

## CHAIRMAN'S STATEMENT

I am pleased to report that the Group's business continued to prosper in the first half of 2006. During this period, the Group's net operating income before loan impairment increased strongly by 26.5% to HK\$10,517 million, the highest since the Group's IPO in 2002. This encouraging growth was led mainly by the substantial rise in net interest income and net fee income by 26.2% and 21.2% respectively year-on-year as well as a net loan impairment release of HK\$642 million and an investment property revaluation gain of HK\$477 million. Pre-provision operating profit was up by an even stronger 34.3% to HK\$7,546 million. Profit attributable to shareholders increased by 8.4% year-on-year to HK\$7,093 million whereas earnings per share were up 8.4% to HK\$0.6709 (2005 interim earnings per share (restated): HK\$0.6191). The Group's asset quality continued to improve side by side with the financial results. Our impaired loan ratio dropped to 1.09% versus 1.28% as at the end of 2005.

As a result of our good business results and healthy financial position, the Board has declared an interim dividend for the first half of 2006 of HK\$0.401 per share (2005 interim dividend: HK\$0.328 per share), an increase of 22.3% as compared to the same period last year. Payout ratio for the first half of the year increased to 59.8% (2005 interim payout ratio (restated): 53.0%).

In line with our expectation, the Hong Kong economy continued to perform well. External trade experienced robust growth, fuelled primarily by strong demand from the Mainland and, to a lesser extent, Europe. Private consumption spending increased as the local labour market kept improving and wages were on the rise. Business sentiments were buoyant, leading to increased investment in machinery and equipment. The local stock market was particularly upbeat in the first two quarters with a considerable number of large-scale IPOs, including that of BOC. However, local interest rates continued to rise, trailing the US trend, which led to the lackluster performance of the property market.

Under this largely benign business climate and with the intrinsic strengths and growth momentum built up within the Group in the past three to four years, we have been able to forge ahead with our 2006-2011 Strategic Plan approved by the Board last year. Our vision is to evolve into a full-fledged top-quality financial services group with a powerful base in Hong Kong, a solid presence in China and a strategic foothold in the region. We have made some significant headway in the first half of 2006 in that direction.

The first major step we have taken was the acquisition of a 51% controlling stake in BOC Life, which was indirectly and wholly owned by our parent, BOC. The acquisition was made at a consideration of HK\$900 million and was financed by our internal cash reserves. BOC Life's main business is in offering life insurance policies in Hong Kong and to a lesser extent, in writing life insurance policies linked to investment products and retirement scheme management. The acquisition is in line with our strategy and represents a concrete step in our pursuit of new capabilities and business that can in the course of time allow us to move further up the value chain, diversify our income base and further improve our overall profit margin.

A crucial part of our strategy has been to deepen our corporate culture and reinforce our human resources management. We made steady progress in that connection in the period under review. Major initiatives were taken to enhance the team spirit throughout the Group and promote BOCHK's corporate image. On the other hand, we continued to improve our staff's remuneration package, having regard to the job market conditions and our policy of giving due recognition to the staff's contribution to the Group's business performance.

In terms of business development, our priority in the interim period was to pursue qualitative growth, focusing more on the higher-yielding business segments than on



across-the-board volume growth as in the recent past. Our key objective in this regard has been to achieve higher segmental profit and, hence, higher overall profit. I am satisfied that we have been on track in that regard and making good progress in delivering higher operating profit as well as net profit.

On the back of its strong market position, our retail banking continued to achieve encouraging growth in business volume and operating profit due mainly to the rise in net interest income and net fees and commissions income, notwithstanding the negative impact of keen competition on the growth of personal loans and residential mortgage lending. Our corporate banking business also experienced comparable growth in net operating income before loan impairment due to a strong increase in net interest income. On the treasury front, we recorded strong growth through investment portfolio diversification as well as increasing investment level under an asset allocation plan. The Group's net interest margin increased to 1.84% whereas the gross yield on average loans and securities also improved as a result of our conscious effort to drive yield growth. At the same time, in line with our strategic priority, the Group's net fees and commission income, particularly from stockbroking and asset management, grew at a much faster pace than our traditional lending business.

In accordance with our Strategic Plan, we have been striving to grow our business and build a stronger presence in the Mainland of China. The Group's operating income in this market reported healthy double-digit growth and recorded a marginal increase in total loans to customers. We continued to collaborate with BOC on various business fronts, including cross-border and wealth management businesses. In the first half of this year, two more of our branches in the Mainland were approved to conduct RMB business, which is conducive to our position in the Mainland.

Meanwhile, the Group has continued to practice good

corporate governance and comply with the Code on Corporate Governance Practices under the Listing Rules. We have also further enhanced our Board structure recently. Of the 13 Board Members, an overwhelming majority of 12 are Non-executive Directors or Independent Non-executive Directors (INEDs) after the joining of two Independents late last year and earlier this year respectively. Of the 12 Non-executives, six are INEDs. The Audit Committee, Risk Committee and Strategy & Budget Committee, are all chaired by INEDs.

Overall speaking, I am pleased that we have been on course in implementing the Group's 2006-2011 Strategic Plan. Looking ahead, we expect the Hong Kong economy to remain in a state of steady growth. Consumer spending is likely to grow in view of a better job market and rising household income. Capital investments should continue to be active. A higher degree of uncertainty, however, is expected of the external environment due to the volatility in oil prices, less favourable trade prospects and the Mainland's macroeconomic adjustment measures. Regardless of all these uncertainties, we will move forward with implementing our Strategic Plan in the remainder of the year, with special emphasis on achieving higher profitability and higher profit margin. BOC Life will allow us to tap the potential of our extensive customer base even further.

To conclude, I would like to extend my appreciation to the Board of Directors for their guidance and to all our staff for their good work.



**XIAO Gang**  
Chairman

Hong Kong, 29 August 2006