2007 witnessed the 90th year of our operation and the fifth anniversary of the Group's public listing in Hong Kong. In the year under review, we once again achieved encouraging business growth as we pushed forward with our strategic plan for 2006-2011. Having reinforced our business model and core competencies, we made significant progress in expanding our major businesses, particularly the high-yield segments, and capturing new business opportunities arising from the economic upturn.

Key Business Achievements

Let me first highlight our major business achievements in 2007.

- We accomplished or exceeded our growth targets on nearly all business fronts, with improvements in our key financial ratios.

- Broad-based growth was achieved in our core lending business, coupled with an advancement in our credit structure. In particular, we witnessed sturdy performance in high-yield segments such as trade finance, SME loans and Mainland lending.

- In our established business areas, we managed to maintain our market leadership and growth momentum, including loan syndication, residential mortgage and RMB banking services in Hong Kong.

- We substantially expanded our personal banking segment by boosting the growth of wealth management, retail stock brokerage and insurance service.

- Exceptionally strong growth was recorded in net fees and commission income by drastically expanding the investment and insurance segments.

- In the Mainland market, we sped up the growth of income and profit, expanded our business scope, strengthened our presence and commenced the operation of NCB (China).

- We enhanced our asset and liability management and widened our net interest margin.

- The implementation of the Relationship-Product-Channel (RPC) model, launched in early 2007, has been highly successful as witnessed by the strength of our business platform in driving organic growth and new product development while further improving our workflow, operational efficiency and service quality.

- We continued to pursue high standards of corporate governance, risk management and internal control.

Financial Performance

Thanks to the robust economic environment in our major markets and underpinned by our internal strengths, we were able to achieve remarkable business performance across the board. Net operating income before impairment allowances increased by 27.9% to HK$27,254 million. Operating profit before impairment allowances grew by 32.1% to HK$19,481 million.

Despite a significant reduction in net loan impairment write-back and the charges for impairment allowances on securities investments amid the volatile financial markets, our earnings continued to grow at a steady pace during the year. Profit attributable to shareholders grew by 10.3% to HK$15,446 million. Earnings per share increased by 10.3% to HK$1.4609.

Return on average total assets (ROA) and return on average shareholders' funds (ROE) were 1.53% and 17.40% respectively, versus 1.56% and 17.02% respectively for 2006. As a reflection of strong growth in our business, ROA and ROE before impairment allowances rose by 0.28 percentage point and 4.03 percentage points to 1.89% and 21.95% respectively.

The Group's net interest income increased by 22.5% to HK$19,395 million due, firstly, to the growth in interest-earning assets and, secondly, to the widening of net interest margin. The Group's average interest-earning assets saw a healthy growth of 12.3% which was driven by both the expansion of its lending business and the increase in customer deposits. Our efforts in facilitating loan growth paid off well, with loans and advances to customers up by 19.0% year-on-year to HK$413,062 million. While maintaining our market leadership in residential mortgage and loan syndication, we effectively expanded the high-margin segments such as trade finance, SME loans and Mainland lending.

Against the backdrop that market interest rates became more volatile and the yield curve steepened in the latter part of the year, we succeeded in widening the Group's net interest margin due to an improved asset mix, better management in funding costs as well as higher investment yield. As net interest spread generally improved, our net interest margin widened to 2.07% from 1.90% of 2006.

Our strenuous effort in expanding the Group's fee-based income was rewarding. Net fees and commission income grew strongly, surging by 68.8% to HK$6,274 million, attributable primarily to the robust performance of the Group's stock brokerage segment. On the back of an active stock market and having enhanced our e-channels for retail customers, we boosted stock transaction volume substantially by 187.5%. Stock brokerage commission increased by 157.4% to HK$3,560 million. At the same time, by promoting our asset management business, we saw an impressive growth of 115.5% in related fee income as the sales of open-end funds surged by 125.8%. Fee income from the sales of bonds also increased by an impressive 101.0% after the introduction of private placement services which drove up the sales of structured notes by 195.8%.

Net trading income fell by 35.4% to HK$1,013 million as a result of a decrease of 28.1% in net trading income from foreign exchange and foreign exchange-related products. Should we exclude the net trading loss of foreign exchange swap contracts which arose from the Group's funding activities, the income from other foreign exchange activities would have gone up by 26.8%.

We continued to exercise a high degree of prudence in managing costs while equipping ourselves sufficiently for business growth and service enhancement. The Group's total operating expenses for 2007 increased by 18.5% to HK$7,773 million. This was due partly to our continued investment in human resources and technology and partly to salary adjustment to maintain the competitiveness of our remuneration package in the market. Notwithstanding such increases, our cost-to-income ratio was 28.52% (versus 30.78% in 2006), which was low by industry standards.

The Group's total assets increased by a healthy 14.9% to top the HK$1,000 billion mark and reached HK$1,067.6 billion by end-2007. Customer deposits increased by 13.6% to HK$799,565 million. With effective risk management and internal control, the Group's loan quality improved further. Classified or impaired loan ratio declined by 0.13 percentage point to 0.44%.

The Group's capital and liquidity positions remained strong. Consolidated capital adequacy ratio was 13.08% at the end of 2007, versus 13.99% (based on Basel I) at end-2006. Average liquidity ratio stood at 50.92% for the year of 2007, as compared with 50.46% for 2006. Our exposure to US sub-prime asset-backed securities was reduced significantly to HK$4.1 billion as at 31 December 2007, versus HK$12.8 billion as at 30 June 2007.

Business Review

The performance of our various major business streams in 2007 reflects the prowess of the Group's new business model and enhanced operating platforms in driving income and profit growth.

Personal Banking

The Group's Personal Banking business continued to expand and posted strong growth in 2007. Most strikingly we improved our income base by drastically increasing fees and commission income from stock brokerage, sales of funds and bonds, etc. while maintaining healthy growth in net interest income.

Net operating income before impairment allowances rose by a strong 40.0% to HK$14,075 million. Net interest income went up by 16.3% to HK$8,144 million with the growth of mortgage loans and other consumer lending. Other operating income soared by 94.5% to HK$5,931 million as a result of the 106.5% growth in net fees and commission income. Profit before taxation increased by 58.0% to HK$8,129 million.

The surge in fees and commission income was the result of the Group's effort in driving the growth of investment and insurance agency services through product innovation and service enhancement. To capture demand arising from the robust stock market, the Group actively promoted its stock brokerage service during the year. By reinforcing our internet and telephone banking service platform, we grew the stock brokerage business considerably by 187.5%, which was led by the 287.4% increase via automated channels. As the receiving bank for most of the large-scale IPOs in Hong Kong over the previous year, our IPO-related fees and commission income increased by 75.0%. Meanwhile, our product offerings have been expanded to meet customers' demand for more sophisticated investment products. As a result, the sales of structured notes rose by 195.8% while the sales of open-end funds grew by 125.8%. We also recorded an impressive sales growth of 45.2% in life insurance products through initiatives in product manufacturing, brand building, marketing and service enhancement. All in all, the Group's investment and insurance fee income saw a strong growth of 143.7% in 2007.

The local property market continued to revive during the year, giving rise to the demand for mortgage loans. In response, we promoted our mortgage services aggressively with a wider range of innovative mortgage products to serve the diverse needs of customers, thus growing our residential mortgage business by 9.9% year-on-year, versus the market average of 5.4%. In 2007, we have maintained our position as the market leader in mortgage business.

The wealth management segment also posted impressive results in 2007 as we placed special emphasis on customer stratification and expanded our service portfolio targeting high net-worth customers. We launched private placement services in early 2007 to offer wealth management customers various investment choices. Our brokerage service in bonds was also enhanced. Meanwhile we engaged in innovative marketing campaigns and upgraded our service quality through more vigorous staff training. By the end of the year, the number of wealth management customers and the amount of assets under our management were up significantly by 68% and 46% respectively.

The credit card segment continued to grow in terms of card issuance, cardholder spending and merchant acquiring volume, which increased by 10.2%, 24.1% and 32.3% respectively year-on-year. We owed these encouraging results to our innovative efforts in product development, marketing and system upgrade. Aside from expanding in the local market, we made a strategic move by forming a joint venture, BOC Services Company Limited, between BOC-CC and BOC in November to provide back-end support to BOC Group Bank Card in the Mainland, which will give us an advantage in developing card business in China.

We remained the market leader and further expanded our RMB banking business in Hong Kong. By end-2007, our RMB deposits grew by 41.3% year-on-year. We led the market in RMB credit card issuance and RMB card merchant acquiring businesses as well as other RMB-related banking services. With the further expansion of RMB banking business in Hong Kong, we commenced the RMB bond service in June 2007 that comprises subscription, custody and coupon collection. Furthermore, we acted as the joint lead manager, bookrunner and placing bank for the RMB bonds issued by all the three Mainland banks in Hong Kong last year.

To cope with business growth and to improve service quality, we continued to optimise our branch network by setting up more wealth management centres to serve high net-worth customers. Our internet and telephone banking platform was further reinforced to support the growth of automated stock trading.

Corporate Banking

Corporate Banking business delivered solid growth and optimised its business structure in 2007. While maintaining our market leadership in loan syndication, we focused on expanding the high-margin segments for better returns.

Net operating income before impairment allowances increased by a healthy 14.5% to HK$7,669 million. Net interest income went up by 14.6% to HK$5,739 million due mainly to loan growth in various segments. Other operating income grew by 14.4% to HK$1,930 million benefiting from the increases in loan and bills commission income as well as in fees income from both trust and payment services. Owing to a significant reduction in net release of loan impairment allowances, profit before taxation fell by 5.0% to HK$6,526 million.

The Group continued to be the top arranger in the loan syndication market covering Hong Kong, Macau and the Mainland of China. One of the syndicated loans we arranged was ranked among the top three financing projects in the Asia-Pacific region in 2007. In this connection, I am pleased to report that in early 2008 BOCHK has been appointed by the BOC group as the principal bank for its Asia-Pacific Loan Syndication Centre. This appointment enhances our position in loan syndication and facilitates us in reaching out to the Region.

The Group recorded outstanding growth in its IPO financing business. Spurred by the robust stock market and our own intense marketing effort, our IPO financing volume grew by 162.1% to HK$528 billion covering some 48 newly listed entities.

In accordance with our strategic plan, we put emphasis on growing the high-margin segments and improving our loan mix with great success in 2007. By refining our SME business model, establishing a SME marketing team, streamlining the credit approval procedure and strengthening product innovation, we attained an impressive growth of 32.2% in SME lending. At the same time, through our intensive marketing and sales effort, the outstanding balance of trade finance and the volume of trade bills increased by 43.9% and 22.9% respectively, of which SMEs accounted for an increased proportion.

In terms of new business development, we have made much headway in cash management and custody services. A cash management team has been set up to take charge of product development and marketing. In 2007, we embarked on cross-border cash management projects for large Mainland enterprises seeking global expansion. Concurrently, we have established a custody business team to provide securities settlement and custody services for institutional clients and Qualified Domestic Institutional Investors (QDIIs). Relevant service platforms have been put in place for local custody, global custody and escrow services.

Mainland Business

Our Mainland branches registered remarkable results in 2007. Operating profit before impairment allowances increased by HK$200 million or 53.5%. Total advances to customers were up by 60.9% to HK$30 billion, of which RMB loans increased by 194.2%. Customer deposits increased by 48.4% to HK$5.8 billion. Loan quality remained good with the classified loan ratio standing at 0.68%. The business scope of our branch network in China continued to expand. Of our 15 branches and sub-branches in the Mainland, 12 have been permitted to conduct RMB business (except for Mainland residents) while 13 have been qualified as QDIIs. During the year, we formed strategic alliances with a number of insurance companies to develop insurance agency business in China. Moreover, we introduced a number of QDII products that were met with enthusiastic response from Mainland customers.

The Group's wholly-owned subsidiary Nanyang Commercial Bank (China) Limited – NCB (China) in short – was officially incorporated in China on 14 December 2007 and commenced operation at its Shanghai headquarters as from 24 December 2007. This is a milestone for the Group on its way to attaining a solid presence in China as NCB (China) is an integral part of the Group's dualistic approach in developing its Mainland business. It will offer comprehensive banking services in China while BOCHK and Chiyu Banking Corporation remain foreign-funded banks focusing on corporate banking and foreign exchange businesses in China.

Treasury

The Group's Treasury business continued to grow by diversifying its investment portfolio, expanding its product offerings and capturing new demand.

Net operating income before impairment allowances increased by 18.0% to HK$6,075 million, due primarily to the 33.2% rise in net interest income which was attributable to the growth of surplus funds and higher investment yield. Other operating income decreased by 72.3% to HK$206 million, caused mainly by the net trading loss from foreign exchange swap contracts and lower net trading income from interest rate instruments and commodities. Profit before taxation decreased by 28.3% to HK$3,315 million. Impairment allowances of HK$2,133 million have been provided for the Group's portfolio of US asset-backed securities.

In view of the increasing volatility in the market, the Group closely monitored its asset and liability structure as well as the movements of credit spread. Appropriate investment strategies were adopted to grow the return on surplus funds. In addition, we captured a substantial chunk of the local IPO business during the year. In our role as receiving bank for 36 IPOs, we managed a total of over HK$1,900 billion in IPO-related funds.

We expanded our treasury product portfolio with concrete results. We embarked on a notes programme by issuing the first batch of structured notes in February 2007. Our equity warrants were also launched and are now traded on the Stock Exchange of Hong Kong. These products have attracted keen response from customers. To further diversify our product range and solidify our position in the local RMB market, we stepped up the marketing of RMB non-deliverables forward contracts.

Insurance

The Insurance segment achieved satisfactory growth in 2007 by enhancing its product offerings and service quality.

Net operating income before impairment allowances increased by a strong 58.2% to HK$378 million. Net interest income surged by 66.6% to HK$788 million due mainly to increased investment in debt securities made possible by significant growth in premium income. Other operating income grew by 40.6% to HK$9,030 million with higher net insurance premium income. Profit before taxation increased by 50.0% to HK$261 million.

The synergy effect expected of the acquisition by the Group of BOC Life in 2006 was becoming increasingly evident. Supported by the Group's extensive distribution network and through product innovation, service enhancement, and brand building, we not only heightened income and profit but also strengthened our market position and captured a larger market share in the insurance business.

Outlook

Looking ahead, we are cautiously positive about the economic prospects of our two major markets – Hong Kong and the Mainland – in 2008. The Hong Kong economy is forecast to sustain stable GDP growth as investor and consumer sentiments remain favourable. Continued improvement in the local labour market and household income will be conducive to consumer spending, property sales and the demand for banking services. Across the border, the Chinese economy is expected to stay on a healthy growth track and give rise to fresh business opportunities for Hong Kong. However, we will not underestimate the negative impact of the higher degree of uncertainty hovering over the global credit market in general and the US economy in particular. The investment market and interest rate movements would likely be subject to greater volatility. At the same time, inflationary pressure is expected to persist with internal demand and imports, thus resulting in higher operating costs – something we need to manage more proactively.

We are now into the third year of our 2006-2011 strategic plan. Our priority this year is to make the most of our successfully implemented RPC model to fortify our leading market position in Hong Kong. We will take advantage of our significantly reinforced customer relationship platforms to drive growth in product distribution through cross-selling. We will leverage our enhanced product manufacturing capabilities to develop and diversify our service portfolio. With better channel utilisation and workflow, we are now in a better position to achieve more effective marketing and sales.

Given the momentum and the good results achieved in the past year, we will strive to maintain our lead in the Group's strong segments, including mortgage lending, loan syndication and RMB banking services in Hong Kong. We will focus on further improving our loan structure by growing high ROE segments, including SME loans, trade finance, as well as personal loans and credit card business. By exploiting our enhanced customer platform and segmentation, we aim to drive the growth of wealth management services for high net-worth customers. We will also solidify our market position in fast growing areas such as investment and insurance agency services and place special emphasis on increasing non-interest income.

The Mainland sector is expected to grow in importance in the Group's development. Now that NCB (China) is in full swing, we will expand our services to customers and identify suitable locations in targeted cities to enlarge our branch network in China. At the same time, we will continue to forge closer cooperation with BOC for business development and mutual gains. In the area of personal banking, we will introduce our wealth management services to Mainland customers and expand our credit card business. On the corporate banking front, with initial success in 2007, our key emphases in the coming year are to grow our cash management and custodian services in collaboration with BOC and play an active role as service provider for big corporations, institutional clients and QDIIs in the Mainland. BOC Services Company Limited, our new joint venture with BOC, will help us strengthen bank card-related service and support in the rapidly growing Mainland market. By leveraging our position as the principal bank for BOC's Asia-Pacific Loan Syndication Centre, we will work closely with BOC to explore business opportunities in the Region.

In concluding, I wish to thank the Board of Directors for their guidance. I also wish to extend my heartfelt appreciation to my Management team and all the staff for their commitment and ingenuity that have enabled us to deliver growth, quality and excellence year after year.

HE Guangbei
Vice Chairman & Chief Executive

Hong Kong, 25 March 2008

SWIFTER,

In celebration of the 500-day countdown to Beijing Olympic Games, we launched a host of "Great Olympic Offers", including deposit, mortgage, commercial lending and credit card services, to our customers.

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Welcome the Year of
the Olympics With Joy