed companies became effective on 1 January 2013. The Company attaches high importance to the principles of information disclosure with regard to timeliness, fairness and transparency, and proactively discloses information that may have an impact on investment decision-making. In accordance with relevant legislation and statutory requirements, the Company has prepared an Information Disclosure Policy, which is available on the Company's website for public reference. The policy contains clear guidelines to ensure the following:

1. information disclosure is in compliance with the Listing Rules and other regulatory requirements;

2. all communications with the public, including the investment community and the media, follow the principles of timeliness, fairness, truthfulness, accuracy and compliance; and

3. effective monitoring of procedures for information disclosure is in place.

Access to Corporate Information

The Investor Relations section of the Company's website (www.bochk.com) provides shareholders and investors with access to information on the Company's latest developments according to the principles of the Information Disclosure Policy. These include information in relation to the Company's key developments, interim and annual results as well as quarterly financial and business review updates. Members of the public can access important announcements through the Stock Exchange of Hong Kong. The website also includes regulatory disclosure information that complies with the applicable requirements set out in the Banking (Disclosure) Rules as stipulated by the Hong Kong Monetary Authority.

The Investor Relations section also includes information on credit ratings, shares and dividends, as well as a corporate calendar with dates of important events.

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

Overview of Investor Relations Activities in 2016

In 2016, the Company continued its efforts to provide effective channels for communication with the investment community.

Annual General Meeting

At the Annual General Meeting held in June 2016, the Vice Chairmen of the Board, the Chairmen of the Remuneration Committee, Risk Committee and the Strategy and Budget Committee, members of the Nomination Committee and the Audit Committee respectively, the Company's senior management and external auditor were present to respond to questions and comments from shareholders. A total of 1,523 registered shareholders, 578 authorised corporate representatives and 808 authorised proxies holding an aggregate of 8,560,639,164 shares, representing 80.97% of the total issued share capital of the Company, were present. Minutes of the 2016 Annual General Meeting were made available to shareholders on the Company's website.

Results Announcements

At the Company's 2015 annual results announcement and 2016 interim results announcement, the senior management led by the Chief Executive conducted briefings with analysts and the press to apprise them of the Company's operating and financial results, business strategies and outlook. The presentation materials, announcements and webcasts were available to the public on the Company's website.

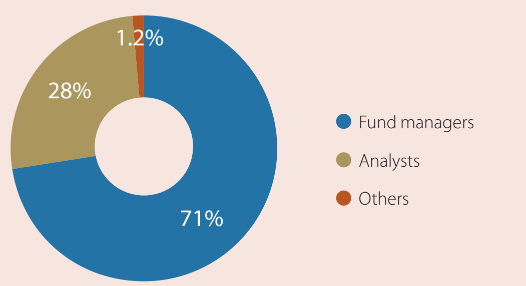
In addition to the interim and annual results announcements, the Company published quarterly financial and business reviews to keep shareholders up to date about the Company's performance and financial position.

Communication with the Investment Community

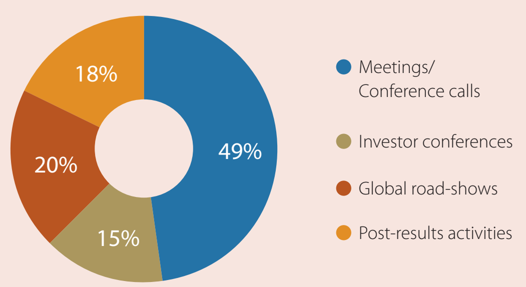
In 2016, the Company held approximately 150 meetings with investors and analysts across the world, with a total attendance of over 410. These meetings, which were conducted to give investors a better understanding of the Company's strategies and new business initiatives, were held during global road-shows, investor conferences, company visits, workshop and conference calls. The Company is widely covered by more than 15 securities research institutions. In order to expand investor base and optimise its geographical distribution, the Company proactively diversified its choices of roadshow destinations that covered the Mainland of China, Southeast Asia, Japan as well as Australia, in addition to the traditional routes including New York, London and Singapore. At the same time, the Company hosted a thematic workshop on hot financial topics and deepened investors' understanding of the development of the relevant areas.

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

Investor Meetings by Category



Investors Met by Event



Going Forward

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

Investor Relations Contact

Enquiries can be directed to:

Investor Relations Division
BOC Hong Kong (Holdings) Limited
24th Floor, Bank of China Tower
1 Garden Road, Hong Kong

Telephone: (852) 2826 6314
Facsimile: (852) 2810 5830
E-mail: investor_relations@bochk.com

Shareholder Information

Financial Calendar 2017

Major Events	Dates
Announcement of 2016 annual results	31 March (Friday)
Latest time for lodging transfers for entitlement to attend and vote at the 2017 Annual General Meeting and Extraordinary General Meeting	21 June (Wednesday) 4:30 p.m.
Book closure period (both days inclusive)	22 June (Thursday) to 28 June (Wednesday)
Latest time for lodging proxy forms for the 2017 Annual General Meeting and Extraordinary General Meeting	26 June (Monday) 2:00 p.m.
2017 Annual General Meeting and Extraordinary General Meeting	28 June (Wednesday) 2:00 p.m. and 2:30 p.m. or immediately after the conclusion of the 2017 Annual General Meeting, whichever is later
Last day in Hong Kong for dealing in the Company's shares with entitlement to final dividend	29 June (Thursday)
Ex-dividend date	30 June (Friday)
Latest time for lodging transfers for entitlement to final dividend	3 July (Monday) 4:30 p.m.
Book closure period (both days inclusive)	4 July (Tuesday) to 7 July (Friday)
Record date for final dividend	7 July (Friday)
Final dividend payment date	14 July (Friday)
Announcement of 2017 interim results	Mid to late August

Annual General Meeting

The 2017 Annual General Meeting will be held at 2:00 p.m. on Wednesday, 28 June 2017 at Four Seasons Grand Ballroom, Level 2, Four Seasons Hotel Hong Kong, 8 Finance Street, Central, Hong Kong.

Share Information

Listing and Stock Codes

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

Market Capitalisation and Index Recognition

As at 31 December 2016, the Company's market capitalisation was HK$293.4 billion, among the top 20 leading stocks on the Main Board of Hong Kong Stock Exchange in terms of market capitalisation. Given the Company's market capitalisation and liquidity, its shares are a constituent of Hang Seng Index, MSCI Index and FTSE Index series. In addition, the Company is a constituent of Hang Seng Corporate Sustainability Index Series and Hang Seng High Dividend Yield Index, which recognises its performance in related areas.

Debt Securities

Issuer	:	Bank of China (Hong Kong) Limited, a wholly-owned and principal subsidiary of the Company
Listing	:	The Notes are listed and traded on The Stock Exchange of Hong Kong Limited

Subordinated Notes

Description	:	Bank of China (Hong Kong) Limited 5.55% Subordinated Notes due 2020	
Issue size	:	US$2,500 million	
Stock codes	:	HKEX	4316
		ISIN	USY1391CAJ00 (Regulation S)
			US061199AA35 (Rule 144A)
		Bloomberg	EI1388897

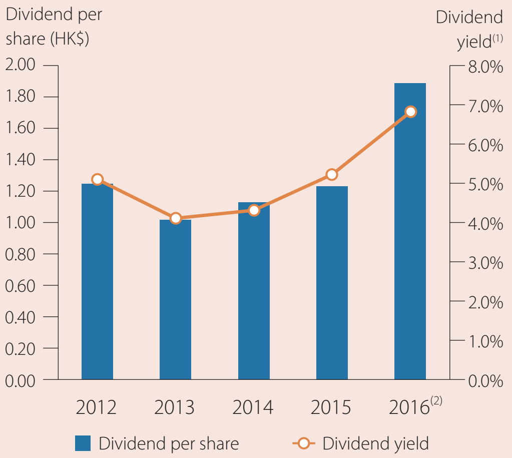
Share Price and Trading Information

Share price (HK$)	2016	2015	2014
Closing price at year end	27.75	23.70	25.95
Highest trading price during the year	29.85	33.70	27.95
Lowest trading price during the year	18.82	22.30	21.50
Average daily trading volume (m shares)	11.55	12.75	11.05
Number of ordinary shares issued (shares)	10,572,780,266		
Public float	Approximately 34%		

Dividends

The Board of Directors has recommended a final dividend of HK$0.625 per share, which is subject to the approval of shareholders at the 2017 Annual General Meeting. With the interim dividend per share of HK$0.545 and the special dividend per share of HK$0.710 paid during 2016, the total dividend per share will amount to HK$1.880 for the full year.

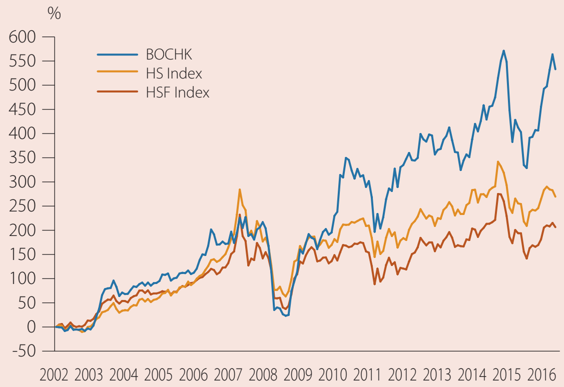
Dividend Per Share and Dividend Yield[1]



(1) Annual dividend yield is calculated based on dividends of the year (i.e. interim dividend and proposed final dividend of the year) and closing share price at that year-end.

(2) 2016 proposed final dividend will be subject to shareholders' approval at the Company's forthcoming Annual General Meeting.

Total Shareholder Return since Initial Public Offering



Source: Bloomberg

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

Credit Ratings (long-term)

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

Shareholding Structure and Shareholder Base

As at 31 December 2016, the Company had 10,572,780,266 shares in issue of which approximately 34% was held by the public and 0.43% was held in the form of ADSs. The Company's 78,453 registered shareholders were distributed in various parts of the world, including Asia, Europe, North America and Australia. Apart from BOC, the Company is not aware of any major shareholders with a shareholding of more than 5% which has to be reported under the SFO.

During the year, the shareholder structure of the Company remained stable. The following table shows the distribution of ownership according to the register of members which includes registered shareholders and shareholders recorded in the participant shareholding report generated from the Central Clearing and Settlement System as at 31 December 2016:

Category	Number of registered shareholders	% of registered shareholders	Number of shares held by registered shareholders	Approximate % of total issued shares
Individuals	78,316	99.83	232,898,628	2.20
Institutions, corporates and nominees Note	136	0.17	3,398,803,882	32.15
Bank of China Group Note	1	0.00	6,941,077,756	65.65
Total	78,453	100.00	10,572,780,266	100.00

Note:
As recorded in the register maintained by the Company pursuant to section 336 of the SFO, the total number of shares held by Bank of China Group was 6,984,274,213 shares, representing approximately 66.06% of the total number of shares in issue of the Company as at 31 December 2016. This figure included certain numbers of shares held for Bank of China Group in the securities account opened with BOCI Securities Limited, a participant of Central Clearing and Settlement System. Accordingly, these shares are included under the category of 'Institutions, corporates and nominees'.

Shareholder Enquiries

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

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

Other Information

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

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


ROAD
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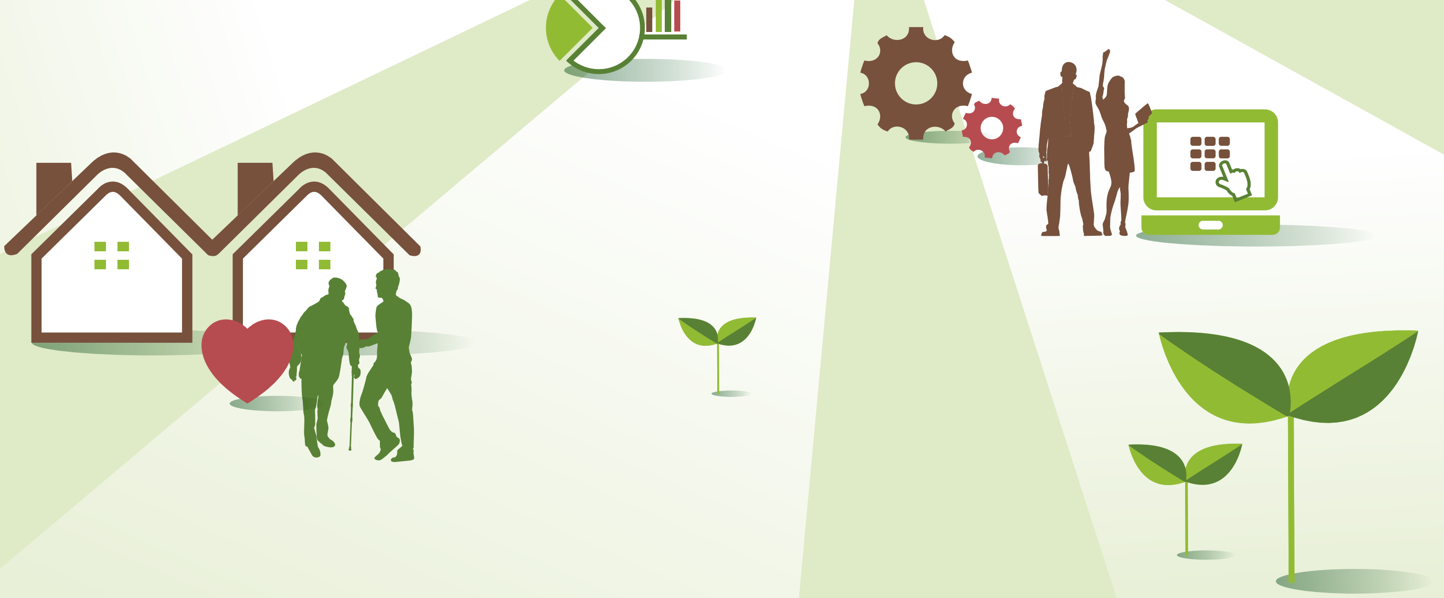
BELT

Regional Development

CORPORATE SOCIAL RESPONSIBILITY

By adhering to the strategic goal of "Serving Society, Delivering Excellence", the Group achieved sustainable growth, created momentum to the long-term development of Hong Kong and continued to generate greater value for our stakeholders. During the year, while expanding our business and accelerating our development pace, we also actively implemented various corporate social responsibility (CSR) initiatives. This section gives an overview of the Group's CSR activities. For details of our CSR initiatives, please refer to the Company's CSR Report.

Our efforts to promote CSR have been widely recognised. The Company has been a constituent of the Hang Seng Corporate Sustainability Index since 2010 and was selected as a top 20 constituent stock of the Hong Kong Business Sustainability Index for two consecutive years, in recognition of our efforts in upholding the principles of sustainability, CSR initiatives and performance. Since 2003, the Group has been named a Caring Company by the Hong Kong Council of Social Service for 14 consecutive years.



ACCESS TO BANKING AND FINANCE

As a leading banking group in Hong Kong, we are well aware of the role we play in contributing to Hong Kong's long-term economic development and enhancing its status as an international financial centre. We are committed to integrating our CSR principles into our service and business operations, providing high quality, convenient and secure banking services for different strata of society.

Supporting Economic Growth

The Group is committed to promoting the long-term economic development of Hong Kong and enhancing its status as an international financial centre. In particular, we make every effort to strengthen Hong Kong's position as a major offshore RMB hub and facilitate its role as a "super-connector" to grasp the opportunities arising from the national Belt and Road Initiative.

As the sole clearing bank for Hong Kong's offshore RMB business, we strive to develop Hong Kong's offshore RMB business. BOCHK currently serves more than 200 local and overseas participating banks. Our RMB clearing system is the most advanced among offshore markets, which handles the largest amount of RMB clearings and has the longest real time gross settlement operating hours. During the year, BOCHK was approved by the People's Bank of China (PBOC) to participate in the Cross-border Interbank Payment System (CIPS). As the first overseas bank to join the system as a direct participant, we not only helped reinforce Hong Kong's status as an offshore RMB centre but also promote the internationalisation of RMB.

The Group attaches great importance to supporting SMEs which form an important pillar of the Hong Kong economy. We introduced various measures to address the issues encountered by SMEs when opening bank accounts, obtaining bank loans and getting market information. To fully capitalise on BOCHK's most extensive branch network in Hong Kong, we launched a full scale branch transformation project to provide customer-centric services and enhance our service capabilities to SMEs.

The Group has launched a full scale branch transformation project to enhance our service capabilities for SMEs.

We have organised different seminars to help promote the development of e-finance.

We are the first bank to expand the Reverse Mortgage Programme to the subsidised sale flats with unpaid land premium to help retirees plan for their financial security.

Furthermore, the Group is participating in the construction of a financial artery for the Belt and Road Initiative as part of our development strategy, riding on the national development initiatives. We actively transformed BOCHK from a local bank to a regional bank, extending the reach of our services, products, resources along the Belt and Road. During the year, we completed the acquisition of BOC Malaysia and set up our first branch in Brunei. Our strengthened ties and greater financial cooperation with ASEAN countries have significant meaning in enhancing Hong Kong's status as an international financial centre and extending the influence of Hong Kong to the Southeast Asian region.

Promoting Financial Inclusion

With our unique edges, the Group supports the development of financial inclusion by providing convenient and quality banking services to all sectors of the community. BOCHK has the most extensive and convenient as well as largest number of service network in Hong Kong. This comprises 197 branches and more than 1,000 self-service banking machines, as well as Internet and Mobile Banking channels. We endeavour to meet the needs of customers with comprehensive financial products and services.

The Group has launched BOCHK iService 24-hour Video Banking Service in support of financial inclusion.

During the year, we added 44 self-service banking centres in different sites including public housing estates, public hospitals, Hong Kong International Airport, etc. We also launched BOCHK iService 24-hour Video Banking Service in a remote public housing estate, further enhancing our service to residents there.

We demonstrate a high standard of care in providing banking services to the disabled, senior customers, underprivileged groups and non-profit organisations. All of our ATMs are installed with protruding symbols; 99% of ATMs, up from 95% last year, now have soft keypads installed on both sides of the screens for account and service selection. Our ATMs are also designed to give better wheelchair access.

BOCHK has been the major bank in Hong Kong participating in the Reverse Mortgage Programme. In 2016, the Programme was extended to subsidised sale flats with unpaid land premium. We were the first Bank to support this extension, accepting applications from senior citizens aged over 60 years old who use their subsidised sale flats with unpaid land premium as collateral to apply for reverse mortgage loans. This gives the elderly greater flexibility in planning for retirement.

We provide HKD savings accounts with low balance monthly fee and ATM card annual fee waiver. Account holders aged 65 or above, or below 18, as well as recipients of Government Disability Allowances/Comprehensive Social Security Assistance enjoy a service fee waiver for counter transactions. No service fee is charged on dormant accounts in support of the HKMA's Treat Customers Fairly Charter. We also offer NGOs comprehensive banking solutions with preferential fees on our service.

INVESTING IN COMMUNITIES

The Group has been committed to building a caring and harmonious community, as well as providing assistance to those in need. By supporting a diverse range of community activities, we promote the steady development of the community and bring positive energy to society. As a way of contributing to the community, BOCHK and BOCHK Charitable Foundation donated over HK$13 million in 2016 to a total of 28 projects, for causes in charity, education, environmental protection, sports and arts. We also encourage our staff to participate in various volunteer activities, and to share the success of the Company with those in need.

Nurturing Talent

The Group offers scholarships and bursaries to encourage tertiary students for studies and to support students who have financial needs. Since 1990, we have been successively providing scholarships and bursaries to ten local universities. During the year, we sponsored the Upward Mobility Scholarship of Future Stars, organised by the Commission on Poverty of the Hong Kong SAR Government for youngsters who have demonstrated positive attitude in the face of adversity. In order to promote among teenagers a greater understanding of the Chinese culture and national development, we sponsored an Excellence Scholarship in Chinese History set up by the Endeavour Education Centre.

We promote among teenagers a greater understanding of the Chinese culture and national development by supporting an Excellence Scholarship in Chinese History set up by the Endeavour Education Centre.

To widen the horizon of the young people, we supported the New Media Internship Programme 2016 and Operation Zhang Qian – Student Summer Internship Programme 2016 organised by Maritime Silk Road Society. These programmes allowed them to gain a deeper understanding of our national strategic development and opportunities.

During the year, we also organised Career Sharing Session for a number of local educational institutions and overseas universities. In this programme, we introduced to students our major businesses, organisational structure, corporate culture and career development opportunities, enriching their knowledge about the banking industry that will be useful for their career planning .

Apart from local education programmes, we also provided a subsidy to a national grade poverty county in Xianyang City of Shaanxi Province. The subsidy supported the education development in Xunyi County of Shaanxi Province to improve school conditions and give underprivileged students the chance to receive education. In Malaysia, our Kuching Branch continued to participate in fund raising events organised by Chinese schools to support local Chinese communities in education.

We have been providing scholarships and bursaries to local universities since 1990.

The Group was the title sponsor of the 2016/17 Season Opening Concerts of the Hong Kong Philharmonic Orchestra.

Caring for the Community

During the year, BOCHK sponsored a Food Angel's programme, Food Station, to recycle edible food, make hot meals and food packages that will be given away to grassroot elderly and low-income people, benefiting nearly 400,000 people. The programme has also helped minimise the environmental problem of huge food wastage in Hong Kong.

In addition, we continued our partnership with the New Home Association ("NHA") in the BOCHK-NHA Computer Donation Programme to donate recycled computers to members of ethnic minorities, new immigrants, underprivileged families and the elderly to help them integrate into the digital age. We also continued to sponsor the Government's Child Development Fund and offer account opening services to grassroot children. Through this programme, they will learn about the importance of saving and financial planning as well as fostering self-discipline.

As a longstanding supporter of the Community Chest of Hong Kong ("the Chest"), we encourage our staff members not only to make donations but also to take part in fund-raising programmes organised by the Chest. These events include the Community Chest Corporate Challenge, Community Chest Swim for Millions, Community Chest Walkathon and charity concert jointly organised by the Chest and Hong Kong Police Force. We received the Platinum Award from the Chest in 2016. We also sponsored the Hospital Authority in organising the HA New Year Run, a fundraising event to benefit patients who suffer from chronic illnesses as well as related patient organisations.

The Group's Malaysia Branch is active in fulfilling its CSR. Staff from the Kuching Branch visit local orphanages from time to time. They also provide financial support for food purchases on a regular basis. For "Donate with Hearts" activities organised by the Teenage House in Kuala Lumpur (KL) staff members from KL not only made donations but also participated in a marathon run for charity.

BOCHK has sponsored the Hong Kong Corporate Citizenship Programme of the Hong Kong Productivity Council for seven consecutive years to enhance corporate awareness of CSR. During the past seven years, more than 800 enterprises have participated in this programme.

Food Station, sponsored by BOCHK, benefits elderly and people in need through the provision of meals.

To spread the new year blessings, we have invited grassroot families to enjoy the "BOCHK Hong Kong New Year Countdown Celebrations 2017" pyromusical show at the ceremony.

We support the Hong Kong Premier League to promote Hong Kong's football development.

Promoting Sports, Arts and Culture

We are a steadfast advocate of sports to promote the message of physical and mental health, team spirit and positive life attitude. Since 1999, we have supported the development of badminton sport and organised various badminton competitions, activities and training courses that have attracted the participation of over 1.4 million people. We support the nurturing of badminton players and Ng Ka Long, Angus, a recognised player on Hong Kong's professional team, is an excellent example.

Since 2002, we have been sponsoring the Hong Kong Island & Kowloon Regional Inter-school Sports Competition to widely promote sports development in secondary schools in order to encourage sportsmanship among students. In 2016, approximately 80,100 athletes participated in over 8,000 matches in 20 sports events. Also, more than 510 students participated in the BOCHK Schools Sports Volunteer Scheme, contributing over 9,800 hours of volunteer time.

Football is one of the most popular sports in Hong Kong. In cooperation with the Hong Kong Football Association Limited (HKFA), BOC Life was the title sponsor of the 2015 to 2017 season of the Hong Kong Premier League. Through our sponsorship, we aim to promote the development of football in Hong Kong and encourage more people to take up this healthy sport.

The Group supports a diverse range of cultural activities. One of the key sponsorships during the year was the Hong Kong Philharmonic Orchestra's 2016/17 Season Opening Concerts by the world renowned cellist Yo-Yo Ma. The concert attracted around 2,000 audience. For the fourth consecutive year, BOCHK Private Bank sponsored the Hong Kong Art Week organised by the Hong Kong Gallery Association. This 12-day art event gathered 50 galleries and presented over 100 shows and activities for the public. Our volunteer team also actively participated in the Family Art Day with their family members, fully reflecting the Group's commitment to CSR. Furthermore, to promote tea culture, we sponsored the Hong Kong Trade Development Council's Tea Rendezvous event for six consecutive years.

As 2016 marked the 150th anniversary of the birth of Dr Sun Yat-sen, we sponsored a large-scale exhibition to commemorate Dr Sun's patriotism and progressive spirit.

We were also the title sponsor for the "BOCHK Hong Kong New Year Countdown Celebrations 2017" organised by the Hong Kong Tourism Board. The gala event not only conveyed a positive message of joy and harmony to all Hong Kong people, but also marked the beginning of the year-long celebration of Bank of China's centenary of service in Hong Kong. It has attracted over 330,000 citizens and visitors who enjoyed the pyromusical show together at the Victoria Harbour. About 50 audience from the grassroot families and minority groups were also invited to the countdown ceremony.

PROTECTING THE ENVIRONMENT

We are committed to reducing carbon footprint generated from our daily operations and minimising the environmental impact of business development. We also promote environmentally responsible practices to our staff, customers, suppliers and other stakeholders for more sustainable development.

Our "Small Value Transfer" service provides customers with secure and reliable P2P payment service.

Number of customers opting for e-statements

▲ 20.3%

Average customer transaction time

▼ 24%

Promoting a Green Bank

To reduce paper consumption, we encourage customers to use electronic banking services, including e-cheques and e-statements. In 2016, the number of customers opting to receive e-statements rose significantly by 20.3%. In addition, we implemented a paperless branch teller model across our extensive branch network, shortening the average customer transaction time by 24%.

We have incorporated elements related to environmental protection, energy and emissions reduction as well as public health and safety in our credit risk policy and procedures. We also take into consideration our customers' environmental performance when making credit decisions. In 2016, we continued to provide loans to enterprises involved in developing new energy sources, renewable energy and water conservation projects, in support of environmental protection and community development.

We have participated in Charter on External Lighting to save energy.

"BOCHK Corporate Environmental Leadership Awards" is successful in promoting environmental practices among the manufacturing and services enterprises in Hong Kong and the Pan Pearl River Delta region.

Annual Water Usage

▼ 21.7 million tons

= volume of 5,490 standard 50-metre swimming pools

Annual Waste

▼ 1.1 million tons

= an amount covering 410 times Shing Mun Reservoir

Recycled Materials

> 350,000 tons

= an amount covering the area of 9,300 times Victoria Park

During the year, BOCHK was the Joint Global Coordinator, Joint Bookrunner and Joint Lead Manager for the issuance of a three-year US$500 million bond for Bank of China London Branch. It was also the first Bank of China offshore Green Covered Bond. We continued to participate in the Energy Efficiency Loan Scheme launched jointly by two local electricity companies. The Scheme provides loans to commercial and industrial customers interested in implementing energy conservation projects.

Raising Awareness of Environmental Issues

Since 2015, the Group, together with the Federation of Hong Kong Industries, has organised the "BOCHK Corporate Environmental Leadership Awards" programme to encourage enterprises to support environmental protection.

In 2016, there were over 530 corporate participants, completing 1,118 green projects, which have collectively reduced annual electricity consumption by more than 223 gigawatt hours – equivalent to the electricity consumed by 24,600 average four-member households in one year. Other collective achievements included the reduction of annual water usage by 21.7 million tons (approximately equivalent to the volume of 5,490 standard 50-metre swimming pools) and the reduction of annual waste by 1.1 million tons (an amount that would cover Shing Mun Reservoir by 410 times). Almost 350,000 tons of materials were also recycled (an amount that would cover an area equivalent to 9,300 times the size of the Victoria Park in Hong Kong).

In 2016, we sponsored WWF's environmental education programmes to promote sustainable living. The programme featured environmental seminars and workshops for about 750 primary students. We also continued our sponsorship of WWF's Earth Hour initiative, where all non-essential lighting in major office buildings was switched off for an hour on 28 March, bringing public awareness to the reduction of energy consumption.

For three consecutive years, we have supported Greeners Action's "Red Packets Recycling Campaign", setting up red packet collection points at key office buildings and 60 branches. The whole event has received a total number of 8.8 million recycled red packets in 2016 with an estimate weight of 27 tons. This helps encourage people to develop the habit of reclaiming and reusing red packets.

We are actively developing financial technology and promoting product and service innovation.

CARING FOR OUR PEOPLE

The Group's people-oriented philosophy is apparent in the way we manage human resources to continuously attract, acquire and nurture talent. We are committed to providing a harmonious, diverse and friendly work environment for our staff to realise their potentials. As of the end of 2016, the Group had a total of 12,836 employees, with diverse backgrounds and experience.

Developing Our Staff

We strive to provide an ideal career development platform for employees and offer a wide variety of training programmes to promote internal mobility and development.

We have a well-established talent pool made up of people from a broad range of professional backgrounds. Our staff development plan is aligned with the Group's medium- and long-term business strategies and is based on Leadership and Fundamental Competency models. These provide clear objectives for personal development and serve as the foundation for talent recruitment and staff performance assessments.

Through the Management Trainee Programme, every year the Group attracts new graduates who aspire to develop their career in the financial services industry in order to give fresh perspectives to the Group and to nurture new talent for the industry. We select talented students for internship opportunities from tertiary institutions in Hong Kong, the Mainland and overseas. Interns can join the Group through our Management Trainee Programme or Graduate Programme for their long-term career development.

Staff of the Group have ready access to continuing education opportunities. In addition to subsidies for further studies, we also provide diversified learning programmes and development platforms to meet our staff's personal goals and the Group's long-term development objectives. By making compliance training courses mandatory for every employee, we have strengthened our compliance and risk prevention culture throughout the Group.

We are the Overall Champion in the 7th Athletic Meet organised by the Hong Kong Chinese Enterprise Association.

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

We have organised various activities for our colleagues and their families such as Disneyland Fun Day and InnoTech Expo 2016 etc.

Supporting Our People

We make every effort to provide our staff with a pleasant and caring work environment. To better understand the needs and expectations of employees, we have constant communication with staff through various channels. The Group attracts, motivates and retains outstanding employees by offering competitive compensation and incentives as well as comprehensive benefits. An award presentation ceremony is held annually to recognise outstanding staff and teams.

BOCHK attaches great importance to "work-life balance" and encourages employees to pursue their career as well as lead a fulfilling personal life. During the year, various recreational activities were organised for staff. In 2016, we hosted a Staff and Family Members Carnival at Hong Kong Disneyland for over 28,000 staff and their family members.

The Group has organised various team building activities to enhance cohesion among staff.

Serving the Community

We encourage our employees to contribute their time and effort to serve the community. There are about 1,400 employees in our Dynamic Volunteer Team. Every year, we arrange training programmes for our volunteers to strengthen their skills in helping others. In 2016, our volunteer team, together with their family and friends, participated in some 90 volunteer activities, with more than 49,000 hours of community service, up 10% from 2015. The number of people participated in volunteer service surged over three times to 11,818. The beneficiaries of these volunteer activities included children and youth, the elderly, the physically challenged with special needs as well as environmental organisations. The enthusiasm of our volunteers has been recognised by the Social Welfare Department through its Gold Award for Volunteer Service for seven consecutive years.

We have participated in different charitable activities such as the Carol Singing Festival, Trail Walker, Blood Donation Day and the Walk for Millions.

Awards and Recognition

Given our solid financial strength and outstanding performance, we received various industry awards which have further reinforced our leading position in the market. We were named the Strongest Bank in Asia Pacific and Hong Kong by *The Asian Banker* in recognition of our ability to continuously increase profitability. In addition, we won a number of accolades acknowledging the achievements we have made in enhancing customer experience through continuous product and service innovation. These include awards for our RMB business, cash management, SME, Internet and mobile banking, and credit card services. The Group is also highly commended for its commitment to promote corporate social responsibility.

Financial Strength and Corporate Governance

- Strongest Bank in Asia Pacific and Hong Kong, Best Retail Bank in Hong Kong, Wealth Management Business of the Year, Best Cash Management Bank in Hong Kong, Best Transaction Bank in Hong Kong, Best Trade Finance Deal in Hong Kong and Best Mobile Social Media Engagement Project in Technology Innovation Awards ***(The Asian Banker)***
- Best Bank in Hong Kong – Chinese Financial Institutions and Best FIG Deal ***(FinanceAsia)***
- Hong Kong Domestic Cash Management Bank of the Year, Hong Kong Domestic Foreign Exchange Bank of the Year, Hong Kong Mobile Banking Initiative of the Year, Hong Kong Digital Banking Initiative of the Year and Hong Kong Social Media Initiative of the Year ***(Asian Banking & Finance)***
- Best Consumer Digital Banks in Hong Kong ***(Global Finance)***

Service Excellence

- Rank No. 1 as mandated lead arranger in the Hong Kong and Macau syndicated loan market for 12 consecutive years ***(Basis Point)***
- The Best SME's Partner Award **(The Hong Kong General Chamber of Small and Medium Business)**
- Outstanding Import & Export Industry Partner Award **(The Hong Kong Chinese Importers' and Exporters' Association)**
- Eleven honours in the Outstanding Financial Management Planner Awards **(The Hong Kong Institute of Bankers)**
- Top Performer (Bank and Services) and Mid-Year Encouragement Award in the Quality Service Scheme **(Mass Transit Railway Corporation Limited)**
- Outstanding Claims Management Award Finalist **(The Hong Kong Federation of Insurers and Metro Finance)**
- The Hong Kong Leaders' Choice Brand Awards **(Metro Finance** and **Metro Finance Digital)**:
  Excellent Brand of Mobile Banking
  Excellent Brand of Foreign Exchange Services
  Excellent Brand of Corporate Banking Services
  Excellent Brand of Mobile Payments
  Excellent Brand of Personal Credit Cards
  Excellent Brand of Mortgage – Banking
  Excellent Brand of Fund Investment Banking Services
  Excellent Brand of Securities Services – Banking
- Financial Services Industry – Gold Bauhinia Award **(China Xinhua News Network Corporation)**
- Best Custody Specialist – China ***(The Asset)***
- Saving Plan – Excellence and Insurance Company of the Year – Outstanding Performance ***(Bloomberg Businessweek)***
- Best Total Return of Greater China Equity (1 Year) – BOCHK All Weather CNY Equity Fund **(Chinese Asset Management Association of Hong Kong** and **Bloomberg)**
- Fund of the Year Awards 2016 ***(Benchmark)***:
  High Yield Fixed Income – Outstanding Achiever of Mutual Fund House
  Best-In-Class, Manager of the Year Award – High Yield Fixed Income
- 2016 Best of the Best Awards ***(Asia Asset Management)***:
  Best China Fund House in Hong Kong
  Best RMB Manager in Hong Kong
  Best of the Best Award – RMB Bonds in offshore category (5 Years)
- Wealth Management Awards 2016 ***(Benchmark)***:
  Customer Insights – Best-in-Class
  Innovation – Best-in-Class
  Customer Support Team – Best-in-Class
  High Net Worth Team – Outstanding Achiever
- Listed Company Award of Excellence (Blue Chip) ***(Hong Kong Economic Journal)***
- Outstanding Brand Award – Wealth Protection Insurance ***(Economic Digest)***
- Mortgage Services Award and Banking – Dual Currency Credit Card Services Award ***(Sing Tao Daily)***
- My Favourite Wealth Management Banking Service Award and My Favourite "Belt and Road" Banking Service Award ***(Sky Post)***
- My Favourite Dual Currency Credit Card Award and My Favourite Overseas Spending Award ***(Hong Kong Economic Times*** and ***Sky Post)***

Awards and Recognition

- The Best Life Insurance Award
  (Metro Daily and ***Metro Prosperity)***
- 2016 Metro Creative Awards: The Best Digital Campaign
  (Metro Daily)
- My Most Favourite Credit Card for Travelling Award
  (U Magazine)
- 2016 Wealth Money Management Awards – Best for Retail Focused Investment Solutions in Hong Kong
  (Wealth & Finance International)

MasterCard Worldwide:

- Highest Market Share of Cross-border Cardholder Spending Volume in Macau
- Highest Market Share of Open Cards in Macau
- Highest Market Share of Cardholder Spending in Macau
- Highest Market Share of Open Cards in Hong Kong – 1st Runner Up
- Highest Market Share of Merchant Purchase Volume in Hong Kong – 2nd Runner Up

UnionPay International:

- Bank of the Year Award in Hong Kong & Macau
- Largest Card Number (Credit Card) in Hong Kong – Gold Award
- Highest Card Volume (Credit Card) in Hong Kong – Gold Award
- Highest Card Number Growth (Debit Card) in Hong Kong – Gold Award
- Highest Card Volume Growth (Debit Card) in Hong Kong – Gold Award
- Highest Acquiring Volume in Hong Kong – Gold Award
- Highest QuickPass Acquiring Volume in Hong Kong & Macau – Gold Award
- U-Plan – Innovative Acquiring Award in Hong Kong & Macau
- Highest UPOP Issuing Volume in Hong Kong & Macau – Gold Award
- Highest UPOP Acquiring Volume in Hong Kong & Macau – Gold Award
- Largest Active POS Number in Hong Kong – Silver Award
- Largest Card Number (Debit Card) in Hong Kong – Silver Award

RMB Business

- RMB Business Outstanding Awards
  (Metro Finance, Metro Finance Digital and **Hong Kong Ta Kung Wen Wei Media Group)**:
  Outstanding Innovation – Innovative Products and Services for the Belt and Road Initiative
  Outstanding Retail Banking – Comprehensive Investment Services
  Outstanding Retail Banking – Comprehensive Banking Services
  Outstanding Retail Banking – Insurance Services
  Outstanding Retail Banking – E-banking
  Outstanding Retail Banking – Credit Cards
  Outstanding Retail Banking – Cross-border Mobile Payment Services
  Outstanding Corporate/Commercial Banking – Cross-border All-round Services
  Outstanding Treasury Business – (Foreign Exchange) Derivatives Trading
  Outstanding Treasury Business – Dim Sum Bond Market Maker
  Outstanding Insurance Business – Endowment Award
  Outstanding Insurance Business – Annuity Award
  Outstanding Insurance Business – Universal Life Award
  Outstanding Insurance Business – Customer Service Award
- The Hong Kong Leaders' Choice Brand Awards
  (Metro Finance and **Metro Finance Digital)**:
  Excellent Brand of RMB Banking Services
- Outstanding RMB Business Award – Innovative and Comprehensive Cross-border Financial Services ***(Wen Wei Po)***
- My Favourite Renminbi Business Award ***(Sky Post)***

Social Responsibility

Caring for Society

- Included as a constituent of the **Hang Seng Corporate Sustainability Index** and **Hang Seng (Mainland and HK) Corporate Sustainability Index** respectively, and a constituent of the **Hang Seng Corporate Sustainability Benchmark Index**
- A top 20 constituent stock of the **Hong Kong Business Sustainability Index**
- 10 Years Plus Caring Company Logo
  (The Hong Kong Council of Social Service)
- President's Award **(The Community Chest of Hong Kong)**
- Family-Friendly Employer, Special Mention Award and Award for Breastfeeding Support **(Family Council)**
- Barrier-free Facilities Caring Award
  (People of Fortitude • International Mutual-aid Association for the Disabled)

BOC Life:

- Employer of Choice Award 2016 ***(JobMarket)***
- Outstanding Social Caring Organization Award
  (Social Enterprise Research Institute)
- Distinguished Family-Friendly Employer, Award for Innovation and Award for Breastfeeding Support **(Family Council)**

BOCCC:

- 5 Years Plus Caring Company Logo
  (The Hong Kong Council of Social Service)
- Gold Award for Volunteer Service – Organization
  (Social Welfare Department)

Environmental Protection

- Excellence of Environmental Contribution ***(U Magazine)***
- My Favourite Green Banking Service Award ***(Sky Post)***

BOC Life:

- Wastewi$e Certificate – Excellence Level
  (Environmental Campaign Committee)

Talent Development Management

- Change Management Legal Team of the Year
  (In - House Community)
- Manpower Developer 1st **(Employees Retraining Board)**
- The Award for Excellence in Training and Development – Excellence Award **(Hong Kong Management Association)**
- FT Asia Pacific Innovative Lawyers Outstanding Individuals Awards
  (Financial Times)

Contact Us

Bank of China (Hong Kong)

Enquiry Hotline

Contents	Telephone	Contents	Telephone
Personal Customer Service Hotline	(852) 3988 2388	BOC Credit Card Hotline	(852) 2853 8828
Wealth Management Service Hotline	(852) 3988 2888	BOC Credit Card Loss Card Hotline	(852) 2544 2222
Enrich Banking Service Hotline	(852) 3988 2988	ATM Card Hotline	(852) 2691 2323
Corporate Customer Service Hotline	(852) 3988 2288	BOC Express Cash Customer Service Hotline	(852) 2108 3611

Branch Locator

www.bochk.com/en/branch.html

Internet Banking and Mobile Banking

Internet Banking:
www.bochk.com

Download on the App Store

Google play

Social Media

BOCHK_CC

YouTube 中銀香港BOCHK

www.youtube.com/user/bankofchinahk

Independent Auditor's Report

Ernst & Young
22/F, CITIC Tower
1 Tim Mei Avenue
Central, Hong Kong

To the members of BOC Hong Kong (Holdings) Limited
(Incorporated in Hong Kong with limited liability)

Opinion

We have audited the consolidated financial statements of BOC Hong Kong (Holdings) Limited (the "Company") and its subsidiaries (the "Group") set out on pages 125 to 282, which comprise the consolidated balance sheet as at 31 December 2016, and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2016, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and have been properly prepared in compliance with the Hong Kong Companies Ordinance.

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing ("HKSAs") issued by the HKICPA. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the *HKICPA's Code of Ethics for Professional Accountants* ("the Code"), and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matters:	How our audit addressed the key audit matters:
Impairment assessment of advances to customers	
Refer to summary of significant accounting policies in Note 2.14, critical accounting estimates and judgements in applying accounting policies in Note 3.1, and disclosures on credit risk and loan impairment allowances respectively in Note 4.1 and Note 26 to the financial statements. As at 31 December 2016, gross advances to customers amounted to HK$973,071 million, representing 41.80% of total assets; and the impairment allowance for advances to customers amounted to HK$3,124 million. The assessment of impairment for advances to customers involved significant management judgements and estimates of the losses incurred within the loan portfolios at the reporting date. The Group adopted an individual impairment assessment approach in respect of individually significant loans or impaired loans; and a collective impairment assessment approach in respect of loans not individually significant or not individually impaired. Under the collective approach, the assessment of future cash flows for loan portfolios was based on the historical loss experience of loans with similar credit risk characteristics, with adjustments based on economic factors and judgemental overlays. Parameters associated with the historical loss experience included probability of default, loss given default and loss identification period.	We obtained an understanding of the Group's credit policy and evaluated and tested the design and the operating effectiveness of the key controls over the processes of credit assessment, loan classification and loan impairment assessment. Our control testing on the loan impairment process included the identification of impairment indicators and assessment of the assumptions used in the individual and collective impairment models. In assessing the individually assessed impairment allowances made by the Group, we adopted a risk-based sampling approach for our loan review procedures. We selected samples based on risk characteristics of individual items including the industry and geographic location of the operations of borrowers, internal loan grading and past due history. We formed an independent view on the classification of the loans and the level of provisions recognised by the Group through reviewing the borrowers' detailed information about their financial performance, recoverable cash flows and valuation of collaterals, as well as re-calculating samples of discounted cash flows for the impaired loans. We assessed the collective impairment model, data input and related management's assumptions on the impact of macro-economic trends and judgemental overlays for the various types of loan portfolios. We evaluated these assumptions by considering various factors including the period of historical data used in the model, observable economic data, market information and specific industry trends. We also performed testing on the relevant data quality by sample checking to the relevant data source and re-computed management's calculation of the collective impairment. Furthermore, we evaluated and tested the design and operating effectiveness of the Group's key controls related to disclosures on credit risk in Note 4.1 to the financial statements.

Key audit matters:	How our audit addressed the key audit matters:
Valuation of financial instruments	
Refer to summary of significant accounting policies in Note 2.12, critical accounting estimates and judgements in applying accounting policies in Note 3.3, and disclosures on fair values of financial instruments in Notes 5.1 and 5.2 to the financial statements. The Group has applied valuation techniques to determine the fair value of financial instruments that are not quoted in active markets. These valuation techniques, in particular those that include significant unobservable inputs, involve management using subjective judgements and assumptions. With different valuation techniques and assumptions applied, the valuation results can vary significantly. As at 31 December 2016, the Group's financial assets and liabilities measured at fair value amounted to HK$662,708 million and HK$62,660 million respectively, representing 28.47% and 2.99% of total assets and total liabilities respectively. Financial instruments which had significant unobservable inputs in the valuation, and hence were categorised within level 3 of the fair value hierarchy, involved a higher degree of uncertainty in their valuation. As at 31 December 2016, 77.03% and 0.83% of the Group's financial assets measured at fair value were categorised within level 2 and level 3, respectively.	We evaluated and tested the design and operating effectiveness of key controls related to the valuation of financial instruments, including independent price verification, independent model validation and approval. We focused on the valuation methodologies and assumptions of financial instruments that were classified as level 2 and level 3 in the fair value hierarchy. We involved our valuation specialists in evaluating the valuation techniques, inputs and assumptions through comparison with the valuation techniques that are commonly used in the market, the validation of observable inputs using external market data, and comparison with valuation outcomes obtained from various pricing sources. We also evaluated and tested the design and operating effectiveness of the Group's key controls related to the fair value disclosures in Notes 5.1 and 5.2 to the financial statements.

Key audit matters:	How our audit addressed the key audit matters:
Recognition of deferred tax assets	
Refer to summary of significant accounting policies in Note 2.23, critical accounting estimates and judgements in applying accounting policies in Note 3.6, and disclosures on deferred taxation in Note 37 to the financial statements. As at 31 December 2016, the Group recognised deferred tax assets of HK$430 million relating to temporary differences arising from impairment allowances and HK$1,132 million relating to other temporary differences and tax credits. The majority of the other temporary differences and tax credits related to tax credits recoverable from the tax authorities in Hong Kong under double tax treaty arrangements, arising from withholding income taxes payable in other jurisdictions on certain interest income. Application on such tax credits will be made to the tax authorities in Hong Kong after the corresponding withholding income taxes payable is settled and evidenced by respective payment receipts issued from the corresponding tax authorities. These deferred tax assets, where required by accounting standards, were offset against and included within deferred tax liabilities as shown in Note 37 to the financial statements. The recognition of the deferred tax assets involved significant management judgements and assumptions, based upon the estimation of available tax credits and the possibility to recover such deferred tax assets recognised.	Our audit procedures included, amongst others, the involvement of our tax specialists to assist in evaluating the judgements and assumptions adopted by management to determine the recognition and recoverability of the deferred tax assets, in light of current tax laws. We also assessed management's estimates of the Group's entitlement to the tax credits and examined correspondences between the Group and relevant tax authorities. In addition, we also assessed the adequacy of disclosures in Note 37 to the financial statements with respect to compliance with HKAS 12 – Income Taxes.

Key audit matters:	How our audit addressed the key audit matters:
Valuation of insurance contract liabilities	
Refer to summary of significant accounting policies in Note 2.19, critical accounting estimates and judgements in applying accounting policies in Note 3.5, and disclosures on insurance contract liabilities in Note 38 to the financial statements. As at 31 December 2016, the Group, through its consolidated subsidiary BOC Group Life Assurance Company Limited, had insurance contract liabilities amounting to HK$86,534 million, representing 4.13% of the Group's total liabilities. The measurement of insurance contract liabilities involved significant judgements over uncertain future outcomes, mainly the estimated ultimate total settlement value of insurance contract liabilities, including any guarantees provided to policyholders. Economic assumptions, such as investment return and associated discount rates, and operating assumptions, such as mortality and morbidity, were the key inputs used to estimate these insurance contract liabilities as reported in the consolidated balance sheet.	We used our actuarial specialists to assist in the performance of our audit procedures. These included a review of the product features and the methodology used in valuing the insurance contract liabilities in accordance with the relevant regulations and accounting requirements. We also tested the internal controls performed by management over the valuation process. We also assessed the economic assumptions and operating assumptions used in the insurance contract liabilities valuation with reference to market data and policyholder experience and assessed the accuracy of the calculation of policy reserves through performing independent recalculation. In addition, we assessed the validity of the Group's liability adequacy test under HKFRS 4 – Insurance Contracts. Our assessment included an evaluation of management's projected cash flows based on relevant product features. We tested the associated assumptions by comparing with industry experience data.

Other information included in the Annual Report

The directors of the Company are responsible for the other information. The other information comprises the information included in the Annual Report, other than the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors for the consolidated financial statements

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

In preparing the consolidated financial statements, the directors of the Company are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors of the Company either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The directors of the Company are assisted by the Audit Committee in discharging their responsibilities for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Our report is made solely to you, as a body, in accordance with section 405 of the Hong Kong Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with HKSAs, we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Tso Pui Sze.

Ernst & Young

Ernst & Young
Certified Public Accountants
Hong Kong, 31 March 2017

Consolidated Income Statement

For the year ended 31 December	Notes	2016 HK$'m	(Restated) 2015 HK$'m
CONTINUING OPERATIONS			
Interest income		**35,890**	37,492
Interest expense		**(10,462)**	(12,316)
Net interest income	6	**25,428**	25,176
Fee and commission income		**14,772**	15,572
Fee and commission expense		**(4,231)**	(4,299)
Net fee and commission income	7	**10,541**	11,273
Gross earned premiums		**19,339**	22,645
Gross earned premiums ceded to reinsurers		**(8,705)**	(10,200)
Net insurance premium income		**10,634**	12,445
Net trading gain	8	**4,605**	2,597
Net gain/(loss) on financial instruments designated at fair value through profit or loss		**101**	(751)
Net gain on other financial assets	9	**1,006**	1,286
Other operating income	10	**814**	810
Total operating income		**53,129**	52,836
Gross insurance benefits and claims and movement in liabilities		**(21,140)**	(23,975)
Reinsurers' share of benefits and claims and movement in liabilities		**9,765**	11,320
Net insurance benefits and claims and movement in liabilities	11	**(11,375)**	(12,655)
Net operating income before impairment allowances		**41,754**	40,181
Net charge of impairment allowances	12	**(578)**	(755)
Net operating income		**41,176**	39,426
Operating expenses	13	**(12,213)**	(11,611)
Operating profit		**28,963**	27,815
Net gain from disposal of/fair value adjustments on investment properties	14	**429**	774
Net loss from disposal/revaluation of properties, plant and equipment	15	**(14)**	(68)
Share of profits less losses after tax of associates and joint ventures	28	**74**	54
Profit before taxation		**29,452**	28,575
Taxation	16	**(4,622)**	(4,286)
Profit from continuing operations		**24,830**	24,289
DISCONTINUED OPERATIONS			
Profit from discontinued operations	40	**31,493**	3,392
Profit for the year		**56,323**	27,681

Consolidated Income Statement

For the year ended 31 December	Notes	2016 HK$'m	(Restated) 2015 HK$'m
Profit attributable to:			
Equity holders of the Company			
– from continuing operations		**24,201**	23,757
– from discontinued operations	40	**31,302**	3,225
		55,503	26,982
Non-controlling interests			
– from continuing operations		**629**	532
– from discontinued operations	40	**191**	167
		820	699
		56,323	27,681
Dividends	17	**19,877**	12,941
		HK$	HK$
Earnings per share for profit attributable to the equity holders of the Company			
Basic and diluted	18		
– profit for the year		**5.2496**	2.5520
– profit from continuing operations		**2.2890**	2.2470

The notes on pages 132 to 282 are an integral part of these financial statements.

Consolidated Statement of Comprehensive Income

For the year ended 31 December	Note	2016 HK$'m	(Restated) 2015 HK$'m
Profit for the year		**56,323**	27,681
Items that will not be reclassified subsequently to income statement:			
Premises:			
Revaluation of premises		**(135)**	3,652
Deferred tax		**311**	(483)
		176	3,169
Items that may be reclassified subsequently to income statement:			
Available-for-sale securities:			
Change in fair value of available-for-sale securities		**(102)**	(866)
Release upon disposal of available-for-sale securities reclassified to income statement		**(1,072)**	(1,474)
Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities reclassified to income statement		**134**	246
Deferred tax		**179**	416
		(861)	(1,678)
Change in fair value of hedging instruments under net investment hedges		**–**	51
Currency translation difference		**(210)**	(677)
Release upon disposal of discontinued operations reclassified to income statement	40	**(370)**	–
		(1,441)	(2,304)
Other comprehensive income for the year, net of tax		**(1,265)**	865
Total comprehensive income for the year		**55,058**	28,546
Total comprehensive income attributable to:			
Equity holders of the Company		**54,427**	27,881
Non-controlling interests		**631**	665
		55,058	28,546

The notes on pages 132 to 282 are an integral part of these financial statements.

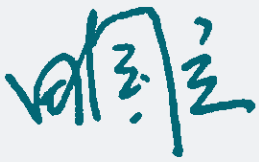
Consolidated Balance Sheet

As at 31 December	Notes	2016 HK$'m	(Restated) 2015 HK$'m
ASSETS			
Cash and balances with banks and other financial institutions	21	**229,073**	234,272
Placements with banks and other financial institutions maturing between one and twelve months	22	**70,392**	66,140
Financial assets at fair value through profit or loss	23	**67,358**	57,777
Derivative financial instruments	24	**64,314**	43,211
Hong Kong SAR Government certificates of indebtedness		**123,390**	101,950
Advances and other accounts	25	**992,137**	928,871
Investment in securities	27	**592,165**	517,938
Interests in associates and joint ventures	28	**319**	376
Investment properties	29	**18,227**	15,262
Properties, plant and equipment	30	**45,732**	50,517
Deferred tax assets	37	**73**	63
Other assets	31	**71,308**	65,965
Assets held for sale	40	**53,293**	300,473
Total assets		**2,327,781**	2,382,815
LIABILITIES			
Hong Kong SAR currency notes in circulation	32	**123,390**	101,950
Deposits and balances from banks and other financial institutions		**192,413**	209,526
Financial liabilities at fair value through profit or loss	33	**13,371**	10,942
Derivative financial instruments	24	**49,289**	40,074
Deposits from customers	34	**1,504,076**	1,415,487
Debt securities and certificates of deposit in issue	35	**1,121**	6,976
Other accounts and provisions	36	**52,397**	34,582
Current tax liabilities		**3,013**	2,784
Deferred tax liabilities	37	**5,590**	6,457
Insurance contract liabilities	38	**86,534**	82,645
Subordinated liabilities	39	**19,014**	19,422
Liabilities associated with assets held for sale	40	**47,013**	251,805
Total liabilities		**2,097,221**	2,182,650

As at 31 December	Notes	**2016 HK$'m**	(Restated) 2015 HK$'m
EQUITY			
Share capital	41	**52,864**	52,864
Reserves		**171,789**	141,886
Capital and reserves attributable to the equity holders of the Company		**224,653**	194,750
Non-controlling interests		**5,907**	5,415
Total equity		**230,560**	200,165
Total liabilities and equity		**2,327,781**	2,382,815

The notes on pages 132 to 282 are an integral part of these financial statements.

Approved by the Board of Directors on 31 March 2017 and signed on behalf of the Board by:



TIAN Guoli
Director

YUE Yi
Director

Consolidated Statement of Changes in Equity

	Attributable to the equity holders of the Company									
		Reserves								
	Share capital HK$'m	Premises revaluation reserve HK$'m	Reserve for fair value changes of available-for-sale securities HK$'m	Regulatory reserve* HK$'m	Translation reserve HK$'m	Merger reserve** HK$'m	Retained earnings HK$'m	Total HK$'m	Non-controlling interests HK$'m	Total equity HK$'m
At 1 January 2015, as previously reported	52,864	37,510	1,930	10,011	778	–	73,621	176,714	4,758	181,472
Effect of merger of entity under common control	–	–	–	–	(526)	1,789	734	1,997	–	1,997
At 1 January 2015, as restated	52,864	37,510	1,930	10,011	252	1,789	74,355	178,711	4,758	183,469
Profit for the year	–	–	–	–	–	–	26,982	26,982	699	27,681
Other comprehensive income:										
Premises	–	3,142	–	–	–	–	–	3,142	27	3,169
Available-for-sale securities	–	–	(1,632)	–	–	–	–	(1,632)	(46)	(1,678)
Change in fair value of hedging instruments under net investment hedges	–	–	–	–	49	–	–	49	2	51
Currency translation difference	–	(9)	(4)	–	(647)	–	–	(660)	(17)	(677)
Total comprehensive income	–	3,133	(1,636)	–	(598)	–	26,982	27,881	665	28,546
Release upon disposal of premises	–	(365)	–	–	–	–	365	–	–	–
Transfer from retained earnings	–	–	–	917	–	–	(917)	–	–	–
Dividends	–	–	–	–	–	–	(11,842)	(11,842)	(253)	(12,095)
Increase in non-controlling interests arising from capital issuance of a subsidiary	–	–	–	–	–	–	–	–	245	245
At 31 December 2015	52,864	40,278	294	10,928	(346)	1,789	88,943	194,750	5,415	200,165
At 1 January 2016, as previously reported	**52,864**	**40,278**	**294**	**10,879**	**191**	**–**	**88,072**	**192,578**	**5,415**	**197,993**
Effect of merger of entity under common control	**–**	**–**	**–**	**49**	**(537)**	**1,789**	**871**	**2,172**	**–**	**2,172**
At 1 January 2016, as restated	**52,864**	**40,278**	**294**	**10,928**	**(346)**	**1,789**	**88,943**	**194,750**	**5,415**	**200,165**
Profit for the year	**–**	**–**	**–**	**–**	**–**	**–**	**55,503**	**55,503**	**820**	**56,323**
Other comprehensive income:										
Premises	**–**	**186**	**–**	**–**	**–**	**–**	**–**	**186**	**(10)**	**176**
Available-for-sale securities	**–**	**–**	**(703)**	**–**	**–**	**–**	**–**	**(703)**	**(158)**	**(861)**
Currency translation difference	**–**	**–**	**(16)**	**–**	**(173)**	**–**	**–**	**(189)**	**(21)**	**(210)**
Release upon disposal of discontinued operations reclassified to income statement	**–**	**–**	**(167)**	**–**	**(203)**	**–**	**–**	**(370)**	**–**	**(370)**
Total comprehensive income	**–**	**186**	**(886)**	**–**	**(376)**	**–**	**55,503**	**54,427**	**631**	**55,058**
Acquisition of entity under common control	**–**	**–**	**–**	**–**	**–**	**(4,076)**	**–**	**(4,076)**	**–**	**(4,076)**
Transfer from retained earnings	**–**	**–**	**–**	**539**	**–**	**2,287**	**(2,826)**	**–**	**–**	**–**
Release upon disposal of discontinued operations	**–**	**(4,856)**	**–**	**(2,240)**	**–**	**–**	**7,096**	**–**	**–**	**–**
Dividends	**–**	**–**	**–**	**–**	**–**	**–**	**(20,448)**	**(20,448)**	**(139)**	**(20,587)**
At 31 December 2016	**52,864**	**35,608**	**(592)**	**9,227**	**(722)**	**–**	**128,268**	**224,653**	**5,907**	**230,560**

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

** Merger reserve was arising on the application of merger accounting method in relation to the combination with entity under common control.

The notes on pages 132 to 282 are an integral part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December	Notes	2016 HK$'m	(Restated) 2015 HK$'m
Cash flows from operating activities			
Operating cash outflow before taxation	42(a)	**(68,686)**	(68,957)
Hong Kong profits tax paid		**(4,497)**	(4,653)
Overseas profits tax paid		**(434)**	(838)
Net cash outflow from operating activities		**(73,617)**	(74,448)
Cash flows from investing activities			
Purchase of properties, plant and equipment		**(1,501)**	(1,242)
Proceeds from disposal of properties, plant and equipment		**2**	468
Purchase of investment properties		**(6)**	(47)
Dividend received from associates and joint ventures	28	**2**	2
Acquisition of entity under common control	57	**(4,076)**	–
Net cash inflow from disposal of discontinued operations	40	**26,992**	–
Net cash inflow/(outflow) from investing activities		**21,413**	(819)
Cash flows from financing activities			
Dividend paid to the equity holders of the Company		**(20,448)**	(11,842)
Dividend paid to non-controlling interests		**(139)**	(253)
Proceeds from non-controlling interests for capital issuance of a subsidiary		**–**	245
Interest paid for subordinated liabilities		**(476)**	(409)
Net cash outflow from financing activities		**(21,063)**	(12,259)
Decrease in cash and cash equivalents		**(73,267)**	(87,526)
Cash and cash equivalents at 1 January		**313,095**	411,862
Effect of exchange rate changes on cash and cash equivalents		**1,132**	(11,241)
Cash and cash equivalents at 31 December	42(b)	**240,960**	313,095

The notes on pages 132 to 282 are an integral part of these financial statements.

Notes to the Financial Statements

1. Principal activities

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

The Company is a limited liability company incorporated and listed in Hong Kong. The address of its registered office is 24/F, Bank of China Tower, 1 Garden Road, Hong Kong.

2. Significant accounting policies

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

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

2.1 Basis of preparation

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

The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale securities, financial assets and financial liabilities (including derivative financial instruments) at fair value through profit or loss, precious metals at fair value, investment properties which are carried at fair value and premises which are carried at fair value or revalued amount less accumulated depreciation and accumulated impairment losses. Disposal group and repossessed assets held for sale are stated at the lower of their carrying amounts and fair values less costs to sell as further explained in Notes 2.2 and 2.24 respectively.

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

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(a) Standards and amendments issued that are already mandatorily effective for accounting periods beginning on 1 January 2016

Standards/ Amendments	Content	Applicable for financial years beginning on/after	Currently relevant to the Group
HKAS 1 (Amendment)	Disclosure Initiative	1 January 2016	Yes
HKAS 16 and HKAS 38 (Amendments)	Clarification of Acceptable Methods of Depreciation and Amortisation	1 January 2016	No
HKAS 16 and HKAS 41 (Amendments)	Agriculture: Bearer Plants	1 January 2016	No
HKAS 27 (2011) (Amendment)	Equity Method in Separate Financial Statements	1 January 2016	Yes
HKAS 28 (2011), HKFRS 10 and HKFRS 12 (Amendments)	Investment Entities: Applying the Consolidation Exception	1 January 2016	No
HKFRS 11 (Amendment)	Accounting for Acquisitions of Interests in Joint Operations	1 January 2016	No
HKFRS 14	Regulatory Deferral Accounts	1 January 2016	No

- HKAS 1 (Amendment), "Disclosure Initiative". The amendments to HKAS 1 are designed to further encourage companies to apply professional judgement in determining what information to disclose in their financial statements. For example, the amendments make clear that materiality applies to the whole of financial statements and that the inclusion of immaterial information can inhibit the usefulness of financial disclosures. Furthermore, the amendments clarify that companies should use professional judgement in determining where and in what order information is presented in the financial disclosures. The adoption of this amendment does not have a material impact on the Group's financial statements.

- HKAS 27 (2011) (Amendment), "Equity Method in Separate Financial Statements". The amendment restores the option to allow an entity to apply the equity method to account for its investments in subsidiaries, joint ventures and associates in its separate financial statements. Entities electing to change to the equity method in its separate financial statements shall have to apply the same accounting for each category of investments so elected and are required to apply this change retrospectively. The adoption of this amendment does not have a material impact on the Group's financial statements.

- "Improvements to HKFRSs" contains numerous amendments to HKFRSs which the HKICPA considers not urgent but necessary. It comprises amendments that result in accounting changes for presentation, recognition or measurement purpose as well as terminology or editorial amendments related to a variety of individual HKFRSs. The adoption of these improvements does not have a material impact on the Group's financial statements.

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards and amendments issued that are not yet mandatorily effective and have not been early adopted by the Group in 2016

Standards/ Amendments	Content	Applicable for financial years beginning on/after	Currently relevant to the Group
HKAS 7 (Amendment)	Statement of Cash Flows: Disclosure Initiative	1 January 2017	Yes
HKAS 12 (Amendment)	Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses	1 January 2017	No
HKAS 28 (2011) and HKFRS 10 (Amendments)	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	To be determined	Yes
HKFRS 2 (Amendment)	Share-Based Payment: Classification and Measurement of Share-Based Payment Transactions	1 January 2018	No
HKFRS 9	Financial Instruments	1 January 2018	Yes
HKFRS 15	Revenue from Contracts with Customers	1 January 2018	Yes
HKFRS 16	Leases	1 January 2019	Yes

Further information about those HKFRSs that are expected to be applicable to the Group is as follows:

- HKAS 7 (Amendment), "Statement of Cash Flows: Disclosure Initiative". The amendments are part of the Disclosure Initiative project and require entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. No comparative information is required for first time application of these amendments. The amendments will result in additional disclosure to be provided in the financial statements.

- HKAS 28 (2011) and HKFRS 10 (Amendments), "Sale or Contribution of Assets between an Investor and its Associate or Joint Venture". The amendments address an acknowledged inconsistency between the requirements in HKFRS 10 and those in HKAS 28 (2011), in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognised when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognised when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary. The amendments are to be applied prospectively, early application is permitted. The application of these amendments will not have a material impact on the Group's financial statements.

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards and amendments issued that are not yet mandatorily effective and have not been early adopted by the Group in 2016 (continued)

- HKFRS 9, "Financial Instruments". The issuance of IFRS 9 "Financial Instruments" completes the International Accounting Standards Board's comprehensive response to the financial crisis. HKFRS 9, the equivalent standard of IFRS 9 under HKFRS, includes a logical model for classification and measurement, a single, forward-looking "expected loss" impairment model and a tighter linkage of risk management to hedge accounting. The changes introduced in HKFRS 9 are highlighted as follows:

(i) Classification and Measurement

Financial assets

Financial assets are required to be classified into one of the following measurement categories: (1) measured subsequently at amortised cost, (2) measured subsequently at fair value through other comprehensive income (all fair value changes other than interest accrual, amortisation and impairment will be recognised in other comprehensive income) or (3) measured subsequently at fair value through profit or loss. Classification is to be made on transition, and subsequently on initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instruments.

A financial instrument is subsequently measured at amortised cost only if it is a debt instrument, and the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and the asset's contractual cash flows characteristics represent only unleveraged payments of principal and interest. A debt instrument is subsequently measured at fair value through other comprehensive income if it is held in a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and the instrument fulfils the contractual cash flows characteristics. All other debt instruments are to be measured at fair value through profit or loss.

Equity instruments are generally measured subsequently at fair value with limited circumstances that cost may be an appropriate estimate of fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition to recognise unrealised and realised fair value gains and losses in other comprehensive income without subsequent reclassification of fair value gains and losses to the income statement even upon disposal. Dividend income is recognised in the income statement when the right to receive payment is established.

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards and amendments issued that are not yet mandatorily effective and have not been early adopted by the Group in 2016 (continued)

(i) Classification and Measurement (continued)

Financial liabilities

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

The accounting for fair value option of financial liabilities were changed to address own credit risk. The amount of change in fair value attributable to changes in the credit risk of the financial liabilities will be presented in other comprehensive income. The remaining amount of the total gain or loss is included in the income statement. If this creates or enlarges an accounting mismatch in profit or loss, then the whole fair value change is presented in the income statement. The determination of whether there will be a mismatch will need to be made at initial recognition of individual liabilities and will not be re-assessed. Amounts presented in other comprehensive income are not subsequently reclassified to the income statement but may be transferred within equity. This removes the volatility in profit or loss that was caused by changes in the credit risk of liabilities elected to be measured at fair value. It also means that gains caused by the deterioration of an entity's own credit risk on such liabilities will no longer be recognised in profit or loss.

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

(ii) Impairment

The standard introduces a new, expected-loss impairment model that will require more timely recognition of expected credit losses. Specifically, it requires entities to account for 12 months expected credit losses from inception when financial instruments are first recognised and to recognise full lifetime expected credit losses on a more timely basis when there have been significant increases in credit risk since initial recognition. The impairment for financial instruments that are subsequently measured at amortised cost, fair value through other comprehensive income (debt instruments), loan commitments and financial guarantees will be governed by this standard.

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards and amendments issued that are not yet mandatorily effective and have not been early adopted by the Group in 2016 (continued)

(iii) Hedge accounting

The requirements related to hedge accounting would better align the accounting treatments with risk management activities and enable entities to better reflect these activities in their financial statements. It relaxes the requirements for assessing hedge effectiveness which more risk management strategies may be eligible for hedge accounting. It also relaxes the rules on using non-derivative financial instruments as hedging instruments and allows greater flexibility on hedged items. Users of the financial statements will be provided with more relevant information about risk management and the effect of hedge accounting on the financial statements.

Early application of HKFRS 9 in its entirety at the same time is permitted. Only the part related to own credit risk can be elected to be early applied in isolation. The Group has already formed a groupwide project team to assess the impact of HKFRS 9, formulate the work plan and implement the standard. Significant works has been done on analysing our financial instruments, building models and designing new workflows. Due to the complication of the project, no quantitative information of the potential effect is concluded yet.

- HKFRS 15, "Revenue from Contracts with Customers". HKFRS 15 applies a single model and specifies the accounting treatment for all revenue arising from contracts with customers. The new standard is based on the core principle that revenue is recognised to reflect the consideration expected to be entitled when control of promised good or service transfers to customer. It is also applicable to the recognition and measurement of gains or losses on the sale of some non-financial assets such as properties or equipment that are not an output of ordinary activities. HKFRS 15 also includes a set of disclosure requirements about revenue from customer contracts. The new standard will replace the separate models for goods, services and construction contracts stipulated in different standards under the current HKFRS. The Group is considering the financial impact of the standard.

- HKFRS 16, "Leases". HKFRS 16 supersedes the existing standard and interpretations related to leases. It applies a single control model to identify leases and distinguish between leases and service contracts. Significant changes to lessee accounting are introduced, with the distinction between operating and finance leases removed and the right-of-use assets and lease liabilities recognised except under short term and low value leases. There are no significant changes to the lessor accounting requirements. The standard is applied retrospectively. Early application is permitted for entities that have also adopted HKFRS 15 "Revenue from Contracts with Customers". The Group is considering the financial impact of the standard and the timing of its application.

2. Significant accounting policies (continued)

2.2 Consolidation

The consolidated financial statements include the financial statements of the Company and all of its subsidiaries for the year ended 31 December.

(1) Subsidiaries

Subsidiaries are entities (including structured entities), directly or indirectly, controlled by the Group. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e. existing rights that give the Group the current ability to direct the relevant activities of the investee). When the Company has, directly or indirectly, less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including: (a) the contractual arrangement with the other vote holders of the investee; (b) rights arising from other contractual arrangements; and (c) the Group's voting rights and potential voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment in that former subsidiary retained; reclassifies the amounts previously recognised in other comprehensive income to the income statement or retained earnings, as appropriate, on the same basis as directly disposed of the related assets or liabilities; recognises any resulting differences as gain or loss in income statement.

If the Group is committed by the Board to a sale plan involving loss of control of a subsidiary (a disposal group) that is unlikely to be withdrawn or changed significantly, the Group shall classify all the assets and liabilities of that subsidiary as held for sale only when the following criteria are met on or before the end of the reporting period: (i) the carrying amount will be recovered principally through a sale transaction rather than through continuing use; (ii) the subsidiary is available for immediate sale in its present condition subject only to terms that are usual and customary for the sale of its kind and its sale must be highly probable, including a high probability of shareholders' approval, if needed; (iii) an active programme to locate a buyer at a reasonable price has been initiated and to complete the sale within one year, regardless of whether the Group will or will not retain a non-controlling interest after the sale. Disposal group (other than investment properties and financial instruments) is initially recognised and subsequently remeasured at the lower of its carrying amount and fair value less costs to sell. Property, plant and equipment classified as held for sale are not depreciated.

(i) Business combinations not under common control

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

2. Significant accounting policies (continued)

2.2 Consolidation (continued)

(1) Subsidiaries (continued)

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

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

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

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

(ii) Business combinations under common control

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

2. Significant accounting policies (continued)

2.2 Consolidation (continued)

(1) Subsidiaries (continued)

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

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

(2) Transactions with non-controlling interests

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

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

(3) Associates and joint ventures

Associate is the entity over which the Group has significant influence but not control or joint control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

Investments in associates and joint ventures are accounted for using the equity method of accounting and are initially recognised at cost, unless it is classified as held for sale (or included in a disposal group that is classified as held for sale). The Group's investments in associates and joint ventures include goodwill, net of accumulated impairment loss and any related accumulated foreign currency translation difference.

2. Significant accounting policies (continued)

2.2 Consolidation (continued)

(3) Associates and joint ventures (continued)

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

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

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

2.3 Segmental reporting

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

2.4 Foreign currency translation

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

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

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

2. Significant accounting policies (continued)

2.4 Foreign currency translation (continued)

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

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

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

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

2.5 Derivative financial instruments and hedge accounting

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

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

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

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

(a) hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge); or

(b) hedges of a particular risk associated with a highly probable future cash flow attributable to a recognised asset or liability, or a highly probable forecasted transaction (cash flow hedge).

2. Significant accounting policies (continued)

2.5 Derivative financial instruments and hedge accounting (continued)

Hedge accounting is used for derivatives designated in this way.

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

(a) Fair value hedge

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

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

If the hedge relationship no longer meets the criteria for hedge accounting or is terminated for reasons other than derecognition, e.g. due to repayment of the hedged item, the unamortised carrying value adjustment (the difference between the carrying value of the hedged item at the time of termination and the value at which it would have been carried had the hedge never existed) to the hedged item is amortised to the income statement over the remaining life of the hedged item by the effective interest method. If the hedged item is derecognised, the unamortised carrying value adjustment is recognised immediately in the income statement.

(b) Cash flow hedge

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

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

2. Significant accounting policies (continued)

2.5 Derivative financial instruments and hedge accounting (continued)

(c) Net investment hedge

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

2.6 Offsetting financial instruments

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

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

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

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

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

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

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

2. Significant accounting policies (continued)

2.8 Financial assets

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

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

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

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

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

- eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mismatch") that would otherwise arise from measuring the financial assets or recognising the gains and losses on them on different bases; or

- applies to a group of financial assets, financial liabilities or both that is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the key management; or

- relates to financial assets containing one or more embedded derivative that significantly modifies the cash flow resulting from those financial assets.

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

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

2. Significant accounting policies (continued)

2.8 Financial assets (continued)

(2) Loans and receivables

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

(3) Held-to-maturity

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

(4) Available-for-sale

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

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

For a financial asset reclassified from the available-for-sale category, the fair value carrying amount at the date of reclassification becomes its new amortised cost and any previous gain or loss on that asset that has been recognised in other comprehensive income is amortised to profit or loss over the remaining life of the investment using the effective interest method. Any difference between the new amortised cost and the maturity amount is also amortised over the remaining life of the financial asset using the effective interest method. If the financial asset is subsequently determined to be impaired, the amount recorded in other comprehensive income is reclassified to profit or loss immediately.

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

2. Significant accounting policies (continued)

2.9 Financial liabilities

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

(1) Trading liabilities

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

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

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

- eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mismatch") that would otherwise arise from measuring the financial liabilities or recognising the gains and losses on them on different bases; or

- applies to a group of financial assets, financial liabilities or both that is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the key management; or

- relates to financial liabilities containing one or more embedded derivative that significantly modifies the cash flow resulting from those financial liabilities.

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

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

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

2. Significant accounting policies (continued)

2.10 Financial guarantee contracts

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

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

2.11 Recognition and derecognition of financial instruments

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

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

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

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

2. Significant accounting policies (continued)

2.12 Fair value measurement

The Group measures its premises and investment properties, precious metals and certain financial instruments at fair value at the end of each reporting period. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants in its principal market or the most advantageous market accessible by the Group at the measurement date.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The Group uses the price within the bid-offer spread that is most representative of the fair value of financial instruments, where appropriate, includes using on the residual of the net offsetting risk position of portfolios of financial assets and financial liabilities in cases the Group manages such groups of financial assets and liabilities according to their net market risk exposures. Despite the Group measures the fair value of these groups of financial instruments on a net basis, the underlying financial assets and financial liabilities are separately presented in the financial statements unless the offsetting criteria stated in Note 2.6 are fulfilled.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

If the market for assets or liabilities is not active, the Group uses valuation techniques, including the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants, that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

2.13 Precious metals

Precious metals comprise gold, silver and other precious metals. Precious metals are initially recognised and subsequently re-measured at fair value. Mark-to-market gains or losses on precious metals are included in net trading gain/loss.

2.14 Impairment of financial assets

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

(i) significant financial difficulty of the issuer or obligor;

(ii) a breach of contract, such as a default or delinquency in interest or principal payment;

2. Significant accounting policies (continued)

2.14 Impairment of financial assets (continued)

(iii) the Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;

(iv) it becoming probable that the borrower will enter into bankruptcy or other financial reorganisation;

(v) the disappearance of an active market or downgrading below investment grade level for that financial asset because of financial difficulties; or

(vi) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

- adverse changes in the payment status of borrowers in the group; or

- national or local economic conditions that correlate with defaults on the assets in the group.

(1) Assets carried at amortised cost

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

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

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

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

2. Significant accounting policies (continued)

2.14 Impairment of financial assets (continued)

(1) Assets carried at amortised cost (continued)

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

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

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

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

(2) Assets classified as available-for-sale

If evidence of impairment exists for available-for-sale financial assets, the accumulated losses, measured as the difference between the acquisition cost or amortised cost and the current fair value, less any impairment loss on that financial asset previously recognised in the income statement, is removed from equity and recognised in the income statement. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss to the extent of its decrease is reversed through the income statement. With respect to equity instruments, further fair value changes are recognised in the reserve for fair value change of available-for-sale securities through other comprehensive income, impairment losses are not reversed through the income statement.

2.15 Impairment of investment in subsidiaries, associates, joint ventures and non-financial assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Potential indications of impairment may include significant adverse changes in the technological, market, economic or legal environment in which the assets operate or whether there has been a significant or prolonged decline in value below their cost. "Significant" is evaluated against the original cost of the investment and "prolonged" against the period in which the fair value has been below its original cost.

2. Significant accounting policies (continued)

2.15 Impairment of investment in subsidiaries, associates, joint ventures and non-financial assets (continued)

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash generating units). Assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

In the Company's balance sheet, impairment testing of the investment in a subsidiary, associate or joint venture is also required upon receiving dividend from that entity if the dividend exceeds the total comprehensive income of that entity concerned in the period the dividend is declared or if the carrying amount of that entity in the Company's balance sheet exceeds the carrying amount of that entity's net assets including goodwill in its consolidated balance sheet.

2.16 Investment properties

Properties that are held for long-term rental yields or for capital appreciation or both, and that are not occupied by the companies in the Group, are classified as investment properties. Properties leased out within Group companies are classified as investment properties in individual companies' financial statements and as premises in consolidated financial statements. Land held under operating lease is classified and accounted for as investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it is a finance lease.

Investment properties are recognised initially at cost, including related transaction costs. After initial recognition, investment properties are measured at fair value.

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The item is stated at cost less impairment and is included in the carrying amount of investment properties. Once the item begins to generate economic benefits, it is then measured at fair value. All other repairs and maintenance costs are expensed in the income statement during the financial period in which they are incurred.

Any changes in fair value are recognised directly in the income statement.

If an investment property becomes owner-occupied, it is reclassified as premises, and its fair value at the date of reclassification becomes its cost for accounting purposes. If an item of premises becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of this item at the date of transfer is recognised in other comprehensive income as a revaluation of premises under HKAS 16 "Property, Plant and Equipment". However, if a fair value gain reverses a previous revaluation loss or impairment loss, the gain is recognised in the income statement up to the amount previously debited.

2.17 Properties, plant and equipment

Properties are mainly branches and office premises. Premises are stated at fair value based on periodic, at least annually, valuations by external independent valuers less any subsequent accumulated depreciation and impairment losses. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. In the intervening periods, the directors review the carrying amount of premises, by reference to the open market value of similar properties, and adjustments are made when there has been a material change.

2. Significant accounting policies (continued)

2.17 Properties, plant and equipment (continued)

Increases in the carrying amount arising on revaluation of premises are credited to the premises revaluation reserve through other comprehensive income. Decreases that offset previous increases of the same individual asset are charged against premises revaluation reserve through other comprehensive income; all other decreases are expensed in the income statement. Any subsequent increases are credited to the income statement up to the amount previously debited, and then to the premises revaluation reserve. Upon disposal of premises, the relevant portion of the premises revaluation reserve realised in respect of previous valuations is released and transferred from the premises revaluation reserve to retained earnings.

All plant and equipment are stated at historical cost less accumulated depreciation and impairment losses. Historical cost includes expenditures that are directly attributable to the acquisition and installation of the items.

Subsequent costs are included in an asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The item is stated at cost less impairment until it begins to generate economic benefits, then the item is subsequently measured according to the measurement basis of its respective assets class. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred.

Depreciation is calculated on the straight-line method to write down the cost or revalued amount of such assets over their estimated useful lives as follows:

- Properties — Over the life of government land leases
- Plant and equipment — 3 to 15 years

The useful lives of assets are reviewed, and adjusted if appropriate, as at the end of each reporting period.

At the end of each reporting period, both internal and external sources of information are considered to determine whether there is any indication that properties, plant and equipment, are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such an impairment loss is recognised in the income statement except where the asset is carried at valuation and the impairment loss does not exceed the revaluation surplus for that same asset, in which case it is treated as a revaluation decrease. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. Impairment loss is reversed through the premises revaluation reserve or the income statement as appropriate.

Gains or losses on disposals are determined as the difference between the net disposal proceeds and the carrying amount, relevant taxes and expenses. These are recognised in the income statement on the date of disposal. Any related revaluation surplus is transferred from the revaluation reserve to retained earnings and is not reclassified to the income statement.

2. Significant accounting policies (continued)

2.18 Leases

(1) Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. The total payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease. Contingent rental payable is recognised as expense in the accounting period in which they are incurred.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place. Rental income from operating leases is recognised on a straight-line basis over the lease term.

(2) Finance leases

Leases of assets where lessee have obtained substantially all the risks and rewards of ownership are classified as finance leases. Government land leases in Hong Kong are classified as finance leases as the present value of the minimum lease payments (i.e. transaction price) of the land amounted to substantially all of the fair value of the land as if it were freehold.

Finance leases are capitalised at the lease's commencement at the lower of the fair value of the leased asset and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in other liabilities. Investment properties acquired under finance leases are carried at their fair value.

When assets are leased out under a finance lease, the present value of the lease payments is recognised as a receivable. Lease income is recognised over the term of the lease using net investment method, which reflects a constant periodic rate of return.

2.19 Insurance and investment contracts

(1) Insurance and investment contract classification, recognition and measurement

The Group follows the local regulatory requirements to measure the liabilities of its insurance contracts and investment contracts with discretionary participation feature ("DPF").

The Group issues insurance contracts, which are contracts that transfer significant insurance risk and may also transfer financial risk. As a general guideline, the Group defines significant insurance risk as the possibility of having to pay benefits on the occurrence of an insured event that are at least 10% more than the benefit payable if the insured event did not occur. The Group issues long term business insurance contracts, which insure events covered by life policies (for example death, survival, or total permanent disability) over a long duration. A liability for contractual benefits that are expected to be incurred in the future is recorded when premiums are recognised. In addition, the Group issues investment contracts. Investment contracts transfer financial risk with no significant insurance risk. They contain a DPF which entitles the holders to receive additional benefits (supplement to guaranteed benefits) that are likely to be significant based on the performance and return of a specified pool or type of contracts.

2. Significant accounting policies (continued)

2.19 Insurance and investment contracts (continued)

(1) Insurance and investment contract classification, recognition and measurement (continued)

Linked long term insurance contracts with embedded derivatives (which are closely related to the host insurance contracts) linking payments on the contract to units of the investment funds which the Group has invested with the consideration received from the contract holders, the liability is adjusted for all changes in the fair value of the underlying assets, and includes a liability for contractual benefits that are expected to be incurred in the future which is recorded when the premiums are recognised.

Retirement scheme management category I contracts are classified as investment contracts. They also include an investment guarantee element in the determination of the credit rate to policyholders' accounts. The liability for these contracts is determined using a retrospective calculation method which represents an account balance based on the premiums received to date plus interest or bonus credited to the policyholders less policy charges.

Retirement scheme management category III insurance contracts, as defined in the Insurance Companies Ordinance, insure events associated with the cessation of employment due to death. A liability for contractual benefits that are expected to be incurred in the future is recorded when premiums are recognised. The portion of the premium received on in-force contracts that relates to unexpired risks at the end of the reporting period is reported as the unearned premium liability, which is included in insurance liabilities.

Premiums are recognised as revenue when they become payable by the contract holders before the deduction of commissions and are gross of any taxes or duties levied on the premium. Benefits and claims are recorded as an expense when they are incurred.

The Group does not separately measure embedded derivatives that meet the definition of an insurance contract or options to surrender insurance contracts for a fixed amount (or an amount based on a fixed amount and an interest rate).

Contracts entered into by the Group with reinsurers under which the Group is compensated for losses on one or more contracts issued by the Group and that meet the classification requirement for insurance contracts as noted above are classified as reinsurance contracts held.

The benefits to which the Group is entitled under its reinsurance contracts held are recognised as reinsurance assets. These reinsurance assets consist of short-term amounts due from reinsurers as well as longer term receivables that are dependent on the expected claims and benefits arising from the related reinsured insurance contracts. Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the underlying insurance contracts and in accordance with the terms of each reinsurance contract. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised as an expense when due.

2. Significant accounting policies (continued)

2.19 Insurance and investment contracts (continued)

(2) Liability adequacy test

At the end of each reporting period, liability adequacy tests are performed to ensure the adequacy of the insurance contract liabilities. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from the assets backing such liabilities, are used. Any deficiency is immediately charged to the consolidated income statement, with a provision established for losses arising from the liability adequacy tests.

2.20 Cash and cash equivalents

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise balances with original maturity less than three months from the date of acquisition, including cash, balances with banks and other financial institutions, short-term bills and notes classified as investment securities and certificates of deposit.

2.21 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

2.22 Employee benefits

(1) Retirement benefit costs

The Group contributes to defined contribution retirement schemes under either recognised ORSO schemes or MPF schemes that are available to the Group's employees. Contributions to the schemes by the Group and employees are calculated as a percentage of employees' basic salaries for the ORSO schemes and in accordance with the MPF rules for MPF schemes. The retirement benefit scheme costs are charged to the income statement as incurred and represent contributions payable by the Group to the schemes. Contributions made by the Group that are forfeited by those employees who leave the ORSO scheme prior to the full vesting of their entitlement to the contributions are used by the Group to reduce the existing level of contributions or to meet its expenses under the trust deed of the ORSO schemes.

The assets of the schemes are held in independently-administered funds separate from those of the Group.

(2) Leave entitlements

Employee entitlements to annual leave and sick leave are recognised when they accrue to employees. A provision is made for the estimated liability for unused annual leave and the amount of sick leave expected to be paid as a result of services rendered by employees up to the end of the reporting period.

Compensated absences other than sick leave and special approved annual leaves are non-accumulating; they lapse if the current period's entitlement is not used in full. Except for unexpired annual leaves, they do not entitle employees to a cash payment for unused entitlement on leaving the Group.

2. Significant accounting policies (continued)

2.22 Employee benefits (continued)

(3) Bonus plans

The expected cost of bonus payments are recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made. Liabilities for bonus plans that are expected to be settled longer than twelve months will be discounted if the amounts are significant.

2.23 Current and deferred income taxes

Tax expenses for the period comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised directly in other comprehensive income. In this case, the tax is also recognised in other comprehensive income.

Income tax payable on profits, based on the applicable tax law enacted or substantially enacted at the end of the reporting period in each jurisdiction where the Company and the subsidiaries, associates and joint ventures operate and generate taxable income, is recognised as a current income tax expense in the period in which profits arise.

Deferred income tax is provided in full, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from asset impairment provisions, depreciation of premises and equipment, and revaluation of certain assets including available-for-sale securities and premises. However, the deferred income tax is not recognised if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Deferred income tax liabilities are provided in full on all taxable temporary differences. Deferred income tax assets are recognised on deductible temporary differences, the carry forward of any unused tax credits and unused tax losses to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences, the carry forward of unused tax credits and unused tax losses can be utilised.

Deferred income tax is charged or credited in the income statement except for deferred income tax relating to fair value re-measurement of available-for-sale securities and revaluation of premises which are charged or credited to other comprehensive income, in which case the deferred income tax is also credited or charged to other comprehensive income and is subsequently recognised in the income statement together with the realisation of the deferred gain and loss.

Deferred tax liability or deferred tax asset arising from investment property is determined based on the presumption that the revaluation amount of such investment property will be recovered through sale with the relevant tax rate applied.

2. Significant accounting policies (continued)

2.24 Repossessed assets

Repossessed assets are initially recognised at the lower of their fair value less costs to sell and the amortised cost of the related outstanding loans on the date of repossession, and the related loans and advances together with the related impairment allowances are derecognised from the balance sheet. Subsequently, repossessed assets are measured at the lower of their cost and fair values less costs to sell and are reported as "non-current assets held for sale" included in "Other assets".

2.25 Fiduciary activities

The Group commonly acts as a trustee, or in other fiduciary capacities, that result in its holding or managing assets on behalf of individuals, trusts and other institutions. These assets and any gains or losses arising thereon are excluded from these financial statements, as they are not assets of the Group.

2.26 Contingent liabilities and contingent assets

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that an outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised as a provision but is disclosed in the notes to the financial statements. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group.

Contingent assets are not recognised but are disclosed in the notes to the financial statements when an inflow of economic benefits is probable. When the inflow is virtually certain, it will be recognised as an asset.

2.27 Related parties

For the purposes of these financial statements, a party is considered to be related to the Group if that party (i) controls, jointly controls or has significant influence over the Group; (ii) is a member of the same financial reporting group, such as parents, subsidiaries and fellow subsidiaries; (iii) is an associate or a joint venture of the Group or parent reporting group; (iv) is a key management personnel of the Group or parents; (v) is subject to common control with the Group; (vi) is an entity in which a person identified in (iv) controls; and (vii) provides key management personnel services to the Group or its parent. Related parties may be individuals or entities.

3. Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the carrying amounts of assets and liabilities within the next reporting period. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Areas susceptible to changes in essential estimates and judgements, which affect the carrying amount of assets and liabilities, are set out below. The effect of changes to either the key assumptions or other estimation uncertainties will be presented below if it is practicable to determine. It is possible that actual results may require material adjustments to the estimates referred to below.

3.1 Impairment allowances on loans and advances

The Group reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and advances before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group (e.g. payment delinquency or default), or economic conditions that correlate with defaults on assets in the group. The Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when estimating expected future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly.

Carrying amounts of loans and advances as at 31 December 2016 are shown in Note 25.

3.2 Impairment of held-to-maturity and available-for-sale securities

The Group reviews its held-to-maturity and available-for-sale investment portfolios to assess impairment at least on a quarterly basis. In determining whether any of these investments is impaired, risk characteristics and performance such as external credit rating and market price, will be assessed. The Group makes estimates on the default rate and loss severity of each investment with reference to market performance of the portfolios, current payment status of the issuers or performance of the underlying assets, or economic conditions that correlate with defaults on the collateralised assets. The methodology and assumptions used for impairment assessments are reviewed regularly.

Carrying amounts of investment in securities as at 31 December 2016 are shown in Note 27.

3. Critical accounting estimates and judgements in applying accounting policies (continued)

3.3 Fair values of derivative financial instruments

The fair values of derivative financial instruments that are not quoted in active markets are determined by using valuation techniques. Valuation techniques used include discounted cash flows analysis and models with built-in functions available in externally acquired financial analysis or risk management systems widely used by the industry such as option pricing models. To the extent practical, the models use observable data. In addition, valuation adjustments may be adopted if factors such as credit risk are not considered in the valuation models. Management judgement and estimates are required for the selection of appropriate valuation parameters, assumptions and modeling techniques. Further details will be discussed in Note 5.

Carrying amounts of derivative financial instruments as at 31 December 2016 are shown in Note 24.

3.4 Held-to-maturity securities

The Group follows the guidance of HKAS 39 in classifying certain non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity securities. This classification requires significant management judgement to evaluate the Group's intention and ability to hold such investments to maturity. If the Group fails to hold these investments to maturity other than for specific circumstances defined in HKAS 39, such as selling an insignificant amount, selling close to maturity or due to significant credit deterioration of such investments, it will be required to reclassify the entire portfolio of financial assets as available-for-sale securities. The investments would then be measured at fair value and not amortised cost.

Carrying amounts of held-to-maturity securities as at 31 December 2016 are shown in Note 27.

3.5 Estimate of future benefit payments and premiums arising from long term insurance contracts

In determining the Group's long term business fund liabilities (a component of insurance contract liabilities), the Group follows the Insurance Companies (Determination of Long Term Liabilities) Regulation under the Insurance Companies Ordinance and makes prudent assumptions which include appropriate margins for adverse deviation of the relevant factors. Estimates are made as to the expected number of deaths for each of the years in which the Group is exposed to risk. The Group bases these estimates on Hong Kong Assured Lives Mortality Table HKA01 that reflects recent historical mortality experience, adjusted where appropriate to reflect the Group's own experience. For contracts that insure the risk of longevity, appropriate prudent allowances are made for expected mortality improvements. The estimated number of deaths determines the value of the benefit payments and the value of the valuation premiums. The main source of uncertainty is that epidemics such as AIDS, SARS, avian flu and wide-ranging lifestyle changes, such as in eating, smoking and exercise habits, could result in future mortality being significantly worse than in the past for the age groups in which the Group has significant exposure to mortality risk. However, continuing improvements in medical care and social conditions could result in improvements in longevity in excess of those allowed for in the estimates used to determine the liability for contracts where the Group is exposed to longevity risk.

3. Critical accounting estimates and judgements in applying accounting policies (continued)

3.5 Estimate of future benefit payments and premiums arising from long term insurance contracts (continued)

Were the number of deaths in future years to differ by 10% (2015: 10%) from the Management's estimate, the long term business fund liability would increase by approximately HK$131 million (2015: approximately HK$87 million), which accounts for 0.22% (2015: 0.14%) of the liability. In this case, it is assumed there is no relief arising from reinsurance contracts held.

For linked long term insurance contracts with a life cover component, it is assumed that the Group will be able to increase mortality risk charges in future years in line with emerging mortality experience.

Estimates are also made as to future investment income arising from the assets backing long term insurance contracts. These estimates are based on current market returns as well as expectations about future economic and financial developments. Were the average future investment returns to decrease by 50 basis points (2015: 50 basis points) from the Management's estimates, the long term business fund liability would increase by approximately HK$1,225 million (2015: approximately HK$1,088 million). In this case, it is assumed there is no relief arising from reinsurance contracts held.

The Group has also assessed whether a provision for expense is necessary in accordance with the Insurance Companies Ordinance. A provision for expense is the amount required to meet the total net cost that would likely be incurred in fulfilling contracts if the Group were to cease to transact new business 12 months after the valuation date. As of 31 December 2016, nil of provision for maintenance expenses was provided (2015: Nil).

A resilience reserve was set up and included in long term business fund liabilities in accordance with the Insurance Companies (Determination of Long Term Liabilities) Regulation to provide a prudent provision against the effects of possible future changes to the value of the assets to meet the liabilities. The resilience reserve was set up based on the appointed actuary's advice of a 30 basis points (2015: 30 basis points) change in market yield of the underlying assets and valuation interest rates. The amount of resilience reserve set up depends on the degree of change in interest rate assumed.

3.6 Deferred tax assets

Deferred tax assets on unused tax losses are recognised to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits.

Deferred tax assets on unused tax credits are recognised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the estimation of available tax credits and the possibility to recover such deferred tax assets recognised.

4. Financial risk management

The Group is exposed to financial risks as a result of engaging in a variety of business activities. The principal financial risks are credit risk, market risk (including currency risk and interest rate risk) and liquidity risk. This note summarises the Group's exposures to these risks, as well as its objectives, risk management governance structure, policies and processes for managing and the methods used to measure these risks.

Financial risk management framework

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

The Board of Directors, representing the interests of shareholders, is the highest decision-making authority of the Group and has the ultimate responsibility for risk management. The Board, with the assistance of its committees, has the primary responsibility for the formulation of risk management strategies and ensuring that the Group has an effective risk management system to implement these strategies.

The RC, a standing committee established by the Board of Directors, is responsible for overseeing the Group's various types of risks, approving Level I risk management policies and monitoring their implementation, reviewing significant or high risk exposures or transactions and exercising its power of veto if it considers that any transaction should not proceed. The Audit Committee assists the Board in fulfilling its role in overseeing the internal control system.

The Chief Executive ("CE") is responsible for managing the Group's various types of risks, and material risk exposures or transactions within his authority delegated by the Board of Directors. The Deputy Chief Executives ("DCEs") assist the CE in fulfilling his responsibilities on the day-to-day management of various types of risk, and are responsible for approving material risk exposures or transactions within their authorities delegated by the CE. The Chief Risk Officer ("CRO") assists the CE in fulfilling his responsibilities for the day-to-day management of risks. The CRO is responsible for initiating new risk management strategies, projects and measures in response to regulatory changes that will enable the Group to better monitor and manage new risk issues or areas that may arise from time to time from new businesses, products and changes in the operating environment. The CRO is also responsible for reviewing material risk exposures or transactions within his delegated authority. In accordance with the principle of setting the hierarchy of risk management policies approved by the Board, Senior Management are also responsible for approving the detailed risk management policies of their responsible areas.

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

The Group's principal banking subsidiaries are subject to risk management policies that are consistent with those of the Group. Moreover, the Group's non-banking subsidiaries, such as BOC Life, are subject to the Group's risk management requirements. These subsidiaries are required to formulate their respective risk management policies based on the characteristics of their own industries, perform daily risk management responsibilities and report to BOCHK on a regular basis. Risk management units of BOCHK monitor the risk management status of these subsidiaries.

4. Financial risk management (continued)

Financial risk management framework (continued)

The Group has put in place appropriate internal control systems, including establishment of an organisation structure that sets clear lines of authority and responsibility for monitoring compliance with policies, procedures and limits. Proper reporting lines also provide sufficient independence of the control functions from the business areas, as well as adequate segregation of duties throughout the organisation which helps to promote an appropriate internal control environment.

Product development and risk monitoring

To ensure the effectiveness of risk assessment and monitoring, the Group has a comprehensive product development and risk monitoring system where roles and responsibilities of all related units are clearly defined and proper due diligence processes on product development are in place.

In accordance with the strategic objectives set by the Board and the Management, respective product management units are responsible for formulating business and product development plans, and proceeding to specific product development activities. The department of strategic development shall ensure the plans are aligned with the Group's overall strategies. Departments that are responsible for risk management, legal, compliance and finance, etc. are accountable for risk assessment and review.

Apart from product development, respective product management units shall work closely with relevant risk evaluating departments to identify and assess the risks of new products. Risk evaluating departments shall conduct independent review on the risk assessment results and the corresponding risk management measures. Products can only be launched upon completion of the product due diligence process to the satisfaction of all risk evaluating departments.

A prudent approach is adopted in offering treasury products to our clients. All new treasury products require approval from a special committee before launching.

4.1 Credit risk

Credit risk is the risk of loss that a customer or counterparty is unable to or unwilling to meet its contractual obligations. Credit risk exists in the trading book and banking book, as well as from on- and off-balance sheet transactions of the Group. It arises principally from lending, trade finance and treasury businesses. The Group's exposures set out in Note 4.1 below exclude assets held for sale.

Credit risk management framework

The Group has formulated a comprehensive set of credit risk management policies and procedures, and appropriate credit risk limits to manage and control credit risk that may arise. These policies, procedures and credit risk limits are regularly reviewed and updated to cope with changes in market conditions and business strategies.

The Group's organisation structure establishes a clear set of authority and responsibility for monitoring compliance with policies, procedures and limits.

4. Financial risk management (continued)

4.1 Credit risk (continued)

Credit risk management framework (continued)

The Chief Credit Officer, who reports directly to the CRO, takes charge of credit risk management and is also responsible for the control of credit risk exposures of subsidiaries in line with the credit risk management principles and requirements set by the Group. Various units of the Group have their respective credit risk management responsibilities. Business units act as the first line of defence. The Risk Management Department ("RMD"), which is independent from the business units, is responsible for the day-to-day management of credit risks and has the primary responsibility for providing an independent due diligence through identifying, measuring, monitoring and controlling credit risk to ensure an effective checks and balances, as well as drafting, reviewing and updating credit risk management policies and procedures. It is also responsible for the design, development and maintenance of the Group's internal rating system and ensures the system complies with the relevant regulatory requirements.

In accordance with Group's operating principle, the Group's principal banking subsidiaries have to formulate their own credit risk policies that are consistent with those of the Group's core principles. These subsidiaries are required to submit their risk management reports to the Group's Management on a regular basis.

The Board of Directors delegates credit approval authority to the CE. The CE can further delegate to the subordinates within his limit authorised by the Board of Directors. The Group sets the limits of credit approval authority according to the credit business nature, rating, the level of transaction risk, and the extent of the credit exposure.

Credit risk measurement and control

In view of the rapidly changing market conditions, the Group has been continuously revisiting its credit strategies and conducting rigorous reviews on the concerned portfolios.

Advances

Different credit approval and control procedures are adopted according to the level of risk associated with the customer, counterparty or transaction. The Credit Risk Assessment Committee, comprising experts from credit and other functions, is responsible for making an independent assessment of material credit applications which require the approval of Deputy Chief Executives ("DCE") or above. Credit applications for non-retail exposures are independently reviewed and objectively assessed by risk management units. Obligor ratings (in terms of probability of default) and facility ratings (in terms of loss given default) are assigned to these portfolios to support credit approval. Retail internal rating systems are deployed in the risk assessment of retail credit transactions, including small business retail exposures, residential mortgage loans, personal loans and credit cards. Loan grades, obligor and facility ratings as well as loss estimates (if applicable) are used to support credit approval.

The Group also uses loan grades, obligor ratings and loss estimates (if applicable) to support credit monitoring, reporting and analysis of credit risk information. For non-retail exposures, more frequent rating review and closer monitoring are required for higher-risk customers. For retail exposures, monthly updated internal ratings and loss estimates are used for credit monitoring on a portfolio basis. More comprehensive review is required for obligors being identified under high-risk pools.

4. Financial risk management (continued)

4.1 Credit risk (continued)

Credit risk measurement and control (continued)

Advances (continued)

The Group employs an internal master rating scale that can be mapped to Standard & Poor's external credit ratings. The structure of internal master rating scale is in compliance with the requirement of the Banking (Capital) Rules under the Hong Kong Banking Ordinance.

RMD provides regular credit management information reports and ad hoc reports to the MC, RC and Board of Directors to facilitate their continuous monitoring of credit risk.

In addition, the Group identifies credit concentration risk by industry, geography, customer and counterparty. The Group monitors changes to counterparty credit risk, quality of the credit portfolio and credit risk concentrations, and reports regularly to the Group's Management.

The Group adopts loan grading criteria which divides credit assets into five categories with reference to the HKMA's guidelines, as below:

"Pass" represents loans where the borrower is current in meeting its repayment obligations and full repayment of interest and principal is not in doubt.

"Special Mention" represents loans where the borrower is experiencing difficulties which may threaten the Group's position. Ultimate loss is not expected at this stage but could occur if adverse conditions persist.

"Substandard" represents loans where the borrower displays a definable weakness that is likely to jeopardise repayment.

"Doubtful" represents loans where collection in full is improbable and the Group expects to sustain a loss of principal and/or interest, taking into account the net realisable value of the collateral.

"Loss" represents loans which are considered uncollectible after all collection options (such as the realisation of collateral or the institution of legal proceedings) have been exhausted.

4. Financial risk management (continued)

4.1 Credit risk (continued)

Credit risk measurement and control (continued)

Debt securities and derivatives

For investments in debt securities and securitisation assets, the obligor ratings or external credit ratings, assessment of the underlying assets and credit limits setting on customer/security issuer basis are used for managing credit risk associated with the investment. For derivatives, the Group sets customer limits to manage the credit risk involved and follows the same approval and control processes as applied for advances. On-going monitoring and stop-loss procedures are established.

The methodology and assumptions used for impairment assessments are reviewed regularly. In evaluating impairment of asset backed securities ("ABS") and mortgage backed securities ("MBS"), the Group continued to use a significant decline in market price and credit deterioration of the underlying assets to be the key indicators of impairment. The Group also considered other objective evidence of impairment, taking into account the impact of liquidity on market prices and the movement in loss coverage ratios of individual ABS and MBS held by the Group.

Settlement risk arises mainly from foreign exchange transactions with counterparties and also from derivatives transactions in any situation where a payment in cash, securities or equities is made in the expectation of a corresponding receipt in cash, securities or equities. Daily settlement limits are established for each counterparty or customer to cover all settlement risk arising from the Group's market transactions on any single day.

Collateral held as security and other credit enhancements

The valuation and management of collateral have been documented in the credit risk management policies and procedures which cover acceptance criteria, validity of collateral, loan-to-value ratio, haircut ratio, valuation and insurance, etc. The collateral is revalued on a regular basis, though the frequency and the method used varies with the type of collateral involved and the nature and the risk of the underlying credit. The Group has established a mechanism to update the value of its main type of collateral, real estate properties, with the use of public indices on a portfolio basis. Collateral is insured with the Group as the beneficiary. In the personal sector, the main types of collateral are real estate properties, cash deposits and securities. In the commercial and industrial sector, the main types of collateral are real estate properties, securities, receivables, cash deposits and machinery.

For loans guaranteed by a third party, the Group will assess the guarantor's financial condition, credit history and ability to meet obligations.

As at 31 December 2016, the fair value of collateral held by the Group that was permitted to sell or re-pledge in the absence of default by the borrower amounted to HK$7,013 million (2015: HK$1,018 million). The Group had not sold or re-pledged such collateral (2015: Nil). These transactions are conducted under terms that are usual and customary to reverse repurchase and securities borrowing agreements.

4. Financial risk management (continued)

4.1 Credit risk (continued)

(A) Credit exposures

The maximum credit exposure is the worst case scenario of exposure to the Group without taking into account any collateral held or other credit enhancements. For on-balance sheet assets, the maximum exposure to credit risk equals their carrying amount. For letters of guarantee issued, the maximum exposure to credit risk is the maximum amount that the Group could be required to pay if the guarantees are called upon. For loan commitment and other credit related liabilities, the maximum exposure to credit risk is the full amount of the committed facilities.

The nature of the collateral held and other credit enhancements and their financial effect to the different classes of the Group's financial assets are as follows.

Balances and placements with banks and other financial institutions

These exposures are generally considered to be low risk due to the nature of the counterparties. Collateral is generally not sought on these assets.

Financial assets at fair value through profit or loss and investment in securities

Collateral is generally not sought on debt securities.

Derivative financial instruments

The Master Agreement published by the International Swaps and Derivatives Association, Inc. ("ISDA Master Agreement") is the preferred agreement for documenting derivatives activities of the Group. It provides the contractual framework under which dealing activities of over-the-counter ("OTC") transactions are conducted, and sets out close-out netting provisions upon termination following the occurrence of an event of default or a termination event. In addition, if deemed necessary, Credit Support Annex ("CSA") will be included to form part of the Schedule to the ISDA Master Agreement. Under a CSA, collateral is passed from one counterparty to another, as appropriate, to mitigate the exposures.

Advances and other accounts, contingent liabilities and commitments

The general types of collateral are disclosed on page 166. Advances and other accounts, contingent liabilities and commitments are collateralised to the extent considered appropriate by the Group taking account of the risk assessment of individual exposures. The collateral coverage of advances to customers is analysed on pages 175 to 176. The components and nature of contingent liabilities and commitments are disclosed in Note 43. Regarding the commitments that are unconditionally cancellable without prior notice, the Group would assess the necessity to withdraw the credit line in case where the credit quality of a borrower deteriorates. For contingent liabilities and commitments, 10.91% (2015: 10.28%) was covered by collateral as at 31 December 2016.

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts

Gross advances and other accounts before impairment allowances are summarised by product type as follows:

	2016 HK$'m	2015 HK$'m
Advances to customers		
Personal		
– Mortgages	**227,987**	218,846
– Credit cards	**13,819**	13,833
– Others	**50,119**	42,424
Corporate		
– Commercial loans	**609,025**	544,205
– Trade finance	**72,121**	79,305
	973,071	898,613
Trade bills	**16,174**	32,372
Advances to banks and other financial institutions	**6,016**	969
	995,261	931,954

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

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

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

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include:

– Significant financial difficulty incurred by the borrower;

– A breach of contract, such as a default or delinquency in principal or interest payment;

– For economic or legal reasons related to the borrower's financial difficulty, the Group has granted to the borrower a concession that it would not otherwise consider;

– Probable that the borrower will become bankrupt or undergo other financial reorganisation; or

– Other observable data indicating that there is a measurable decrease in the estimated future cash flows from such advances.

(a) Advances neither overdue nor impaired

Advances that were neither overdue nor impaired are analysed by internal credit grade as follows:

	2016			
	Pass HK$'m	Special mention HK$'m	Substandard or below HK$'m	Total HK$'m
Advances to customers				
Personal				
– Mortgages	225,767	181	41	225,989
– Credit cards	13,472	–	–	13,472
– Others	49,718	78	2	49,798
Corporate				
– Commercial loans	606,545	332	650	607,527
– Trade finance	72,019	44	10	72,073
	967,521	635	703	968,859
Trade bills	16,174	–	–	16,174
Advances to banks and other financial institutions	6,016	–	–	6,016
	989,711	635	703	991,049

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(a) Advances neither overdue nor impaired (continued)

	2015			
	Pass HK$'m	Special mention HK$'m	Substandard or below HK$'m	Total HK$'m
Advances to customers				
Personal				
– Mortgages	216,722	167	31	216,920
– Credit cards	13,346	–	–	13,346
– Others	41,829	54	12	41,895
Corporate				
– Commercial loans	540,936	983	657	542,576
– Trade finance	78,913	131	–	79,044
	891,746	1,335	700	893,781
Trade bills	32,372	–	–	32,372
Advances to banks and other financial institutions	969	–	–	969
	925,087	1,335	700	927,122

The occurrence of loss event(s) may not necessarily result in impairment loss where the advances are fully collateralised. While such advances are of "substandard" or lower grades, they are regarded as not being impaired and have been included in the above tables.

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(b) Advances overdue but not impaired

The gross amount of advances overdue but not impaired is analysed as follows:

	2016				
	Overdue for three months or less HK$'m	Overdue for six months or less but over three months HK$'m	Overdue for one year or less but over six months HK$'m	Overdue for over one year HK$'m	Total HK$'m
Advances to customers					
Personal					
– Mortgages	**1,953**	**18**	**17**	**7**	**1,995**
– Credit cards	**306**	**–**	**–**	**–**	**306**
– Others	**281**	**1**	**3**	**1**	**286**
Corporate					
– Commercial loans	**443**	**–**	**–**	**5**	**448**
– Trade finance	**3**	**–**	**–**	**2**	**5**
	2,986	**19**	**20**	**15**	**3,040**

	2015				
	Overdue for three months or less HK$'m	Overdue for six months or less but over three months HK$'m	Overdue for one year or less but over six months HK$'m	Overdue for over one year HK$'m	Total HK$'m
Advances to customers					
Personal					
– Mortgages	1,885	15	19	–	1,919
– Credit cards	448	–	–	–	448
– Others	496	–	1	1	498
Corporate					
– Commercial loans	485	2	–	28	515
– Trade finance	41	32	2	4	79
	3,355	49	22	33	3,459

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(c) Impaired advances

Advances individually identified to be impaired are analysed by product type as follows:

	2016		2015	
	Gross advances HK$'m	**Market value of collateral HK$'m**	Gross advances HK$'m	Market value of collateral HK$'m
Advances to customers				
Personal				
– Mortgages	**3**	**6**	7	11
– Credit cards	**41**	**–**	39	–
– Others	**35**	**25**	31	20
Corporate				
– Commercial loans	**1,050**	**815**	1,114	1,072
– Trade finance	**43**	**14**	182	57
	1,172	**860**	1,373	1,160
Impairment allowances made in respect of such advances	**501**		624	

	2016 HK$'m	2015 HK$'m
Current market value of collateral held against the covered portion of such advances to customers	**860**	1,160
Covered portion of such advances to customers	**786**	920
Uncovered portion of such advances to customers	**386**	453

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

As at 31 December 2016, there were no impaired trade bills and advances to banks and other financial institutions (2015: Nil).

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(c) Impaired advances (continued)

Classified or impaired advances to customers are analysed as follows:

	2016 HK$'m	2015 HK$'m
Gross classified or impaired advances to customers	**1,955**	2,176
Gross classified or impaired advances to customers as a percentage of gross advances to customers	**0.20%**	0.24%
Individually assessed impairment allowances made in respect of such advances	**449**	578

Classified or impaired advances to customers represent advances which are either classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

(d) Advances overdue for more than three months

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

	2016		2015	
	Amount HK$'m	% of gross advances to customers	Amount HK$'m	% of gross advances to customers
Gross advances to customers which have been overdue for:				
– six months or less but over three months	**92**	**0.01%**	128	0.01%
– one year or less but over six months	**54**	**0.01%**	170	0.02%
– over one year	**106**	**0.01%**	217	0.03%
Advances overdue for over three months	**252**	**0.03%**	515	0.06%
Individually assessed impairment allowances made in respect of such advances	**60**		163	

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(d) Advances overdue for more than three months (continued)

	2016 HK$'m	2015 HK$'m
Current market value of collateral held against the covered portion of such advances to customers	**324**	694
Covered portion of such advances to customers	**130**	346
Uncovered portion of such advances to customers	**122**	169

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

As at 31 December 2016, there were no trade bills and advances to banks and other financial institutions overdue for more than three months (2015: Nil).

(e) Rescheduled advances

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

As at 31 December 2016, there were no rescheduled advances to customers net of amounts included in "Advances overdue for more than three months" (2015: Nil).

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers

(i) Sectoral analysis of gross advances to customers

The following analysis of the gross advances to customers by industry sector is based on the categories with reference to the completion instructions for the HKMA return of loans and advances.

	2016					
	Gross advances to customers HK$'m	% covered by collateral or other security	Classified or impaired HK$'m	Overdue HK$'m	Individually assessed impairment allowances HK$'m	Collectively assessed impairment allowances HK$'m
Loans for use in Hong Kong						
Industrial, commercial and financial						
– Property development	73,336	22.91%	–	1	–	245
– Property investment	53,908	81.58%	27	133	–	180
– Financial concerns	5,438	3.53%	–	–	–	45
– Stockbrokers	2,647	95.17%	–	–	–	9
– Wholesale and retail trade	34,997	37.24%	39	183	26	127
– Manufacturing	25,981	17.60%	49	51	7	98
– Transport and transport equipment	53,074	31.31%	1,239	17	289	186
– Recreational activities	2,510	1.59%	–	–	–	8
– Information technology	17,938	1.30%	–	–	–	58
– Others	105,062	24.96%	15	89	10	341
Individuals						
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	8,562	99.84%	10	170	–	5
– Loans for purchase of other residential properties	218,426	99.93%	89	1,812	2	101
– Credit card advances	13,819	–	41	524	–	123
– Others	47,717	71.08%	36	495	3	68
Total loans for use in Hong Kong	663,415	58.03%	1,545	3,475	337	1,594
Trade finance	72,121	14.00%	56	49	21	256
Loans for use outside Hong Kong	237,535	13.48%	354	201	91	825
Gross advances to customers	973,071	43.89%	1,955	3,725	449	2,675

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

	2015					
	Gross advances to customers HK$'m	% covered by collateral or other security	Classified or impaired HK$'m	Overdue HK$'m	Individually assessed impairment allowances HK$'m	Collectively assessed impairment allowances HK$'m
Loans for use in Hong Kong						
Industrial, commercial and financial						
– Property development	65,148	26.15%	1	1	–	224
– Property investment	57,101	88.21%	4	93	–	205
– Financial concerns	11,453	3.57%	–	1	–	64
– Stockbrokers	1,743	81.56%	–	–	–	6
– Wholesale and retail trade	28,633	53.04%	62	268	24	109
– Manufacturing	21,798	26.70%	24	32	7	83
– Transport and transport equipment	45,616	33.07%	1,478	4	360	159
– Recreational activities	393	18.84%	–	–	–	1
– Information technology	13,064	0.72%	–	1	–	42
– Others	55,817	42.91%	16	123	7	186
Individuals						
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	8,523	99.94%	16	180	–	5
– Loans for purchase of other residential properties	209,777	99.92%	67	1,728	1	99
– Credit card advances	13,834	–	39	487	–	101
– Others	38,587	72.76%	36	440	7	67
Total loans for use in Hong Kong	571,487	65.73%	1,743	3,358	406	1,351
Trade finance	79,305	13.11%	195	255	103	281
Loans for use outside Hong Kong	247,821	17.71%	238	354	69	873
Gross advances to customers	898,613	47.84%	2,176	3,967	578	2,505

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

The amounts of new impairment allowances charged to the income statement, and classified or impaired loans written off during the year are shown below:

	2016		2015	
	New impairment allowances HK$'m	Classified or impaired loans written off HK$'m	New impairment allowances HK$'m	Classified or impaired loans written off HK$'m
Loans for use in Hong Kong				
Industrial, commercial and financial				
– Property development	25	–	45	–
– Property investment	–	–	–	1
– Financial concerns	–	–	21	–
– Stockbrokers	2	–	1	–
– Wholesale and retail trade	50	18	24	3
– Manufacturing	19	2	13	1
– Transport and transport equipment	50	1	361	–
– Recreational activities	5	–	–	–
– Information technology	11	–	3	–
– Others	125	8	15	3
Individuals				
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	–	–	–	–
– Loans for purchase of other residential properties	6	–	–	–
– Credit card advances	248	228	222	214
– Others	190	182	173	166
Total loans for use in Hong Kong	731	439	878	388
Trade finance	18	62	169	159
Loans for use outside Hong Kong	117	–	208	203
Gross advances to customers	866	501	1,255	750

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers

The following geographical analysis of advances to customers is based on the locations of the counterparties, after taking into account the transfer of risk. For an advance to customer guaranteed by a party situated in a country different from the customer, the risk will be transferred to the country of the guarantor.

Gross advances to customers

	2016 HK$'m	2015 HK$'m
Hong Kong	**780,886**	727,625
Mainland of China	**119,882**	119,279
Others	**72,303**	51,709
	973,071	898,613
Collectively assessed impairment allowances in respect of the gross advances to customers		
Hong Kong	**2,017**	1,913
Mainland of China	**379**	377
Others	**279**	215
	2,675	2,505

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

Overdue advances

	2016 HK$'m	2015 HK$'m
Hong Kong	**3,407**	3,289
Mainland of China	**139**	406
Others	**179**	272
	3,725	3,967
Individually assessed impairment allowances in respect of the overdue advances		
Hong Kong	**109**	126
Mainland of China	**7**	78
Others	**3**	10
	119	214
Collectively assessed impairment allowances in respect of the overdue advances		
Hong Kong	**96**	84
Mainland of China	**2**	5
Others	**2**	2
	100	91

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

Classified or impaired advances

	2016 HK$'m	2015 HK$'m
Hong Kong	**1,705**	1,699
Mainland of China	**52**	394
Others	**198**	83
	1,955	2,176
Individually assessed impairment allowances in respect of the classified or impaired advances		
Hong Kong	**408**	407
Mainland of China	**10**	157
Others	**31**	14
	449	578
Collectively assessed impairment allowances in respect of the classified or impaired advances		
Hong Kong	**52**	45
Mainland of China	**1**	3
Others	**1**	–
	54	48

(C) Repossessed assets

During the year, the Group obtained assets by taking possession of collateral held as security. The nature and carrying value of these assets held as at 31 December are summarised as follows:

	2016 HK$'m	2015 HK$'m
Residential properties	**38**	44

4. Financial risk management (continued)

4.1 Credit risk (continued)

(C) Repossessed assets (continued)

The estimated market value of repossessed assets held by the Group as at 31 December 2016 amounted to HK$72 million (2015: HK$55 million). The repossessed assets comprise properties in respect of which the Group has acquired access or control (e.g. through court proceedings or voluntary actions by the proprietors concerned) for release in full or in part of the obligations of the borrowers.

When the repossessed assets are not readily convertible into cash, the Group may consider the following alternatives:

– adjusting the selling prices

– selling the loans together with the assets

– arranging loan restructuring

(D) Balances and placements with banks and other financial institutions

The following tables present an analysis of balances and placements with banks and other financial institutions that are neither overdue nor impaired as at 31 December by rating agency designation.

	2016			
	Aaa to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Central banks	**68,724**	**–**	**4,589**	**73,313**
Banks and other financial institutions	**186,394**	**26,297**	**752**	**213,443**
	255,118	**26,297**	**5,341**	**286,756**

	2015			
	Aaa to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Central banks	110,225	–	2,304	112,529
Banks and other financial institutions	159,001	17,490	3,439	179,930
	269,226	17,490	5,743	292,459

As at 31 December 2016, there were no overdue or impaired balances and placements with banks and other financial institutions (2015: Nil).

4. Financial risk management (continued)

4.1 Credit risk (continued)

(E) Debt securities and certificates of deposit

The following tables present an analysis of the carrying value of debt securities and certificates of deposit by issue rating. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	2016					
	Aaa HK$'m	Aa1 to Aa3 HK$'m	A1 to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Available-for-sale securities	**106,276**	**171,851**	**186,790**	**41,056**	**20,654**	**526,627**
Held-to-maturity securities	**19,805**	**21,671**	**12,365**	**4,434**	**1,919**	**60,194**
Loans and receivables	**–**	**149**	**786**	**–**	**–**	**935**
Financial assets at fair value through profit or loss	**14,927**	**16,615**	**14,817**	**6,501**	**3,456**	**56,316**
	141,008	**210,286**	**214,758**	**51,991**	**26,029**	**644,072**

	2015					
	Aaa HK$'m	Aa1 to Aa3 HK$'m	A1 to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Available-for-sale securities	84,691	88,062	207,071	28,073	22,286	430,183
Held-to-maturity securities	29,958	30,602	12,898	4,717	3,668	81,843
Loans and receivables	–	–	3,166	–	–	3,166
Financial assets at fair value through profit or loss	8,943	21,953	12,344	5,250	4,612	53,102
	123,592	140,617	235,479	38,040	30,566	568,294

4. Financial risk management (continued)

4.1 Credit risk (continued)

(E) Debt securities and certificates of deposit (continued)

The following tables present an analysis of debt securities and certificates of deposit neither overdue nor impaired as at 31 December by issue rating. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	2016					
	Aaa HK$'m	Aa1 to Aa3 HK$'m	A1 to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Available-for-sale securities	106,276	171,851	186,790	41,056	20,654	526,627
Held-to-maturity securities	19,804	21,671	12,365	4,434	1,919	60,193
Loans and receivables	–	149	786	–	–	935
Financial assets at fair value through profit or loss	14,927	16,615	14,817	6,501	3,456	56,316
	141,007	210,286	214,758	51,991	26,029	644,071

	2015					
	Aaa HK$'m	Aa1 to Aa3 HK$'m	A1 to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Available-for-sale securities	84,691	88,062	207,071	28,073	22,286	430,183
Held-to-maturity securities	29,955	30,602	12,898	4,717	3,668	81,840
Loans and receivables	–	–	3,166	–	–	3,166
Financial assets at fair value through profit or loss	8,943	21,953	12,344	5,250	4,612	53,102
	123,589	140,617	235,479	38,040	30,566	568,291

4. Financial risk management (continued)

4.1 Credit risk (continued)

(E) Debt securities and certificates of deposit (continued)

The following tables present an analysis of impaired debt securities by issue rating. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	2016					
	Aaa HK$'m	Aa1 to Aa3 HK$'m	A1 to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Held-to-maturity securities	1	–	–	–	–	1

	2015					
	Aaa HK$'m	Aa1 to Aa3 HK$'m	A1 to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Held-to-maturity securities	3	–	–	–	–	3

As at 31 December 2016, there were no impaired certificates of deposit and no overdue debt securities and certificates of deposit (2015: Nil).

4.2 Market risk

Market risk refers to the risk of loss arising from movements in the value of foreign exchange, interest rate, equity and commodity positions held by the Group due to the volatility of financial market price (foreign exchange rate, interest rate, equity price, commodity price). The Group adopts a moderate market risk appetite to achieve a balance between risk and return. The Group's objective in managing market risk is to secure healthy growth of the treasury business, by effective management of potential market risk in the Group's business, according to the Group's overall risk appetite and strategy of treasury business on the basis of a well-established risk management regime and related management measures.

In accordance with the Group's corporate governance principles in respect of risk management, the Board and RC, senior management and functional departments/units perform their duties and responsibilities to manage the Group's market risk. The RMD is mainly responsible for managing market risk, assisting senior management to perform their day-to-day duties, independently monitoring the market risk profile and compliance of management policies and limits of the Group and BOCHK, and ensuring that the aggregate and individual market risks are within acceptable levels.

The Group's market risk management covers BOCHK and its subsidiaries. The Group establishes consistent market risk management policies to regulate BOCHK's and subsidiaries' market risk management; meanwhile, the Group sets up the Group VAR and stress test limits, which are allocated and monitored across the Group, according to the subsidiaries' business requirements and risk tolerance levels. In line with the requirements set in the Group policy, the management of subsidiaries may, subject to prior consent by BOCHK, formulate the detailed policies and procedures and are responsible for managing their daily market risk.

4. Financial risk management (continued)

4.2 Market risk (continued)

The Group sets up market risk indicators and limits to identify, measure, monitor and control market risk. Major risk indicators and limits include but are not limited to VAR, Stop Loss, Open Position, Stress Testing and Sensitivity Analysis (Basis Point Value, Greeks), etc. To meet management requirements, major risk indicators and limits are classified into four levels, and are approved by the RC, MC, CRO and the DCE in charge of the treasury business or the head of the respective business unit respectively. Treasury business units of BOCHK and subsidiaries (as for Group Limit) are required to conduct their business within approved market risk indicators and limits.

(A) VAR

The Group uses the VAR to measure and report general market risks to the RC and senior management on a periodic basis. The Group adopts a uniformed VAR calculation model, using a historical simulation approach and two years of historical market data, to calculate the VAR of the Group and subsidiaries over a one-day holding period with a 99% confidence level, and sets up the VAR limit of the Group and subsidiaries.

The following table sets out the VAR for all general market risk exposure[1] of the Group.

	Year	At 31 December HK$'m	Minimum for the year HK$'m	Maximum for the year HK$'m	Average for the year HK$'m
VAR for all market risk	2016	61.2	29.4	70.5	45.9
	2015	17.8	17.8	38.4	25.4
VAR for foreign exchange risk	2016	57.1	24.3	62.4	35.8
	2015	12.9	8.8	20.3	13.2
VAR for interest rate risk	2016	44.9	15.3	57.4	28.8
	2015	14.7	12.8	37.6	20.7
VAR for equity risk	2016	3.2	0.0	5.7	2.1
	2015	0.0	0.0	0.4	0.2
VAR for commodity risk	2016	1.2	0.0	1.4	0.3
	2015	0.0	0.0	0.2	0.0

Note:
1. Structural FX positions have been excluded.

4. Financial risk management (continued)

4.2 Market risk (continued)

(A) VAR (continued)

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

- the use of historical market data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;

- the use of a one-day holding period assumes that all positions can be liquidated or hedged in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day holding period may be insufficient to liquidate or hedge all positions fully;

- the use of a 99% confidence level, by definition, does not take into account losses that might occur beyond this level of confidence; and

- VAR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

The Group recognises these limitations by formulating stress test indicators and limits to assess and manage the market risk uncovered by VAR. The stress testing programme of the market risk includes sensitivity testing on changes in risk factors with various degrees of severity, as well as scenario analysis on historical events including the 1987 Equity Market Crash, 1994 Bond Market Crash, 1997 Asian Financial Crisis, 2001 9-11 event and 2008 Financial Tsunami, etc.

(B) Currency risk

The Group's assets and liabilities are denominated in major currencies, particularly the HK dollar, the US dollar and Renminbi. To ensure the currency risk exposure of the Group is kept to an acceptable level, risk limits (e.g. Position and VAR limit) are used to serve as a monitoring tool. Moreover, the Group seeks to minimise the gap between assets and liabilities in the same currency. Foreign exchange contracts (e.g. FX swaps) are usually used to manage FX risk associated with foreign currency-denominated assets and liabilities.

4. Financial risk management (continued)

4.2 Market risk (continued)

(B) Currency risk (continued)

The following is a summary of the Group's major foreign currency exposures arising from trading, non-trading and structural positions and is prepared with reference to the completion instructions for the HKMA return of foreign currency position. The net options position is calculated based on the basis of delta-weighted positions of all foreign exchange options contracts.

	2016							
	Equivalent in million of HK$							
	US Dollars	Japanese Yen	Euro	Australian Dollars	Pound Sterling	Renminbi	Other foreign currencies	Total foreign currencies
Spot assets	**729,472**	**128,359**	**40,591**	**22,537**	**20,711**	**260,636**	**28,637**	**1,230,943**
Spot liabilities	**(617,520)**	**(9,056)**	**(28,397)**	**(19,823)**	**(14,351)**	**(250,559)**	**(32,101)**	**(971,807)**
Forward purchases	**1,095,599**	**58,711**	**56,669**	**28,125**	**26,200**	**579,902**	**55,743**	**1,900,949**
Forward sales	**(1,196,764)**	**(178,070)**	**(68,865)**	**(30,925)**	**(32,618)**	**(588,688)**	**(52,907)**	**(2,148,837)**
Net options position	**1,123**	**1**	**1**	**(3)**	**2**	**(733)**	**1**	**392**
Net long/(short) position	**11,910**	**(55)**	**(1)**	**(89)**	**(56)**	**558**	**(627)**	**11,640**

	2015							
	Equivalent in million of HK$							
	US Dollars	Japanese Yen	Euro	Australian Dollars	Pound Sterling	Renminbi	Other foreign currencies	Total foreign currencies
Spot assets	666,562	94,198	25,741	22,886	7,829	484,356	10,131	1,311,703
Spot liabilities	(512,219)	(13,853)	(23,822)	(21,357)	(14,534)	(467,809)	(16,722)	(1,070,316)
Forward purchases	1,239,554	53,057	90,200	30,789	43,772	805,959	41,144	2,304,475
Forward sales	(1,380,890)	(133,356)	(92,281)	(32,412)	(36,962)	(822,094)	(34,042)	(2,532,037)
Net options position	1,518	(1)	2	26	(13)	(1,425)	1	108
Net long/(short) position	14,525	45	(160)	(68)	92	(1,013)	512	13,933

4. Financial risk management (continued)

4.2 Market risk (continued)

(B) Currency risk (continued)

	2016				
	Equivalent in million of HK$				
	US Dollars	Renminbi	Malaysian Ringgit	Other foreign currencies	Total foreign currencies
Net structural position	**–**	**791**	**2,175**	**160**	**3,126**

	2015				
	Equivalent in million of HK$				
	US Dollars	Renminbi	Malaysian Ringgit	Other foreign currencies	Total foreign currencies
Net structural position	293	9,355	–	–	9,648

(C) Interest rate risk

Interest rate risk means the risks to a bank's earnings and economic value arising from movements in interest rate and term structures of the bank's asset and liability positions. The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

- Repricing risk: mismatches in the maturity or repricing periods of assets and liabilities that may affect net interest income;
- Basis risk: different pricing basis for different transactions resulting that the yield on assets and cost of liabilities may change by different amounts within the same repricing period;
- Yield curve risk: non-parallel shifts in the yield curve that may have an adverse impact on net interest income or economic value; and
- Option risk: exercise of the options embedded in assets, liabilities or off-balance sheet items that can cause a change in the cash flows of assets and liabilities.

4. Financial risk management (continued)

4.2 Market risk (continued)

(C) Interest rate risk (continued)

The Group's risk management framework applies also to interest rate risk management. The ALCO exercises its oversight of interest rate risk in accordance with the "BOCHK Group Banking Book Interest Rate Risk Management Policy" approved by RC. RMD (Interest Rate and Liquidity Risk Management) is responsible for interest rate risk management. With the cooperation of the Asset and Liability Management Division of Financial Management Department and Investment Management, RMD assists the ALCO to perform day-to-day interest rate risk management. Its roles include, but are not limited to, the formulation of management policies, selection of methodologies, setting of risk indicators and limits, assessment of target balance sheet, monitoring of the compliance with policies and limits, and submission of interest rate risk management reports to the senior management and RC, etc.

The Group sets out interest rate risk indicators and limits to identify, measure, monitor and control interest rate risk. The indicators and limits include, but are not limited to, repricing gap limits, basis risk, duration, price value of a basis point ("PVBP"), Greeks, net interest income sensitivity ratio ("NII"), economic value sensitivity ratio ("EV"), etc. The indicators and limits are classified into different levels, which are approved by the CFO and CRO, ALCO, RC accordingly. Risk-taking business units are required to conduct their business within the boundary of the interest rate risk limits. Before launching a new product or business in the banking book, the relevant departments are required to go through a risk assessment process, which includes the assessment of underlying interest rate risk and consideration of the adequacy of current risk monitoring mechanism. Any material impact on interest rate risk noted during the risk assessment process will be submitted to RC for approval.

NII and EV assess the impact of interest rate movement on the Group's net interest income and capital base. They are the Group's key interest rate risk indicators. The former assesses the impact of interest rate movement on net interest income as a percentage to the projected net interest income for the year. The latter assesses the impact of interest rate movement on economic value (i.e. the net present value of cash flows of assets, liabilities and off-balance sheet items discounted using market interest rate) as a percentage to the latest capital base. Limits are set by the RC on these two indicators to monitor and control the Group's banking book interest rate risk.

The Group uses scenario analyses and stress tests to assess the banking book interest rate risk that the Group would face under adverse circumstances. Scenario analyses and stress tests are also used to assess the impact on net interest income and economic value arising from the optionality of savings deposits, the prepayment of mortgage loans and the prepayment of debt securities with embedded options.

4. Financial risk management (continued)

4.2 Market risk (continued)

(C) Interest rate risk (continued)

The Group is principally exposed to HK Dollar, US Dollar and Renminbi in terms of interest rate risk. As at 31 December 2016, if HK Dollar, US Dollar and Renminbi market interest rates had a 100 basis point parallel upward shift of the yield curve in relevant currency with other variables held constant, the sensitivities on net interest income over a twelve-month period and on reserves for the Group would have been as follows:

	Impact on net interest income over the next twelve months at 31 December		Impact on reserves at 31 December	
	2016 HK$'m	2015 HK$'m	**2016 HK$'m**	2015 HK$'m
HK Dollar	**1,572**	985	**(523)**	(488)
US Dollar	**(525)**	(345)	**(8,220)**	(5,332)
Renminbi	**(583)**	(738)	**(747)**	(1,020)

The overall impact on net interest income of the above currencies is positive in 2016, which is mainly because of the increase in HKD non-interest bearing funding. Reserves would have been reduced because of the expected reduction in valuation of available-for-sale securities due to a parallel shift up of 100 basis points in the yield curve. The reduction of reserves is increased compared with 2015 because the size of available-for-sale securities in capital market is increased.

The sensitivities above are for illustration only and are based on several assumptions, including, but not limited to, the change in the correlation between interest rates of relevant currencies, parallel movement of interest rates, the absence of actions that would be taken to mitigate the impact of interest rate risk, the effectiveness of hedge accounting, all positions being assumed to run to maturity, behavioural assumptions of products in which actual repricing date differs from contractual repricing date or products without contractual maturity. The above exposures form only a part of the Group's overall interest rate risk exposures.

4. Financial risk management (continued)

4.2 Market risk (continued)

(C) Interest rate risk (continued)

The tables below summarise the Group's on-balance sheet exposure to interest rate risk as at 31 December. Included in the tables are the assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing date and maturity date.

	2016						
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Non-interest bearing HK$'m	Total HK$'m
Assets							
Cash and balances with banks and other financial institutions	210,590	–	–	–	–	18,483	229,073
Placements with banks and other financial institutions maturing between one and twelve months	–	28,195	42,197	–	–	–	70,392
Financial assets at fair value through profit or loss	5,510	8,217	13,224	15,326	19,816	5,265	67,358
Derivative financial instruments	–	–	–	–	–	64,314	64,314
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	123,390	123,390
Advances and other accounts	779,681	106,980	53,703	39,535	4,807	7,431	992,137
Investment in securities							
– Available-for-sale securities	54,896	119,040	105,886	142,045	104,760	4,409	531,036
– Held-to-maturity securities	779	3,979	17,001	23,982	14,453	–	60,194
– Loans and receivables	–	–	935	–	–	–	935
Interests in associates and joint ventures	–	–	–	–	–	319	319
Investment properties	–	–	–	–	–	18,227	18,227
Properties, plant and equipment	–	–	–	–	–	45,732	45,732
Other assets (including deferred tax assets)	3,383	–	–	–	–	67,998	71,381
Assets held for sale	32,358	6,837	6,394	5,197	4	2,503	53,293
Total assets	1,087,197	273,248	239,340	226,085	143,840	358,071	2,327,781
Liabilities							
Hong Kong SAR currency notes in circulation	–	–	–	–	–	123,390	123,390
Deposits and balances from banks and other financial institutions	151,036	14,210	7,031	394	–	19,742	192,413
Financial liabilities at fair value through profit or loss	3,705	5,578	2,161	1,335	592	–	13,371
Derivative financial instruments	–	–	–	–	–	49,289	49,289
Deposits from customers	1,133,516	183,833	79,008	322	–	107,397	1,504,076
Debt securities and certificates of deposit in issue	–	–	–	1,121	–	–	1,121
Other accounts and provisions (including current and deferred tax liabilities)	15,803	–	–	–	–	45,197	61,000
Insurance contract liabilities	–	–	–	–	–	86,534	86,534
Subordinated liabilities	–	–	–	19,014	–	–	19,014
Liabilities associated with assets held for sale	28,917	7,428	7,145	67	–	3,456	47,013
Total liabilities	1,332,977	211,049	95,345	22,253	592	435,005	2,097,221
Interest sensitivity gap	(245,780)	62,199	143,995	203,832	143,248	(76,934)	230,560

4. Financial risk management (continued)

4.2 Market risk (continued)

(C) Interest rate risk (continued)

	2015						
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Non-interest bearing HK$'m	Total HK$'m
Assets							
Cash and balances with banks and other financial institutions	199,016	–	–	–	–	35,256	234,272
Placements with banks and other financial institutions maturing between one and twelve months	–	39,148	26,992	–	–	–	66,140
Financial assets at fair value through profit or loss	1,742	6,980	9,223	18,895	16,442	4,495	57,777
Derivative financial instruments	–	–	–	–	–	43,211	43,211
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	101,950	101,950
Advances and other accounts	717,440	108,780	62,019	32,770	943	6,919	928,871
Investment in securities							
– Available-for-sale securities	39,481	124,945	86,792	119,560	59,405	2,746	432,929
– Held-to-maturity securities	440	3,481	13,296	43,618	21,008	–	81,843
– Loans and receivables	–	1,005	2,161	–	–	–	3,166
Interests in associates and joint ventures	–	–	–	–	–	376	376
Investment properties	–	–	–	–	–	15,262	15,262
Properties, plant and equipment	–	–	–	–	–	50,517	50,517
Other assets (including deferred tax assets)	3,024	–	–	–	–	63,004	66,028
Assets held for sale	168,400	44,587	49,217	25,704	528	12,037	300,473
Total assets	1,129,543	328,926	249,700	240,547	98,326	335,773	2,382,815
Liabilities							
Hong Kong SAR currency notes in circulation	–	–	–	–	–	101,950	101,950
Deposits and balances from banks and other financial institutions	159,968	29,366	2,343	886	–	16,963	209,526
Financial liabilities at fair value through profit or loss	2,583	4,446	1,968	1,479	466	–	10,942
Derivative financial instruments	–	–	–	–	–	40,074	40,074
Deposits from customers	1,059,319	184,611	81,544	622	–	89,391	1,415,487
Debt securities and certificates of deposit in issue	59	–	5,728	1,189	–	–	6,976
Other accounts and provisions (including current and deferred tax liabilities)	8,884	–	–	–	–	34,939	43,823
Insurance contract liabilities	–	–	–	–	–	82,645	82,645
Subordinated liabilities	–	–	–	19,422	–	–	19,422
Liabilities associated with assets held for sale	149,045	40,917	40,634	5,967	19	15,223	251,805
Total liabilities	1,379,858	259,340	132,217	29,565	485	381,185	2,182,650
Interest sensitivity gap	(250,315)	69,586	117,483	210,982	97,841	(45,412)	200,165

4. Financial risk management (continued)

4.3 Liquidity risk

Liquidity risk is the risk that banks fail to provide sufficient funds to grow assets or pay due obligations, and need to bear an unacceptable loss. The Group maintains sound liquidity risk appetite to provide stable, reliable and adequate sources of cash to meet liquidity needs under normal circumstances or stressed scenarios; and to survive with net positive cumulative cash flow in extreme scenarios, without requesting the HKMA to act as the lender of last resort.

The Group's liquidity risk management objective is to effectively manage the liquidity of on- and off-balance sheet items with reasonable cost based on the liquidity risk appetite to achieve sound operation and sustainable profitability. Deposits from customers are the Group's primary source of funds. To ensure stable and sufficient source of funds are in place, the Group actively attracts new deposits, keeps the core deposit and obtains supplementary funding from the interbank market and by issuing bills in the capital market. According to different term maturities and the results of funding needs estimated from stressed scenarios, the Group adjusts its asset structure (including loans, bonds investment, interbank placement, etc.) to maintain sufficient liquid assets which provides adequate funds in support of normal business needs and ensure its ability to raise funds at a reasonable cost to serve external claims in case of emergency. The Group is committed to diversify the source of funds and the use of funds to avoid excessive concentration of assets and liabilities and prevent triggering liquidity risk due to the break of funding strand when problem occurred in one concentrated funding source. The Group has established intra-group liquidity risk management guideline to manage the liquidity funding among different entities within the Group, and to restrict their reliance of funding on each other. The Group also pays attention to manage liquidity risk created by off-balance sheet activities, such as loan commitments, derivatives, options and other complex structured products. The Group has an overall liquidity risk management strategy to cover the liquidity management of foreign currency assets and liabilities, collateral, intra-day liquidity, intra-group liquidity, the liquidity risk arising from other risks, etc., and has formulated corresponding contingency plan.

The RC is the decision-making authority of liquidity risk management, and assumes the ultimate responsibility of liquidity risk management. As authorised by RC, ALCO exercises its oversight of liquidity risk and ensures the daily operations of the Group are in accordance with risk appetite and policies as set by RC. RMD (Interest Rate and Liquidity Risk Management) is responsible for overseeing the Group's liquidity risk. It cooperates with the Asset and Liability Management Division of Financial Management Department, Investment Management, etc. to assist the ALCO to perform liquidity management functions according to their specific responsibilities.

The Group established liquidity risk management indicators and limits to identify, measure, monitor and control liquidity risk on daily basis. These indicators and limits include, but are not limited to liquidity coverage ratio ("LCR"), loan-to-deposit ratio, Maximum Cumulative Cash Outflow ("MCO") and liquidity cushion. The Group applies cash flow analysis to assess the Group's liquidity condition under normal conditions and also performs a liquidity stress test (including institution specific, general market crisis and combined crisis) and other methods at least on monthly basis to assess the Group's capability to withstand various severe liquidity crises. Also, relevant management information systems such as Assets and Liabilities Management System and Basel Liquidity Ratio Management System are developed to provide data and the preparation for regular management reports to facilitate liquidity risk management duties.

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

In accordance with the requirements of Supervisory Policy Manual LM-2 "Sound Systems and controls for Liquidity Risk Management" issued by the HKMA, the Group has implemented behaviour model and assumptions of cash flow analysis and stress test to enhance the Group's cash flow analysis under both normal and stressed conditions. In cash flow analysis under normal circumstances, assumptions have been made relating to on-balance sheet items (such as deposits from customers) and off-balance sheet items (such as loan commitments). According to various characteristics of the assets, liabilities and off-balance sheet items, the Group forecasts the future cash flow based on contractual maturity date and the assumptions of customer behaviour and balance sheet changes. The Group establishes MCO indicator which predicts the future 30 days maximum cumulative net cash outflow in normal situations based on the above assumptions, to assess if the Group has sufficient financing capacity to meet the cash flow gap in order to achieve the objective of continuing operation. As at 31 December 2016, before taking the cash inflow through the sale of outstanding marketable securities into consideration, BOCHK's 30 day cumulative cash flow was a net cash inflow, amounting to HK$64,212 million (2015: HK$74,742 million) and was in compliance with the internal limit requirements.

In the liquidity stress test, institution specific, general market crisis and combined crisis scenarios have been set up, combined crisis scenario is a combination of institution specific and general market crisis to assess the Group's capability to withstand a more severe liquidity crisis, with a more stringent set of assumptions being adopted. Stress test assumptions include the run-off rate of retail, wholesale and interbank deposits; drawdown rate of loan commitments and trade-related contingent liabilities; delinquency ratio and rollover rate of customer loans; and haircut of interbank placement and marketable securities. As at 31 December 2016, the Group was able to maintain a net cash inflow under the three stressed scenarios, indicating the Group has the ability to meet financing needs under stressed conditions. In addition, the Group has a policy in place to maintain a liquidity cushion which includes high quality or comparable quality marketable securities issued or guaranteed by sovereigns, central banks, public sector entities or multilateral development banks with 0% or 20% risk weight or marketable securities issued by non-financial corporate with a corresponding external credit rating of A- or above to ensure funding needs even under stressed scenarios. As at 31 December 2016, the liquidity cushion (before haircut) of BOCHK was HK$353,048 million (2015: HK$309,969 million). A contingency plan is being established which details the conditions to trigger the plan based on stress test results and early warning indicators, the action plans and relevant procedures and responsibility of relevant departments.

The LCR is calculated in accordance with the Banking (Liquidity) Rules effective from 1 January 2015, the Group, being classified as category 1 authorised institution by the HKMA, is required to calculate LCR on consolidated basis. During the year of 2016, the Group is required to maintain a LCR not less than 70%.

In certain derivative contracts, the counterparties have right to request from the Group additional collateral if they have concerns about the Group's creditworthiness.

The Group's liquidity risk management also covers new products or business developments. Before launching a new product or business, the relevant departments are required to go through a risk assessment process, which includes the assessment of underlying liquidity risk and consideration of the adequacy of the current risk management mechanism. Any material impact on liquidity risk noted during the risk assessment process will be reported to RC for approval.

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

The Group has established a set of uniform liquidity risk management policies which serve as standards and guidance to all the Group's members for liquidity risk management. On the basis of the Group's uniform policy, each of the subsidiaries develops its own liquidity management policies according to its own characteristics, and assumes its own liquidity risk management responsibility. Subsidiaries are required to report their respective liquidity positions on a regular basis to RMD (Interest Rate and Liquidity Risk Management) of BOCHK, which consolidates this information and evaluates group-wide liquidity risk.

(A) Liquidity coverage ratio

	2016	2015
Average value of liquidity coverage ratio		
– First quarter	**112.92%**	101.90%
– Second quarter	**109.70%**	109.89%
– Third quarter	**118.69%**	104.00%
– Fourth quarter	**107.02%**	106.52%

The average value of liquidity coverage ratio is calculated based on the arithmetic mean of the liquidity coverage ratio as at the end of each working day in the quarter and the calculation methodology and instructions set out in the HKMA return of liquidity position.

The liquidity coverage ratio is computed on the consolidated basis which comprises the positions of BOCHK and certain subsidiaries specified by the HKMA in accordance with the Banking (Liquidity) Rules.

The additional information of liquidity coverage ratio disclosures is available under section "Regulatory Disclosures" on the Bank's website at www.bochk.com.

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(B) Maturity analysis

The tables below analyse the Group's assets and liabilities as at 31 December into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

	2016							
	On demand HK$'m	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Indefinite HK$'m	Total HK$'m
Assets								
Cash and balances with banks and other financial institutions	111,852	104,538	–	–	–	–	12,683	229,073
Placements with banks and other financial institutions maturing between one and twelve months	–	–	28,195	42,197	–	–	–	70,392
Financial assets at fair value through profit or loss								
– Held for trading								
– Debt securities	–	1,415	3,723	9,430	13,083	3,417	–	31,068
– Certificates of deposit	–	–	1,140	412	591	–	–	2,143
– Designated at fair value through profit or loss								
– Debt securities	–	109	281	3,339	3,054	16,174	–	22,957
– Certificates of deposit	–	2	–	2	144	–	–	148
– Equity securities and fund	–	–	–	–	–	–	5,265	5,265
– Others	–	4,097	1,680	–	–	–	–	5,777
Derivative financial instruments	14,662	8,962	10,104	21,369	6,533	2,684	–	64,314
Hong Kong SAR Government certificates of indebtedness	123,390	–	–	–	–	–	–	123,390
Advances and other accounts								
– Advances to customers	93,182	22,021	61,767	131,998	437,199	221,785	1,995	969,947
– Trade bills	6	4,863	3,831	7,474	–	–	–	16,174
– Advances to banks and other financial institutions	–	3	1	577	5,435	–	–	6,016
Investment in securities								
– Available-for-sale								
– Debt securities	–	37,484	80,502	79,478	167,246	105,014	–	469,724
– Certificates of deposit	–	2,985	16,078	30,274	7,357	209	–	56,903
– Held-to-maturity								
– Debt securities	–	865	3,958	17,329	23,712	14,311	1	60,176
– Certificates of deposit	–	–	–	–	–	18	–	18
– Loans and receivables								
– Debt securities	–	–	–	935	–	–	–	935
– Equity securities and fund	–	–	–	–	–	–	4,409	4,409
Interests in associates and joint ventures	–	–	–	–	–	–	319	319
Investment properties	–	–	–	–	–	–	18,227	18,227
Properties, plant and equipment	–	–	–	–	–	–	45,732	45,732
Other assets (including deferred tax assets)	30,971	15,426	585	931	7,620	15,806	42	71,381
Assets held for sale	6,097	6,304	4,791	9,851	18,486	5,684	2,080	53,293
Total assets	380,160	209,074	216,636	355,596	690,460	385,102	90,753	2,327,781
Liabilities								
Hong Kong SAR currency notes in circulation	123,390	–	–	–	–	–	–	123,390
Deposits and balances from banks and other financial institutions	152,288	18,490	14,110	7,031	494	–	–	192,413
Financial liabilities at fair value through profit or loss	–	3,705	5,582	2,238	1,257	589	–	13,371
Derivative financial instruments	10,511	3,390	7,364	20,140	5,218	2,666	–	49,289
Deposits from customers	969,218	271,695	183,833	79,008	322	–	–	1,504,076
Debt securities and certificates of deposit in issue								
– Debt securities	–	–	–	10	1,111	–	–	1,121
Other accounts and provisions (including current and deferred tax liabilities)	36,101	14,056	1,682	2,517	6,644	–	–	61,000
Insurance contract liabilities	26,730	284	476	1,146	13,969	43,929	–	86,534
Subordinated liabilities	–	–	418	–	18,596	–	–	19,014
Liabilities associated with assets held for sale	24,404	7,694	7,467	7,186	262	–	–	47,013
Total liabilities	1,342,642	319,314	220,932	119,276	47,873	47,184	–	2,097,221
Net liquidity gap	(962,482)	(110,240)	(4,296)	236,320	642,587	337,918	90,753	230,560

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

	2015							
	On demand HK$'m	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Indefinite HK$'m	Total HK$'m
Assets								
Cash and balances with banks and other financial institutions	183,179	50,790	–	–	–	–	303	234,272
Placements with banks and other financial institutions maturing between one and twelve months	–	–	39,148	26,992	–	–	–	66,140
Financial assets at fair value through profit or loss								
– Held for trading								
– Debt securities	–	1,020	5,782	6,800	12,708	3,494	–	29,804
– Certificates of deposit	–	190	80	1,810	137	6	–	2,223
– Designated at fair value through profit or loss								
– Debt securities	–	89	307	770	6,498	12,770	–	20,434
– Certificates of deposit	–	372	–	1	268	–	–	641
– Equity securities and fund	–	–	–	–	–	–	4,495	4,495
– Others	–	180	–	–	–	–	–	180
Derivative financial instruments	12,489	2,727	2,711	18,994	5,504	786	–	43,211
Hong Kong SAR Government certificates of indebtedness	101,950	–	–	–	–	–	–	101,950
Advances and other accounts								
– Advances to customers	106,231	27,153	44,763	135,823	362,408	217,069	2,083	895,530
– Trade bills	1	8,269	8,366	15,736	–	–	–	32,372
– Advances to banks and other financial institutions	–	–	1	–	968	–	–	969
Investment in securities								
– Available-for-sale								
– Debt securities	–	19,917	83,105	59,304	137,708	60,283	–	360,317
– Certificates of deposit	–	2,305	23,450	35,571	8,328	212	–	69,866
– Held-to-maturity								
– Debt securities	–	523	3,563	13,620	43,294	20,822	3	81,825
– Certificates of deposit	–	–	–	–	–	18	–	18
– Loans and receivables								
– Debt securities	–	–	1,005	2,161	–	–	–	3,166
– Equity securities	–	–	–	–	–	–	2,746	2,746
Interests in associates and joint ventures	–	–	–	–	–	–	376	376
Investment properties	–	–	–	–	–	–	15,262	15,262
Properties, plant and equipment	–	–	–	–	–	–	50,517	50,517
Other assets (including deferred tax assets)	28,509	11,403	705	4,056	5,333	15,969	53	66,028
Assets held for sale	18,598	52,792	31,823	65,034	85,341	29,495	17,390	300,473
Total assets	450,957	177,730	244,809	386,672	668,495	360,924	93,228	2,382,815
Liabilities								
Hong Kong SAR currency notes in circulation	101,950	–	–	–	–	–	–	101,950
Deposits and balances from banks and other financial institutions	166,308	10,623	29,366	2,343	886	–	–	209,526
Financial liabilities at fair value through profit or loss	–	2,583	4,447	1,970	1,477	465	–	10,942
Derivative financial instruments	8,813	3,360	2,743	18,851	4,525	1,782	–	40,074
Deposits from customers	854,951	293,759	184,611	81,544	622	–	–	1,415,487
Debt securities and certificates of deposit in issue								
– Debt securities	–	59	–	5,739	1,178	–	–	6,976
Other accounts and provisions (including current and deferred tax liabilities)	20,348	11,969	1,479	2,702	7,322	3	–	43,823
Insurance contract liabilities	21,746	788	786	4,154	12,407	42,764	–	82,645
Subordinated liabilities	–	–	418	–	19,004	–	–	19,422
Liabilities associated with assets held for sale	93,390	68,292	40,563	42,451	7,083	26	–	251,805
Total liabilities	1,267,506	391,433	264,413	159,754	54,504	45,040	–	2,182,650
Net liquidity gap	(816,549)	(213,703)	(19,604)	226,918	613,991	315,884	93,228	200,165

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

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

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

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

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities

(a) Non-derivative cash flows

The tables below summarise the cash flows of the Group as at 31 December for non-derivative financial liabilities by remaining contractual maturity.

	2016					
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Total HK$'m
Financial liabilities						
Hong Kong SAR currency notes in circulation	**123,390**	**–**	**–**	**–**	**–**	**123,390**
Deposits and balances from banks and other financial institutions	**170,783**	**14,155**	**7,085**	**524**	**–**	**192,547**
Financial liabilities at fair value through profit or loss	**3,707**	**5,600**	**2,272**	**1,322**	**625**	**13,526**
Deposits from customers	**1,240,988**	**184,255**	**79,820**	**332**	**–**	**1,505,395**
Debt securities and certificates of deposit in issue	**–**	**–**	**39**	**1,151**	**–**	**1,190**
Subordinated liabilities	**–**	**538**	**538**	**22,077**	**–**	**23,153**
Other financial liabilities	**40,283**	**397**	**459**	**5**	**–**	**41,144**
Financial liabilities associated with assets held for sale	**32,086**	**7,446**	**7,241**	**69**	**–**	**46,842**
Total financial liabilities	**1,611,237**	**212,391**	**97,454**	**25,480**	**625**	**1,947,187**

	2015					
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Total HK$'m
Financial liabilities						
Hong Kong SAR currency notes in circulation	101,950	–	–	–	–	101,950
Deposits and balances from banks and other financial institutions	176,945	29,429	2,366	941	–	209,681
Financial liabilities at fair value through profit or loss	2,586	4,458	1,991	1,519	483	11,037
Deposits from customers	1,148,853	185,099	82,412	653	–	1,417,017
Debt securities and certificates of deposit in issue	59	–	6,072	1,262	–	7,393
Subordinated liabilities	–	538	538	23,138	–	24,214
Other financial liabilities	27,354	218	715	4	–	28,291
Financial liabilities associated with assets held for sale	161,377	40,421	42,794	6,564	26	251,182
Total financial liabilities	1,619,124	260,163	136,888	34,081	509	2,050,765

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(b) Derivative cash flows

The tables below summarise the cash flows (including assets held for sale and liabilities associated with assets held for sale) of the Group by remaining contractual maturity as at 31 December for derivative financial liabilities that will be settled on a net basis, together with all derivative financial instruments that will be settled on a gross basis regardless of whether the contract is in an asset or liability position. The amounts disclosed in the tables are the contractual undiscounted cash flows, except for certain derivatives which are disclosed at fair value.

The Group's derivative financial instruments that will be settled on a net basis mainly include interest rate swaps whereas derivative financial instruments that will be settled on a gross basis mainly include currency forwards and currency swaps.

	2016					
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Total HK$'m
Derivative financial liabilities settled on a net basis	(10,810)	(423)	(574)	(2,631)	(1,213)	(15,651)
Derivative financial instruments settled on a gross basis						
Total inflow	658,439	483,050	845,015	100,984	2,005	2,089,493
Total outflow	(650,816)	(480,202)	(844,041)	(100,928)	(2,021)	(2,078,008)

	2015					
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Total HK$'m
Derivative financial liabilities settled on a net basis	(9,198)	(543)	(860)	(2,072)	(117)	(12,790)
Derivative financial instruments settled on a gross basis						
Total inflow	547,672	344,536	1,321,500	217,775	2,582	2,434,065
Total outflow	(548,293)	(344,586)	(1,321,561)	(217,569)	(2,565)	(2,434,574)

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(c) Off-balance sheet items

Loan commitments

The contractual amounts of the Group's off-balance sheet financial instruments as at 31 December 2016 that the Group commits to extend credit to customers and other facilities amounted to HK$533,322 million (2015: HK$595,987 million). Those loan commitments can be drawn within one year.

Financial guarantees and other financial facilities

Financial guarantees and other financial facilities of the Group as at 31 December 2016 amounting to HK$51,165 million (2015: HK$69,092 million) are maturing no later than one year.

4.4 Insurance risk

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

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

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

For the in-force insurance contracts, most of the underlying insurance liabilities are related to endowment, universal life, whole life and unit-linked insurance products. For most of the insurance policies issued, the Group has a retention limit on any single life insured. The Group cedes the excess of the insured benefit over the limit to reinsurer under an excess of loss reinsurance arrangement. For some of the insurance liabilities, the Group has entered into reinsurance arrangements that reinsure most of insurance risk.

Uncertainty in the estimation of future benefit payments and premium receipts for long-term insurance contracts arises from the unpredictability of long-term changes in overall levels of mortality, morbidity and persistency. In this regard, the Group has conducted relevant experience studies. The results of such studies are considered in determining the assumptions of insurance liability which include appropriate level of prudential margins.

4. Financial risk management (continued)

4.4 Insurance risk (continued)

(A) Process used to decide on assumptions

In determining the long term business fund liabilities, the Group follows the Insurance Companies (Determination of Long Term Liabilities) Regulation and makes prudent assumptions which include appropriate margins for adverse deviation of the relevant factors. It takes account of all prospective liabilities as determined by the policy terms and conditions for each existing contract, taking credit for premiums payable after the valuation date. The determination of liability is based on current assumptions made as at the valuation date as to mortality rates, and takes into account of various appropriate discount rates, and with due regard to the reasonable expectation of policyholders. A prudent margin for adverse deviations is included in the assumptions.

The assumptions adopted for the insurance liabilities disclosed in this note are summarised as follows:

Mortality and Morbidity
The amount of liability in respect of any category of contract shall, where relevant, be determined on the basis of prudent rates of mortality and morbidity, plus a margin for adverse deviation. The assumptions used for determination of future liabilities are based on population statistics or reinsurance information, adjusted where appropriate to reflect the Group's own experience and relevant reinsurance arrangements.

Interest rates adopted for valuation purpose
Homogeneous life insurance policies are grouped into segments and are matched by specific assets. The duration of liabilities under each segment is calculated for valuation purpose.

Investment guarantee of investment contract with discretionary participating feature
The amount of the liability in respect of the investment guarantee provided by the investment contract with discretionary participation feature is determined by stochastic analysis based on historical economic data to reflect the value-at-risk at 99% confidence level.

Acquisition expense
The acquisition expense assumptions used for determination of future liabilities are based on the Group's own experience.

(B) Change in assumptions

The Group has changed the mortality assumption to reflect the Company's own experience, and the interest rates adopted for valuation purposes to reflect the changes in the market interest rates and the yields of investment portfolio backing the policy liabilities. The valuation interest rate assumptions used for the year end valuation purpose were in the range of 0 % to 3.51% in 2016 (2015: 0% to 3.45%).

4. Financial risk management (continued)

4.4 Insurance risk (continued)

(C) Sensitivity analysis

The following table presents the sensitivity of the long-term business fund liabilities to movements in the key assumptions used in the estimation of insurance liabilities:

Sensitivity analysis – life and annuity insurance contracts:

Scenario	Change in variable	Decrease in profit after tax due to changes in insurance liabilities 2016 HK$'m	2015 HK$'m
Worsening of mortality & morbidity	10%	**(84)**	(75)
Lowering of interest rate	50 basis points	**(800)**	(761)

The above analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated – for example, changes in interest rate and in market values; and changes in lapses and in future mortality.

Sensitivity analysis – Linked long term insurance contracts, Retirement scheme management category III insurance contracts, and Retirement scheme management category I investment contracts with "DPF":

The reserves on Retirement scheme management category III insurance contracts, Retirement scheme management category I investment contracts with "DPF" and non-unitised reserve on Linked long term insurance contracts are insignificant to the whole portfolio, and no sensitivity analysis has been performed. The insurance liabilities for these three components contributed to less than 0.04% of the total insurance liabilities at the balance sheet date.

For unit-linked fund liabilities (unitised reserve), the liabilities are backed by the unit-linked fund asset values.

Among linked long term insurance contracts, there are contracts with minimum guaranteed death benefits that expose the Group to the risk arising from declines in the value of underlying investments. This may increase the Group's net exposure to mortality risk.

4. Financial risk management (continued)

4.5 Capital management

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

The Group has developed and maintained a sound framework of policies and controls on capital management to support the development of the Group's business and to meet the statutory capital adequacy ratio. The ALCO monitors the Group's capital adequacy. The Group has complied with all the statutory capital requirements of the HKMA for the reported periods in respect of banking operation as further elaborated below.

The Group has adopted the foundation internal ratings-based ("FIRB") approach to calculate the credit risk capital charge for the majority of its non-securitisation exposures and the internal ratings-based (securitisation) approach to calculate the credit risk capital charge for its securitisation exposures. A small residual credit exposures which includes the credit exposures of oversea subsidiaries or branches are remained under the standardised (credit risk) ("STC") approach. The Group has adopted the standardised credit valuation adjustment ("CVA") method to calculate the capital charge for the CVA risk of the counterparty.

The Group continues to adopt the internal models ("IMM") approach to calculate the general market risk capital charge for foreign exchange and interest rate exposures and, with the approval from the HKMA, exclude its structural FX positions in the calculation of the market risk capital charge. The Group continues to adopt the standardised (market risk) ("STM") approach to calculate the market risk capital charge for the remaining exposures.

The Group continues to adopt standardised (operational risk) ("STO") approach to calculate the operational risk capital charge.

The Group has continued to adopt an internal capital adequacy assessment process ("ICAAP") to comply with the HKMA's requirements in the Supervisory Policy Manual "Supervisory Review Process" in 2016. Based on the HKMA's guidelines on Pillar II, ICAAP has been initiated to assess the extra capital needed to cover the material risks not captured or not adequately captured under Pillar I, and therefore minimum Common Equity Tier 1 capital ratio, minimum Tier 1 capital ratio and minimum Total capital ratio are determined. Meanwhile, operating ranges for the aforementioned capital ratios have also been established which enable the flexibility for future business growth and efficiency of capital utilisation. The Group considers this ICAAP as an on-going process for capital management and periodically reviews and adjusts its capital structure where appropriate in relation to the overall risk profile.

In addition, the capital plan of the Group is drawn up annually and then submitted to the Board for approval after endorsement of the ALCO. The plan is built up by assessing the implications of various factors upon capital adequacy such as the business strategies, return on equity, risk appetite, credit rating, as well as regulatory requirements. Hence, the future capital requirement is determined and capital sources are identified also. The plan is to ensure the Group maintains adequate capital and appropriate capital structure which align with its business development needs, thereby achieving an optimal balance among risk, return and capital adequacy.

4. Financial risk management (continued)

4.5 Capital management (continued)

(A) Basis of regulatory consolidation

The consolidation basis for regulatory purposes comprises the positions of BOCHK and certain subsidiaries specified by the HKMA in accordance with the Banking (Capital) Rules. For accounting purposes, subsidiaries are consolidated in accordance with HKFRSs and the list of subsidiaries is set out in "Appendix – Subsidiaries of the Company".

The Company, its subsidiaries of BOC Group Life Assurance Company Limited and BOCHK Asset Management (Cayman) Limited (including their subsidiaries), and certain subsidiaries of BOCHK are included within the accounting scope of consolidation but not included within the regulatory scope of consolidation.

The particulars of the above-mentioned subsidiaries of BOCHK are as follows:

Name	2016 Total assets HK$'m	2016 Total equity HK$'m	2015 Total assets HK$'m	2015 Total equity HK$'m
Bank of China (Hong Kong) Nominees Limited	**–**	**–**	–	–
Bank of China (Hong Kong) Trustees Limited	**10**	**10**	9	9
BOC Group Trustee Company Limited	**200**	**200**	200	200
BOCHK Information Technology (Shenzhen) Co., Ltd.	**309**	**204**	220	199
BOCHK Information Technology Services (Shenzhen) Co., Ltd.	**313**	**269**	314	270
BOCI-Prudential Trustee Limited	**457**	**429**	462	432
Che Hsing (Nominees) Limited	**1**	**1**	1	1
China Bridge (Malaysia) Sdn. Bhd.[1]	**27**	**23**	–	–
Chiyu Banking Corporation (Nominees) Limited	**139**	**139**	134	134
Grace Charter Limited	**–**	**(11)**	–	(11)
Kwong Li Nam Investment Agency Limited[2]	**–**	**–**	4	4
Nanyang Commercial Bank (Nominees) Limited[2]	**–**	**–**	1	1
Nanyang Commercial Bank Trustee Limited[2]	**–**	**–**	16	16
Po Sang Financial Investment Services Company Limited	**365**	**346**	363	345
Po Sang Securities and Futures Limited	**603**	**466**	496	454
Seng Sun Development Company, Limited	**41**	**41**	41	41
Sin Chiao Enterprises Corporation, Limited	**6**	**6**	7	7
Sin Hua Trustee Limited	**4**	**4**	5	5
Sino Information Services Company Limited[3]	**–**	**–**	8	8

Notes:
1. The acquisition of China Bridge (Malaysia) Sdn. Bhd. was completed on 17 October 2016.
2. The disposal of Kwong Li Nam Investment Agency Limited, Nanyang Commercial Bank (Nominees) Limited and Nanyang Commercial Bank Trustee Limited was completed on 30 May 2016.
3. Sino Information Services Company Limited was dissolved on 14 February 2017.

4. Financial risk management (continued)

4.5 Capital management (continued)

(A) Basis of regulatory consolidation (continued)

The principal activities of the above subsidiaries are set out in "Appendix – Subsidiaries of the Company".

There were no subsidiaries which are included within the regulatory scope of consolidation but not included within the accounting scope of consolidation as at 31 December 2016 (2015: Nil).

There were also no subsidiaries which are included within both the accounting scope of consolidation and the regulatory scope of consolidation where the methods of consolidation differ as at 31 December 2016 (2015: Nil).

(B) Capital ratio

The capital ratios are analysed as follows:

	2016	2015
CET1 capital ratio	**17.64%**	12.83%
Tier 1 capital ratio	**17.69%**	12.89%
Total capital ratio	**22.35%**	17.86%

4. Financial risk management (continued)

4.5 Capital management (continued)

(B) Capital ratio (continued)

The consolidated capital base after deductions used in the calculation of the above capital ratios is analysed as follows:

	2016 HK$'m	2015 HK$'m
CET1 capital: instruments and reserves		
Directly issued qualifying CET1 capital instruments	**43,043**	43,043
Retained earnings	**129,644**	89,915
Disclosed reserves	**41,446**	49,438
Minority interests arising from CET1 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in CET1 capital of the consolidation group)	**722**	733
CET1 capital before regulatory deductions	**214,855**	183,129
CET1 capital: regulatory deductions		
Valuation adjustments	**(78)**	(20)
Deferred tax assets net of deferred tax liabilities	**(77)**	(69)
Gains and losses due to changes in own credit risk on fair valued liabilities	**(202)**	(198)
Cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties)	**(46,443)**	(50,874)
Regulatory reserve for general banking risks	**(9,227)**	(10,879)
Total regulatory deductions to CET1 capital	**(56,027)**	(62,040)
CET1 capital	**158,828**	121,089
AT1 capital: instruments		
AT1 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in AT1 capital of the consolidation group)	**458**	561
AT1 capital	**458**	561
Tier 1 capital	**159,286**	121,650

4. Financial risk management (continued)

4.5 Capital management (continued)

(B) Capital ratio (continued)

	2016 HK$'m	2015 HK$'m
Tier 2 capital: instruments and provisions		
Capital instruments subject to phase out arrangements from Tier 2 capital	**15,435**	18,230
Tier 2 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in Tier 2 capital of the consolidation group)	**221**	226
Collective impairment allowances and regulatory reserve for general banking risks eligible for inclusion in Tier 2 capital	**5,371**	5,537
Tier 2 capital before regulatory deductions	**21,027**	23,993
Tier 2 capital: regulatory deductions		
Add back of cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties) eligible for inclusion in Tier 2 capital	**20,899**	22,893
Total regulatory deductions to Tier 2 capital	**20,899**	22,893
Tier 2 capital	**41,926**	46,886
Total capital	**201,212**	168,536

The capital buffer ratios are analysed as follows:

	2016
Capital conservation buffer ratio	**0.625%**
Higher loss absorbency ratio	**0.375%**
Countercyclical capital buffer ratio	**0.484%**

The capital conservation buffer ratio, higher loss absorbency ratio, countercyclical capital buffer ratio ("CCyB ratio") and the applicable JCCyB ratios for Hong Kong and non-Hong Kong jurisdictions for 2015 are 0% in accordance with the Banking (Capital) Rules.

The additional information of capital disclosures is available under section "Regulatory Disclosures" on the Bank's website at www.bochk.com.

4. Financial risk management (continued)

4.5 Capital management (continued)

(C) Leverage ratio

The leverage ratio is analysed as follows:

	2016 HK$'m	2015 HK$'m
Tier 1 capital	**159,286**	121,650
Leverage ratio exposure	**2,155,889**	2,268,203
Leverage ratio	**7.39%**	5.36%

The additional information of leverage ratio disclosures is available under section "Regulatory Disclosures" on the Bank's website at www.bochk.com.

5. Fair values of assets and liabilities

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy as defined in HKFRS 13, "Fair value measurement". The categorisation are determined with reference to the observability and significance of the inputs used in the valuation methods and based on the lowest level input that is significant to the fair value measurement as a whole:

– Level 1: based on quoted prices (unadjusted) in active markets for identical assets or liabilities. This category includes equity securities listed on exchange, debt instruments issued by certain governments, certain exchange-traded derivative contracts and precious metals.

– Level 2: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly. This category includes majority of the OTC derivative contracts, debt securities and certificates of deposit with quote from pricing services vendors and issued structured deposits. It also includes precious metals and properties with insignificant adjustments made to observable market inputs.

– Level 3: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable. This category includes equity investment, debt instruments and certain OTC derivative contracts with significant unobservable components. It also includes properties with significant adjustments made to observable market inputs.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value

The Group has an established governance structure and controls framework to ensure that fair values are either determined or validated by control units independent of the front offices. Control units have overall responsibility for independent verification of valuation results from front line businesses and all other significant fair value measurements. Specific controls include verification of observable pricing inputs; review and approval for new models and changes to models; calibration and back-testing of models against observed market transactions; analysis and investigation of significant daily valuation movements; review of significant unobservable inputs and valuation adjustments. Significant valuation issues are reported to senior management, Risk Committee and Audit Committee.

Generally, the unit of account for a financial instrument is the individual instrument. HKFRS 13 permits a portfolio exception, through an accounting policy election, to measure the fair value of a portfolio of financial assets and financial liabilities on the basis of the net open risk position when certain criteria are met. The Group applies valuation adjustments at an individual instrument level, consistent with that unit of account. According to its risk management policies and systems to manage derivative financial instruments, the fair value of certain derivative portfolios that meet those criteria is measured on the basis of the price to be received or paid for net open risk. Those portfolio-level adjustments are allocated to the individual assets and liabilities on the basis of the relative size of each of the individual instruments in the portfolio.

The Group uses valuation techniques or broker/dealer quotations to determine the fair value of financial instruments when unable to obtain the open market quotation in active markets.

The main parameters used in valuation techniques for financial instruments held by the Group include bond prices, interest rates, foreign exchange rates, equity and stock prices, commodity prices, volatilities, counterparty credit spreads and others, which are mostly observable and obtainable from open market.

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

The technique used to calculate the fair value of the following financial instruments is as below:

Debt securities and certificates of deposit

The fair value of these instruments is determined by obtaining quoted market prices from exchange, dealer or independent pricing service vendors or using discounted cash flow technique. Discounted cash flow model is a valuation technique that measures present value using estimated expected future cash flows from the instruments and then discounts these flows using a discount rate or discount margin that reflects the credit spreads required by the market for instruments with similar risk. These inputs are observable or can be corroborated by observable or unobservable market data.

Asset backed securities

For this class of instruments, external prices are obtained from independent third parties. The valuation of these securities, depending on the nature of transaction, is estimated from market standard cash flow models with input parameter which include spreads to discount rates, default and recovery rates and prepayment rates that may be observable or compiled through matrix pricing for similar issues.

Derivatives

OTC derivative contracts include forward, swap and option contracts on foreign exchange, interest rate, equity, commodity or credit. The fair values of these contracts are mainly measured using valuation techniques such as discounted cash flow models and option pricing models. The inputs can be observable or unobservable market data. Observable inputs include interest rate, foreign exchange rates, equity and stock prices, commodity prices, credit default swap spreads and volatilities. Unobservable inputs such as volatility surface may be used for less commonly traded option products which are embedded in structured deposits. For certain complex derivative contracts, the fair values are determined based on broker/dealer price quotations.

Credit valuation adjustments ("CVA") and debit valuation adjustments ("DVA") are applied to the Group's OTC derivatives. These adjustments reflect market factors movement, expectations of counterparty creditworthiness and the Group's own credit spread respectively. They are mainly determined for each counterparty and are dependent on expected future values of exposures, default probabilities and recovery rates.

Financial liabilities designated at fair value through profit or loss

This class of instruments includes certain deposits received from customers that are embedded with derivatives. The plain vanilla contracts are valued in the similar way described in previous debt securities section. The fair value of structured deposits is derived from the fair value of the underlying deposit by using discounted cash flow analysis taking the Group's own credit risk into account, and the fair value of the embedded derivatives determined as described in the paragraph above on derivatives.

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy

	2016			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Financial assets				
Financial assets at fair value through profit or loss (Note 23)				
– Trading assets				
– Debt securities and certificates of deposit	587	32,462	162	33,211
– Equity securities	76	–	–	76
– Others	–	5,777	–	5,777
– Financial assets designated at fair value through profit or loss				
– Debt securities and certificates of deposit	–	20,227	2,878	23,105
– Equity securities	2,008	–	–	2,008
– Fund	3,181	–	–	3,181
Derivative financial instruments (Note 24)	14,658	49,656	–	64,314
Available-for-sale securities (Note 27)				
– Debt securities and certificates of deposit	122,789	402,103	1,735	526,627
– Equity securities	3,304	237	718	4,259
– Fund	150	–	–	150
Financial liabilities				
Financial liabilities at fair value through profit or loss (Note 33)				
– Trading liabilities	–	9,946	–	9,946
– Financial liabilities designated at fair value through profit or loss	–	3,425	–	3,425
Derivative financial instruments (Note 24)	10,775	38,514	–	49,289

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy (continued)

	2015			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Financial assets				
Financial assets at fair value through profit or loss (Note 23)				
– Trading assets				
– Debt securities and certificates of deposit	1	32,026	–	32,027
– Equity securities	–	–	–	–
– Others	–	180	–	180
– Financial assets designated at fair value through profit or loss				
– Debt securities and certificates of deposit	75	19,171	1,829	21,075
– Equity securities	1,995	–	–	1,995
– Fund	2,500	–	–	2,500
Derivative financial instruments (Note 24)	12,493	30,718	–	43,211
Available-for-sale securities (Note 27)				
– Debt securities and certificates of deposit	95,982	333,106	1,095	430,183
– Equity securities	2,459	–	287	2,746
– Fund	–	–	–	–
Financial liabilities				
Financial liabilities at fair value through profit or loss (Note 33)				
– Trading liabilities	–	8,371	–	8,371
– Financial liabilities designated at fair value through profit or loss	–	2,571	–	2,571
Derivative financial instruments (Note 24)	8,936	31,138	–	40,074

There were no financial asset and liability transfers between level 1 and level 2 for the Group during the year (2015: Nil).

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items

	2016			
	Financial assets			
	Trading assets	Financial assets designated at fair value through profit or loss	Available-for-sale securities	
	Debt securities and certificates of deposit HK$'m	Debt securities and certificates of deposit HK$'m	Debt securities and certificates of deposit HK$'m	Equity securities HK$'m
At 1 January 2016	–	1,829	1,095	287
(Losses)/gains				
– Income statement				
– Net trading loss	(8)	–	–	–
– Net gain on financial instruments designated at fair value through profit or loss	–	20	–	–
– Other comprehensive income				
– Change in fair value of available-for-sale securities	–	–	(40)	17
Purchases	170	1,029	1,265	419
Sales	–	–	–	–
Transfer out of level 3	–	–	–	–
Classified as assets held for sale	–	–	(585)	(5)
At 31 December 2016	162	2,878	1,735	718
Total unrealised (losses)/gains for the year included in income statement for financial assets held as at 31 December 2016				
– Net trading loss	(8)	–	–	–
– Net gain on financial instruments designated at fair value through profit or loss	–	20	–	–
	(8)	20	–	–

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

	2015		
	Financial assets		
	Financial assets designated at fair value through profit or loss	Available-for-sale securities	
	Debt securities and certificates of deposit HK$'m	Debt securities and certificates of deposit HK$'m	Equity securities HK$'m
At 1 January 2015	1,080	907	267
(Losses)/gains			
– Income statement			
– Net loss on financial instruments designated at fair value through profit or loss	(1)	–	–
– Other comprehensive income			
– Change in fair value of available-for-sale securities	–	2	17
Purchases	901	808	8
Sales	(151)	(78)	–
Transfer out of level 3	–	(544)	–
Classified as assets held for sale	–	–	(5)
At 31 December 2015	1,829	1,095	287
Total unrealised losses for the year included in income statement for financial assets held as at 31 December 2015			
– Net loss on financial instruments designated at fair value through profit or loss	(1)	–	–

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

As at 31 December 2016 and 2015, financial instruments categorised as level 3 are mainly comprised of debt securities and certificates of deposit and unlisted equity shares.

For certain illiquid debt securities and certificates of deposit, the Group obtains valuation quotations from counterparties which may be based on unobservable inputs with significant impact on the valuation. Therefore, these instruments have been classified by the Group as level 3. The Group has established internal control procedures to control the Group's exposure to such financial instruments.

The fair values of unlisted available-for-sale equity shares are determined with reference to multiples of comparable listed companies, such as average of the price/earning ratios of comparables, or net asset value, if appropriate comparables are not available. The fair value is positively correlated to the price/earning ratios of appropriate comparables or net asset values. Had the net asset value of the underlying equity investments increased/decreased by 5%, the Group's other comprehensive income would have increased/decreased by HK$36 million (2015: HK$14 million).

5.2 Financial instruments not measured at fair value

Fair value estimates are made at a specific point in time based on relevant market information and information about various financial instruments. The following methods and assumptions have been used to estimate the fair value of each class of financial instrument as far as practicable.

Balances with/from banks and other financial institutions and trade bills

Substantially all the financial assets and liabilities mature within one year from the balance sheet date and their carrying value approximates fair value.

Advances to customers and banks and other financial institutions

Substantially all the advances to customers and banks and other financial institutions are on floating rate terms, bear interest at prevailing market interest rates and their carrying value approximates fair value.

Held-to-maturity securities

The fair value of held-to-maturity securities is determined by using the same approach as those debt securities and certificates of deposit and asset backed securities measured at fair value as described in Note 5.1.

5. Fair values of assets and liabilities (continued)

5.2 Financial instruments not measured at fair value (continued)

Loans and receivables

A discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity.

Deposits from customers

Substantially all the deposits from customers mature within one year from the balance sheet date and their carrying value approximates fair value.

Debt securities and certificates of deposit in issue

The fair value of these instruments is determined by using the same approach as those debt securities and certificates of deposit measured at fair value as described in Note 5.1.

Subordinated liabilities

Fair value for subordinated notes is based on market prices or broker/dealer price quotations.

The following tables set out the carrying values and fair values of the financial instruments not measured at fair value, except for the above with their carrying values being approximation of fair values.

	2016		2015	
	Carrying value HK$'m	**Fair value HK$'m**	Carrying value HK$'m	Fair value HK$'m
Financial assets				
Held-to-maturity securities (Note 27)	**60,194**	**60,623**	81,843	83,759
Loans and receivables (Note 27)	**935**	**935**	3,166	3,171
Financial liabilities				
Debt securities and certificates of deposit in issue (Note 35)	**1,121**	**1,126**	6,976	7,222
Subordinated liabilities (Note 39)	**19,014**	**21,143**	19,422	21,507

5. Fair values of assets and liabilities (continued)

5.2 Financial instruments not measured at fair value (continued)

The following tables show the fair value hierarchy for financial instruments with fair values disclosed.

	2016			
	Level 1 HK$'m	**Level 2 HK$'m**	**Level 3 HK$'m**	**Total HK$'m**
Financial assets				
Held-to-maturity securities	**498**	**60,125**	**–**	**60,623**
Loans and receivables	**–**	**935**	**–**	**935**
Financial liabilities				
Debt securities and certificates of deposit in issue	**–**	**1,126**	**–**	**1,126**
Subordinated liabilities	**–**	**21,143**	**–**	**21,143**

	2015			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Financial assets				
Held-to-maturity securities	1,133	82,626	–	83,759
Loans and receivables	–	3,171	–	3,171
Financial liabilities				
Debt securities and certificates of deposit in issue	–	7,222	–	7,222
Subordinated liabilities	–	21,507	–	21,507

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value

The Group uses valuation techniques or quoted market prices in active market to determine the fair value of non-financial instruments.

Investment properties and premises

The Group's properties can be divided into investment properties and premises. All of the Group's investment properties and premises were revalued as at year end. This year, the valuations were carried out by an independent firm of chartered surveyors, Knight Frank Petty Limited, who have among their staff Fellow and Members of The Hong Kong Institute of Surveyors with recent experience in the locations and categories of properties being valued. The Group's Management had discussions with the surveyors on the valuation methods, valuation assumptions and valuation results when the valuation is performed at each interim and annual reporting date. There has been no change in valuation methods during the year and the methods used are consistent with last year.

(i) Valuation methods and inputs used in Level 2 fair value measurements

The fair value of properties classified as Level 2 is determined using either the market comparison approach by reference to recent sales price of comparable properties or the income capitalisation approach by reference to market rent and capitalisation rate, with appropriate adjustments to reflect the differences between the comparable properties and the subject properties. These adjustments are considered as insignificant to the entire measurement.

The Group's properties are located in Hong Kong, major cities in the PRC and Malaysia where the property markets are considered active and transparent. Sales price, market rent and capitalisation rate of comparable properties are generally observable either directly or indirectly in these markets.

(ii) Information about Level 3 fair value measurements

The fair value of all of the Group's properties classified as Level 3, except for the bank vault, is determined using either the market comparison approach or the income capitalisation approach, adjusted for a premium or a discount specific to the features of the Group's properties compared to the comparable properties.

The fair value of the bank vault is determined using the depreciated replacement cost approach as no direct comparable is available given the specialised nature of the property. The major inputs are the market value of the existing land, the current cost of replacing the property and the depreciation rate. Appropriate adjustments are made to reflect the specialised nature of the property.

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value (continued)

Investment properties and premises (continued)

(ii) Information about Level 3 fair value measurements (continued)

The valuation methods and significant unobservable inputs used in the fair value measurement of the Group's properties classified as Level 3 are as follows:

	Valuation method	Significant unobservable inputs	Weighted average	Relationship of unobservable inputs to fair value
Bank vault	Depreciated replacement cost approach	Depreciation rate	2% (2015: 2%) per year	The higher the depreciation rate, the lower the fair value.
		Premium on specialised nature of the property	+15% (2015: +20%) to building cost	The higher the premium, the higher the fair value.
Other properties	Market comparison approach or income capitalisation approach	Premium/(discount) on features of the property compared to comparable properties	-6% (2015: -9%)	The higher the premium, the higher the fair value. The higher the discount, the lower the fair value.

Premium/(discount) on features of a property is determined after taken into account various factors, such as time for market movement, location, accessibility, building age/condition, floor level, size, layout, etc., with reference to the differences in features with comparable properties.

Precious metals

The fair values of precious metals are determined by obtaining quoted market prices in active market or market quote with certain adjustments.

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value (continued)

(A) Fair value hierarchy

	2016			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Non-financial assets				
Investment properties (Note 29)	**–**	**862**	**17,365**	**18,227**
Properties, plant and equipment (Note 30)				
– Premises	**–**	**1,659**	**41,698**	**43,357**
Other assets (Note 31)				
– Precious metals	**4,511**	**1,122**	**–**	**5,633**

	2015			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Non-financial assets				
Investment properties (Note 29)	–	627	14,635	15,262
Properties, plant and equipment (Note 30)				
– Premises	–	2,338	45,906	48,244
Other assets (Note 31)				
– Precious metals	2,105	1,569	–	3,674

There were no non-financial asset transfers between level 1 and level 2 for the Group during the year (2015: Nil).

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items

	2016	
	Non-financial assets	
		Properties, plant and equipment
	Investment properties HK$'m	Premises HK$'m
At 1 January 2016, as previously reported	14,635	45,849
Effect of merger of entity under common control	–	57
At 1 January 2016, as restated	14,635	45,906
Gains/(losses)		
– Income statement		
– Net gain from fair value adjustments on investment properties	427	–
– Net loss from revaluation of premises	–	(9)
– Other comprehensive income		
– Revaluation of premises	–	(70)
Depreciation	–	(1,021)
Additions	6	483
Disposals	–	–
Transfer into level 3	–	778
Transfer out of level 3	(215)	(167)
Reclassification	2,709	(2,709)
Exchange difference	–	(3)
Classified as assets held for sale	(197)	(1,490)
At 31 December 2016	17,365	41,698
Total unrealised gains/(losses) for the year included in income statement for non-financial assets held as at 31 December 2016		
– Net gain from fair value adjustments on investment properties	441	–
– Net loss from revaluation of premises	–	(7)
	441	(7)

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

	2015	
	Non-financial assets	
		Properties, plant and equipment
	Investment properties HK$'m	Premises HK$'m
At 1 January 2015, as previously reported	14,201	49,784
Effect of merger of entity under common control	–	26
At 1 January 2015, as restated	14,201	49,810
Gains/(losses)		
– Income statement		
– Net gain from fair value adjustments on investment properties	789	–
– Net loss from revaluation of premises	–	(136)
– Other comprehensive income		
– Revaluation of premises	–	3,438
Depreciation	–	(1,019)
Additions	43	442
Disposals	–	(363)
Transfer into level 3	199	1,698
Transfer out of level 3	(384)	(1,128)
Reclassification	202	(202)
Exchange difference	(1)	(27)
Classified as assets held for sale	(414)	(6,607)
At 31 December 2015	14,635	45,906
Total unrealised gains/(losses) for the year included in income statement for non-financial assets held as at 31 December 2015		
– Net gain from fair value adjustments on investment properties	753	–
– Net loss from revaluation of premises	–	(137)
	753	(137)

The transfer of properties into and out of level 3 is due to change in the premium/(discount) on features applied between the subject and comparable properties during the year. Premium/(discount) on features is determined with reference to differences in features between the subject properties and the comparable properties recently transacted in the market. As comparable properties that come from recent market transactions may be different in each year, the premium/(discount) on features applied between the subject and comparable properties would change from year to year accordingly. As a result, the significance of adjustments made to observable market inputs may vary and lead to the transfer of properties into and out of level 3.

6. Net interest income

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Interest income		
Due from banks and other financial institutions	**4,473**	8,138
Advances to customers	**20,945**	18,575
Investment in securities and financial assets at fair value through profit or loss	**10,276**	10,569
Others	**196**	210
	35,890	37,492
Interest expense		
Due to banks and other financial institutions	**(1,712)**	(1,896)
Deposits from customers	**(7,612)**	(9,297)
Debt securities and certificates of deposit in issue	**(318)**	(308)
Subordinated liabilities	**(594)**	(441)
Others	**(226)**	(374)
	(10,462)	(12,316)
Net interest income	**25,428**	25,176

Included within interest income is HK$5 million (2015: HK$6 million) of interest with respect to income accrued on advances classified as impaired for the year ended 31 December 2016. Interest income accrued on impaired investment in securities amounted to HK$1 million (2015: HK$3 million).

Included within interest income and interest expense are HK$35,609 million (2015: HK$37,312 million) and HK$10,945 million (2015: HK$12,871 million), before hedging effect, for financial assets and financial liabilities that are not recognised at fair value through profit or loss respectively.

7. Net fee and commission income

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Fee and commission income		
Credit card business	**3,702**	3,726
Loan commissions	**3,500**	3,239
Securities brokerage	**1,954**	3,255
Insurance	**1,630**	1,467
Funds distribution	**735**	901
Bills commissions	**631**	561
Payment services	**593**	561
Trust and custody services	**470**	473
Currency exchange	**336**	302
Safe deposit box	**277**	248
Others	**944**	839
	14,772	15,572
Fee and commission expense		
Credit card business	**(2,841)**	(2,802)
Insurance	**(292)**	(262)
Securities brokerage	**(244)**	(374)
Others	**(854)**	(861)
	(4,231)	(4,299)
Net fee and commission income	**10,541**	11,273
Of which arise from:		
Financial assets or financial liabilities not at fair value through profit or loss		
– Fee and commission income	**3,771**	3,439
– Fee and commission expense	**(34)**	(22)
	3,737	3,417
Trust and other fiduciary activities		
– Fee and commission income	**654**	654
– Fee and commission expense	**(22)**	(25)
	632	629

8. Net trading gain

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Net gain from:		
Foreign exchange and foreign exchange products	**3,618**	2,051
Interest rate instruments and items under fair value hedge	**867**	295
Commodities	**32**	57
Equity and credit derivative instruments	**88**	194
	4,605	2,597

9. Net gain on other financial assets

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Net gain on available-for-sale securities	**999**	1,275
Net gain on held-to-maturity securities	**12**	7
Others	**(5)**	4
	1,006	1,286

10. Other operating income

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Dividend income from investment in securities		
– Listed investments	**87**	90
– Unlisted investments	**45**	32
Gross rental income from investment properties	**494**	450
Less: Outgoings in respect of investment properties	**(72)**	(61)
Others	**260**	299
	814	810

Included in the "Outgoings in respect of investment properties" is HK$6 million (2015: HK$4 million) of direct operating expenses related to investment properties that were not let during the year.

11. Net insurance benefits and claims and movement in liabilities

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Gross insurance benefits and claims and movement in liabilities		
Claims, benefits and surrenders paid	**(15,561)**	(13,010)
Movement in liabilities	**(5,579)**	(10,965)
	(21,140)	(23,975)
Reinsurers' share of benefits and claims and movement in liabilities		
Reinsurers' share of claims, benefits and surrenders paid	**10,925**	5,843
Reinsurers' share of movement in liabilities	**(1,160)**	5,477
	9,765	11,320
Net insurance benefits and claims and movement in liabilities	**(11,375)**	(12,655)

12. Net charge of impairment allowances

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Advances to customers		
Individually assessed		
– New allowances	**(171)**	(505)
– Releases	**140**	93
– Recoveries	**90**	98
Net reversal/(charge) of individually assessed loan impairment allowances	**59**	(314)
Collectively assessed		
– New allowances	**(695)**	(538)
– Releases	**1**	1
– Recoveries	**46**	45
Net charge of collectively assessed loan impairment allowances	**(648)**	(492)
Net charge of loan impairment allowances	**(589)**	(806)
Others	**11**	51
Net charge of impairment allowances	**(578)**	(755)

13. Operating expenses

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Staff costs (including directors' emoluments)		
– Salaries and other costs	**6,374**	6,022
– Pension cost	**413**	398
	6,787	6,420
Premises and equipment expenses (excluding depreciation)		
– Rental of premises	**648**	609
– Information technology	**510**	412
– Others	**399**	391
	1,557	1,412
Depreciation	**1,788**	1,713
Auditor's remuneration		
– Audit services	**26**	20
– Non-audit services	**13**	11
Other operating expenses	**2,042**	2,035
	12,213	11,611

Contingent rent included in the "Rental of premises" amounted to HK$16 million during the year (2015: HK$16 million).

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

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Net gain from fair value adjustments on investment properties	**429**	774

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

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Net gain from disposal of premises	**–**	95
Net loss from disposal of equipment, fixtures and fittings	**(7)**	(26)
Net loss from revaluation of premises	**(7)**	(137)
	(14)	(68)

16. Taxation

Taxation in the income statement represents:

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Current tax		
Hong Kong profits tax		
– Current year taxation	**4,586**	4,348
– Over-provision in prior years	**(60)**	(63)
	4,526	4,285
Overseas taxation		
– Current year taxation	**390**	746
– Over-provision in prior years	**–**	(31)
	4,916	5,000
Deferred tax		
Origination and reversal of temporary differences and unused tax credits	**(294)**	(714)
	4,622	4,286

Hong Kong profits tax has been provided at the rate of 16.5% (2015: 16.5%) on the estimated assessable profits arising in Hong Kong during the year. Taxation on overseas profits has been calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the countries in which the Group operates.

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

	2016 HK$'m	2015 HK$'m
CONTINUING OPERATIONS		
Profit before taxation	**29,452**	28,575
Calculated at a taxation rate of 16.5% (2015: 16.5%)	**4,860**	4,715
Effect of different taxation rates in other countries	**19**	22
Income not subject to taxation	**(242)**	(320)
Expenses not deductible for taxation purposes	**43**	110
Tax losses not recognised	**1**	–
Over-provision in prior years	**(60)**	(94)
Foreign withholding tax	**1**	(147)
Taxation charge	**4,622**	4,286
Effective tax rate	**15.7%**	15.0%

17. Dividends

	2016		2015	
	Per share HK$	**Total HK$'m**	Per share HK$	Total HK$'m
Interim dividend paid	**0.545**	**5,762**	0.545	5,762
Special dividend paid	**0.710**	**7,507**	–	–
Proposed final dividend	**0.625**	**6,608**	0.679	7,179
	1.880	**19,877**	1.224	12,941

At a meeting held on 30 August 2016, the Board declared an interim dividend of HK$0.545 per ordinary share for the first half of 2016 amounting to approximately HK$5,762 million and special dividend of HK$0.710 per ordinary share amounting to approximately HK$7,507 million.

At a meeting held on 31 March 2017, the Board proposed to recommend to the Annual General Meeting on 28 June 2017 a final dividend of HK$0.625 per ordinary share for the year ended 31 December 2016 amounting to approximately HK$6,608 million. This proposed final dividend is not reflected as a dividend payable in these financial statements, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2017.

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

The calculation of basic earnings per share for the year ended 31 December 2016 is based on the consolidated profit for the year and profit from continuing operations attributable to the equity holders of the Company of approximately HK$55,503 million and HK$24,201 million (2015: HK$26,982 million and HK$23,757 million) respectively and on the ordinary shares in issue of 10,572,780,266 shares (2015: 10,572,780,266 ordinary shares).

There was no dilution of earnings per share as no potential ordinary shares were in issue for the year ended 31 December 2016 (2015: Nil).

19. Retirement benefit costs

Retirement benefits are provided to eligible employees of the Group. In Hong Kong, defined contribution schemes for the Group's employees are ORSO schemes exempted under the MPF Schemes Ordinance and the BOC-Prudential Easy Choice MPF Scheme.

Under the ORSO schemes, employees make monthly contributions to the ORSO schemes equal to 5% of their basic salaries, while the employer makes monthly contributions equal to 5% to 15% of the employees' monthly basic salaries, depending on years of service. The employees are entitled to receive 100% of the employer's contributions upon retirement, early retirement or termination of employment after completing 10 years of service. Employees with 3 to 9 years of service are entitled to receive the employer's contributions at a scale ranging from 30% to 90% upon termination of employment for other reasons other than summary dismissal. All employer's contributions received by employee are subject to MPF Schemes Ordinance.

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

19. Retirement benefit costs (continued)

The Group's total contributions made to the ORSO schemes for the year ended 31 December 2016 amounted to approximately HK$354 million (2015: approximately HK$367 million), after a deduction of forfeited contributions of approximately HK$9 million (2015: approximately HK$9 million). For the MPF Scheme, the Group contributed approximately HK$85 million (2015: approximately HK$83 million) for the year ended 31 December 2016.

20. Directors', senior management's and key personnel's emoluments

(a) Directors' and senior management's emoluments

(i) Directors' emoluments

Details of the emoluments paid to or receivable by the directors of the Company in respect of their services rendered for the Company and managing the subsidiaries within the Group during the year are as follows:

	2016			
	Directors' fee HK$'000	Basic salaries, allowances and benefits in kind HK$'000	Bonus HK$'000	Total HK$'000
Executive Directors				
YUE Yi (Chief Executive)	–	6,750	3,953	10,703
LI Jiuzhong	–	4,480	2,311	6,791
	–	11,230	6,264	17,494
Non-executive Directors				
TIAN Guoli	–	–	–	–
CHEN Siqing	–	–	–	–
REN Deqi	–	–	–	–
GAO Yingxin	–	–	–	–
XU Luode	–	–	–	–
CHENG Eva*	300	–	–	300
CHOI Koon Shum* Note 1	199	–	–	199
KOH Beng Seng*	450	–	–	450
TUNG Savio Wai-Hok*	528	–	–	528
SHAN Weijian* Note 2	173	–	–	173
	1,650	–	–	1,650
	1,650	11,230	6,264	19,144

Note 1: Appointed during the year.
Note 2: Retired during the year.

20. Directors', senior management's and key personnel's emoluments (continued)

(a) Directors' and senior management's emoluments (continued)

(i) Directors' emoluments (continued)

	2015			
	Directors' fee HK$'000	Basic salaries, allowances and benefits in kind HK$'000	Bonus HK$'000	Total HK$'000
Executive Directors				
YUE Yi (Chief Executive)	–	5,246	3,107	8,353
HE Guangbei (Chief Executive)	91	1,893	1,123	3,107
GAO Yingxin	67	1,163	656	1,886
LI Jiuzhong	–	3,284	2,222	5,506
	158	11,586	7,108	18,852
Non-executive Directors				
TIAN Guoli	–	–	–	–
CHEN Siqing	–	–	–	–
YUE Yi	–	–	–	–
REN Deqi	–	–	–	–
GAO Yingxin	–	–	–	–
XU Luode	–	–	–	–
LI Zaohang	–	–	–	–
ZHU Shumin	–	–	–	–
CHENG Eva*	300	–	–	300
KOH Beng Seng*	450	–	–	450
TUNG Savio Wai-Hok*	500	–	–	500
SHAN Weijian*	400	–	–	400
	1,650	–	–	1,650
	1,808	11,586	7,108	20,502

* Independent Non-executive Directors

There were no directors waived emoluments for the year ended 31 December 2016 (2015: Nil).

20. Directors', senior management's and key personnel's emoluments (continued)

(a) Directors' and senior management's emoluments (continued)

(ii) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include two (2015: two) directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining three (2015: three) individuals during the year are as follows:

	2016 HK$'m	2015 HK$'m
Basic salaries and allowances	**11**	11
Bonus	**8**	7
Contributions to pension schemes	**1**	1
	20	19

Emoluments paid to or receivable by individuals during the year with reference to their tenure are within the following bands:

	Number of individuals	
	2016	2015
HK$6,000,001 to HK$6,500,000	**1**	3
HK$6,500,001 to HK$7,000,000	**2**	–

(iii) Senior management's emoluments

Emoluments paid to or receivable by individuals during the year with reference to their tenure as senior management are within the following bands:

	Number of individuals	
	2016	2015
HK$500,001 to HK$1,000,000	**–**	1
HK$1,000,001 to HK$1,500,000	**–**	2
HK$1,500,001 to HK$2,000,000	**–**	3
HK$2,000,001 to HK$2,500,000	**–**	1
HK$3,000,001 to HK$3,500,000	**–**	2
HK$4,500,001 to HK$5,000,000	**1**	–
HK$5,000,001 to HK$5,500,000	**2**	2
HK$5,500,001 to HK$6,000,000	**1**	–
HK$6,000,001 to HK$6,500,000	**–**	1
HK$6,500,001 to HK$7,000,000	**2**	–
HK$8,000,001 to HK$8,500,000	**–**	1
HK$10,500,001 to HK$11,000,000	**1**	–

20. Directors', senior management's and key personnel's emoluments (continued)

(b) Remuneration for Senior Management and Key Personnel under CG-5

Pursuant to CG-5 Guideline on a Sound Remuneration System issued by the HKMA, details of the remuneration for Senior Management and Key Personnel of the Group during the year are as follows:

(i) Remuneration awarded during the year

	2016					
	Senior Management			Key Personnel		
	Non-deferred HK$'m	Deferred HK$'m	Total HK$'m	Non-deferred HK$'m	Deferred HK$'m	Total HK$'m
Fixed remuneration						
Cash	**36**	**–**	**36**	**60**	**–**	**60**
Variable remuneration						
Cash	**13**	**5**	**18**	**29**	**9**	**38**
	49	**5**	**54**	**89**	**9**	**98**

	2015					
	Senior Management			Key Personnel		
	Non-deferred HK$'m	Deferred HK$'m	Total HK$'m	Non-deferred HK$'m	Deferred HK$'m	Total HK$'m
Fixed remuneration						
Cash	34	–	34	55	–	55
Variable remuneration						
Cash	14	3	17	28	10	38
	48	3	51	83	10	93

The remuneration above includes 10 (2015: 15) members of Senior Management and 26 (2015: 23) members of Key Personnel.

20. Directors', senior management's and key personnel's emoluments (continued)

(b) Remuneration for Senior Management and Key Personnel under CG-5 (continued)

(ii) Deferred remuneration

	2016		2015	
	Senior Management HK$'m	**Key Personnel HK$'m**	Senior Management HK$'m	Key Personnel HK$'m
Deferred remuneration				
Vested	**4**	**9**	5	7
Unvested	**9**	**18**	8	18
	13	**27**	13	25
At 1 January	**8**	**18**	10	15
Awarded	**5**	**9**	3	10
Paid out	**(4)**	**(9)**	(5)	(7)
Reduced through performance adjustments	**–**	**–**	–	–
At 31 December	**9**	**18**	8	18

For the purpose of disclosure, Senior Management and Key Personnel mentioned in this section are defined according to the HKMA's Guideline on a Sound Remuneration System.

– Senior Management: The senior executives designated by the Board who are responsible for oversight of the firm-wide strategy or material business lines, including Chief Executive, Deputy Chief Executives, Chief Financial Officer, Chief Risk Officer, Chief Operating Officer, Board Secretary and General Manager of Group Audit.

– Key Personnel: The employees whose individual business activities involve the assumption of material risk which may have significant impact on risk exposure, or whose individual responsibilities are directly and materially linked to the risk management, or those who have direct influence to the profit, including heads of material business lines, heads of major subsidiaries and overseas institutions, head of trading, as well as heads of risk control functions.

21. Cash and balances with banks and other financial institutions

	2016 HK$'m	2015 HK$'m
Cash	**12,709**	7,953
Balances with central banks	**69,082**	110,473
Balances with banks and other financial institutions	**42,744**	65,056
Placements with central banks maturing within one month	**4,075**	2,056
Placements with banks and other financial institutions maturing within one month	**100,463**	48,734
	229,073	234,272

22. Placements with banks and other financial institutions maturing between one and twelve months

	2016 HK$'m	2015 HK$'m
Placements with central banks maturing between one and twelve months	**156**	–
Placements with banks and other financial institutions maturing between one and twelve months	**70,236**	66,140
	70,392	66,140

23. Financial assets at fair value through profit or loss

	Trading assets		Financial assets designated at fair value through profit or loss		Total	
	2016 HK$'m	2015 HK$'m	2016 HK$'m	2015 HK$'m	2016 HK$'m	2015 HK$'m
At fair value						
Treasury bills	**10,448**	9,504	**–**	–	**10,448**	9,504
Other debt securities	**20,620**	20,300	**22,957**	20,434	**43,577**	40,734
	31,068	29,804	**22,957**	20,434	**54,025**	50,238
Certificates of deposit	**2,143**	2,223	**148**	641	**2,291**	2,864
Total debt securities and certificates of deposit	**33,211**	32,027	**23,105**	21,075	**56,316**	53,102
Equity securities	**76**	–	**2,008**	1,995	**2,084**	1,995
Fund	**–**	–	**3,181**	2,500	**3,181**	2,500
Total securities	**33,287**	32,027	**28,294**	25,570	**61,581**	57,597
Others	**5,777**	180	**–**	–	**5,777**	180
	39,064	32,207	**28,294**	25,570	**67,358**	57,777

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

Total securities are analysed by place of listing as follows:

	Trading assets		Financial assets designated at fair value through profit or loss	
	2016 HK$'m	2015 HK$'m	**2016 HK$'m**	2015 HK$'m
Debt securities and certificates of deposit				
– Listed in Hong Kong	**10,913**	11,650	**5,861**	5,841
– Listed outside Hong Kong	**4,096**	3,993	**9,953**	8,570
	15,009	15,643	**15,814**	14,411
– Unlisted	**18,202**	16,384	**7,291**	6,664
	33,211	32,027	**23,105**	21,075
Equity securities				
– Listed in Hong Kong	**76**	–	**1,624**	1,436
– Listed outside Hong Kong	**–**	–	**384**	559
	76	–	**2,008**	1,995
Fund				
– Unlisted	**–**	–	**3,181**	2,500
Total securities	**33,287**	32,027	**28,294**	25,570

Total securities are analysed by type of issuer as follows:

	Trading assets		Financial assets designated at fair value through profit or loss	
	2016 HK$'m	2015 HK$'m	**2016 HK$'m**	2015 HK$'m
Sovereigns	**21,473**	18,802	**1,247**	1,529
Public sector entities*	**660**	607	**–**	–
Banks and other financial institutions	**7,720**	6,914	**18,421**	15,447
Corporate entities	**3,434**	5,704	**8,626**	8,594
Total securities	**33,287**	32,027	**28,294**	25,570

* Included trading assets of HK$660 million (2015: HK$607 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

24. Derivative financial instruments and hedge accounting

The Group enters into exchange rate, interest rate, commodity, equity and credit related derivative financial instrument contracts for trading and risk management purposes.

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

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

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

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

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments

The Group trades derivative products (both exchange-traded or OTC) mainly for customer business. The Group strictly follows risk management policies and requirement in providing derivative products to our customers and in trading of derivative products in the interbank market.

Derivatives are also used to manage the interest rate risk of the banking book. A derivative instrument must be included in the approved product list before any transactions for that instrument can be made. There are limits to control the notional amount of exposure arising from derivative transactions, and the maximum tenor of the deal is set. Every derivative transaction must be input into the relevant system for settlement, mark-to-market revaluation, reporting and control.

The following tables summarise the contract/notional amounts of each class of derivative financial instrument (excluding assets held for sale and liabilities associated with assets held for sale) as at 31 December:

	2016			
	Trading HK$'m	Hedging HK$'m	Not qualified for hedge accounting HK$'m	Total HK$'m
Exchange rate contracts				
Spot, forwards and futures	317,796	–	8,434	326,230
Swaps	1,825,313	–	14,067	1,839,380
Foreign currency options				
– Options purchased	19,901	–	–	19,901
– Options written	22,128	–	–	22,128
	2,185,138	–	22,501	2,207,639
Interest rate contracts				
Futures	2,543	–	–	2,543
Swaps	748,737	124,266	2,807	875,810
	751,280	124,266	2,807	878,353
Commodity contracts	26,091	–	–	26,091
Equity contracts	4,628	–	–	4,628
Credit derivative contracts	388	–	–	388
	2,967,525	124,266	25,308	3,117,099

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

	2015			
	Trading HK$'m	Hedging HK$'m	Not qualified for hedge accounting HK$'m	Total HK$'m
Exchange rate contracts				
Spot, forwards and futures	321,958	–	4,675	326,633
Swaps	2,063,424	–	15,863	2,079,287
Foreign currency options				
– Options purchased	31,947	–	–	31,947
– Options written	32,821	–	–	32,821
	2,450,150	–	20,538	2,470,688
Interest rate contracts				
Futures	2,700	–	–	2,700
Swaps	397,099	77,144	2,416	476,659
	399,799	77,144	2,416	479,359
Commodity contracts	6,905	–	–	6,905
Equity contracts	3,348	–	–	3,348
Credit derivative contracts	–	–	–	–
	2,860,202	77,144	22,954	2,960,300

Not qualified for hedge accounting: derivative contracts which do not qualify as hedges for accounting purposes but are managed in conjunction with the financial instruments designated at fair value through profit or loss are separately disclosed in compliance with the requirements set out in the Banking (Disclosure) Rules.

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

The following tables summarise the fair values of each class of derivative financial instrument (excluding assets held for sale and liabilities associated with assets held for sale) as at 31 December:

	2016							
	Fair value assets				Fair value liabilities			
	Trading HK$'m	Hedging HK$'m	Not qualified for hedge accounting HK$'m	Total HK$'m	Trading HK$'m	Hedging HK$'m	Not qualified for hedge accounting HK$'m	Total HK$'m
Exchange rate contracts								
Spot, forwards and futures	17,612	–	7	17,619	(11,487)	–	(22)	(11,509)
Swaps	38,468	–	1	38,469	(31,237)	–	(68)	(31,305)
Foreign currency options								
– Options purchased	349	–	–	349	–	–	–	–
– Options written	–	–	–	–	(391)	–	–	(391)
	56,429	–	8	56,437	(43,115)	–	(90)	(43,205)
Interest rate contracts								
Futures	1	–	–	1	(8)	–	–	(8)
Swaps	3,755	2,797	3	6,555	(4,249)	(1,065)	(6)	(5,320)
	3,756	2,797	3	6,556	(4,257)	(1,065)	(6)	(5,328)
Commodity contracts	1,240	–	–	1,240	(675)	–	–	(675)
Equity contracts	78	–	–	78	(81)	–	–	(81)
Credit derivative contracts	3	–	–	3	–	–	–	–
	61,506	2,797	11	64,314	(48,128)	(1,065)	(96)	(49,289)

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

	2015							
	Fair value assets				Fair value liabilities			
	Trading HK$'m	Hedging HK$'m	Not qualified for hedge accounting HK$'m	Total HK$'m	Trading HK$'m	Hedging HK$'m	Not qualified for hedge accounting HK$'m	Total HK$'m
Exchange rate contracts								
Spot, forwards and futures	15,781	–	20	15,801	(9,689)	–	–	(9,689)
Swaps	22,817	–	87	22,904	(25,870)	–	–	(25,870)
Foreign currency options								
– Options purchased	513	–	–	513	–	–	–	–
– Options written	–	–	–	–	(487)	–	–	(487)
	39,111	–	107	39,218	(36,046)	–	–	(36,046)
Interest rate contracts								
Futures	3	–	–	3	(1)	–	–	(1)
Swaps	1,640	1,877	–	3,517	(2,108)	(1,516)	(27)	(3,651)
	1,643	1,877	–	3,520	(2,109)	(1,516)	(27)	(3,652)
Commodity contracts	392	–	–	392	(294)	–	–	(294)
Equity contracts	81	–	–	81	(82)	–	–	(82)
Credit derivative contracts	–	–	–	–	–	–	–	–
	41,227	1,877	107	43,211	(38,531)	(1,516)	(27)	(40,074)

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

The table below gives the credit risk-weighted amounts of the derivative financial instruments (including assets held for sale) and is prepared with reference to the completion instructions for the HKMA return of capital adequacy ratio.

	2016 HK$'m	2015 HK$'m
Exchange rate contracts		
Spot, forwards and futures	**4,050**	2,237
Swaps	**11,277**	10,614
Foreign currency options		
– Options purchased	**329**	361
	15,656	13,212
Interest rate contracts		
Futures	**–**	1
Swaps	**494**	656
	494	657
Commodity contracts	**53**	2
Equity contracts	**191**	181
Credit derivative contracts	**17**	–
	16,411	14,052

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

The total fair values of derivatives subject to valid bilateral netting agreements for the Group amounted to HK$39,436 million (2015: HK$11,332 million) and the effect of valid bilateral netting agreements amounted to HK$29,477 million (2015: HK$9,682 million).

(b) Hedge accounting

The fair values of derivative financial instruments designated as hedging instruments as at 31 December are as follows:

	2016		2015	
	Assets HK$'m	Liabilities HK$'m	Assets HK$'m	Liabilities HK$'m
Fair value hedges	**2,797**	**(1,065)**	1,877	(1,516)

24. Derivative financial instruments and hedge accounting (continued)

(b) Hedge accounting (continued)

The Group uses interest rate swaps to hedge against change in fair value of financial assets and liabilities arising from movements in market interest rates.

Gains or losses on fair value hedges reflected in net trading gain for the year are as follows:

	2016		2015	
	Hedged assets HK$'m	**Hedged liabilities HK$'m**	Hedged assets HK$'m	Hedged liabilities HK$'m
Net gain/(loss)				
– Hedging instruments	**1,962**	**(487)**	(356)	(278)
– Hedged items	**(1,372)**	**483**	622	284
	590	**(4)**	266	6

25. Advances and other accounts

	2016 HK$'m	2015 HK$'m
Personal loans and advances	**291,925**	275,103
Corporate loans and advances	**681,146**	623,510
Advances to customers	**973,071**	898,613
Loan impairment allowances (Note 26)		
– Individually assessed	**(449)**	(578)
– Collectively assessed	**(2,675)**	(2,505)
	969,947	895,530
Trade bills	**16,174**	32,372
Advances to banks and other financial institutions	**6,016**	969
	992,137	928,871

As at 31 December 2016, advances to customers included accrued interest of HK$1,273 million (2015: HK$1,444 million).

As at 31 December 2016, no impairment allowance was made in respect of trade bills and advances to banks and other financial institutions (2015: Nil).

26. Loan impairment allowances

	2016		
	Individually assessed		
	Personal HK$'m	Corporate HK$'m	Total HK$'m
At 1 January 2016, as previously reported	8	556	564
Effect of merger of entity under common control	1	13	14
At 1 January 2016, as restated	9	569	578
Credited to income statement	(4)	(18)	(22)
Loans written off during the year as uncollectible	(3)	(107)	(110)
Recoveries	7	90	97
Unwind of discount on impairment allowances	–	(6)	(6)
Exchange difference	–	(5)	(5)
Classified as assets held for sale	–	(83)	(83)
At 31 December 2016	9	440	449

	2016		
	Collectively assessed		
	Personal HK$'m	Corporate HK$'m	Total HK$'m
At 1 January 2016, as previously reported	274	2,171	2,445
Effect of merger of entity under common control	4	56	60
At 1 January 2016, as restated	278	2,227	2,505
Charged to income statement	393	282	675
Loans written off during the year as uncollectible	(408)	(5)	(413)
Recoveries	46	–	46
Exchange difference	–	1	1
Classified as assets held for sale	(5)	(134)	(139)
At 31 December 2016	304	2,371	2,675

26. Loan impairment allowances (continued)

	2015		
	Individually assessed		
	Personal HK$'m	Corporate HK$'m	Total HK$'m
At 1 January 2015, as previously reported	26	1,070	1,096
Effect of merger of entity under common control	–	2	2
At 1 January 2015, as restated	26	1,072	1,098
Charged to income statement	12	1,254	1,266
Loans written off during the year as uncollectible	(16)	(1,384)	(1,400)
Recoveries	7	123	130
Unwind of discount on impairment allowances	–	(15)	(15)
Exchange difference	(2)	(66)	(68)
Classified as assets held for sale	(18)	(415)	(433)
At 31 December 2015	9	569	578

	2015		
	Collectively assessed		
	Personal HK$'m	Corporate HK$'m	Total HK$'m
At 1 January 2015, as previously reported	360	3,160	3,520
Effect of merger of entity under common control	4	45	49
At 1 January 2015, as restated	364	3,205	3,569
Charged/(credited) to income statement	436	(64)	372
Loans written off during the year as uncollectible	(495)	(3)	(498)
Recoveries	45	–	45
Exchange difference	(8)	(23)	(31)
Classified as assets held for sale	(64)	(888)	(952)
At 31 December 2015	278	2,227	2,505

27. Investment in securities

	2016			
	At fair value	At amortised cost		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m	Total HK$'m
Treasury bills	**142,263**	**–**	**–**	**142,263**
Other debt securities	**327,461**	**60,176**	**935**	**388,572**
	469,724	**60,176**	**935**	**530,835**
Certificates of deposit	**56,903**	**18**	**–**	**56,921**
Total debt securities and certificates of deposit	**526,627**	**60,194**	**935**	**587,756**
Equity securities	**4,259**	**–**	**–**	**4,259**
Fund	**150**	**–**	**–**	**150**
	531,036	**60,194**	**935**	**592,165**

	2015			
	At fair value	At amortised cost		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m	Total HK$'m
Treasury bills	124,306	–	–	124,306
Other debt securities	236,011	81,825	3,166	321,002
	360,317	81,825	3,166	445,308
Certificates of deposit	69,866	18	–	69,884
Total debt securities and certificates of deposit	430,183	81,843	3,166	515,192
Equity securities	2,746	–	–	2,746
Fund	–	–	–	–
	432,929	81,843	3,166	517,938

27. Investment in securities (continued)

Investment in securities is analysed by place of listing as follows:

	2016		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
Debt securities and certificates of deposit			
– Listed in Hong Kong	**55,218**	**8,214**	**–**
– Listed outside Hong Kong	**168,241**	**24,040**	**–**
	223,459	**32,254**	**–**
– Unlisted	**303,168**	**27,940**	**935**
	526,627	**60,194**	**935**
Equity securities			
– Listed in Hong Kong	**2,906**	**–**	**–**
– Listed outside Hong Kong	**635**	**–**	**–**
– Unlisted	**718**	**–**	**–**
	4,259	**–**	**–**
Fund			
– Unlisted	**150**	**–**	**–**
	531,036	**60,194**	**935**
Market value of listed held-to-maturity securities		**32,483**	

	2015		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
Debt securities and certificates of deposit			
– Listed in Hong Kong	39,490	6,974	–
– Listed outside Hong Kong	112,363	32,804	–
	151,853	39,778	–
– Unlisted	278,330	42,065	3,166
	430,183	81,843	3,166
Equity securities			
– Listed in Hong Kong	2,459	–	–
– Listed outside Hong Kong	–	–	–
– Unlisted	287	–	–
	2,746	–	–
Fund	–	–	–
	432,929	81,843	3,166
Market value of listed held-to-maturity securities		40,021	

27. Investment in securities (continued)

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

	2016		
	Available-for-sale securities HK$'m	**Held-to-maturity securities HK$'m**	**Loans and receivables HK$'m**
Sovereigns	**187,059**	**498**	**–**
Public sector entities*	**29,819**	**11,608**	**–**
Banks and other financial institutions	**214,576**	**27,248**	**935**
Corporate entities	**99,582**	**20,840**	**–**
	531,036	**60,194**	**935**

	2015		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
Sovereigns	155,327	1,557	–
Public sector entities*	18,498	19,011	–
Banks and other financial institutions	177,429	33,871	3,166
Corporate entities	81,675	27,404	–
	432,929	81,843	3,166

* Included available-for-sale securities of HK$25,171 million (2015: HK$17,491 million) and held-to-maturity securities of HK$4,086 million (2015: HK$4,614 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

27. Investment in securities (continued)

The movements in investment in securities are summarised as follows:

	2016		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
At 1 January 2016, as previously reported	**432,929**	**81,126**	**3,166**
Effect of merger of entity under common control	**–**	**717**	**–**
At 1 January 2016, as restated	**432,929**	**81,843**	**3,166**
Additions	**759,064**	**9,679**	**2,230**
Disposals, redemptions and maturity	**(641,226)**	**(29,031)**	**(4,080)**
Amortisation	**(260)**	**(163)**	**21**
Change in fair value	**(1,471)**	**–**	**–**
Net reversal of impairment allowances	**–**	**–**	**–**
Reclassification	**1,437**	**(1,437)**	**–**
Exchange difference	**(6,581)**	**(697)**	**129**
Classified as assets held for sale	**(12,856)**	**–**	**(531)**
At 31 December 2016	**531,036**	**60,194**	**935**

	2015		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
At 1 January 2015, as previously reported	357,110	76,848	4,868
Effect of merger of entity under common control	–	826	–
At 1 January 2015, as restated	357,110	77,674	4,868
Additions	702,242	14,351	9,557
Disposals, redemptions and maturity	(558,836)	(15,089)	(9,839)
Amortisation	(608)	220	(15)
Change in fair value	(244)	–	–
Net reversal of impairment allowances	–	1	–
Reclassification	(8,967)	8,967	–
Exchange difference	(5,713)	(1,815)	(819)
Classified as assets held for sale	(52,055)	(2,466)	(586)
At 31 December 2015	432,929	81,843	3,166

27. Investment in securities (continued)

The Group reclassified certain debt securities with fair value of HK$1,828 million (2015: HK$8,967 million) out of available-for-sale category into held-to-maturity category during the year. The Group had the intention and ability to hold these reclassified debt securities until maturity at the date of reclassification.

In order to align with the Group's asset liability matching, certain debt securities with amortised cost of HK$3,265 million (2015: Nil) were reclassified out of held-to-maturity category into available-for-sale category during the year.

28. Interests in associates and joint ventures

	2016 HK$'m	2015 HK$'m
At 1 January	**376**	324
Share of results	**96**	72
Share of tax	**(22)**	(18)
Dividend received	**(2)**	(2)
Derecognition	**(129)**	–
At 31 December	**319**	376

The particulars of the Group's associates and joint ventures, all of which are unlisted, are as follows:

Name	**Place of incorporation and operation**	**Issued share capital/ registered capital**	**Interest held**	**Principal activities**
Associates:				
BOC Services Company Limited	PRC	Registered capital RMB50,000,000	45%	Credit card back-end service support
Joint Ventures:				
Joint Electronic Teller Services Limited	Hong Kong	Ordinary shares HK$10,025,300	19.96%	Operation of a private inter-bank message switching network in respect of ATM services

As interest held has been changed on 27 October 2016, BOC Expresspay Company Limited is no longer an associate of the Group.

	Associates		**Joint ventures**	
	2016 HK$'m	2015 HK$'m	**2016 HK$'m**	2015 HK$'m
Interests in associates/joint ventures	**256**	315	**63**	61
Share of profit/total comprehensive income for the year of associates/joint ventures	**69**	51	**5**	3

29. Investment properties

	2016 HK$'m	2015 HK$'m
At 1 January	**15,262**	14,559
Additions	**6**	47
Fair value gains	**415**	826
Reclassification from properties, plant and equipment (Note 30)	**2,748**	245
Exchange difference	**–**	(1)
Classified as assets held for sale	**(204)**	(414)
At 31 December	**18,227**	15,262

The carrying value of investment properties is analysed based on the remaining terms of the leases as follows:

	2016 HK$'m	2015 HK$'m
Held in Hong Kong		
On long-term lease (over 50 years)	**4,153**	3,724
On medium-term lease (10 to 50 years)	**13,799**	11,312
Held outside Hong Kong		
On long-term lease (over 50 years)	**59**	–
On medium-term lease (10 to 50 years)	**194**	207
On short-term lease (less than 10 years)	**22**	19
	18,227	15,262

As at 31 December 2016, investment properties were included in the balance sheet at valuation carried out at 31 December 2016 on the basis of their fair value by an independent firm of chartered surveyors, Knight Frank Petty Limited. The fair value represents the price that would be received to sell each investment property in an orderly transaction with market participants at the measurement date.

30. Properties, plant and equipment

	Premises HK$'m	Equipment, fixtures and fittings HK$'m	Total HK$'m
Net book value at 1 January 2016, as previously reported	**48,187**	**2,246**	**50,433**
Effect of merger of entity under common control	**57**	**27**	**84**
Net book value at 1 January 2016, as restated	**48,244**	**2,273**	**50,517**
Additions	**560**	**914**	**1,474**
Disposals	**(1)**	**(8)**	**(9)**
Revaluation	**(144)**	**–**	**(144)**
Depreciation for the year	**(1,060)**	**(754)**	**(1,814)**
Reclassification to investment properties (Note 29)	**(2,748)**	**–**	**(2,748)**
Exchange difference	**(4)**	**(6)**	**(10)**
Classified as assets held for sale	**(1,490)**	**(44)**	**(1,534)**
Net book value at 31 December 2016	**43,357**	**2,375**	**45,732**
At 31 December 2016			
Cost or valuation	**43,357**	**8,193**	**51,550**
Accumulated depreciation and impairment	**–**	**(5,818)**	**(5,818)**
Net book value at 31 December 2016	**43,357**	**2,375**	**45,732**
The analysis of cost or valuation of the above assets is as follows:			
At 31 December 2016			
At cost	**–**	**8,193**	**8,193**
At valuation	**43,357**	**–**	**43,357**
	43,357	**8,193**	**51,550**
Net book value at 1 January 2015, as previously reported	52,639	2,568	55,207
Effect of merger of entity under common control	26	17	43
Net book value at 1 January 2015, as restated	52,665	2,585	55,250
Additions	456	786	1,242
Disposals	(371)	(27)	(398)
Revaluation	3,516	–	3,516
Depreciation for the year	(1,072)	(778)	(1,850)
Reclassification to investment properties (Note 29)	(245)	–	(245)
Exchange difference	(27)	(11)	(38)
Classified as assets held for sale	(6,678)	(282)	(6,960)
Net book value at 31 December 2015	48,244	2,273	50,517
At 31 December 2015			
Cost or valuation	48,244	7,658	55,902
Accumulated depreciation and impairment	–	(5,385)	(5,385)
Net book value at 31 December 2015	48,244	2,273	50,517
The analysis of cost or valuation of the above assets is as follows:			
At 31 December 2015			
At cost	–	7,658	7,658
At valuation	48,244	–	48,244
	48,244	7,658	55,902

30. Properties, plant and equipment (continued)

The carrying value of premises is analysed based on the remaining terms of the leases as follows:

	2016 HK$'m	2015 HK$'m
Held in Hong Kong		
On long-term lease (over 50 years)	**13,821**	15,934
On medium-term lease (10 to 50 years)	**29,212**	31,963
Held outside Hong Kong		
On long-term lease (over 50 years)	**4**	94
On medium-term lease (10 to 50 years)	**256**	196
On short-term lease (less than 10 years)	**64**	57
	43,357	48,244

As at 31 December 2016, premises were included in the balance sheet at valuation carried out at 31 December 2016 on the basis of their fair value by an independent firm of chartered surveyors, Knight Frank Petty Limited. The fair value represents the price that would be received to sell each premises in an orderly transaction with market participants at the measurement date.

As a result of the above-mentioned revaluations, changes in value of the premises were recognised in the premises revaluation reserve, the income statement and non-controlling interests as follows:

	2016 HK$'m	2015 HK$'m
(Decrease)/increase in valuation (charged)/credited to premises revaluation reserve	**(123)**	3,621
Decrease in valuation charged to income statement	**(9)**	(136)
(Decrease)/increase in valuation (charged)/credited to non-controlling interests	**(12)**	31
	(144)	3,516

As at 31 December 2016, the net book value of premises that would have been included in the Group's balance sheet had the premises been carried at cost less accumulated depreciation and impairment losses was HK$7,117 million (2015: HK$8,027 million).

31. Other assets

	2016 HK$'m	2015 HK$'m
Repossessed assets	**38**	44
Precious metals	**5,633**	3,674
Reinsurance assets	**38,605**	38,514
Accounts receivable and prepayments	**27,032**	23,733
	71,308	65,965

32. Hong Kong SAR currency notes in circulation

The Hong Kong SAR currency notes in circulation are secured by deposit of funds in respect of which the Hong Kong SAR Government certificates of indebtedness are held.

33. Financial liabilities at fair value through profit or loss

	2016 HK$'m	2015 HK$'m
Trading liabilities		
– Short positions in Exchange Fund Bills and Notes	**9,946**	8,371
Financial liabilities designated at fair value through profit or loss		
– Structured deposits (Note 34)	**3,425**	2,571
	13,371	10,942

The carrying amount of financial liabilities designated at fair value through profit or loss as at 31 December 2016 was less than the amount that the Group would be contractually required to pay at maturity to the holders by HK$9 million (2015: HK$5 million). The amount of change in the fair values of financial liabilities at fair value through profit or loss, during the year and cumulatively, attributable to changes in own credit risk was insignificant.

34. Deposits from customers

	2016 HK$'m	2015 HK$'m
Current, savings and other deposit accounts (per balance sheet)	**1,504,076**	1,415,487
Structured deposits reported as financial liabilities at fair value through profit or loss (Note 33)	**3,425**	2,571
	1,507,501	1,418,058
Analysed by:		
Demand deposits and current accounts		
– Corporate	**126,671**	101,736
– Personal	**45,756**	34,189
	172,427	135,925
Savings deposits		
– Corporate	**319,129**	304,593
– Personal	**477,442**	413,426
	796,571	718,019
Time, call and notice deposits		
– Corporate	**359,791**	349,577
– Personal	**178,712**	214,537
	538,503	564,114
	1,507,501	1,418,058

35. Debt securities and certificates of deposit in issue

	2016 HK$'m	2015 HK$'m
Debt securities, at amortised cost		
– Senior notes under the Medium Term Note Programme	**–**	5,728
– Other debt securities	**1,121**	1,248
	1,121	6,976

36. Other accounts and provisions

	2016 HK$'m	2015 HK$'m
Other accounts payable	**52,155**	34,314
Provisions	**242**	268
	52,397	34,582

37. Deferred taxation

Deferred tax is recognised in respect of the temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements and unused tax credits in accordance with HKAS 12 "Income Taxes".

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

	2016					
	Accelerated tax depreciation HK$'m	**Property revaluation HK$'m**	**Losses HK$'m**	**Impairment allowances HK$'m**	**Others HK$'m**	**Total HK$'m**
At 1 January 2016, as previously reported	**596**	**7,192**	**–**	**(459)**	**(930)**	**6,399**
Effect of merger of entity under common control	**1**	**–**	**–**	**–**	**(6)**	**(5)**
At 1 January 2016, as restated	**597**	**7,192**	**–**	**(459)**	**(936)**	**6,394**
Charged/(credited) to income statement	**29**	**(206)**	**–**	**(63)**	**(65)**	**(305)**
Credited to other comprehensive income	**–**	**(311)**	**–**	**–**	**(164)**	**(475)**
Exchange difference	**–**	**–**	**–**	**2**	**–**	**2**
Classified as assets held for sale and liabilities associated with assets held for sale	**(14)**	**(208)**	**–**	**90**	**33**	**(99)**
At 31 December 2016	**612**	**6,467**	**–**	**(430)**	**(1,132)**	**5,517**

	2015					
	Accelerated tax depreciation HK$'m	Property revaluation HK$'m	Losses HK$'m	Impairment allowances HK$'m	Others HK$'m	Total HK$'m
At 1 January 2015, as previously reported	607	7,858	–	(645)	94	7,914
Effect of merger of entity under common control	1	–	–	–	(7)	(6)
At 1 January 2015, as restated	608	7,858	–	(645)	87	7,908
Charged/(credited) to income statement	7	(112)	(35)	40	(701)	(801)
Charged/(credited) to other comprehensive income	–	483	–	–	(416)	67
Exchange difference	–	(3)	2	9	–	8
Classified as assets held for sale and liabilities associated with assets held for sale	(18)	(1,034)	33	137	94	(788)
At 31 December 2015	597	7,192	–	(459)	(936)	6,394

37. Deferred taxation (continued)

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

	2016 HK$'m	2015 HK$'m
Deferred tax assets	**(73)**	(63)
Deferred tax liabilities	**5,590**	6,457
	5,517	6,394

	2016 HK$'m	2015 HK$'m
Deferred tax assets to be recovered after more than twelve months	**(10)**	(58)
Deferred tax liabilities to be settled after more than twelve months	**6,605**	7,284
	6,595	7,226

As at 31 December 2016, the Group has not recognised deferred tax assets in respect of tax losses amounting to HK$13 million (2015: HK$8 million). Of the amount, HK$9 million (2015: HK$8 million) for the Group has no expiry date and HK$4 million (2015: Nil) for the Group is scheduled to expire within six years under the current tax legislation in different countries.

38. Insurance contract liabilities

	2016 HK$'m	2015 HK$'m
At 1 January	**82,645**	73,796
Benefits paid	**(14,935)**	(12,807)
Claims incurred and movement in liabilities	**18,824**	21,656
At 31 December	**86,534**	82,645

The insurance contract liabilities that are covered by reinsurance arrangements amounted to HK$33,471 million (2015: HK$36,071 million) and the associated reinsurance assets of HK$38,605 million (2015: HK$38,514 million) are included in "Other assets" (Note 31).

39. Subordinated liabilities

	2016 HK$'m	2015 HK$'m
Subordinated notes, at amortised cost with fair value hedge adjustment		
USD2,500m*	**19,014**	19,422

In 2010, BOCHK issued listed subordinated notes with an aggregate amount of USD2,500 million.

Amounts qualified as Tier 2 capital instruments for regulatory purposes are shown in Note 4.5(B).

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

40. Discontinued operations and assets held for sale

(a) Disposal of NCB

According to the announcement made on 14 July 2015, BOC obtained the in-principle approval from the Ministry of Finance of the People's Republic of China (the "Ministry of Finance") for the undertaking of the disposal of 100% interest in NCB held by BOCHK in accordance with the relevant regulations of the Administrative Measures for the Transfer of State-owned Assets of Financial Enterprises (No. 54 Decree of the Ministry of Finance), by way of public bidding via the Beijing Financial Assets Exchange on 15 July 2015.

On 18 December 2015, BOCHK (as seller) entered into a sale and purchase agreement with Cinda Financial Holdings Co., Limited (as buyer) and China Cinda (HK) Holdings Company Limited (as buyer's guarantor) in relation to the sale and purchase of all the issued shares of NCB. The completion of the disposal was conditional upon the satisfaction of the conditions precedent set out in the sale and purchase agreement.

All the conditions precedent set out in the sale and purchase agreement were satisfied, and completion of the disposal took place on 30 May 2016 in accordance with the terms and conditions of the sale and purchase agreement. Upon completion, NCB ceased to be a subsidiary of BOCHK.

(b) Proposed disposal of Chiyu

On 22 December 2016, BOCHK (as seller) entered into a sale and purchase agreement with Xiamen International Investment Limited and the Committee of Jimei Schools (each as a buyer) in relation to the proposed disposal of a total of 2,114,773 ordinary shares of Chiyu (the "Proposed Disposal"). The completion of the Proposed Disposal is conditional upon the satisfaction of all the conditions precedent set out in the sale and purchase agreement. Upon completion of the Proposed Disposal, BOCHK will cease to hold any share in Chiyu and Chiyu will cease to be a subsidiary of BOCHK.

The comparative amounts of consolidated income statement have been restated as if the discontinued operations had been discontinued at the beginning of year 2015.

40. Discontinued operations and assets held for sale (continued)

The results of discontinued operations for the year are as follows:

DISCONTINUED OPERATIONS	2016 HK$'m	2015 HK$'m
Interest income	**4,030**	9,635
Interest expense	**(1,398)**	(4,068)
Net interest income	**2,632**	5,567
Fee and commission income	**769**	1,453
Fee and commission expense	**(13)**	(50)
Net fee and commission income	**756**	1,403
Net trading gain	**40**	105
Net loss on financial instruments designated at fair value through profit or loss	**(8)**	(23)
Net gain on other financial assets	**108**	279
Other operating income	**9**	20
Net operating income before impairment allowances	**3,537**	7,351
Net charge of impairment allowances	**(420)**	(832)
Net operating income	**3,117**	6,519
Operating expenses	**(1,275)**	(2,630)
Operating profit	**1,842**	3,889
Net (loss)/gain from disposal of/fair value adjustments on investment properties	**(14)**	52
Net (loss)/gain from disposal/revaluation of properties, plant and equipment	**(2)**	2
Profit before taxation	**1,826**	3,943
Taxation	**(289)**	(551)
Profit after taxation	**1,537**	3,392
Gain on disposal of discontinued operations	**29,956**	–
Profit from discontinued operations	**31,493**	3,392
Profit attributable to:		
Equity holders of the Company	**31,302**	3,225
Non-controlling interests	**191**	167
	31,493	3,392
	HK$	HK$
Earnings per share for profit attributable to the equity holders of the Company		
Basic and diluted		
– profit from discontinued operations	**2.9606**	0.3050

40. Discontinued operations and assets held for sale (continued)

The net cash flows incurred by discontinued operations are as follows:

	2016 HK$'m	2015 HK$'m
Operating activities	**(17,543)**	5,132
Investing activities	**(67)**	(110)
Financing activities	**–**	(985)
Net cash (outflow)/inflow incurred by discontinued operations	**(17,610)**	4,037

The gain on disposal of discontinued operations is analysed as follows:

	2016 HK$'m
Total consideration	**68,000**
Net assets disposed	**(38,048)**
Cumulative translation reserve and reserve for fair value changes of available-for-sale securities reclassified to income statement	**370**
Transaction costs incurred in connection with the disposal	**(366)**
Gain on disposal of discontinued operations	**29,956**

40. Discontinued operations and assets held for sale (continued)

The net assets of NCB at the date of disposal are as follows:

	At the date of disposal HK$'m
Cash and balances with banks and other financial institutions	45,126
Placements with banks and other financial institutions maturing between one and twelve months	6,394
Financial assets at fair value through profit or loss	5,560
Derivative financial instruments	517
Advances and other accounts	168,185
Investment in securities	56,934
Investment properties	354
Properties, plant and equipment	7,049
Current tax assets	64
Deferred tax assets	71
Other assets	2,745
Deposits and balances from banks and other financial institutions	(18,495)
Financial liabilities at fair value through profit or loss	(4,579)
Derivative financial instruments	(229)
Deposits from customers	(215,253)
Other accounts and provisions	(15,346)
Current tax liabilities	(236)
Deferred tax liabilities	(813)
Net assets disposed	**38,048**

The net cash inflow from disposal of discontinued operations is analysed as follows:

	2016 HK$'m
Total consideration received, satisfied by cash	68,000
Transaction costs incurred in connection with the disposal	(366)
Cash and cash equivalents disposed	(40,642)
Net cash inflow from disposal of discontinued operations	**26,992**

40. Discontinued operations and assets held for sale (continued)

The major classes of assets held for sale and liabilities associated with assets held for sale are as follows:

	2016 HK$'m	2015 HK$'m
ASSETS HELD FOR SALE		
Cash and balances with banks and other financial institutions	**5,233**	53,124
Placements with banks and other financial institutions maturing between one and twelve months	**1,038**	7,057
Financial assets at fair value through profit or loss	**654**	7,263
Derivative financial instruments	**98**	653
Advances and other accounts	**30,844**	168,924
Investment in securities	**13,387**	55,107
Investment properties	**204**	414
Properties, plant and equipment	**1,534**	6,960
Current tax assets	**–**	47
Deferred tax assets	**61**	11
Other assets	**240**	913
Total assets held for sale	**53,293**	300,473
LIABILITIES ASSOCIATED WITH ASSETS HELD FOR SALE		
Deposits and balances from banks and other financial institutions	**977**	18,040
Financial liabilities at fair value through profit or loss	**–**	4,576
Derivative financial instruments	**12**	284
Deposits from customers	**45,370**	215,311
Other accounts and provisions	**438**	12,607
Current tax liabilities	**56**	188
Deferred tax liabilities	**160**	799
Total liabilities associated with assets held for sale	**47,013**	251,805
	6,280	48,668

The cumulative income recognised in other comprehensive income relating to assets held for sale is as follows:

	2016 HK$'m	2015 HK$'m
Cumulative income recognised in other comprehensive income	**1,014**	5,963

41. Share capital

	2016 HK$'m	2015 HK$'m
Issued and fully paid:		
10,572,780,266 ordinary shares	**52,864**	52,864

42. Notes to consolidated cash flow statement

(a) Reconciliation of operating profit to operating cash outflow before taxation

	2016 HK$'m	2015 HK$'m
Operating profit		
– from continuing operations	**28,963**	27,815
– from discontinued operations	**1,842**	3,889
	30,805	31,704
Depreciation	**1,814**	1,850
Net charge of impairment allowances	**998**	1,587
Unwind of discount on impairment allowances	**(9)**	(15)
Advances written off net of recoveries	**(457)**	(1,723)
Change in subordinated liabilities	**68**	155
Change in balances with banks and other financial institutions with original maturity over three months	**(16,262)**	1,618
Change in placements with banks and other financial institutions with original maturity over three months	**(20,479)**	(21,799)
Change in financial assets at fair value through profit or loss	**(9,294)**	(10,128)
Change in derivative financial instruments	**(11,893)**	9,060
Change in advances and other accounts	**(93,910)**	(73,646)
Change in investment in securities	**(80,982)**	(131,090)
Change in other assets	**(7,427)**	(14,917)
Change in deposits and balances from banks and other financial institutions	**(15,681)**	(16,155)
Change in financial liabilities at fair value through profit or loss	**2,432**	3,258
Change in deposits from customers	**133,901**	141,556
Change in debt securities and certificates of deposit in issue	**(5,855)**	(4,925)
Change in other accounts and provisions	**20,992**	(4,759)
Change in insurance contract liabilities	**3,889**	8,849
Effect of changes in exchange rates	**(1,336)**	10,563
Operating cash outflow before taxation	**(68,686)**	(68,957)
Cash flows from operating activities included		
– interest received	**40,697**	50,077
– interest paid	**11,302**	16,868
– dividend received	**135**	126

42. Notes to consolidated cash flow statement (continued)

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

	2016 HK$'m	2015 HK$'m
Cash and balances with banks and other financial institutions with original maturity within three months	**216,857**	275,672
Placements with banks and other financial institutions with original maturity within three months	**6,844**	24,174
Treasury bills with original maturity within three months	**15,892**	12,359
Certificates of deposit with original maturity within three months	**1,367**	890
	240,960	313,095

43. Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liability and commitment and the aggregate credit risk-weighted amount and is prepared with reference to the completion instructions for the HKMA return of capital adequacy ratio.

	2016 HK$'m	2015 HK$'m
Direct credit substitutes	**6,247**	24,360
Transaction-related contingencies	**12,649**	7,600
Trade-related contingencies	**32,269**	31,713
Asset sales with recourse	**–**	5,419
Commitments that are unconditionally cancellable without prior notice	**388,739**	471,092
Other commitments with an original maturity of		
– up to one year	**12,095**	10,519
– over one year	**132,488**	114,376
	584,487	665,079
Credit risk-weighted amount	**60,730**	74,880

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

44. Capital commitments

The Group has the following outstanding capital commitments not provided for in the financial statements:

	2016 HK$'m	2015 HK$'m
Authorised and contracted for but not provided for	**404**	223
Authorised but not contracted for	**11**	16
	415	239

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

45. Operating lease commitments

(a) As lessee

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

	2016 HK$'m	2015 HK$'m
Land and buildings		
– Not later than one year	**630**	787
– Later than one year but not later than five years	**750**	1,394
– Later than five years	**4**	112
	1,384	2,293

Certain non-cancellable operating leases included in the table above were subject to renegotiation and rent adjustment with reference to market rates prevailing at specified agreed dates or according to the special conditions as stipulated in the leases.

(b) As lessor

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

	2016 HK$'m	2015 HK$'m
Land and buildings		
– Not later than one year	**396**	421
– Later than one year but not later than five years	**392**	330
	788	751

The Group leases its investment properties under operating lease arrangements, with leases typically for a period from one to three years. The terms of the leases generally require the tenants to pay security deposits and provide for rent adjustments according to the prevailing market conditions at the expiration of the lease.

46. Litigation

The Group has been served a number of claims and counterclaims by various independent parties. These claims and counterclaims are in relation to the normal commercial activities of the Group.

No material provision was made against these claims and counterclaims because the directors believe that the Group has meritorious defences against the claimants or the amounts involved in these claims are not expected to be material.

47. Segmental reporting

The Group manages the business mainly from a business segment perspective and over 90% of the Group's revenues, profits before tax and assets are derived from Hong Kong. Currently, four operating segments are identified: Personal Banking, Corporate Banking, Treasury and Insurance. The classification of the Group's operating segments is based on customer segment and product type, which is aligned with the RPC (relationship, product and channel) management model of the Group.

Both Personal Banking and Corporate Banking provide general banking services including various deposit products, overdrafts, loans, credit cards, trade related products and other credit facilities, investment and insurance products, and foreign currency and derivative products. Personal Banking mainly serves retail customers and small enterprises, while Corporate Banking mainly deals with corporate customers. Treasury manages the funding and liquidity, and the interest rate and foreign exchange positions of the Group in addition to proprietary trades. The Insurance segment represents business mainly relating to life insurance products, including individual life insurance and group life insurance products. "Others" mainly represents the Group's holdings of premises, investment properties, equity investments and interests in associates and joint ventures.

Measurement of segment assets, liabilities, income, expenses, results and capital expenditure is based on the Group's accounting policies. The segment information includes items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group, which is primarily based on market rates with the consideration of specific features of the product.

As the Group derives a majority of revenue from interest and the senior management relies primarily on net interest income in managing the business, interest income and expense for all reportable segments are presented on a net basis. Under the same consideration, insurance premium income and insurance benefits and claims are also presented on a net basis.

47. Segmental reporting (continued)

	Personal Banking HK$'m	Corporate Banking HK$'m	Treasury HK$'m	Insurance HK$'m	Others HK$'m	Subtotal HK$'m	Eliminations HK$'m	Consolidated HK$'m
Year ended 31 December 2016								
CONTINUING OPERATIONS								
Net interest income/(expense)								
– External	3,462	10,566	9,017	2,379	4	25,428	–	25,428
– Inter-segment	4,984	(49)	(4,241)	(12)	(682)	–	–	–
	8,446	10,517	4,776	2,367	(678)	25,428	–	25,428
Net fee and commission income/(expense)	5,587	4,851	108	(415)	691	10,822	(281)	10,541
Net insurance premium income	–	–	–	10,651	–	10,651	(17)	10,634
Net trading gain/(loss)	668	153	4,085	(332)	3	4,577	28	4,605
Net (loss)/gain on financial instruments designated at fair value through profit or loss	–	–	(1)	97	–	96	5	101
Net (loss)/gain on other financial assets	–	(5)	623	388	–	1,006	–	1,006
Other operating income	29	2	8	216	1,818	2,073	(1,259)	814
Total operating income	14,730	15,518	9,599	12,972	1,834	54,653	(1,524)	53,129
Net insurance benefits and claims and movement in liabilities	–	–	–	(11,375)	–	(11,375)	–	(11,375)
Net operating income before impairment allowances	14,730	15,518	9,599	1,597	1,834	43,278	(1,524)	41,754
Net (charge)/reversal of impairment allowances	(417)	(183)	22	–	–	(578)	–	(578)
Net operating income	14,313	15,335	9,621	1,597	1,834	42,700	(1,524)	41,176
Operating expenses	(6,770)	(2,715)	(1,069)	(367)	(2,816)	(13,737)	1,524	(12,213)
Operating profit/(loss)	7,543	12,620	8,552	1,230	(982)	28,963	–	28,963
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	429	429	–	429
Net loss from disposal/revaluation of properties, plant and equipment	(5)	(6)	–	–	(3)	(14)	–	(14)
Share of profits less losses after tax of associates and joint ventures	–	–	–	–	74	74	–	74
Profit/(loss) before taxation	7,538	12,614	8,552	1,230	(482)	29,452	–	29,452
At 31 December 2016								
ASSETS								
Segment assets	318,053	698,314	1,090,598	111,186	67,948	2,286,099	(11,930)	2,274,169
Interests in associates and joint ventures	–	–	–	–	319	319	–	319
Assets held for sale	9,299	23,999	19,142	–	1,660	54,100	(807)	53,293
	327,352	722,313	1,109,740	111,186	69,927	2,340,518	(12,737)	2,327,781
LIABILITIES								
Segment liabilities	794,434	734,585	416,653	103,783	13,283	2,062,738	(12,530)	2,050,208
Liabilities associated with assets held for sale	35,820	10,823	288	–	289	47,220	(207)	47,013
	830,254	745,408	416,941	103,783	13,572	2,109,958	(12,737)	2,097,221
Year ended 31 December 2016								
CONTINUING OPERATIONS								
Other information								
Capital expenditure	26	3	–	18	1,393	1,440	–	1,440
Depreciation	380	148	72	13	1,175	1,788	–	1,788
Amortisation of securities	–	–	(398)	(8)	–	(406)	–	(406)

47. Segmental reporting (continued)

	Personal Banking HK$'m	Corporate Banking HK$'m	Treasury HK$'m	Insurance HK$'m	Others HK$'m	Subtotal HK$'m	Eliminations HK$'m	Consolidated HK$'m
Year ended 31 December 2015								
CONTINUING OPERATIONS								
Net interest income/(expense)								
– External	2,687	7,706	12,549	2,228	6	25,176	–	25,176
– Inter-segment	5,251	1,339	(6,009)	8	(589)	–	–	–
	7,938	9,045	6,540	2,236	(583)	25,176	–	25,176
Net fee and commission income/(expense)	6,579	4,483	78	(169)	549	11,520	(247)	11,273
Net insurance premium income	–	–	–	12,462	–	12,462	(17)	12,445
Net trading gain/(loss)	640	198	1,762	(20)	1	2,581	16	2,597
Net loss on financial instruments designated at fair value through profit or loss	–	–	(6)	(745)	–	(751)	–	(751)
Net gain on other financial assets	642	4	489	151	–	1,286	–	1,286
Other operating income	46	6	13	33	1,728	1,826	(1,016)	810
Total operating income	15,845	13,736	8,876	13,948	1,695	54,100	(1,264)	52,836
Net insurance benefits and claims and movement in liabilities	–	–	–	(12,655)	–	(12,655)	–	(12,655)
Net operating income before impairment allowances	15,845	13,736	8,876	1,293	1,695	41,445	(1,264)	40,181
Net (charge)/reversal of impairment allowances	(300)	(516)	61	–	–	(755)	–	(755)
Net operating income	15,545	13,220	8,937	1,293	1,695	40,690	(1,264)	39,426
Operating expenses	(6,460)	(2,466)	(1,090)	(356)	(2,503)	(12,875)	1,264	(11,611)
Operating profit/(loss)	9,085	10,754	7,847	937	(808)	27,815	–	27,815
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	774	774	–	774
Net loss from disposal/revaluation of properties, plant and equipment	(15)	(2)	(1)	(5)	(45)	(68)	–	(68)
Share of profits less losses after tax of associates and joint ventures	–	–	–	–	54	54	–	54
Profit/(loss) before taxation	9,070	10,752	7,846	932	(25)	28,575	–	28,575
At 31 December 2015								
ASSETS								
Segment assets	303,185	648,296	988,335	98,282	68,548	2,106,646	(24,680)	2,081,966
Interests in associates and joint ventures	–	–	–	–	376	376	–	376
Assets held for sale	39,480	134,506	123,419	–	7,541	304,946	(4,473)	300,473
	342,665	782,802	1,111,754	98,282	76,465	2,411,968	(29,153)	2,382,815
LIABILITIES								
Segment liabilities	755,625	684,283	400,517	91,593	11,879	1,943,897	(13,052)	1,930,845
Liabilities associated with assets held for sale	91,705	138,603	35,993	–	1,605	267,906	(16,101)	251,805
	847,330	822,886	436,510	91,593	13,484	2,211,803	(29,153)	2,182,650
Year ended 31 December 2015								
CONTINUING OPERATIONS								
Other information								
Capital expenditure	34	5	–	28	1,107	1,174	–	1,174
Depreciation	366	147	70	11	1,119	1,713	–	1,713
Amortisation of securities	–	–	(170)	(86)	–	(256)	–	(256)

48. Assets pledged as security

As at 31 December 2016, the liabilities of the Group amounting to HK$10,686 million (2015: HK$11,650 million) were secured by assets deposited with central depositories to facilitate settlement operations. In addition, the liabilities of the Group amounting to HK$19,260 million (2015: HK$9,111 million) were secured by debt securities and bills related to sale and repurchase arrangements. The amount of assets pledged by the Group to secure these liabilities was HK$30,903 million (2015: HK$22,594 million) mainly included in "Trading assets", "Investment in securities" and "Trade bills".

49. Offsetting financial instruments

The following tables present details of the Group's financial instruments subject to offsetting, enforceable master netting arrangements and similar agreements.

	2016					
				Related amounts not set off in the balance sheet		
	Gross amounts of recognised financial assets HK$'m	Gross amounts of recognised financial liabilities set off in the balance sheet HK$'m	Net amounts of financial assets presented in the balance sheet HK$'m	Financial instruments HK$'m	Cash collateral received HK$'m	Net amount HK$'m
Assets						
Derivative financial instruments	63,869	–	63,869	(36,951)	(6,795)	20,123
Reverse repurchase agreements	5,949	–	5,949	(5,949)	–	–
Securities borrowing agreements	1,000	–	1,000	(1,000)	–	–
Other assets	15,931	(9,044)	6,887	–	–	6,887
	86,749	(9,044)	77,705	(43,900)	(6,795)	27,010

	2016					
				Related amounts not set off in the balance sheet		
	Gross amounts of recognised financial liabilities HK$'m	Gross amounts of recognised financial assets set off in the balance sheet HK$'m	Net amounts of financial liabilities presented in the balance sheet HK$'m	Financial instruments HK$'m	Cash collateral pledged HK$'m	Net amount HK$'m
Liabilities						
Derivative financial instruments	48,972	–	48,972	(36,951)	(4,446)	7,575
Repurchase agreements	19,260	–	19,260	(19,260)	–	–
Other liabilities	9,693	(9,044)	649	–	–	649
	77,925	(9,044)	68,881	(56,211)	(4,446)	8,224

49. Offsetting financial instruments (continued)

	2015					
				Related amounts not set off in the balance sheet		
	Gross amounts of recognised financial assets HK$'m	Gross amounts of recognised financial liabilities set off in the balance sheet HK$'m	Net amounts of financial assets presented in the balance sheet HK$'m	Financial instruments HK$'m	Cash collateral received HK$'m	Net amount HK$'m
Assets						
Derivative financial instruments	30,223	–	30,223	(14,915)	(945)	14,363
Reverse repurchase agreements	1,016	–	1,016	(1,016)	–	–
Securities borrowing agreements	–	–	–	–	–	–
Other assets	11,110	(8,277)	2,833	–	–	2,833
	42,349	(8,277)	34,072	(15,931)	(945)	17,196

	2015					
				Related amounts not set off in the balance sheet		
	Gross amounts of recognised financial liabilities HK$'m	Gross amounts of recognised financial assets set off in the balance sheet HK$'m	Net amounts of financial liabilities presented in the balance sheet HK$'m	Financial instruments HK$'m	Cash collateral pledged HK$'m	Net amount HK$'m
Liabilities						
Derivative financial instruments	31,173	–	31,173	(14,915)	(8,972)	7,286
Repurchase agreements	5,557	–	5,557	(5,557)	–	–
Other liabilities	9,179	(8,277)	902	–	–	902
	45,909	(8,277)	37,632	(20,472)	(8,972)	8,188

For master netting agreements of OTC derivative, sale and repurchase and securities lending and borrowing transactions entered into by the Group, related amounts with the same counterparty can be offset if an event of default or other predetermined events occur.

50. Transfers of financial assets

The transferred financial assets of the Group below that do not qualify for derecognition are debt securities held by counterparties as collateral under sale and repurchase agreements.

	2016		2015	
	Carrying amount of transferred assets HK$'m	**Carrying amount of associated liabilities HK$'m**	Carrying amount of transferred assets HK$'m	Carrying amount of associated liabilities HK$'m
Repurchase agreements	**20,080**	**19,260**	5,841	5,557

51. Loans to directors

Particulars of loans made to directors of the Company pursuant to section 383 of the Hong Kong Companies Ordinance and Part 3 of the Companies (Disclosure of Information about Benefits of Directors) Regulation are as follows:

	2016 HK$'m	2015 HK$'m
Aggregate amount of relevant transactions outstanding at year end	**874**	2,206
Maximum aggregate amount of relevant transactions outstanding during the year	**2,243**	2,857

52. Significant related party transactions

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

52. Significant related party transactions (continued)

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

General information of the parent companies:

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

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

The Group enters into banking and other transactions with these entities in the normal course of business which include loans, investment securities, money market and reinsurance transactions.

The majority of transactions with BOC arise from money market activities. As at 31 December 2016, the related aggregate amounts due from and to BOC of the Group were HK$106,281 million (2015: HK$102,324 million) and HK$58,654 million (2015: HK$55,448 million) respectively. The aggregate amounts of income and expenses of the Group arising from these transactions with BOC for the year ended 31 December 2016 were HK$1,436 million (2015: HK$3,303 million) and HK$306 million (2015: HK$474 million) respectively. The related party transactions above constitute connected transactions as defined in Chapter 14A of the Listing Rules but under exemption from its disclosure requirement.

The transaction with BOC disclosed in Note 57 also constitutes connected transactions as defined in Chapter 14A of the Listing Rules and announcements had been made by the Group on 30 June 2016 and 17 October 2016.

Transactions with other companies controlled by BOC are not considered material.

(b) Transactions with government authorities, agencies, affiliates and other state controlled entities

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

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

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

52. Significant related party transactions (continued)

(c) Summary of transactions entered into during the ordinary course of business with associates, joint ventures and other related parties

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

	2016 HK$'m	2015 HK$'m
Income statement items		
Associates		
– Other operating expenses	**70**	65
Joint ventures		
– Other operating expenses	**–**	1
Other related parties		
– Administrative services fees received/receivable	**9**	9
Balance sheet item		
Associates		
– Other accounts and provisions	**3**	–

The related party transactions in respect of the other operating expenses arising from associates above constitute connected transactions as defined in Chapter 14A of the Listing Rules and the required disclosures are provided in "Connected transactions" on pages 308 to 309.

(d) 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 and senior management. The Group accepts deposits from and grants loans and credit facilities to key management personnel in the ordinary course of business. During both the current and prior years, no material transaction was conducted with key management personnel of the Company and its holding companies, as well as parties related to them.

The compensation of key management personnel for the year ended 31 December is detailed as follows:

	2016 HK$'m	2015 HK$'m
Salaries and other short-term employee benefits	**46**	47
Post-employment benefits	**–**	1
	46	48

53. International claims

The below analysis is prepared with reference to the completion instructions for the HKMA return of international banking statistics. International claims are exposures to counterparties on which the ultimate risk lies based on the locations of the counterparties after taking into account the transfer of risk, and represent the sum of cross-border claims in all currencies and local claims in foreign currencies. For a claim guaranteed by a party situated in a country different from the counterparty, the risk will be transferred to the country of the guarantor. For a claim on an overseas branch of a bank whose head office is located in another country, the risk will be transferred to the country where its head office is located.

Claims on individual countries or areas, after risk transfer, amounting to 10% or more of the aggregate international claims of the Group are shown as follows:

	2016				
			Non-bank private sector		
	Banks HK$'m	**Official sector HK$'m**	**Non-bank financial institutions HK$'m**	**Non-financial private sector HK$'m**	**Total HK$'m**
Mainland of China	**317,073**	**83,649**	**19,218**	**130,223**	**550,163**
Hong Kong	**4,557**	**3,516**	**16,287**	**271,107**	**295,467**

	2015				
			Non-bank private sector		
	Banks HK$'m	Official sector HK$'m	Non-bank financial institutions HK$'m	Non-financial private sector HK$'m	Total HK$'m
Mainland of China	329,425	110,765	8,795	157,064	606,049
Hong Kong	7,916	25	10,379	286,594	304,914

54. Non-bank Mainland exposures

The analysis of non-bank Mainland exposures is based on the categories of non-bank counterparties and the types of direct exposures with reference to the completion instructions for the HKMA return of Mainland activities, which includes the Mainland exposures extended by BOCHK and its local banking subsidiaries.

		2016		
	Items in the HKMA return	On-balance sheet exposure HK$'m	Off-balance sheet exposure HK$'m	Total exposure HK$'m
Central government, central government-owned entities and their subsidiaries and joint ventures	1	247,107	47,259	294,366
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	65,980	10,126	76,106
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	51,955	11,584	63,539
Other entities of central government not reported in item 1 above	4	26,874	1,812	28,686
Other entities of local governments not reported in item 2 above	5	–	–	–
PRC nationals residing outside Mainland or entities incorporated outside Mainland where the credit is granted for use in Mainland	6	60,043	11,796	71,839
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	4,144	199	4,343
Total	8	456,103	82,776	538,879
Total assets after provision	9	2,176,247		
On-balance sheet exposures as percentage of total assets	10	20.96%		

54. Non-bank Mainland exposures (continued)

		2015		
	Items in the HKMA return	On-balance sheet exposure HK$'m	Off-balance sheet exposure HK$'m	Total exposure HK$'m
Central government, central government-owned entities and their subsidiaries and joint ventures	1	269,836	26,994	296,830
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	84,329	15,508	99,837
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	85,364	37,350	122,714
Other entities of central government not reported in item 1 above	4	16,899	157	17,056
Other entities of local governments not reported in item 2 above	5	83	–	83
PRC nationals residing outside Mainland or entities incorporated outside Mainland where the credit is granted for use in Mainland	6	59,033	15,253	74,286
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	7,272	–	7,272
Total	8	522,816	95,262	618,078
Total assets after provision	9	2,282,058		
On-balance sheet exposures as percentage of total assets	10	22.91%		

55. Balance sheet and statement of changes in equity

(a) Balance sheet

As at 31 December	2016 HK$'m	2015 HK$'m
ASSETS		
Bank balances with a subsidiary	**62**	149
Investment in securities	**2,532**	2,459
Investment in subsidiaries	**55,089**	55,089
Amounts due from a subsidiary	**3,659**	3,616
Other assets	**–**	1
Total assets	**61,342**	61,314
LIABILITIES		
Amounts due to a subsidiary	**1**	2
Total liabilities	**1**	2
EQUITY		
Share capital	**52,864**	52,864
Reserves	**8,477**	8,448
Total equity	**61,341**	61,312
Total liabilities and equity	**61,342**	61,314

Approved by the Board of Directors on 31 March 2017 and signed on behalf of the Board by:

TIAN Guoli
Director

YUE Yi
Director

55. Balance sheet and statement of changes in equity (continued)

(b) Statement of changes in equity

		Reserves		
	Share capital HK$'m	Reserve for fair value changes of available-for-sale securities HK$'m	Retained earnings HK$'m	Total equity HK$'m
At 1 January 2015	52,864	1,408	6,507	60,779
Profit for the year	–	–	12,580	12,580
Other comprehensive income:				
Available-for-sale securities	–	(205)	–	(205)
Total comprehensive income	–	(205)	12,580	12,375
Dividends	–	–	(11,842)	(11,842)
At 31 December 2015	52,864	1,203	7,245	61,312
At 1 January 2016	**52,864**	**1,203**	**7,245**	**61,312**
Profit for the year	**–**	**–**	**20,404**	**20,404**
Other comprehensive income:				
Available-for-sale securities	**–**	**73**	**–**	**73**
Total comprehensive income	**–**	**73**	**20,404**	**20,477**
Dividends	**–**	**–**	**(20,448)**	**(20,448)**
At 31 December 2016	**52,864**	**1,276**	**7,201**	**61,341**

56. Principal subsidiaries

The particulars of all direct and indirect subsidiaries of the Company are set out in "Appendix – Subsidiaries of the Company". The following is a list of principal subsidiaries as at 31 December 2016:

Name	Place of incorporation and operation	Issued share capital	Interest held	Principal activities
Bank of China (Hong Kong) Limited	Hong Kong	Ordinary shares HK$43,042,840,858	*100%	Banking business
BOC Group Life Assurance Company Limited	Hong Kong	Ordinary shares HK$3,538,000,000	*51%	Life insurance business
Chiyu Banking Corporation Limited	Hong Kong	Ordinary shares HK$300,000,000	70.49%	Banking business
BOC Credit Card (International) Limited	Hong Kong	Ordinary shares HK$480,000,000	100%	Credit card services
Po Sang Securities and Futures Limited	Hong Kong	Ordinary shares HK$335,000,000	100%	Securities and futures brokerage

* Shares held directly by the Company

The particulars of a subsidiary with significant non-controlling interests are as follows:

BOC Group Life Assurance Company Limited

	2016	2015
Proportion of ownership interests and voting rights held by non-controlling interests	**49%**	49%

	2016 HK$'m	2015 HK$'m
Profit attributable to non-controlling interests	**510**	406
Accumulated non-controlling interests	**3,627**	3,278
Summarised financial information:		
– total assets	**111,186**	98,282
– total liabilities	**103,783**	91,593
– profit for the year	**1,041**	829
– total comprehensive income for the year	**754**	743

57. Application of merger accounting

On 17 October 2016, BOCHK acquired the entire issued share capital of BOC Malaysia for a total consideration of HK$4,076 million in cash. BOC Malaysia and BOCHK are both under the common control of BOC before and after the combination. The Group has applied the merger accounting method in accordance with the Accounting Guideline 5 "Merger Accounting for Common Control Combinations" issued by the HKICPA in the preparation of financial statements. The comparative amounts for the year 2015 have been restated accordingly as if the combination had occurred at the beginning of year 2015.

The statements of the adjustments to the consolidated equity as at 31 December are as follows:

	2016			
	Before combination HK$'m	**Entity under common control HK$'m**	**Adjustment HK$'m**	**After combination HK$'m**
Share capital	**52,864**	**1,789**	**(1,789)**	**52,864**
Merger reserve	**–**	**–**	**(2,287)**	**(2,287)**
Retained earnings and other reserves	**173,618**	**458**	**–**	**174,076**
	226,482	**2,247**	**(4,076)**	**224,653**
Non-controlling interests	**5,907**	**–**	**–**	**5,907**
	232,389	**2,247**	**(4,076)**	**230,560**

	2015			
	Before combination HK$'m	Entity under common control HK$'m	Adjustment HK$'m	After combination HK$'m
Share capital	52,864	1,789	(1,789)	52,864
Merger reserve	–	–	1,789	1,789
Retained earnings and other reserves	139,714	383	–	140,097
	192,578	2,172	–	194,750
Non-controlling interests	5,415	–	–	5,415
	197,993	2,172	–	200,165

58. Ultimate holding company

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

59. Comparative amounts

As explained in Note 40, the proposed disposal of Chiyu was classified as a discontinued operation in the year. Comparative amounts relating to the discontinued operation have been restated in the consolidated income statement and relevant notes in accordance with HKFRS 5, "Non-current Assets Held for Sale and Discontinued Operations".

In addition, in respect of the acquisition of BOC Malaysia from BOC, as explained in Note 57, the Group has applied merger accounting method for the business combination under common control. Comparative amounts in the financial statements have been restated as if the combination had occurred at the beginning of year 2015.

60. Events after the balance sheet date

On 9 January 2017, completion of the acquisition of the entire issued share capital of Bank of China (Thai) Public Company Limited ("BOC Thailand") by BOCHK (the "Thailand Acquisition") took place in accordance with the terms and conditions of the sale and purchase agreement in relation to the Thailand Acquisition entered into with BOC. Upon completion, BOC Thailand became a subsidiary of BOCHK, and the assets, liabilities and financial results of BOC Thailand will be consolidated into the financial accounts of BOCHK.

On 28 February 2017, BOCHK entered into Asset Purchase Agreements with BOC in relation to the acquisition of the Indonesia Business and the Cambodia Business, respectively. The completion of each proposed acquisition is subject to the satisfaction of the conditions precedent stated in the respective Asset Purchase Agreement. Upon completion, all the assets and liabilities arising in connection with the Indonesia Business and Cambodia Business will be transferred to and assumed by BOCHK. For further information on the acquisitions, please refer to the announcement made by the Group on 28 February 2017.

In relation to the Proposed Disposal of Chiyu as mentioned in Note 40, all the conditions precedent set out in the sale and purchase agreement were satisfied, and completion of the disposal took place on 27 March 2017 in accordance with the terms and conditions of the sale and purchase agreement. Upon completion, Chiyu ceased to be a subsidiary of BOCHK. For details, please refer to the announcements made by the Group on 22 December 2016 and 24 March 2017.

61. Approval of financial statements

The financial statements were approved and authorised for issue by the Board of Directors on 31 March 2017.

Unaudited Supplementary Financial Information

1. Regulatory capital for credit, market and operational risks

The bases of regulatory capital calculation for credit risk, market risk and operational risk are described in Note 4.5 to the Financial Statements.

Sections 1 to 9 of the supplementary financial information have been prepared on a consolidated basis for regulatory purposes. The basis of regulatory consolidation is set out in Note 4.5(A) to the Financial Statements.

The table below summarises the regulatory capital computed on the same consolidation basis for credit, market, and operational risks.

	2016 **HK$'m**	2015 HK$'m
Credit risk	**66,750**	69,906
Market risk	**1,651**	1,683
Operational risk	**5,675**	6,170
	74,076	77,759

For details of capital management and capital ratios of the Group, please refer to Note 4.5 to the Financial Statements.

2. Capital requirements for credit risk

The tables below show the capital requirements for each class and subclass of credit risk exposures as specified in the Banking (Capital) Rules.

	2016 HK$'m	2015 HK$'m
Capital required for exposures under the IRB approach		
Corporate		
Specialised lending under supervisory slotting criteria approach		
– Project finance	**–**	62
Small-and-medium sized corporates	**3,438**	4,355
Other corporates	**34,370**	35,414
Bank		
Banks	**12,017**	14,150
Securities firms	**89**	49
Retail		
Residential mortgages		
– Individuals	**3,057**	2,586
– Property-holding shell companies	**92**	90
Qualifying revolving retail	**1,122**	1,041
Other retail to individuals	**457**	668
Small business retail	**60**	73
Others		
Cash items	**–**	–
Other items	**6,196**	6,640
Securitisation	**2**	3
Credit valuation adjustment	**702**	597
Total capital requirements for exposures under the IRB approach	**61,602**	65,728
Capital required for exposures under the standardised (credit risk) approach		
On-balance sheet exposures		
Sovereigns	**1,534**	1,302
Public sector entities	**121**	97
Banks	**47**	9
Corporates	**1,416**	934
Regulatory retail	**638**	674
Residential mortgage loans	**20**	487
Other exposures which are not past due	**734**	322
Past due exposures	**8**	11
Off-balance sheet exposures		
Off-balance sheet exposures other than securities financing transactions and derivative contracts	**517**	310
Securities financing transactions and derivative contracts	**113**	32
Securitisation	**–**	–
Total capital requirements for exposures under the standardised (credit risk) approach	**5,148**	4,178
Total capital requirements for credit risk exposures	**66,750**	69,906

3. Credit risk under the internal ratings-based approach

3.1 The internal rating systems and risk components

The Group adopts the FIRB approach to calculate the regulatory capital requirements for most of the corporate and bank exposures, and adopts the supervisory slotting criteria approach to project finance exposures under specialised lending. The Group adopts retail IRB approach for retail exposures to individuals and small business. The following is the table showing the Group's different capital calculation approaches to each asset class and sub-classes of exposures (other than securitisation exposures).

Asset class	Exposure sub-class	Capital calculation approach
Corporate exposures	Specialised lending under supervisory slotting criteria approach (project finance)	Supervisory Slotting Criteria Approach
	Small-and-medium sized corporates	FIRB Approach
	Other corporates	
Sovereign exposures	Sovereigns	Standardised (credit risk) Approach
	Sovereign foreign public sector entities	
	Multilateral development banks	
Bank exposures	Banks	FIRB Approach
	Securities firms	
	Public sector entities (excluding sovereign foreign public sector entities)	Standardised (credit risk) Approach
Retail exposures	Residential mortgages to individuals	Retail IRB Approach
	Residential mortgages to property-holding shell companies	
	Qualifying revolving retail	
	Other retail to individuals	
	Small business retail	
Equity exposures	–	Standardised (credit risk) Approach
Other exposures	Cash items	Specific Risk-weight Approach
	Other items	

3. Credit risk under the internal ratings-based approach (continued)

3.1 The internal rating systems and risk components (continued)

(A) The structure of internal rating systems and the relationship between internal ratings and external ratings

The Group's internal rating system is a two dimensional rating system that provides separate assessment of borrower and transaction characteristics. For corporate and bank portfolios, the obligor rating dimension reflects exclusively the risk of borrower default and the facility rating dimension reflects transaction specific factors that affect the loss severity in the case of borrower default.

The Group developed statistical models to provide own estimated probability of default ("PD") for its corporate, bank and retail borrowers, and loss given default ("LGD") and exposure at default ("EAD") for retail exposures under retail IRB approach.

The Group uses internal rating system to assess the borrower's likelihood of default for all IRB portfolios. PD estimates the risk of borrower default over a one-year period. A borrower credit grade means a grouping of similar credit-worthiness to which borrowers are assigned on the basis of specified and distinct set of rating criteria, from which the average PD are derived for risk-weighted assets calculation.

In the process of obligor rating assignment, variables of latest financial performance, management quality, industry risks, group connection and negative warning signals of each obligor are assessed as critical factors to predict borrower's ability and willingness to meet with the contractual obligations under different economic conditions.

The obligors for corporate and bank, and retail PD pools are assigned into eight broad obligor ratings including seven grades for non-defaulted obligors with sub-divisions into 26 minor credit grades and one for defaulted obligors. In the supervisory slotting criteria approach for the project finance exposures, there are four grades for non-defaulted borrowers and one for defaulted borrowers in accordance with the HKMA guidance. The estimates for retail IRB portfolios are pooled by nature of obligors, facility types, collateral types and delinquency status into different PD, EAD and LGD pools. This pooling process provides the basis of accurate and consistent estimation for PD, LGD and EAD at the pool level for exposures arising from residential mortgages to both individuals and property-holding shell companies, qualifying revolving retail exposures and other retail exposures to individuals and small business retail exposures. All credit transactions for corporates and banks are assigned facility ratings (in terms of LGD) in accordance with the HKMA guidance. LGD estimates multiplied by the PD estimates produce the expected loss ("EL") estimates, which are used to assess credit risk quantitatively.

3. Credit risk under the internal ratings-based approach (continued)

3.1 The internal rating systems and risk components (continued)

(A) The structure of internal rating systems and the relationship between internal ratings and external ratings (continued)

For each internal rating, the equivalent external rating in terms of default risk is as below:

Internal Credit Grades	Definition of Internal Ratings	Standard & Poor's Equivalent
1	The obligors in grades "1" and "2" have extremely low default risk.	AAA
2	The obligor's capacity to meet its financial commitment on the obligation is extremely strong.	AA+ AA AA-
3	The obligors in grade "3" have low default risk but are somewhat susceptible to the adverse effects of changes in circumstances and economic conditions. However, the obligor's capacity to meet its financial commitment on the obligation is very strong.	A+ A A-
4	The obligors in grade "4" have relatively low default risk and are currently under adequate protection. However, adverse economic conditions or changing circumstances are likely to lead to a weakened capacity of the obligor to meet its financial commitment on the obligation.	BBB+ BBB BBB-
5	The obligors in grade "5" have medium default risk which are less vulnerable to nonpayment than other speculative obligors. However, they face major ongoing uncertainties or exposure to adverse business, financial, or economic conditions which could lead to the obligor's inadequate capacity to meet its financial commitment on the obligation.	BB+ BB BB-
6	The obligors in grade "6" have significant to very high default risk and are vulnerable to nonpayment. The obligors currently and in the near term have the capacity to meet its financial commitment on the obligation but adverse business, financial, or economic conditions will very likely impair the obligor's capacity or willingness to meet its financial commitment on the obligation.	B+ B B-
7	The obligors in grade "7" have very high default risk and are currently quite vulnerable to nonpayment. The obligors' ability to meet their financial commitment and obligation are dependent upon favorable business, financial, and economic conditions. In the event of adverse business, financial, or economic conditions, these obligors are not likely to have the capacity to meet its financial commitment on the obligation.	CCC CC C
8	Obligors rated "8" are in payment default.	D

3. Credit risk under the internal ratings-based approach (continued)

3.1 The internal rating systems and risk components (continued)

(B) Use of internal estimates

Besides using PD estimates for regulatory capital calculation in corporate and bank exposures, the Group uses the PD together with the LGD and EAD estimates in the credit approval, credit monitoring, reporting and analysis of credit risk information, etc., for the purpose of strengthening the daily management on all credit related matters.

(C) Process of managing and recognising credit risk mitigation

For collateral recognised under capital management, the Group has well-defined policies and procedures for collateral valuation and management which are compliant with the operational requirements for recognised collateral of credit risk mitigation as stated in the Banking (Capital) Rules.

For the credit exposures adopting FIRB approach for capital calculation purpose, the recognised eligible guarantees include the guarantees provided by banks, corporates and securities firms with a lower risk weights than the counterparty. The Group takes into account the credit risk mitigation effect of recognised collateral through its determination of the net credit exposures and the effective LGD.

For retail IRB approach, the effect of the credit risk mitigation is incorporated into the internal risk parameters of PD or LGD depending on the nature of the guarantees and collateral for calculating the risk exposures.

The credit and market risk concentrations within the credit risk mitigation (recognised collateral and guarantees for capital calculation) used by the Group are under a low level.

Up to the date of report, for capital calculation, except OTC derivative transactions cleared by central counterparties and derivatives subject to valid bilateral netting agreements, the Group has not used any other on-balance sheet or off-balance sheet recognised netting for credit risk mitigation. The Group also has not used any recognised credit derivative contracts for credit risk mitigation.

(D) The control mechanisms used for internal rating systems

The Group has established a comprehensive control mechanism to ensure the integrity, accuracy and consistency of the rating systems including the processes for using the risk components in the day-to-day business to assess credit risk.

All of IRB risk models are approved by the RC of the Board on the recommendation of the Asset and Liability Management Committee (“ALCO”). The Management Committee supervises the use of these internal rating models for risk identification and assessments in the Group’s credit decisions.

3. Credit risk under the internal ratings-based approach (continued)

3.1 The internal rating systems and risk components (continued)

(D) The control mechanisms used for internal rating systems (continued)

In order to achieve reasonably accurate risk ratings assignment, the Group has established a rating approval process which is independent from the sales and marketing units. Since internal rating is one of the key inputs to credit decision making, a control mechanism is put in place to ensure the integrity, accuracy and consistency of the rating assignment. For the wholesale (corporate and bank) credit portfolio, internal ratings are normally approved by credit officers who are functionally separated from the sales and marketing units. In some cases where the transactions are in small amount and of low credit risk, the credit ratings can be assigned and approved by the sales and marketing units, subject to the periodic post-approval review of ratings by RMD and other credit monitoring units.

The rating assignment and risk quantification process of retail portfolio are highly automated. As an integral part of the daily credit assessment process, the accuracy and completeness of data input for automatic rating assignment are verified by units independent from business development function.

The obligor rating is reviewed at least annually as required by the Group's credit risk policy. When credit events occur to the obligor, rating review is triggered promptly in accordance with the Group's credit risk policy.

Rating override is designed to allow credit analyst to include any other relevant credit information that has not yet been captured by rating models. For reasons of conservatism and prudential considerations, overrides are unlimited in terms of downgrades but more restricted for upgrades. All upgrades will be limited to a maximum of two sub-grades supported by a very narrowly pre-defined list of appropriate reasons. All overrides need to be signed off by a higher level of credit approval authority. The internal rating policy sets a trigger point of 10% overrides on rating cases. The use of overrides and override reasons are analysed as part of performance review on IRB rating models.

The performance of internal rating system is put under ongoing periodic monitoring. The senior management periodically reviews the performance and predictive ability of the internal rating system. The effectiveness of the internal rating system and processes are reviewed by independent control functions. The model maintenance unit conducts assessment on the discriminatory power, accuracy and stability of the rating systems while the validation unit performs comprehensive review of the internal rating system. Internal audit reviews the internal rating system and the operations of the related credit risk control units. The results of the review are reported to the Board and senior management regularly.

A model validation team which is independent from the model development unit and rating assignment units, conducts periodic model validations using both qualitative and quantitative analysis. Model acceptance standards are established to ensure the discriminatory power, accuracy and stability of the rating systems meet regulatory and management requirements. Review of a rating model will be triggered if the performance of the model deteriorates materially against pre-determined tolerance limit.

(E) Approach for determining provisions

The approach in determining provisions is in line with the Group's accounting policies. For details, please refer to Note 2.14 "Impairment of financial assets" to the Financial Statements.

3. Credit risk under the internal ratings-based approach (continued)

3.2 Exposures by IRB calculation approach

The tables below show the Group's exposures other than securitisation exposures (including the EAD of on-balance sheet exposures and off-balance sheet exposures) by each IRB calculation approach.

	2016				
	FIRB Approach HK$'m	**Supervisory Slotting Criteria Approach HK$'m**	**Retail IRB Approach HK$'m**	**Specific Risk-weight Approach HK$'m**	**Total exposures HK$'m**
Corporate	**885,221**	**–**	**–**	**–**	**885,221**
Bank	**519,508**	**–**	**–**	**–**	**519,508**
Retail					
Residential mortgages to individuals and property-holding shell companies	**–**	**–**	**236,740**	**–**	**236,740**
Qualifying revolving retail	**–**	**–**	**74,660**	**–**	**74,660**
Other retail to individuals	**–**	**–**	**36,535**	**–**	**36,535**
Small business retail	**–**	**–**	**6,223**	**–**	**6,223**
Others	**–**	**–**	**–**	**225,910**	**225,910**
	1,404,729	**–**	**354,158**	**225,910**	**1,984,797**

	2015				
	FIRB Approach HK$'m	Supervisory Slotting Criteria Approach HK$'m	Retail IRB Approach HK$'m	Specific Risk-weight Approach HK$'m	Total exposures HK$'m
Corporate	891,708	971	–	–	892,679
Bank	566,726	–	–	–	566,726
Retail					
Residential mortgages to individuals and property-holding shell companies	–	–	239,873	–	239,873
Qualifying revolving retail	–	–	71,276	–	71,276
Other retail to individuals	–	–	39,747	–	39,747
Small business retail	–	–	8,483	–	8,483
Others	–	–	–	203,613	203,613
	1,458,434	971	359,379	203,613	2,022,397

3. Credit risk under the internal ratings-based approach (continued)

3.3 Exposures subject to supervisory estimates under the IRB approach

The table below shows the total EAD of the Group's exposures subject to supervisory estimates under the use of IRB approach (including the specialised lending subject to the supervisory slotting criteria approach).

	2016 HK$'m	2015 HK$'m
Corporate	**885,221**	892,679
Bank	**519,508**	566,726
Others	**225,910**	203,613
	1,630,639	1,663,018

3.4 Exposures covered by credit risk mitigation used

(A) Exposures covered by recognised collateral

The table below shows the Group's exposures under the use of FIRB approach (after the effect of any on-balance sheet or off-balance sheet recognised netting) which are covered by recognised collateral after the application of haircuts required under the Banking (Capital) Rules. These exposures exclude securities financing transactions and derivative contracts.

	2016 HK$'m	2015 HK$'m
Corporate	**83,587**	118,423
Bank	**2,434**	1,465
	86,021	119,888

(B) Exposures covered by recognised guarantees

The table below shows the Group's exposures (after the effect of any on-balance sheet or off-balance sheet recognised netting) which are covered by recognised guarantees after the application of haircuts required under the Banking (Capital) Rules. These exposures exclude securities financing transactions and derivative contracts.

	2016 HK$'m	2015 HK$'m
Corporate	**325,038**	235,563
Bank	**27,446**	32,615
	352,484	268,178

3. Credit risk under the internal ratings-based approach (continued)

3.5 Risk assessment for corporate and bank exposures under IRB approach

The tables below detail the Group's total EAD of corporate and bank exposures by exposure-weighted average risk-weight and exposure-weighted average PD for each obligor grade as at 31 December.

The EAD and PD disclosed below in respect of corporate and bank exposures have taken into account the effect of recognised collateral, recognised netting and recognised guarantees. The Group did not have any recognised credit derivative contracts.

For definition of each obligor grade, please refer to page 287.

(A) Corporate exposures (other than specialised lending under supervisory slotting criteria approach)

	2016		
Internal Credit Grades	Exposure at default HK$'m	Exposure-weighted average risk-weight %	Exposure-weighted average PD %
Grade 1	–	–	–
Grade 2	**14,872**	**19.21**	**0.03**
Grade 3	**267,323**	**26.75**	**0.08**
Grade 4	**360,831**	**44.33**	**0.23**
Grade 5	**201,296**	**80.42**	**0.98**
Grade 6	**39,307**	**122.04**	**4.57**
Grade 7	**139**	**143.33**	**25.98**
Grade 8/Default	**1,453**	**95.05**	**100.00**
	885,221		

	2015		
Internal Credit Grades	Exposure at default HK$'m	Exposure-weighted average risk-weight %	Exposure-weighted average PD %
Grade 1	–	–	–
Grade 2	28,624	18.25	0.03
Grade 3	220,625	25.68	0.07
Grade 4	337,047	43.91	0.23
Grade 5	249,264	79.84	1.04
Grade 6	53,576	107.35	5.12
Grade 7	331	200.23	29.65
Grade 8/Default	2,241	81.96	100.00
	891,708		

3. Credit risk under the internal ratings-based approach (continued)

3.5 Risk assessment for corporate and bank exposures under IRB approach (continued)

(B) Corporate exposures (specialised lending under supervisory slotting criteria approach)

	2016		2015	
Supervisory Rating Grades	Exposure at default HK$'m	Exposure-weighted average risk-weight %	Exposure at default HK$'m	Exposure-weighted average risk-weight %
Strong	–	–	444	60.96
Good	–	–	527	88.30
Satisfactory	–	–	–	–
Weak	–	–	–	–
Default	–	–	–	–
	–		971	

The supervisory rating grades and risk-weights of specialised lending are determined in accordance with section 158 of the Banking (Capital) Rules.

(C) Bank exposures

	2016		
Internal Credit Grades	Exposure at default HK$'m	Exposure-weighted average risk-weight %	Exposure-weighted average PD %
Grade 1	–	–	–
Grade 2	92,165	20.48	0.04
Grade 3	370,591	26.63	0.06
Grade 4	55,232	44.47	0.16
Grade 5	1,355	26.56	0.60
Grade 6	165	169.38	5.45
Grade 7	–	–	–
Grade 8/Default	–	–	–
	519,508		

3. Credit risk under the internal ratings-based approach (continued)

3.5 Risk assessment for corporate and bank exposures under IRB approach (continued)

(C) Bank exposures (continued)

	2015		
Internal Credit Grades	Exposure at default HK$'m	Exposure-weighted average risk-weight %	Exposure-weighted average PD %
Grade 1	–	–	–
Grade 2	106,191	20.77	0.04
Grade 3	390,155	27.74	0.05
Grade 4	65,903	51.66	0.20
Grade 5	4,392	68.50	0.78
Grade 6	85	140.91	5.66
Grade 7	–	–	–
Grade 8/Default	–	–	–
	566,726		

3.6 Risk assessment for retail exposures under IRB approach

The tables below show breakdown of retail exposures on a pool basis by expected loss percentage (EL%) range as at 31 December.

Residential mortgages to individuals and property-holding shell companies

	2016 HK$'m	2015 HK$'m
Up to 1%	**235,659**	238,766
>1%	**985**	1,025
Default	**96**	82
	236,740	239,873

Qualifying revolving retail

	2016 HK$'m	2015 HK$'m
Up to 10%	**73,915**	70,627
>10%	**661**	607
Default	**84**	42
	74,660	71,276

3. Credit risk under the internal ratings-based approach (continued)

3.6 Risk assessment for retail exposures under IRB approach (continued)

Other retail to individuals

	2016 HK$'m	2015 HK$'m
Up to 2%	**36,081**	39,188
>2%	**363**	466
Default	**91**	93
	36,535	39,747

Small business retail

	2016 HK$'m	2015 HK$'m
Up to 1%	**5,990**	8,225
>1%	**205**	191
Default	**28**	67
	6,223	8,483

3.7 Analysis of actual loss and estimates

The table below shows the actual losses broken down by class of risk exposure, which represent the net charges (including write-offs and individually assessed impairment allowances) made by each class of exposures under the internal ratings-based approach for the year.

	2016 HK$'m	2015 HK$'m
Corporate	**284**	1,340
Bank	**–**	–
Residential mortgages to individuals and property-holding shell companies	**1**	–
Qualifying revolving retail	**211**	186
Other retail to individuals	**14**	16
Small business retail	**14**	26
	524	1,568

Decrease in the loan impairment charge of corporate exposures was mainly due to the decrease in the amount of new classified or impaired loans in 2016.

3. Credit risk under the internal ratings-based approach (continued)

3.7 Analysis of actual loss and estimates (continued)

The table below shows the expected loss broken down by class of risk exposure, which is the estimated loss likely to be incurred arising from the potential default of the obligors in respect of the exposure over a one-year period.

	Expected loss at 31 December 2015 HK$'m	Expected loss at 31 December 2014 HK$'m
Corporate	**3,663**	3,322
Bank	**183**	256
Residential mortgages to individuals and property-holding shell companies	**120**	132
Qualifying revolving retail	**384**	376
Other retail to individuals	**108**	100
Small business retail	**58**	50
	4,516	4,236

The tables below set out the actual default rate compared against the estimated PD of the respective portfolio.

	Actual default rate during 2016 %	**Estimated PD at 31 December 2015 %**
Corporate	**0.33**	**1.59**
Bank	**–**	**0.47**
Residential mortgages to individuals and property-holding shell companies	**0.04**	**0.58**
Qualifying revolving retail	**0.22**	**0.49**
Other retail to individuals	**0.55**	**1.43**
Small business retail	**0.66**	**1.13**

	Actual default rate during 2015 %	Estimated PD at 31 December 2014 %
Corporate	0.73	1.75
Bank	–	0.44
Residential mortgages to individuals and property-holding shell companies	0.05	0.65
Qualifying revolving retail	0.17	0.55
Other retail to individuals	0.56	1.50
Small business retail	0.64	1.24

3. Credit risk under the internal ratings-based approach (continued)

3.7 Analysis of actual loss and estimates (continued)

It should be noted that expected loss and actual loss are measured and calculated using different methodologies compliant with relevant regulatory and accounting standards, which therefore may not be directly comparable. The limitation arises mainly from the fundamental differences in the definition of "loss". The expected loss under Basel Accord which estimates the economic loss arising from the potential default of the obligor by taking into account the time value of money and including the direct and indirect costs associated with the recoveries on the credit exposures during the workout process, while actual loss is the net charge of individually assessed impairment allowances and write-offs made during the year in accordance with the accounting standards.

The actual default rate is measured by using the number of obligors (for wholesale exposures) or number of accounts (for retail exposures) defaulted whereas the estimated PD is an estimate of the long run average default rate over an economic cycle and is the estimated one-year forward-looking PD from the date of rating assignment.

Hence, actual default rate in a particular year ("point-in-time") will typically differ from the estimated PD which is the "through-the-cycle" estimates as economies move above or below the cyclical norms.

The estimated PD is more conservative than the actual default rate for all asset classes.

4. Credit risk under the standardised (credit risk) approach

4.1 Use of ratings from External Credit Assessment Institutions ("ECAI")

The Group adopts STC approach based on external credit rating to determine the risk weight of the small residual credit exposures that was approved by the HKMA to be exempted from FIRB approach and the exposures are listed as below:

- Sovereign
- Public sector entity
- Multilateral development bank
- Credit exposures of overseas banking subsidiaries and branches

The Group performs the ECAI issuer ratings mapping to its exposures in banking book in accordance with Part 4 of the Banking (Capital) Rules. The ECAIs recognised by the Group include Standard & Poor's, Moody's and Fitch.

4.2 Credit risk mitigation

For credit exposures adopting STC approach, the main types of recognised collateral include cash deposits, debt securities and equities for non-past due exposures. In addition, real estate collateral is also recognised for past due exposures. The treatment of recognised collateral is compliant with the comprehensive approach for credit risk mitigation as mentioned in the Banking (Capital) Rules. For credit exposures under STC approach, the recognised guarantees for capital calculation include the guarantees given by sovereigns, public sector entities, multilateral development banks, or banks and corporates with ECAI issuer ratings both exempted from FIRB approach for credit exposures, that have lower risk weights than the counterparty. Besides, the recognised netting for credit risk mitigation includes derivatives subject to valid bilateral netting agreements.

4. Credit risk under the standardised (credit risk) approach (continued)

4.3 Credit risk exposures other than securitisation exposures under the standardised (credit risk) approach

	2016						
		Exposures after CRM*		Risk-weighted amount			
	Total exposures HK$'m	Rated HK$'m	Unrated HK$'m	Rated HK$'m	Unrated HK$'m	Total exposures covered by recognised collateral HK$'m	Total exposures covered by recognised guarantees HK$'m
On-balance sheet exposures							
Sovereigns	267,085	267,085	–	19,169	–	–	–
Public sector entities	32,699	33,244	–	1,513	–	–	–
Multilateral development banks	32,596	32,596	–	–	–	–	–
Banks	1,771	1,614	157	547	41	–	–
Corporates	21,939	4,181	14,659	3,043	14,659	3,099	–
Cash items	35	–	35	–	–	–	–
Regulatory retail	11,058	–	10,642	–	7,981	415	–
Residential mortgage loans	1,050	–	503	–	247	1	545
Other exposures which are not past due	11,300	1,654	5,392	1,654	7,521	4,254	–
Past due exposures	66	–	66	–	98	–	–
Total on-balance sheet exposures	379,599	340,374	31,454	25,926	30,547	7,769	545
Off-balance sheet exposures							
Off-balance sheet exposures other than securities financing transactions and derivative contracts	10,607	5,315	5,292	1,280	5,186	–	1,033
Securities financing transactions and derivative contracts	5,975	51	1,832	7	1,404	4,436	–
Total off-balance sheet exposures	16,582	5,366	7,124	1,287	6,590	4,436	1,033
Total non-securitisation exposures	396,181	345,740	38,578	27,213	37,137	12,205	1,578
Exposures that are risk-weighted at 1,250%	–						

4. Credit risk under the standardised (credit risk) approach (continued)

4.3 Credit risk exposures other than securitisation exposures under the standardised (credit risk) approach (continued)

	2015						
	Total exposures HK$'m	Exposures after CRM* Rated HK$'m	Exposures after CRM* Unrated HK$'m	Risk-weighted amount Rated HK$'m	Risk-weighted amount Unrated HK$'m	Total exposures covered by recognised collateral HK$'m	Total exposures covered by recognised guarantees HK$'m
On-balance sheet exposures							
Sovereigns	301,750	301,991	–	16,274	–	–	–
Public sector entities	25,571	25,662	–	1,212	–	–	240
Multilateral development banks	35,333	35,333	–	–	–	–	–
Banks	553	551	2	111	–	–	–
Corporates	14,167	2,471	9,502	2,176	9,502	2,193	–
Cash items	–	–	–	–	–	–	–
Regulatory retail	11,722	–	11,240	–	8,430	482	–
Residential mortgage loans	12,500	–	12,169	–	6,085	–	331
Other exposures which are not past due	5,195	–	2,543	–	4,019	2,652	–
Past due exposures	102	–	102	–	135	34	–
Total on-balance sheet exposures	406,893	366,008	35,558	19,773	28,171	5,361	571
Off-balance sheet exposures							
Off-balance sheet exposures other than securities financing transactions and derivative contracts	6,455	3,008	3,447	517	3,361	–	702
Securities financing transactions and derivative contracts	532	104	428	18	388	1	–
Total off-balance sheet exposures	6,987	3,112	3,875	535	3,749	1	702
Total non-securitisation exposures	413,880	369,120	39,433	20,308	31,920	5,362	1,273
Exposures that are risk-weighted at 1,250%	–						

* Recognised credit risk mitigation satisfying the requirements and conditions set out in the Banking (Capital) Rules.

5. Counterparty credit risk-related exposures

The Group's counterparty credit risk arising from derivative contracts and securities financing transactions both in trading and banking book is subject to the same risk management framework as mentioned in Note 4 to the Financial Statements. The Group establishes credit limit through formal credit approval procedures to control the pre-settlement credit risk arising from derivative transactions and settlement limit to control the settlement risk arising from foreign exchange-related transactions for counterparties in both the trading book and banking book. The Group monitors the risk exposure due to fluctuations in the market by using the current exposure and the potential exposure value of the transactions. Exceptions or excesses are timely and closely identified and monitored by RMD.

Credit equivalent amount and capital charge for the relevant counterparty credit exposures are determined following the regulatory capital requirements. Currently, the Group has adopted the Current Exposure Method to measure the relevant credit equivalent amount, which comprises current exposures and potential future exposures. The relevant counterparty default risk capital charge is calculated under the FIRB/STC approach. In addition, the Group has adopted standardised credit valuation adjustment ("CVA") method to calculate the relevant counterparty CVA capital charge.

The Group establishes prudent eligibility criteria and haircut policy of debt securities being pledged as collateral for securities financing transactions.

The Group formulates policy for classification of credit assets according to the PD of counterparties and the period of overdue. If there is objective evidence that an impairment loss has been incurred, impairment allowance will be provided according to HKFRS and regulatory requirements.

In controlling and monitoring of wrong-way risk (risk of existence of positive correlation between the PD of a counterparty and credit exposures driven by mark-to-market value of the underlying transactions), specific wrong-way risk transactions are generally not allowed and monitoring measures have been formulated for those counterparties identified by stress testing that would be exposed to potential general wrong-way risk.

5. Counterparty credit risk-related exposures (continued)

5.1 Counterparty credit risk exposures under the internal ratings-based approach

The following table summarises the Group's exposures to counterparty credit risk arising from securities financing transactions and derivative contracts calculated using the Current Exposure Method. There is no effect of valid cross-product netting agreements on these exposures.

	2016		2015	
	Securities financing transactions HK$'m	**Derivative contracts HK$'m**	Securities financing transactions HK$'m	Derivative contracts HK$'m
Gross total positive fair value		**45,274**		29,657
Default risk exposures after the effect of valid bilateral netting agreements	**27,794**	**52,209**	12,808	46,036
Less: Value of recognised collateral				
– Debt securities	**(5,999)**	**–**	(489)	–
– Others	**(19,259)**	**(5,547)**	(9,104)	(1,308)
Default risk exposures after the effect of valid bilateral netting agreements net of recognised collateral	**2,536**	**46,662**	3,215	44,728
Default risk exposures by counterparty type				
Corporate	**1,783**	**6,476**	518	2,266
Bank	**26,011**	**45,733**	12,290	43,770
	27,794	**52,209**	12,808	46,036
Risk-weighted amounts by counterparty type				
Corporate	**63**	**2,331**	50	1,272
Bank	**387**	**12,351**	893	11,782
	450	**14,682**	943	13,054
Notional amounts of recognised credit derivative contracts that provide credit protection	**–**	**–**	–	–

5. Counterparty credit risk-related exposures (continued)

5.2 Counterparty credit risk exposures under the standardised (credit risk) approach

The following table summarises the Group's exposures to counterparty credit risk arising from derivative contracts calculated using the Current Exposure Method. There is no effect of valid cross-product netting agreements on these exposures.

	2016		2015	
	Securities financing transactions HK$'m	**Derivative contracts HK$'m**	Securities financing transactions HK$'m	Derivative contracts HK$'m
Gross total positive fair value		**19,172**		14,098
Default risk exposures after the effect of valid bilateral netting agreements	**–**	**5,975**	–	532
Less: Value of recognised collateral				
– Debt securities	**–**	**–**	–	–
– Others	**–**	**(4,436)**	–	–
Default risk exposures after the effect of valid bilateral netting agreements net of recognised collateral	**–**	**1,539**	–	532
Default risk exposures by counterparty type				
Sovereigns	**–**	**65**	–	105
Public sector entities	**–**	**16**	–	6
Banks	**–**	**9**	–	–
Corporates	**–**	**223**	–	215
Regulatory retail	**–**	**852**	–	132
Other exposures which are not past due	**–**	**4,810**	–	74
Past due exposures	**–**	**–**	–	–
	–	**5,975**	–	532
Risk-weighted amounts by counterparty type				
Sovereigns	**–**	**11**	–	17
Public sector entities	**–**	**3**	–	1
Banks	**–**	**2**	–	–
Corporates	**–**	**189**	–	215
Regulatory retail	**–**	**164**	–	99
Other exposures which are not past due	**–**	**1,042**	–	74
Past due exposures	**–**	**–**	–	–
	–	**1,411**	–	406
Notional amounts of recognised credit derivative contracts that provide credit protection	**–**	**–**	–	–

5. Counterparty credit risk-related exposures (continued)

5.3 Credit derivative contracts which create exposures to counterparty credit risk

The notional amounts of credit derivative contracts which create exposures to counterparty credit risk are shown as follows:

	2016 HK$'m	2015 HK$'m
Used for credit portfolio		
Credit default swaps		
Protection bought	**388**	–
Protection sold	**–**	–

6. Assets securitisation

The Group adopts the ratings-based method under IRB approach to calculate the credit risk for securitisation exposures as an investing institution. Since this approach employs mapping of external credit ratings for risk weights calculations, the Group adopts the three ECAIs (Standard & Poor's, Moody's and Fitch) recognised by the HKMA for this purpose.

The Group monitors the risks inherent in its securitisation assets and re-securitisation assets on an ongoing basis. The external credit ratings, assessment of the underlying assets and market prices are used for managing credit risk associated with the investment. For interest rate risk in its banking book, control measures for asset backed securities and mortgage backed securities include, but not limited to AFS EV and PVBP.

The Group had no outstanding exposures that are held with the intention of transferring exposures booked in the banking book and trading book into securitisation transactions as at 31 December 2016 (2015: Nil).

Securitisation exposures arising from the Group's investing activities are analysed as follows:

6.1 Securitisation exposures

	2016		2015	
	Banking book HK$'m	Trading book HK$'m	Banking book HK$'m	Trading book HK$'m
On-balance sheet exposures				
Residential mortgage loans	70	–	171	–
Student loans	–	–	–	–
	70	–	171	–
Off-balance sheet exposures	–	–	–	–

Reduction in securitisation exposures was due to repayments of principal.

There were no securitisation transactions in trading book subject to the IMM approach as at 31 December 2016 (2015: Nil).

There were no securitisation exposures that the Group has allocated a risk-weight of 1,250% as at 31 December 2016 (2015: Nil).

The Group did not have credit risk mitigations which are treated as part of securitisation transactions as at 31 December 2016 (2015: Nil).

There were no re-securitisation exposures as at 31 December 2016 (2015: Nil).

6. Assets securitisation (continued)

6.2 Breakdown by risk-weights of the securitisation exposures (excluding re-securitisation exposures) under internal ratings-based (securitisation) approach

	2016		2015	
	Securitisation exposures HK$'m	**Capital requirements HK$'m**	Securitisation exposures HK$'m	Capital requirements HK$'m
7%	**3**	**–**	66	–
8%	**18**	**–**	15	–
10%	**1**	**–**	2	–
12%	**19**	**–**	43	1
15%	**–**	**–**	–	–
18%	**–**	**–**	–	–
20%	**4**	**–**	12	–
25%	**–**	**–**	–	–
35%	**–**	**–**	–	–
50%	**–**	**–**	–	–
60%	**19**	**1**	24	1
75%	**–**	**–**	–	–
100%	**6**	**1**	9	1
250%	**–**	**–**	–	–
425%	**–**	**–**	–	–
650%	**–**	**–**	–	–
Deducted from capital	**–**	**–**	–	–
	70	**2**	171	3

Reduction in securitisation exposures and capital requirements were due to repayments of principal.

6.3 Summary of accounting policies for securitisation exposures

The Group held certain securitised debt securities at the end of the reporting period. They are classified and measured for accounting purpose in accordance with the Group's accounting policies as outlined in Notes 2.8 "Financial assets", 2.11 "Recognition and derecognition of financial instruments", 2.12 "Fair value measurement" and 2.14 "Impairment of financial assets" to the Financial Statements. For those investments measured at fair value, further details on their valuation are outlined in Note 5.1 "Financial instruments measured at fair value" to the Financial Statements.

7. Capital charge for market risk

	2016 HK$'m	2015 HK$'m
Under the standardised (market risk) approach		
Foreign exchange exposures (net)	**–**	–
Interest rate exposures		
– Non-securitisation exposure	**190**	230
Commodity exposures	**19**	19
Equity exposures	**37**	1
Under the internal models approach		
General foreign exchange and interest rate exposures	**1,405**	1,433
Capital charge for market risk	**1,651**	1,683

Market risk regulatory capital charge is calculated under the Banking (Capital) (Amendment) Rules 2011 to incorporate capital charge for stressed VAR. The following table sets out the IMM VAR and stressed VAR[1] for the general market risk exposure calculated under the IMM approach of the Group.

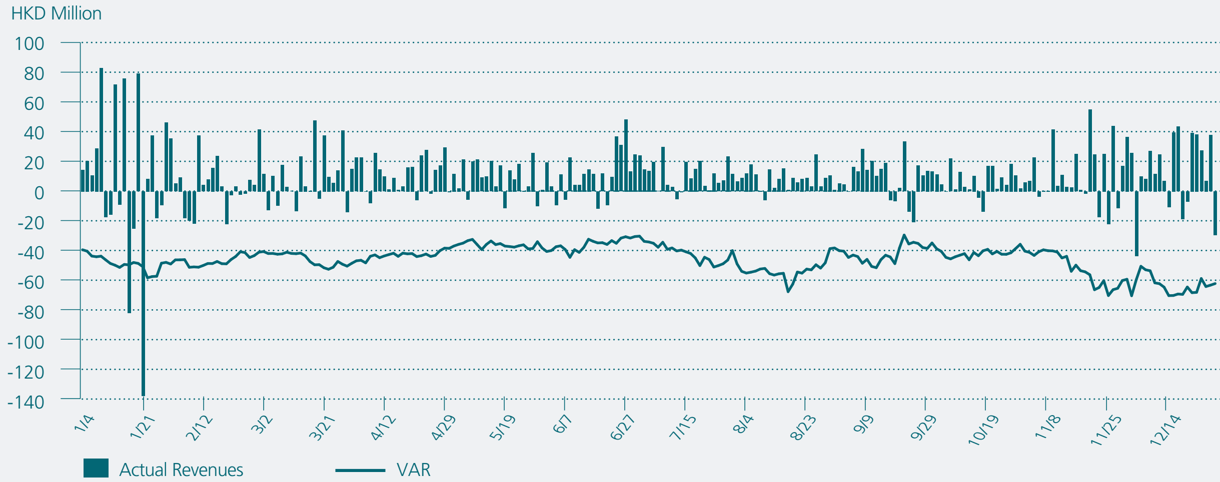
	Year	At 31 December HK$'m	Minimum for the year HK$'m	Maximum for the year HK$'m	Average for the year HK$'m
IMM VAR for foreign exchange and interest rate risk	2016	123.5	45.2	161.0	80.7
	2015	37.4	34.7	155.3	71.6
IMM VAR for foreign exchange risk	2016	103.3	32.3	107.5	56.7
	2015	27.9	25.8	77.7	36.2
IMM VAR for interest rate risk	2016	115.7	29.4	142.5	72.3
	2015	42.5	28.3	134.7	69.1
Stressed VAR for foreign exchange and interest rate risk	2016	336.1	246.3	422.1	339.8
	2015	380.5	246.7	593.0	381.3
Stressed VAR for foreign exchange risk	2016	113.1	62.5	120.9	84.5
	2015	97.1	46.5	139.6	75.6
Stressed VAR for interest rate risk	2016	336.5	259.2	455.2	332.2
	2015	414.1	259.8	618.0	377.0

Note:
1. IMM VAR and stressed VAR measures used for market risk regulatory capital purposes are calculated to a 99% confidence level and use a 10-day holding period. The stressed VAR uses the same methodology as the VAR model and is generated with inputs calibrated to the historical market data from a continuous 12-month period of significant financial stress relevant to the Group's portfolio.

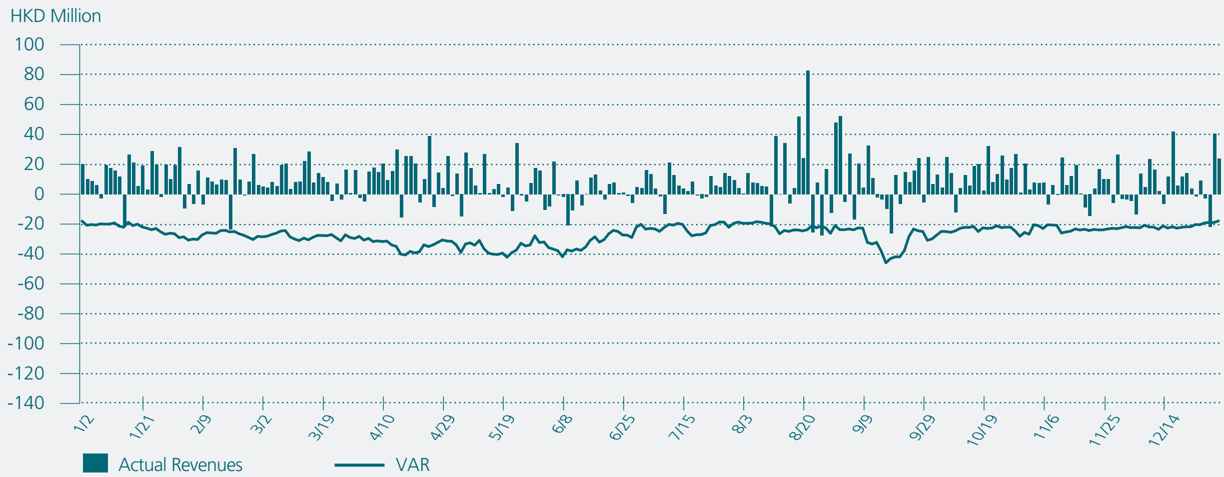
7. Capital charge for market risk (continued)

The graphs below show the regulatory back-testing result of the Group's market risk under IMM approach.

Daily Back-testing in 2016



Daily Back-testing in 2015



There were two actual losses exceeding the VAR for the Group in 2016 as shown in the back-testing results (2015: four).

8. Capital charge for operational risk

	2016 HK$'m	2015 HK$'m
Capital charge for operational risk	**5,675**	6,170

The Group uses the standardised (operational risk) approach to calculate its operational risk capital charge.

9. Equity exposures in banking book

Equity holdings in other entities are accounted for in accordance with the underlying intentions of holdings at the inception of acquisition. The classifications for equity holdings taken for relationship and strategic purposes will be separated from those taken for other purposes (including capital appreciation). Investments in equity shares which are intended to be held on a continuing basis, but which do not comprise investments in associates, joint ventures or subsidiaries, are classified as available-for-sale securities and are reported in the balance sheet as "Investment in securities".

For equity exposures in banking book other than associates, joint ventures or subsidiaries, the Group applies the same accounting treatment and valuation methodologies as detailed in the Notes 2.8(4), 2.11, 2.12 and 2.14 to the Financial Statements, further details on their valuation are outlined in Note 5.1 "Financial instruments measured at fair value" to the Financial Statements. If additional investment is made subsequently such that an investee becomes an associate, joint venture or subsidiary, then the investment is reclassified in accordance with the Group's accounting policies.

Gains or losses related to equity exposures are summarised below:

	2016 HK$'m	2015 HK$'m
Realised gains from sales	–	642
Unrealised gains on revaluation recognised in reserves but not through income statement	**176**	160

10. Connected transactions

In 2016, BOCHK, a wholly-owned subsidiary of the Company, and its subsidiaries engaged on a regular basis in the usual course of their business in numerous transactions with BOC and its Associates. As BOC is the Company's controlling shareholder and therefore a connected person of the Company, all such transactions constituted connected transactions for the purposes of the Listing Rules. The Group is subject to the control of the State Council of the PRC Government through China Investment Corporation ("CIC"), its wholly-owned subsidiary Central Huijin Investment Ltd. ("Central Huijin"), and BOC in which Central Huijin has controlling equity interests. Central Huijin is the ultimate controlling shareholder of the Company. Central Huijin has accepted PRC Government's authorisation in carrying out equity investment in core financial enterprises. For the purposes of this report, therefore, Central Huijin and its Associates have not been treated as connected persons to the Company.

10. Connected transactions (continued)

The transactions fell into the following two categories:

1. exempted transactions entered into in the ordinary and usual course of business and under normal commercial terms or better. Such transactions were (1) fully exempted from shareholders' approval, annual review and all disclosure requirements and/or (2) exempted from shareholders' approval requirement by virtue of Rules 14A.76 and 14A.87 to 14A.101 of the Listing Rules;

2. certain continuing connected transactions conducted pursuant to the Services and Relationship Agreement entered into among, inter alia, the Company and BOC dated 6 July 2002 (as amended and supplemented from time to time, which has been amended for a period of three years commencing 1 January 2014), whereas BOC has agreed to, and agreed to procure its Associates to, enter into all future arrangements with the Group on an arm's length basis, on normal commercial terms and at rates no less favourable than those offered to independent third parties, in relation to certain areas including, among others, information technology services, training services, physical bullion agency services, correspondent banking arrangements, treasury transactions, provision of insurance and syndicated loans, and the Company has agreed to, and agreed to procure its subsidiaries to, enter into all future arrangements on the same basis, provided that the rates offered by the Group to BOC and its Associates will be no more favourable than those offered to independent third parties. The Services and Relationship Agreement is also amended to allow (i) for the provision of call center services, cash management services and card services and other related business between BOC or its Associates and the Group; and (ii) the Group to provide and receive various information technology services to and from BOC's worldwide branches and subsidiaries. On 10 December 2013 the Company made an announcement (the "Announcement") in accordance with Rule 14A.47 (revised to 14A.35 and 14A.64 on 1 July 2014) of the Listing Rules, and has got the approval from the independent shareholders on 11 June 2014. The Announcement listed those continuing connected transactions that exceeded the de minimus threshold and set out caps in respect of such transactions for 2014-2016. These transactions were conducted in the ordinary and usual course of its business and on normal commercial terms or better. Details of these continuing connected transactions are set out below and are described in the announcements which may be viewed at the Company's website. The Company has complied with the disclosure requirements in accordance with Chapter 14A of the Listing Rules.

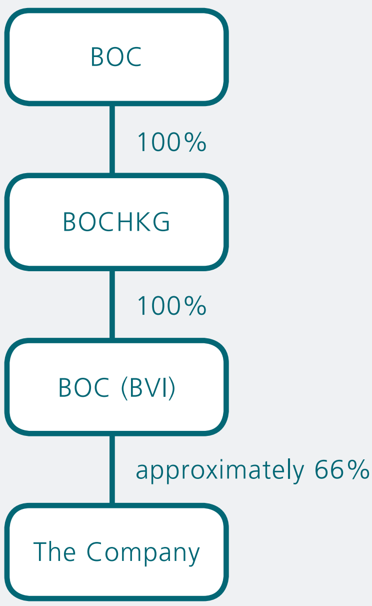
Type of Transaction	2016 Cap (HK$'m)	2016 Actual Amount (HK$'m)
Information Technology Services	1,000	63
Property Transactions	1,000	162
Bank-note Delivery	1,000	240
Provision of Insurance Cover	1,000	160
Card Services	1,000	295
Custody Business	1,000	49
Call Center Services	1,000	71
Securities Transactions	10,000	186
Fund Distribution Transactions	10,000	27
Insurance Agency	10,000	878
Foreign Exchange Transactions	10,000	443
Derivatives Transactions	10,000	145
Trading of Financial Assets	350,000	20,969
Inter-bank Capital Markets	350,000	29,362

11. Reconciliation between HKFRSs vs IFRS/CAS

The Company understands that BOC, an intermediate holding company as well as controlling shareholder of the Company, will prepare and disclose consolidated financial information in accordance with IFRS and CAS for which the Company and its subsidiaries will form part of the consolidated financial statements. The requirements of CAS have substantially converged with HKFRSs and IFRS.

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

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



Second, the Group has prepared its consolidated financial statements in accordance with HKFRSs; whereas the consolidated financial information reported to BOC is prepared in accordance with IFRS and CAS respectively. There is a difference in the election of subsequent measurement basis of bank premises by the Group and by BOC respectively.

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

11. Reconciliation between HKFRSs vs IFRS/CAS (continued)

The major differences which arise from the difference in measurement basis relate to the following:

– restatement of carrying value of bank premises; and

– deferred taxation impact arising from the above different measurement basis.

(a) Restatement of carrying value of bank premises

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

(b) Deferred tax adjustments

These represent the deferred tax effect of the aforesaid adjustments.

Profit after tax/net assets reconciliation

HKFRSs vs IFRS/CAS

	Profit after tax		Net assets	
	2016 HK$'m	2015 HK$'m	**2016 HK$'m**	2015 HK$'m
Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under HKFRSs	**56,323**	27,681	**230,560**	200,165
Add: IFRS/CAS adjustments				
Restatement of carrying value of bank premises	**6,223**	1,274	**(34,426)**	(42,389)
Deferred tax adjustments	**(938)**	(105)	**5,843**	7,104
Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under IFRS/CAS	**61,608**	28,850	**201,977**	164,880

Appendix

Subsidiaries of the Company

The particulars of subsidiaries are as follows:

Name	Place and date of incorporation/ operation	Issued share capital/ registered capital	Interest held	Principal activities
Directly held:				
Bank of China (Hong Kong) Limited	Hong Kong 16 October 1964	Ordinary shares HK$43,042,840,858	100.00%	Banking business
BOC Group Life Assurance Company Limited	Hong Kong 12 March 1997	Ordinary shares HK$3,538,000,000	51.00%	Life insurance business
BOCHK Asset Management (Cayman) Limited	Cayman Islands 7 October 2010	Ordinary shares HK$50,000,000	100.00%	Investment holding
Indirectly held:				
Chiyu Banking Corporation Limited	Hong Kong 24 April 1947	Ordinary shares HK$300,000,000	70.49%	Banking business
Bank of China (Malaysia) Berhad	Malaysia 14 April 2000	Ordinary shares RM760,518,480	100.00%	Banking business
BOC Credit Card (International) Limited	Hong Kong 9 September 1980	Ordinary shares HK$480,000,000	100.00%	Credit card services
Bank of China (Hong Kong) Nominees Limited	Hong Kong 1 October 1985	Ordinary shares HK$2	100.00%	Nominee services
Bank of China (Hong Kong) Trustees Limited	Hong Kong 6 November 1987	Ordinary shares HK$3,000,000	100.00%	Trustee and agency services
BOC Group Trustee Company Limited	Hong Kong 1 December 1997	Ordinary shares HK$200,000,000	66.00%	Trustee services
BOCHK Asset Management Limited	Hong Kong 28 October 2010	Ordinary shares HK$39,500,000	100.00%	Asset management
BOCHK Financial Products (Cayman) Ltd.	Cayman Islands 10 November 2006	Ordinary shares US$50,000	100.00%	Issuing structured notes
BOCHK Information Technology (Shenzhen) Co., Ltd.	PRC 16 April 1990	Registered capital HK$70,000,000	100.00%	Property holding and investment
BOCHK Information Technology Services (Shenzhen) Co., Ltd.	PRC 26 May 1993	Registered capital HK$40,000,000	100.00%	Information technology services
BOCI-Prudential Trustee Limited	Hong Kong 11 October 1999	Ordinary shares HK$300,000,000	42.24%*	Trustee services
Che Hsing (Nominees) Limited	Hong Kong 23 April 1980	Ordinary shares HK$10,000	100.00%	Nominee services
China Bridge (Malaysia) Sdn. Bhd.	Malaysia 24 April 2009	Ordinary shares RM1,000,000	100.00%	China visa application
Chiyu Banking Corporation (Nominees) Limited	Hong Kong 3 November 1981	Ordinary shares HK$100,000	70.49%	Investment holding
Grace Charter Limited	Hong Kong 4 May 2001	Ordinary shares HK$2	70.49%	Investment holding

Subsidiaries of the Company (continued)

Name	Place and date of incorporation/ operation	Issued share capital/ registered capital	Interest held	Principal activities
Po Sang Financial Investment Services Company Limited	Hong Kong 23 September 1980	Ordinary shares HK$335,000,000	100.00%	Gold trading and investment holding
Po Sang Securities and Futures Limited	Hong Kong 19 October 1993	Ordinary shares HK$335,000,000	100.00%	Securities and futures brokerage
Seng Sun Development Company, Limited	Hong Kong 11 December 1961	Ordinary shares HK$2,800,000	70.49%	Investment holding
Sin Chiao Enterprises Corporation, Limited	Hong Kong 13 September 1961	Ordinary shares HK$3,000,000	100.00%	Property holding and investment
Sin Hua Trustee Limited	Hong Kong 27 October 1978	Ordinary shares HK$3,000,000	100.00%	Trustee services
Sino Information Services Company Limited	Hong Kong 11 February 1993	Ordinary shares HK$7,000,000	100.00%	Information services

* BOCI-Prudential Trustee Limited is a subsidiary of a non-wholly-owned subsidiary of the Company and, accordingly, is accounted for as a subsidiary by virtue of the Company's control over it.

The disposal of Nanyang Commercial Bank, Limited, Kwong Li Nam Investment Agency Limited, Nanyang Commercial Bank (China), Limited, Nanyang Commercial Bank (Nominees) Limited and Nanyang Commercial Bank Trustee Limited was completed on 30 May 2016.

The acquisition of Bank of China (Malaysia) Berhad and China Bridge (Malaysia) Sdn. Bhd. was completed on 17 October 2016.

Sino Information Services Company Limited was dissolved on 14 February 2017.

The disposal of Chiyu Banking Corporation Limited, Chiyu Banking Corporation (Nominees) Limited, Grace Charter Limited and Seng Sun Development Company, Limited was completed on 27 March 2017.

Definitions

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

Terms	Meanings
"ABS"	Asset-backed Securities
"ADR"	American Depositary Receipt
"ADS(s)"	American Depositary Share(s)
"ALCO"	the Asset and Liability Management Committee
"AT1"	Additional Tier 1
"ATM"	Automated Teller Machine
"Associates"	has the meaning ascribed to "associates" in the Listing Rules
"BOC"	Bank of China Limited, a joint stock commercial bank with limited liability established under the laws of the PRC, the H shares and A shares of which are listed on the Hong Kong Stock Exchange and the Shanghai Stock Exchange respectively
"BOC (BVI)"	BOC Hong Kong (BVI) Limited, a company incorporated under the laws of the British Virgin Islands and a wholly-owned subsidiary of BOCHKG
"BOCCC"	BOC Credit Card (International) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOCHK
"BOCG Insurance"	Bank of China Group Insurance Company Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOC
"BOCHKG"	BOC Hong Kong (Group) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOC
"BOCHK" or "the Bank"	Bank of China (Hong Kong) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of the Company
"BOCI"	BOC International Holdings Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOC
"BOCI-Prudential Manager"	BOCI-Prudential Asset Management Limited, a company incorporated under the laws of Hong Kong, in which BOCI Asset Management Limited, a wholly-owned subsidiary of BOC International Holdings Limited, and Prudential Corporation Holdings Limited hold equity interests of 64% and 36% respectively
"BOCI-Prudential Trustee"	BOCI-Prudential Trustee Limited, a company incorporated under the laws of Hong Kong, in which BOC Group Trustee Company Limited and Prudential Corporation Holdings Limited hold equity interests of 64% and 36% respectively
"BOC Life"	BOC Group Life Assurance Company Limited, a company incorporated under the laws of Hong Kong, in which the Group and BOCG Insurance hold equity interests of 51% and 49% respectively
"BOC Malaysia"	Bank of China (Malaysia) Berhad, a wholly-owned subsidiary of BOCHK
"Board" or "Board of Directors"	the Board of Directors of the Company
"CAS"	China Accounting Standards for Business Enterprises
"CE"	Chief Executive
"CET1"	Common Equity Tier 1
"CFO"	Chief Financial Officer
"CIC"	China Investment Corporation
"CRM"	Credit Risk Mitigation
"CRO"	Chief Risk Officer
"CVA"	Credit Valuation Adjustment
"Central Huijin"	Central Huijin Investment Ltd.

Terms	Meanings
"Chiyu"	Chiyu Banking Corporation Limited, a company incorporated under the laws of Hong Kong, in which BOCHK holds an equity interest of 70.49%
"DCE"	Deputy Chief Executive
"DVA"	Debit Valuation Adjustment
"EAD"	Exposure at Default
"ECAI(s)"	External Credit Assessment Institution(s)
"EL"	Expected Loss
"EV"	Economic Value Sensitivity Ratio
"FIRB"	Foundation Internal Ratings-based
"Fitch"	Fitch Ratings
"GDP"	Gross Domestic Product
"HIBOR"	Hong Kong Interbank Offered Rate
"HKAS(s)"	Hong Kong Accounting Standard(s)
"HKFRS(s)"	Hong Kong Financial Reporting Standard(s)
"HKICPA"	Hong Kong Institute of Certified Public Accountants
"HKMA"	Hong Kong Monetary Authority
"Hong Kong" or "Hong Kong SAR" or "HKSAR"	Hong Kong Special Administrative Region
"ICAAP"	Internal Capital Adequacy Assessment Process
"IFRS"	International Financial Reporting Standards
"IMM"	Internal Models
"IRB"	Internal Ratings-based
"IT"	Information Technology
"LCO"	the Legal & Compliance and Operational Risk Management Department
"LCR"	Liquidity Coverage Ratio
"LGD"	Loss Given Default
"LIBOR"	London Interbank Offered Rate
"Listing Rules"	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited
"MBS"	Mortgage-backed Securities
"MC"	the Management Committee
"MPF"	Mandatory Provident Fund
"MPF Schemes Ordinance"	the Mandatory Provident Fund Schemes Ordinance, Chapter 485 of the Laws of Hong Kong, as amended
"Mainland" or "Mainland of China"	the mainland of the PRC
"Medium Term Note Programme"	the medium term note programme was established by BOCHK on 2 September 2011
"Moody's"	Moody's Investors Service
"NCB"	Nanyang Commercial Bank, Limited, a company incorporated under the laws of Hong Kong
"NCB (China)"	Nanyang Commercial Bank (China), Limited, a company incorporated under the laws of the PRC

Definitions

Terms	Meanings
"ORSO schemes"	the Occupational Retirement Schemes under Occupational Retirement Schemes Ordinance, Chapter 426 of the Laws of Hong Kong
"OTC"	Over-the-counter
"PD"	Probability of Default
"PRC"	the People's Republic of China
"PVBP"	Price Value of a Basis Point
"QDII"	Qualified Domestic Institutional Investors
"RC"	the Risk Committee
"RMB" or "Renminbi"	Renminbi, the lawful currency of the PRC
"RMD"	the Risk Management Department
"RWA"	Risk-weighted Assets
"SFO"	the Securities and Futures Ordinance, Chapter 571 of the Laws of Hong Kong
"SME(s)"	Small and Medium-sized Enterprise(s)
"STC"	Standardised (Credit Risk)
"STM"	Standardised (Market Risk)
"STO"	Standardised (Operational Risk)
"Standard & Poor's"	Standard & Poor's Ratings Services
"Stock Exchange" or "Hong Kong Stock Exchange" or "Stock Exchange of Hong Kong"	The Stock Exchange of Hong Kong Limited
"the Company"	BOC Hong Kong (Holdings) Limited, a company incorporated under the laws of Hong Kong
"the Group"	the Company and its subsidiaries collectively referred as the Group
"US"	the United States of America
"VAR"	Value at Risk

REVIEW OF ANNUAL RESULTS

The 2016 annual results have been reviewed by the Audit Committee of the Company.

By Order of the Board
LUO Nan
Company Secretary

Hong Kong, 31 March 2017

As at the date of this announcement, the Board comprises Mr TIAN Guoli (Chairman), Mr CHEN Siqing* (Vice Chairman), Mr YUE Yi (Vice Chairman and Chief Executive), Mr REN Deqi*, Mr GAO Yingxin*, Mr XU Luode*, Mr LI Jiuzhong, Madam CHENG Eva**, Dr CHOI Koon Shum**, Mr KOH Beng Seng** and Mr TUNG Savio Wai-Hok**.*

* *Non-executive Directors*
** *Independent Non-executive Directors*