



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

2016 INTERIM REPORT

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FINANCIAL HIGHLIGHTS

	30 June 2016	30 June 2015
For the period	HK\$'m	HK\$'m
Net operating income before impairment allowances ¹	20,745	20,730
Operating profit ¹	14,399	14,759
Profit before taxation ¹	14,540	15,216
Profit from continuing operations ¹	12,228	12,490
Profit from discontinued operations	30,917	1,301
Profit for the period ²	43,145	13,791
Profit attributable to the equity holders of the Company ²	42,731	13,387
Per share	HK\$	HK\$
Basic earnings per share ²	4.0416	1.2662
Dividend per share	1.2550	0.5450
	30 June 2016	31 December 2015
At period/year end	HK\$'m	HK\$'m
Total assets	2,364,232	2,367,864
Issued and fully paid up share capital	52,864	52,864
Capital and reserves attributable to the equity holders of the Company	228,586	192,578
	30 June 2016	30 June 2015
Financial ratios for the period	%	%
Return on average total assets ³	2.30	1.22
Return on average shareholders' equity ⁴	25.90	14.78
Cost to income ratio ¹	28.05	26.55
Average value of liquidity coverage ratio ⁵		
First quarter	112.92	101.90
Second quarter	109.70	109.89
	30 June 2016	31 December 2015
Financial ratios at period/year end	%	%
Loan to deposit ratio ⁶	67.10	63.25
Total capital ratio ⁷	23.30	17.86

- The financial information for the period ended 30 June 2016 is from continuing operations and the comparative information has been restated accordingly.
- The financial information is from continuing operations and discontinued operations.
- Return on average total assets =
$$\frac{\text{Profit for the period}}{\text{Daily average balance of total assets}}$$
- Return on average shareholders' equity
=
$$\frac{\text{Profit attributable to the equity holders of the Company}}{\text{Average of the beginning and ending balance of capital and reserves attributable to the equity holders of the Company}}$$
- 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.
- Loan to deposit ratio is calculated as at period/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".
- 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.

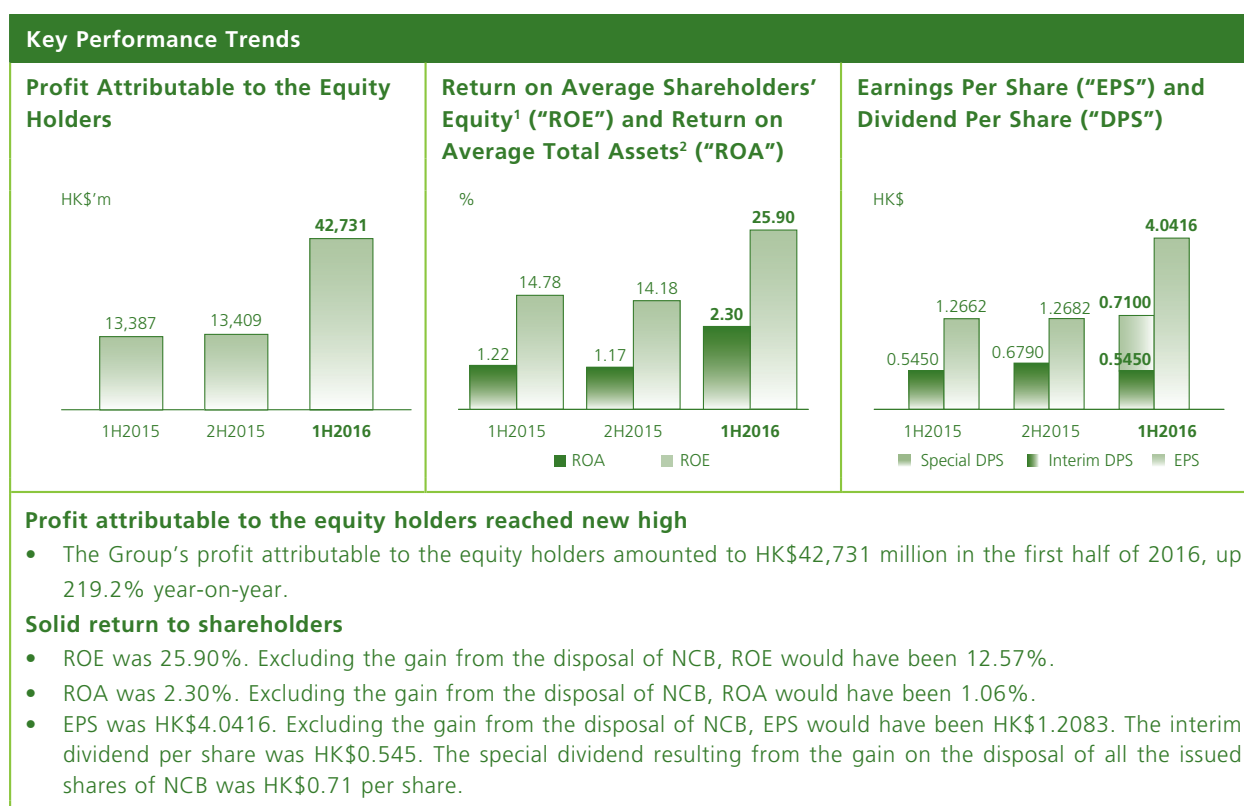
MANAGEMENT'S DISCUSSION AND ANALYSIS

In the first half of 2016, the Group captured development opportunities from the market and achieved a record high in its financial results. With the disposal of NCB and the satisfactory operating performance, profit attributable to the equity holders increased strongly to HK\$42,731 million, up 2.2 times year-on-year, a new high since the Group's listing. Total capital ratio also rose strongly. The Group made good progress in its regional transformation, succeeded in capturing opportunities from the implementation of China's important strategies, including the Belt and Road initiative and RMB internationalisation, and expanded its businesses across the ASEAN region. With the Group's focus on expanding its customer base and proactive management of assets and liabilities, growth in customer deposits and advances to customers outperformed the market with a further improvement in deposit structure. It drove solid business growth in the local market, being the top mandated arranger in the Hong Kong-Macau syndicated loan market and maintained its market leadership in new residential mortgage loans in Hong Kong. At the same time, the Group accelerated the development of its diversified business platforms and made innovative development in Internet finance. It also proactively expanded mobile finance and strengthened its service capabilities of e-Channels. In July, the branch network transformation project was fully implemented to enhance customer experience and service capabilities. The Group continued to adopt prudent risk management to ensure the solid and sustainable business development.

FINANCIAL PERFORMANCE AND CONDITION AT A GLANCE

As a result of the Group's disposal of NCB, the Group reported the operating results of NCB as discontinued operations in the condensed consolidated income statement with comparative information restated. Assets and liabilities of NCB as at 31 December 2015 were presented separately as assets held for sale and liabilities associated with assets held for sale in the condensed consolidated balance sheet. As a result, to facilitate a year-on-year comparison, comparative information for 2015 is restated and analysed in this Management's Discussion and Analysis.

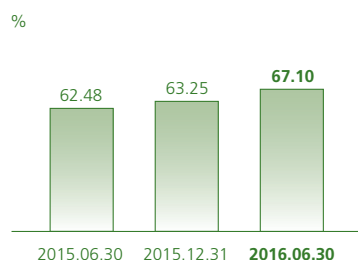
The following chart is a summary of the Group's key financial results for the first half of 2016 in comparison with the previous two half-yearly periods. The average value of the liquidity coverage ratio is reported on a quarterly basis.



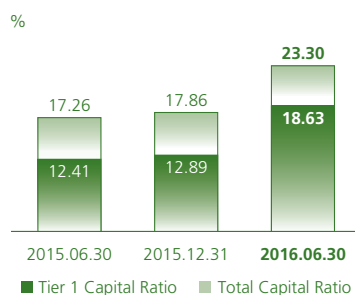
MANAGEMENT'S DISCUSSION AND ANALYSIS

Financial Position

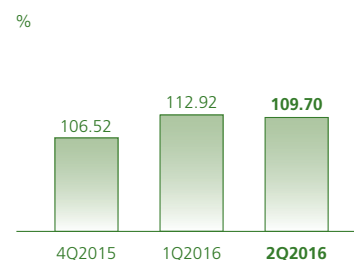
Loan to Deposit Ratio³



Capital Ratio⁴



Average value of Liquidity Coverage Ratio⁵



Loan to deposit ratio at a healthy level

- Advances to customers and deposits from customers grew by 11.1% and 4.7% respectively from the end of 2015, outperforming the market growth. The loan to deposit ratio was 67.10%, up 3.85 percentage points from 63.25% at the end of 2015.

Solid capital position to support business growth

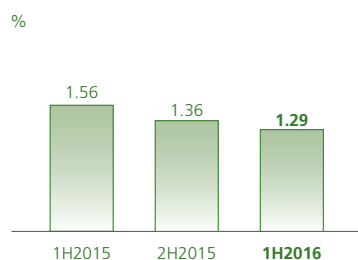
- The total capital ratio was 23.30% while the Tier 1 capital ratio was 18.63%, up 5.44 and 5.74 percentage points from that at the end of 2015. The improvements mainly reflect the gain on disposal of NCB.

Stable liquidity position

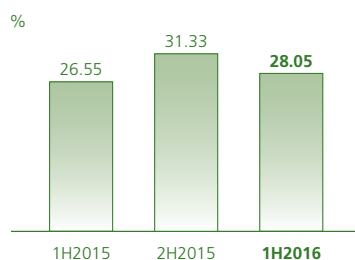
- The average value of the liquidity coverage ratio in the first and second quarter of 2016 was 112.92% and 109.70% respectively, well above the regulatory requirement.

Key Operating Ratios

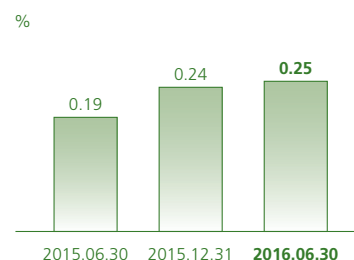
Net Interest Margin ("NIM")



Cost to Income Ratio



Classified or Impaired Loan Ratio⁶



Narrowing NIM with expanded asset size

- NIM was 1.29%, down 27 basis points year-on-year, mainly attributable to the lower average interest spread of RMB business, caused by the decline in RMB market interest rates, the lower long-term interest rates versus short-term interest rates in the first quarter, and the increase of RMB funds from the clearing bank business. NIM was down 7 basis points half-on-half, with the decline slowing down.

Cost to income ratio at a low level

- The cost to income ratio for continuing operations was 28.05%, up 1.50 percentage points year-on-year, a relatively low level in the industry.

Classified or impaired loan ratio stayed at a low level

- The classified or impaired loan ratio remained low at 0.25%.

1. Return on Average Shareholders' Equity as defined in "Financial Highlights".

2. Return on Average Total Assets as defined in "Financial Highlights".

3. Loan represents gross advances to customers while deposits from customers include structured deposits reported as "Financial liabilities at fair value through profit or loss".

4. 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.

5. The average value of the 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 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.

6. 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.

MANAGEMENT'S DISCUSSION AND ANALYSIS

ECONOMIC BACKGROUND AND OPERATING ENVIRONMENT

In the first half of 2016, the global economy continued to grow modestly but global financial market volatilities heightened as markets plummeted at the beginning of the year amid concerns of global economic conditions and fears of reversal of liquidity support. The markets soon stabilised before tumbling again after the United Kingdom voted to leave the European Union in the Brexit referendum. As a result, the global economy entered into a period of profound political, economic and financial uncertainty. In the US, despite a slowdown in GDP growth, the recovery stayed on track with a low unemployment rate and solid residential property market. The accommodative monetary environment continued to provide support to the economic improvement in the Eurozone but the recovery remained fragile and could be held back by the Brexit aftershock. In the Mainland of China, growth momentum eased slightly amid weakened external demand and its own economic restructuring which was still underway with slowdowns in industrial production, investment and consumption.

The Hong Kong economy slowed further in the first half of 2016 with a mere real GDP growth of 1.2% over the previous year. The global and Mainland economic slowdown and recent asset market corrections gradually weakened economic sentiment and adversely affected domestic demand. The continuous slowdown in inbound tourism also created a drag on retail sales. In the first half of 2016, the local residential property market stayed quiet, with a decline in property prices and a slowdown in transaction volume. The local stock market retreated with transaction volumes decreasing significantly year-on-year.

Overall liquidity in the Hong Kong banking sector remained abundant, and market interest rates continued at low levels with increased volatilities compared to previous years. The average 1-month HIBOR and 1-month LIBOR rose from 0.24% and 0.18% respectively in the first half of 2015 to 0.25% and 0.44% respectively in

the first half of 2016. Meanwhile, the average 10-year HKD swap rate and USD swap rate fell from 1.98% and 2.16% respectively to 1.75% and 1.69% respectively over the same period.

In the first half of 2016, the offshore RMB business in Hong Kong continued to grow. A number of initiatives were introduced to promote capital account convertibility and the internationalisation of the RMB. There was relaxation of policies on Free Trade Zones; to allow foreign entities to issue Panda bonds; and to participate in the Mainland's interbank bond market as well as the interbank foreign exchange market. During the period, the People's Bank of China ("PBOC") further refined the reserve requirement regime by charging a reserve requirement ratio for RMB deposits held by offshore participating banks. In addition, the PBOC allowed Hong Kong's RMB clearing bank to join China's Cross-border Interbank Payment System ("CIPS"). All of these initiatives will promote the healthy and steady development of the offshore RMB market.

Banks in Hong Kong continued to operate in a highly challenging environment in the first half of 2016. The global economic slowdown, the economic restructuring in the Mainland and corrections in the Hong Kong residential property market further dampened already softened loan demand and negatively affected certain industries, which put pressure on asset quality. Amid the slow pace of US interest rate hikes, banks continued to operate at low market interest rates with intense market competition. Additionally, the depreciation of the RMB resulted in a decrease in offshore RMB deposits in Hong Kong. Nevertheless, there were also opportunities for banks, especially those arising from the implementation of the Mainland's important strategies, including the Belt and Road initiative, RMB internationalisation, and the Going Global Strategy. The Mainland-Hong Kong Mutual Recognition of Funds, along with Shenzhen-Hong Kong Stock Connect which may come into effect this year, will provide additional fuel for local capital markets.

MANAGEMENT'S DISCUSSION AND ANALYSIS

CONSOLIDATED FINANCIAL REVIEW

Financial Highlights

HK\$m	Half-year ended 30 June 2016	Half-year ended 31 December 2015	(Restated) Half-year ended 30 June 2015
FROM CONTINUING OPERATIONS			
Net interest income	12,172	12,447	13,292
Non-interest income	8,573	7,765	7,438
Net operating income before impairment allowances	20,745	20,212	20,730
Operating expenses	(5,820)	(6,333)	(5,503)
Operating profit before impairment allowances	14,925	13,879	15,227
Operating profit after impairment allowances	14,399	13,416	14,759
Profit before taxation	14,540	13,736	15,216
Profit attributable to the equity holders of the Company	42,731	13,409	13,387
– from continuing operations	11,814	11,883	12,086
– from discontinued operations	30,917	1,526	1,301

In the first half of 2016, the Group focused on leveraging its diversified business platforms and was proactive in managing its balance sheet and overcame challenges in the operating environment, capturing market opportunities to further expand its businesses. At the same time, it continued to strengthen risk control, internal control and compliance management in its operations to achieve sustainable and healthy growth. During the period, the Group successfully completed the disposal of all the issued shares of NCB with a gain of HK\$29,956 million. In the first half of 2016, profit attributable to the equity holders reached HK\$42,731 million, an increase of 219.2% year-on-year. Profit attributable to the equity holders from continuing operations amounted to HK\$11,814 million while that from discontinued operations amounted to HK\$30,917 million, which included the gain on the disposal of NCB and NCB's profit contribution for the period prior to disposal.

For the Group's continuing operations, net operating income before impairment allowances amounted to HK\$20,745 million, up HK\$15 million, or 0.1%, year-

on-year, which was driven by the increase in net trading gain of the banking business, mainly contributed by the higher net gain on foreign exchange swap contracts and the growth in currency exchange income from customer transactions. The increase was, however, partially offset by the decline in net interest income, resulting from the narrowing of net interest margin, and the decrease in net operating income of the Group's insurance segment. Net fee and commission income decreased slightly as investment sentiment weakened notably in the first half of this year. Operating expenses rose as the Group continued to invest in its long-term development. Meanwhile, a lower net gain from fair value adjustments on investment properties was recorded. Taxation reduced, mainly due to the lower overseas taxation incurred by the Group's cross-border businesses. Profit attributable to the equity holders amounted to HK\$11,814 million, down 2.3% year-on-year.

As compared with the second half of 2015, net operating income before impairment allowances for the Group's continuing operations increased by HK\$533 million, or 2.6%. The increase was mainly driven by the growth in

MANAGEMENT'S DISCUSSION AND ANALYSIS

net trading gain of the banking business and the strong rise in net operating income of the Group's insurance segment. The increases were partially offset by the decline in net interest income, resulting from the narrowing of net interest margin, and the lower net fee and commission income. Operating expenses fell as did the net gain from fair value adjustments on investment properties. The

Group also recognised deferred tax assets in the second half of 2015 in respect of the temporary differences arising from taxation incurred by the Group's cross-border businesses, resulting in lower net tax expenses for comparison. Consequently, profit attributable to the equity holders from continuing operations decreased slightly by HK\$69 million, or 0.6%, on a half-on-half basis.

INCOME STATEMENT ANALYSIS

The following income statement analysis is based on the Group's continuing operations and the comparative information has been restated accordingly.

Net Interest Income and Net Interest Margin

HK\$'m, except percentages	Half-year ended 30 June 2016	Half-year ended 31 December 2015	(Restated) Half-year ended 30 June 2015
Interest income	17,767	18,532	19,542
Interest expense	(5,595)	(6,085)	(6,250)
Net interest income	12,172	12,447	13,292
Average interest-earning assets	1,895,300	1,810,640	1,720,778
Net interest spread	1.19%	1.27%	1.45%
Net interest margin*	1.29%	1.36%	1.56%

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

Compared with the first half of 2015, the Group's net interest income decreased by HK\$1,120 million or 8.4%. The decrease was attributable to the lower net interest margin, partially offset by the growth in average interest-earning assets.

Average interest-earning assets expanded by HK\$174,522 million, or 10.1% year-on-year, mainly supported by the increase in deposits from customers as well as deposits and balances from banks. The average balances of both advances to customers and debt securities investments increased.

Net interest margin was 1.29%, down 27 basis points. The drop in net interest margin was due to the lower average interest spread of RMB business caused by the drop in RMB market interest rates, the lower long-term interest rates versus short-term interest rates in the first quarter, and the increase of RMB funds from the clearing bank business. The narrowing of net interest margin was also due to the increase in lower-yielding short-term debt securities investments. The negative impact of these factors on net interest margin was partially offset by the Group's effective control on deposit pricing, an improved deposit mix with the higher proportion of low-interest and interest free deposits, and increased advances to customers.

MANAGEMENT'S DISCUSSION AND ANALYSIS

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

	Half-year ended 30 June 2016		Half-year ended 31 December 2015		(Restated) Half-year ended 30 June 2015	
	Average balance HK\$'m	Average yield %	Average balance HK\$'m	Average yield %	Average balance HK\$'m	Average yield %
ASSETS						
Balances and placements with banks and other financial institutions	336,342	1.43	336,008	1.93	370,970	2.66
Debt securities investments	604,413	1.64	598,385	1.79	517,535	2.10
Advances to customers	932,230	2.22	860,660	2.25	816,982	2.25
Other interest-earning assets	22,315	0.84	15,587	0.93	15,291	1.86
Total interest-earning assets	1,895,300	1.88	1,810,640	2.03	1,720,778	2.29
Non interest-earning assets ¹	513,262	–	541,918	–	549,104	–
Total assets	2,408,562	1.48	2,352,558	1.56	2,269,882	1.74
LIABILITIES						
	Average balance HK\$'m	Average rate %	Average balance HK\$'m	Average rate %	Average balance HK\$'m	Average rate %
Deposits and balances from banks and other financial institutions	246,712	0.75	237,067	0.91	177,319	0.81
Current, savings and time deposits	1,326,234	0.62	1,292,742	0.66	1,261,863	0.81
Subordinated liabilities	19,533	2.72	19,492	2.39	19,628	2.11
Other interest-bearing liabilities	36,336	1.60	38,665	2.28	39,774	1.24
Total interest-bearing liabilities	1,628,815	0.69	1,587,966	0.76	1,498,584	0.84
Shareholders' funds ² and other non interest-bearing deposits and liabilities ¹	779,747	–	764,592	–	771,298	–
Total liabilities	2,408,562	0.47	2,352,558	0.51	2,269,882	0.56

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.

Compared with the second half of 2015, average interest-earning assets grew by HK\$84,660 million, or 4.7%, which was supported by the increase in deposits from customers. Net interest income decreased by HK\$275 million, or 2.2%, due to the narrowing of net interest margin. Net interest margin fell by 7 basis points, owing to the lower average interest spread of RMB business mainly caused by the drop in RMB interest rates, the lower long-term interest rates versus short-term interest rates in the first quarter, and the increase of RMB funds from the

clearing bank business. There were heightened volatilities in RMB interest rates in the offshore market in the first quarter of the year with negative impact on the Group's net interest margin. With the volatility in offshore RMB interest rates stabilising in the second quarter, the Group proactively managed deposit cost and improved deposit mix. As a result of these, together with the increase in advances to customers, net interest margin for the second quarter improved substantially.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Net Fee and Commission Income

HK\$'m	Half-year ended 30 June 2016	Half-year ended 31 December 2015	(Restated) Half-year ended 30 June 2015
Loan commissions	2,216	2,069	1,217
Credit card business	1,863	1,929	1,798
Insurance	896	811	740
Securities brokerage	887	1,253	2,144
Funds distribution	362	341	572
Bills commissions	310	289	254
Payment services	291	291	272
Trust and custody services	225	236	237
Currency exchange	167	153	149
Safe deposit box	151	137	127
Others	385	368	354
Fee and commission income	7,753	7,877	7,864
Fee and commission expense	(2,086)	(2,137)	(2,139)
Net fee and commission income	5,667	5,740	5,725

Net fee and commission income amounted to HK\$5,667 million. With the exception of fee and commission income from securities brokerage, funds distribution and trust and custody services which dropped amid weakening investment sentiment, income from other businesses recorded satisfactory growth year-on-year. The Group leveraged its diversified business platforms to record healthy growth in a number of businesses. In particular, loan commissions grew by 82.1%, due to the strong growth of commission income from corporate loans. During the period, the Group captured opportunities from the Belt and Road, Southeast Asia and Hong Kong and actively explored customers' financing needs which resulted in a satisfactory growth in new loan drawdowns and loan commitments. Income from insurance grew by 21.1% with the rise in business volume. Income from currency exchange rose by 12.1%, driven by the higher demand for foreign currency banknotes in the Mainland of

China. Fee and commission income from bills, safe deposit box, payment services and credit cards also recorded healthy growth. However, fee and commission income from securities brokerage and funds distribution dropped by 58.6% and 36.7% respectively from the high level in the first half of 2015. The decrease in fee and commission expense was mainly due to lower securities brokerage related expenses.

Compared with the second half of 2015, net fee and commission income decreased slightly by HK\$73 million, or 1.3%. The decline mainly resulted from the decrease in commission income from securities brokerage. During the same period, loan commissions and fee and commission income from insurance, funds distribution, bills, currency exchange and safe deposit box grew satisfactorily. Fee and commission expense fell, mainly due to lower credit card and securities brokerage related expenses.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Net Trading Gain

HK\$'m	Half-year ended 30 June 2016	Half-year ended 31 December 2015	(Restated) Half-year ended 30 June 2015
Foreign exchange and foreign exchange products	1,679	1,739	316
Interest rate instruments and items under fair value hedge	531	86	207
Commodities	63	28	29
Equity and credit derivative instruments	32	41	153
Net trading gain	2,305	1,894	705

Net trading gain increased strongly by HK\$1,600 million, or 227.0% year-on-year, to HK\$2,305 million. Net trading gain from foreign exchange and foreign exchange products increased by HK\$1,363 million, primarily due to the net gain from foreign exchange swap contracts* in the first half of 2016 versus the net loss in the same period of 2015, 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\$324 million, mainly attributable to the mark-to-market changes of certain debt securities. The increase in net trading gain from commodities was due

to the increased gain in bullion transactions. The decrease in net trading gain from equity and credit derivative instruments was mainly due to the decreased income from equity-linked products.

Compared with the second half of 2015, the net trading gain increased by HK\$411 million, or 21.7%. The increase was mainly attributable to the mark-to-market changes of certain debt securities, partially offset by the lower currency exchange income from customer transactions in the first half of 2016.

* Foreign exchange swap contracts are usually used for the Group's liquidity management and funding activities. Under the 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	Half-year ended 30 June 2016	Half-year ended 31 December 2015	(Restated) Half-year ended 30 June 2015
Net gain/(loss) on financial instruments designated at fair value through profit or loss	1,032	(600)	(167)

The Group recorded a net gain of HK\$1,032 million on financial instruments designated at FVTPL in the first half of 2016, compared with a net loss of HK\$167 million in the first half of 2015. The change was mainly attributable to the mark-to-market gain of debt securities investments of BOC Life in the first half of 2016, as opposed to the mark-to-market loss in the first half of 2015, which were both caused by market interest rate movements. This was partially offset by the net trading loss from its equity securities investments. 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.

The Group recorded a net gain on financial instruments designated at FVTPL in the first half of 2016, as opposed to a net loss in the second half of 2015. The net loss in the second half of 2015 was mainly attributable to the net trading loss of equity securities investments of BOC Life.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Operating Expenses

HK\$'m	Half-year ended 30 June 2016	Half-year ended 31 December 2015	(Restated) Half-year ended 30 June 2015
Staff costs	3,192	3,503	3,065
Premises and equipment expenses (excluding depreciation)	741	748	688
Depreciation on owned fixed assets	903	881	851
Other operating expenses	984	1,201	899
Total operating expenses	5,820	6,333	5,503

	At 30 June 2016	At 31 December 2015	(Restated) At 30 June 2015
Staff headcount measured in full-time equivalents	12,321	12,576	12,159

Total operating expenses increased by HK\$317 million, or 5.8% year-on-year, to HK\$5,820 million, reflecting the Group's strengthening of resources allocation, continuous investments in service capabilities and infrastructure to support business growth. Nevertheless, the Group remained conscious of the need for disciplined cost control to enhance operational efficiency. The cost to income ratio was 28.05%, below the industry average.

Staff costs increased by 4.1%, reflecting higher salaries following the annual salary increment and increased headcount.

Premises and equipment expenses were up 7.7%, owing to higher IT and rental costs.

Depreciation on owned fixed assets rose by 6.1%, due to a larger depreciation charge on premises following the upward property revaluation in Hong Kong in 2015 and on IT equipment as the Group continued to invest in its IT infrastructure.

Other operating expenses grew by 9.5%, mainly due to higher business tax and promotional expenses.

Compared with the second half of 2015, operating expenses declined by HK\$513 million, or 8.1%. The decrease was mainly attributable to lower staff costs, advertising and promotional expenses as well as business tax in the first half of 2016.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Net Charge of Loan Impairment Allowances

HK\$m	Half-year ended 30 June 2016	Half-year ended 31 December 2015	(Restated) Half-year ended 30 June 2015
Net charge of allowances before recoveries			
– individually assessed	(185)	(351)	(239)
– collectively assessed	(415)	(234)	(314)
Recoveries	56	68	88
Net charge of loan impairment allowances	(544)	(517)	(465)

Net charge of loan impairment allowances increased by HK\$79 million or 17.0% year-on-year. Net charge of individually assessed impairment allowances amounted to HK\$185 million, mainly caused by the downgrade of a few corporate advances. The higher net charge of collectively assessed impairment allowances was mainly due to the growth in advances to customers. During the period, recoveries amounted to HK\$56 million.

Total loan impairment allowances as a percentage of gross advances to customers was 0.34% as at 30 June 2016, unchanged from the end of 2015.

Compared with the second half of 2015, net charge of loan impairment allowances increased by HK\$27 million, or 5.2%. The higher net charge of collectively assessed impairment allowances as a result of the increase in advances to customers was partly offset by the lower net charge of individually assessed impairment allowances.

BALANCE SHEET ANALYSIS

Asset Deployment

HK\$m, except percentages	At 30 June 2016		At 31 December 2015	
	Amount	% of total	Amount	% of total
Cash and balances with banks and other financial institutions	362,789	15.4	230,730	9.7
Placements with banks and other financial institutions maturing between one and twelve months	63,980	2.7	64,208	2.7
Hong Kong SAR Government certificates of indebtedness	108,570	4.6	101,950	4.3
Securities investments ¹	622,809	26.3	574,998	24.3
Advances and other accounts	1,014,095	42.9	920,214	38.9
Fixed assets and investment properties	64,748	2.7	65,695	2.8
Other assets ²	127,241	5.4	109,596	4.6
Assets held for sale	–	–	300,473	12.7
Total assets	2,364,232	100.0	2,367,864	100.0

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

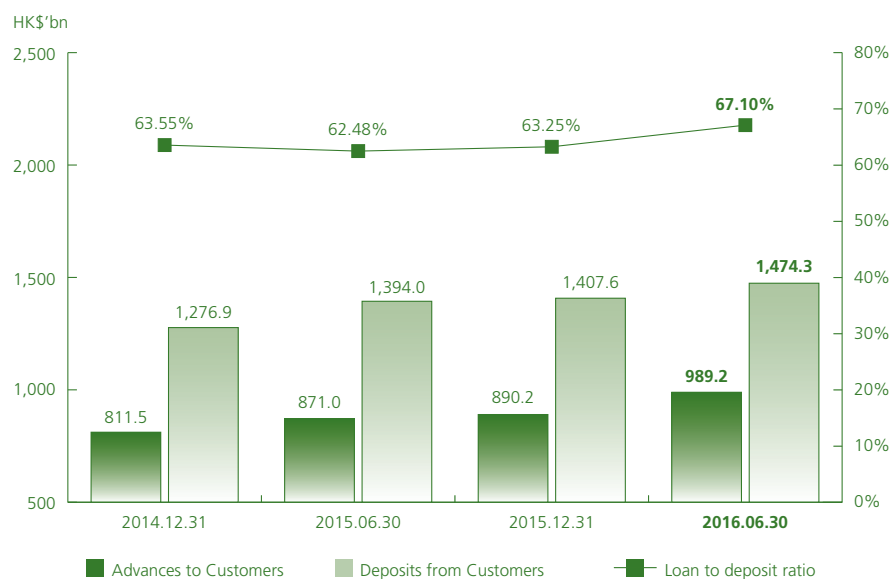
MANAGEMENT'S DISCUSSION AND ANALYSIS

As at 30 June 2016, total assets of the Group amounted to HK\$2,364,232 million, a slight decrease of HK\$3,632 million, or 0.2%, from the end of 2015. The Group maintained its proactive management of assets and liabilities and optimised its asset mix in response to challenges in the operating environment.

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

- Cash and balances with banks and other financial institutions increased by 57.2%, mainly due to the increase in balances with central banks as well as banks and other financial institutions relating to the Group's RMB business.
- Securities investments increased by 8.3%, with increases mainly in high-quality banks and financial institutions as well as corporate bonds.
- Advances and other accounts rose by 10.2%, with the growth in advances to customers by 11.1%.
- Other assets grew by 16.1%, which was led by the increase in account receivable and prepayments, reinsurance assets and derivative financial instruments.
- Assets held for sale dropped to zero as the Group completed the disposal of NCB.

Advances to customers and deposits from customers*



MANAGEMENT'S DISCUSSION AND ANALYSIS

Advances to Customers

HK\$m, except percentages	At 30 June 2016		At 31 December 2015	
	Amount	% of total	Amount	% of total
Loans for use in Hong Kong	660,343	66.8	571,487	64.2
Industrial, commercial and financial	384,549	38.9	300,766	33.8
Individuals	275,794	27.9	270,721	30.4
Trade finance	84,578	8.5	79,108	8.9
Loans for use outside Hong Kong	244,287	24.7	239,648	26.9
Total advances to customers	989,208	100.0	890,243	100.0

In the first half of 2016, the Group captured opportunities from the implementation of China's important strategies, continued to leverage its strong customer base and optimise customer segments. It also stepped up collaboration with BOC and reinforced its financial services to corporates. It remained the top mandated arranger in the Hong Kong-Macau syndicated loan market. To achieve quality loan growth, it remained focused on customer selection. Advances to customers grew by HK\$98,965 million, or 11.1%, to HK\$989,208 million in the first half of 2016.

During the period, the Group was active in capturing opportunities in its lending business to Mainland enterprises going global and leading corporates from the ASEAN region with their loans for use in Hong Kong and overseas. In addition, the Group proactively developed local businesses with leading corporates and SMEs, enhancing servicing and marketing efforts, resulting in a satisfactory growth in advances to customers.

Loans for use in Hong Kong grew by HK\$88,856 million or 15.5%.

- Lending to the industrial, commercial and financial sectors increased by HK\$83,783 million, or 27.9%, representing a broad-based growth in various industry sectors including property development, transport and transport equipment, manufacturing, information technology, property investment and recreational activities.
- Lending to individuals increased by HK\$5,073 million, or 1.9%. Residential mortgage loans (excluding those under the Government-sponsored home purchasing schemes) grew by 1.1%.

Trade finance rose by HK\$5,470 million, or 6.9% while loans for use outside Hong Kong grew by HK\$4,639 million, or 1.9%.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Loan Quality

HK\$m, except percentages	At 30 June 2016	At 31 December 2015
Advances to customers	989,208	890,243
Classified or impaired loan ratio	0.25%	0.24%
Total impairment allowances	3,370	3,009
Total impairment allowances as a percentage of advances to customers	0.34%	0.34%
Residential mortgage loans ¹ – delinquency and rescheduled loan ratio ²	0.02%	0.02%
Card advances – delinquency ratio ²	0.26%	0.20%

	Half-year ended 30 June 2016	Half-year ended 30 June 2015
Card advances – charge-off ratio ³	1.48%	1.40%

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 period to average card receivables during the period.

The Group maintained benign asset quality during the period. The classified or impaired loan ratio was 0.25%. Classified or impaired advances to customers rose by HK\$344 million, or 16.4%, to HK\$2,440 million, due to the downgrade of a few corporate loans.

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 June 2016. The charge-off ratio of card advances remained low at 1.48% in the first half of 2016.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Deposits from Customers*

HK\$'m, except percentages	At 30 June 2016		At 31 December 2015	
	Amount	% of total	Amount	% of total
Demand deposits and current accounts	147,185	10.0	134,069	9.5
Savings deposits	795,535	53.9	717,747	51.0
Time, call and notice deposits	528,961	35.9	553,173	39.3
	1,471,681	99.8	1,404,989	99.8
Structured deposits	2,648	0.2	2,571	0.2
Deposits from customers	1,474,329	100.0	1,407,560	100.0

* Including structured deposits

The Group maintained a flexible deposit strategy to support business growth, while proactively managing deposit pricing with further improvement in deposit mix and hence the higher proportion of low-interest and interest free deposits. Total deposits from customers rose by HK\$66,769 million, or 4.7%, to HK\$1,474,329 million as at 30 June 2016. The proportion of current and savings

deposits improved to 63.9%, up 3.4 percentage points from the end of 2015, as demand deposits and current accounts grew strongly by 9.8% while savings deposits increased by 10.8%. Time, call and notice deposits fell by 4.4%. The loan to deposit ratio was 67.10% at the end of June 2016, up 3.85 percentage points from the end of 2015.

Capital and Reserves Attributable to the Equity Holders of the Company

HK\$'m	At 30 June 2016	At 31 December 2015
Share capital	52,864	52,864
Premises revaluation reserve	35,114	40,278
Reserve for fair value changes of available-for-sale securities	1,253	294
Regulatory reserve	9,278	10,879
Translation reserve	(4)	191
Retained earnings	130,081	88,072
Reserves	175,722	139,714
Capital and reserves attributable to the equity holders of the Company	228,586	192,578

Capital and reserves attributable to the equity holders of the Company amounted to HK\$228,586 million as at 30 June 2016, increasing by HK\$36,008 million, or 18.7%, from the end of 2015. Retained earnings rose by 47.7%, mainly reflecting the profit for the first half of 2016 after the appropriation of the final dividend for 2015. The premises revaluation reserve decreased by 12.8%, which

was attributable to the amount released to retained earnings upon disposal of discontinued operations and the decline in the valuation of premises in the first half of 2016. The regulatory reserve fell by 14.7%, as the growth in advances to customers was more than offset by the amount released to retained earnings upon disposal of discontinued operations.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Capital Ratio and Liquidity Coverage Ratio

HK\$m, except percentages	At 30 June 2016	At 31 December 2015
Consolidated capital after deductions		
Common Equity Tier 1 capital	164,802	121,089
Additional Tier 1 capital	445	561
Tier 1 capital	165,247	121,650
Tier 2 capital	41,346	46,886
Total capital	206,593	168,536
Total risk-weighted assets	886,811	943,802
Common Equity Tier 1 capital ratio	18.58%	12.83%
Tier 1 capital ratio	18.63%	12.89%
Total capital ratio	23.30%	17.86%

	2016	2015
Average value of liquidity coverage ratio		
First quarter	112.92%	101.90%
Second quarter	109.70%	109.89%

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 Group's objective is to maintain a strong capital base to support its sustainable development and to meet higher regulatory capital requirements at all times. Following the Group's designation as one of the domestic systemically important banks in Hong Kong, the Higher Loss Absorbency requirement will be phased-in from 2016 to 2019 in parallel with the Capital Conversation Buffer and Countercyclical Capital Buffer. While the Group continued to adopt proactive measures to manage its capital and risk-weights of its assets, its capital level has been significantly enhanced by the gain from the disposal of NCB.

At 30 June 2016, the Common Equity Tier 1 ("CET1") capital ratio was 18.58% and Tier 1 capital ratio was 18.63%, up 5.75 and 5.74 percentage points respectively from that at the end of 2015. Profits net of dividends paid

for the first half of 2016 and the effect of the Group's disposal of NCB drove up CET1 capital and Tier 1 capital by 36.1% and 35.8% respectively. Total risk-weighted assets ("RWA") were down 6.0%, as the increase in credit RWA due to the growth in advances to customers in the first half of 2016 was more than offset by the reduction in RWA following the disposal of NCB. The total capital ratio was 23.30%.

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 the first half of 2016. The average value of LCR in the first and second quarter of 2016 was 112.92% and 109.70% respectively, above the regulatory minimum.

MANAGEMENT'S DISCUSSION AND ANALYSIS

BUSINESS REVIEW

Business Segment Performance

Profit/(Loss) before Taxation by Business Segments

HK\$'m, except percentages	Half-year ended 30 June 2016		(Restated) Half-year ended 30 June 2015	
	Amount	% of total	Amount	% of total
FROM CONTINUING OPERATIONS				
Personal Banking	3,692	25.4	5,607	36.8
Corporate Banking	6,485	44.6	5,056	33.2
Treasury	3,943	27.1	3,759	24.7
Insurance	611	4.2	649	4.3
Others	(191)	(1.3)	145	1.0
Total profit before taxation	14,540	100.0	15,216	100.0

Note: For additional segmental information, see Note 40 to the Interim Financial Information.

PERSONAL BANKING

Financial Results

Personal Banking's profit before taxation was HK\$3,692 million in the first half of 2016, a decrease of HK\$1,915 million, or 34.2%, year-on-year. The increase in net interest income was offset by the drop in net fee and commission income.

Net interest income increased by 6.3%. This was mainly driven by the improvement in the loan spread coupled with the increase in the average balance of deposits and loans. The growth was partially offset by the decrease in the deposit spread. Net fee and commission income decreased by 30.5% as income from securities brokerage and funds distribution dropped sharply from the high level in the first half of 2015, as investment sentiment weakened notably in the first half of the year. 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 significant net gain in the first half of 2015.

Business operations

Reinforcing market leadership in residential mortgages and expanding other retail loan services

Despite the slowdown in transaction volume of the local residential property market, the Group maintained its leadership position in new residential mortgage

loans in the first half of 2016. To capture new business opportunities, it enriched its mortgage service portfolio and improved the quality of its products and services across all channels. In addition, the Group optimised the approval process which shortens the turnaround time for credit assessment, dedicated to further enhancing customer experience and service efficiency. During the period, the Group also made a conscious effort to enrich the retail lending services by expanding the list of eligible collaterals for secured lending services. This provides flexibility and convenience to the Group's wealth management customers, helping them to capture investment opportunities in a timely manner and to accumulate wealth efficiently.

Enhancing the investment and insurance business product range

Heightened global financial market volatility and general weakness in the 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. Despite sluggish market sentiments during the period, the Group actively acquired new securities customers and provided customers with a series of investor education and market analysis activities, achieving a steady growth in the number of customers.

MANAGEMENT'S DISCUSSION AND ANALYSIS

In the funds distribution business, the Group continued to broaden its product offerings. During the period, a number of currency-hedged share classes, including RMB, EUR and USD were introduced and additional southbound funds under the Mainland-Hong Kong Mutual Recognition of Funds were distributed to broaden the number of investment choices for customers. The Group also enhanced its marketing and promotional campaigns in order to deepen relationships with customers and enhance cross-selling opportunities. It also continued enhancing the sales process to improve the customer experience and sales efficiency.

With regard to the Bancassurance business, the Group maintained its leading position in the Hong Kong RMB insurance market. The Group is committed to offer a diversified range of products to meet customers' needs under different life stages. The Group also conducted a series of marketing campaigns to promote insurance businesses to different customer segments.

Continuous improvement in credit card service

The continuing decline in total retail sales in Hong Kong during the first half of 2016 was reflected in the lower volume of the Group's credit cardholder spending. At the same time, however, the Group recorded a year-on-year growth in the volume of merchant acquiring business as the Group successfully acquired a number of new major merchants in Hong Kong during the period. It also maintained its leadership in the UnionPay merchant acquiring business and card issuing business in Hong Kong. During the review period, focus was made on acquiring mid- to high-end personal customers as well as high-quality corporate customers. It also introduced a number of new credit cards to meet the needs of different customer segments. In view of the weakened retail sales in Hong Kong, the Group launched targeted promotional programmes to increase cardholder spending on daily necessities, online shopping and overseas purchases. It also encouraged the use of e-Channels to improve cost efficiency and the customer experience, and initiated a series of marketing activities to promote the use of the "BOCHK Credit Card" WeChat official account. From July, the Group also introduced Apple Pay, a fast, convenient and secure mobile payment service, to its credit cardholders in order to enhance the payment experience of cardholders.

Recognised wealth management services

The Group made a continuous effort to deepen existing customer relationships and acquire new customers in the mid- to high-end market. During the first half of 2016, the Group enhanced its Wealth Management and Enrich Banking services, organised a series of value-added customer events and launched new services to meet customers' banking and investment needs at different life stages. A series of marketing programmes, including Family Banking-themed promotions, were also launched to strengthen the Group's brand image and increase penetration of targeted customer segments. Following the establishment of the Cross-border Financial Services Centre in 2015, the Group further optimised its cross-border sales and service model by offering tiered promotional offers to different customer groups and standardising account opening procedures. As a result, the Group recorded a continuous increase in the number of new cross-border customers. The total number of Wealth Management and Enrich Banking customers together with their total relationship balances also registered satisfactory growth. 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*.

In the first half of the year, the Group's Private Banking business focused on a number of initiatives to drive its overall business development. It continued to cooperate closely with different units of the Group and BOC's Mainland and overseas entities to expand its customer base. With an enhanced open platform for tailor-made products and services and its expanded professional team, the Group broadened the service capabilities to serve the specific needs of the high net-worth clients. In addition, it continued to optimise its business platform by streamlining its processes and enhancing the Private Banking Internet Banking to enrich the customer experience. Besides, the Group participated in a number of activities, both in Hong Kong and in Southeast Asia, with an aim to raise its brand awareness. As a result, both the number of Private Banking clients and their assets under management achieved satisfactory and encouraging growth.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Optimising distribution channels

The Group continued to optimise its distribution channels to meet the needs of customers. A branch network transformation project was launched in 2015 with an aim to support the integrated service model for personal and corporate customers. The Group divided the branch network into different districts and areas to allow for better branch management. Training, new product and service packages and greater cooperation with the commercial centres enabled the Group to enjoy increased referrals and offer lending and other SME services to targeted customers. At the end of June 2016, the Group's service network in Hong Kong comprised 220 branches, including 92 wealth management centres. At the same time, the Group increased the number of coverage points in its automated banking network. BOCHK was granted approval to set up a branch in Brunei Darussalam, making it the first Chinese financial institution to establish a branch in the country and making a new phase in bilateral financial cooperation between Brunei Darussalam and China. Preparations for the branch opening are currently well underway.

Enhancing Internet finance service capabilities

In line with developments in the Internet, big data and cloud computing, the Group formulated an Internet finance development plan in 2015 in order to integrate Internet technology with its traditional banking business. During the first half of 2016, the Group enriched its applications for mobile finance with services such as e-Cheque Services, Online Loans and Mobile P2P Small Value Transfers. The Group was the first bank in Hong Kong to launch an e-Cheque service for mobile banking and an e-Cheque drop box for bill payments. It also initiated the development of a Big Data platform and research into biometric authentication technology. In addition, cooperation with BOC reinforced synergy in cross-channel integration which further uplifted the Group's servicing capabilities. All these factors pushed up the Group's total number of customers of e-Channels, including Internet and Mobile Banking services, from the end of 2015. Recognising the importance of cyber security, the Group established an independent security workgroup to handle all security-related issues and built a Cyber Intelligence Platform to ensure system and transaction security. In addition, BOCHK signed a Memorandum of

Understanding with Hong Kong Applied Science and Technology Research Institute ("ASTRI") to establish the BOCHK-ASTRI FinTech Collaboration Centre, which aims to develop latest financial technologies (FinTech) which can be applied to the banking industry, fostering FinTech's development in Hong Kong. In acknowledgment of its technological innovations, BOCHK was awarded the Best Mobile Social Media Engagement Project in The Asian Banker Technology Awards 2016.

CORPORATE BANKING

Financial Results

Corporate Banking's profit before taxation was HK\$6,485 million, a growth of HK\$1,429 million, or 28.3%, 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 13.0%, with the positive impact from the increase in the average balance of loans and deposits. Net fee and commission income rose by 54.8%, largely led by the strong growth in loan commissions. During the period, the Group's Corporate Banking succeeded in capturing opportunities in its lending business to leading Mainland corporates expanding overseas, and leading local enterprises. Operating expenses were up 12.4%, mainly due to the increase in staff costs and rental expenses.

Business operations

Regional expansion and continuous business development in ASEAN

The Group succeeded in capturing opportunities arising out of major national strategic initiatives. During the period, it strengthened collaboration with BOC's branches and provided leading Mainland enterprises with funding solutions in support of their expansion into countries along the Belt and Road and in the ASEAN region. The Group also extended lending to key customers for major projects in ASEAN, further raising the Group's market share and influence there. The Group also cooperated with BOC branches to provide trade-related products and services. To accelerate its business development in the ASEAN region, the Group set up a working team to coordinate and manage integration with BOC and its branches.

MANAGEMENT'S DISCUSSION AND ANALYSIS

To capture business opportunities arising from the Going Global Strategy, the Group deepened collaboration with BOC entities in the Mainland and overseas. It also completed financing projects for several cross-border merger and acquisition ("M&A") transactions in support of Mainland enterprises' overseas expansion. In addition, co-operation among BOC's Guangdong, Hong Kong and Macau operations intensified during the period, further raising BOC Group's market influence in these areas. Whatsmore, 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. Through these activities, the Group remained the top mandated arranger in the Hong Kong-Macau syndicated loan market in the first half of 2016.

Enhancing business development in the local commercial sector

In the first half of 2016, the Group further expanded its customer base with an increased number of leading enterprises. Cooperating with these enterprises, the Group was able to establish a convenient and effective financial service platform to help improve their overall market competitiveness. It also stepped up marketing aimed at strengthening relationships with local family-owned businesses and trade associations, and made inroads with second- and third-tier listed companies. With continued progress in its branch network transformation project to drive business integration between commercial centres and branches, the Group reinforced its ability to serve SME customers. For small enterprises, the Group formulated a standardised sales and service model and tailor-made products and services according to the needs of customers. In recognition of the Group's 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.

Enlarged customer base of institutional businesses

The Group continued to extend cooperation and strengthen relationships with other overseas central banks and corresponding banks. In collaboration with BOC, the Group successfully secured business relationships with overseas regional development banks and made a breakthrough in forming relationships with the world's largest sovereign wealth fund. Locally, the Group expanded cooperation with public sector entities and

acted as the receiving bank for a number of major IPOs in Hong Kong, thereby consolidating its leading position in this market.

Product innovation in the transaction banking business

The Group improved its competitiveness in the trade finance business through continuous product innovation and feature enhancements. During the period, the Group launched the USD Trade Finance Incentive programme and the new concept of Trade Buffet programme, both of which are helping to explore customer potential. It also launched innovative financing solutions tailored to customer needs and market changes. At the same time, the Group continued to improve its service capabilities in cross-border cash management. Working closely with BOC, it implemented cross-border cash pooling services for a number of large corporate clients and assisted them in maximising cash liquidity through onshore and offshore two-way cash sweeping. In March 2016, the Group pioneered the launch of payment services by e-Cheque and subsequently introduced solutions to support large corporates issuing e-Cheques via ERP Integration and Corporate File Transfer Service. In recognition of its outstanding transaction banking services, BOCHK was named Best Cash Management Bank in Hong Kong for the fourth consecutive year by *The Asian Banker*. It was also named the Best Transaction Bank in Hong Kong for 2016 and a trade finance project undertaken by BOCHK received the Best Corporate Trade Finance Deal in Hong Kong for 2016.

Enlarging the customer base for custody services

In the first half of 2016, the higher number of M&A activities in the market resulted in a robust demand for escrow deals. Segregated mandates and proprietary accounts fared better than funds in general. However, other client segments were affected to various degrees by market volatility and subdued turnover volumes. With its diversified client base and new clients active in portfolio building, the Group was able to capture new business. During the period, it successfully established business relationships with new client segments from the Mainland of China, Hong Kong and overseas. The Group also collaborated more closely with BOC and its overseas entities to enhance the overall service capabilities of the BOC Group. In recognition of its outstanding custody services, the Group won the award as the Best Custody

MANAGEMENT'S DISCUSSION AND ANALYSIS

Specialist – China from *The Asset* magazine. At the end of June 2016, excluding the RMB fiduciary accounts for participating banks, total assets under the Group's custody were valued at HK\$758.5 billion.

Proactive measures to contain risks

In the first half of 2016, the Group adhered to a prudent credit policy under the Know Your Customers principle. In view of the increasing volatility in RMB exchange rates as well as the downtrend in local retail sales, the Group performed credit monitoring on a more frequent and proactive basis. This included closely monitoring the credit positions of customers and industries that could be adversely affected by the slowdown in global economic growth. More stringent pre- and post-lending monitoring measures were also adopted to track early negative signs. Additionally, it put in place a solution for effectively monitoring the credit of major groups of customers with concentration risk. Finally, to accommodate the Group's business strategy associated with Mainland enterprises going global and the Belt and Road initiative as well as the Group's acquisition of BOC's assets in the ASEAN region, the Group has been raising the underwriting standards of its related credit policies and procedures in view of the risks associated with the local political and economic environment, tax issues and legal risks. Along with these new standards, the Group has been raising related underwriting standards in its credit policies and procedures with the aim of putting in place more efficient and sound risk control measures for the Group's business development in new markets.

TREASURY

Financial Results

Treasury's profit before taxation was HK\$3,943 million, an increase of 4.9% from the same period last year.

Net interest income decreased by 51.3%, mainly due to the decrease in the average balance of RMB balances and placements with banks, coupled with the decline in the average yield on related assets caused by the drop in market interest rates. The average yield of debt securities investments also declined. The decrease was, however, partially offset by the increase in the average balance of debt securities investments. Net trading gain was up strongly, primarily due to the net gain from foreign exchange swap contracts in the first half of 2016 versus the net loss in the same period of 2015, the increase in currency exchange income from customer transactions

as well as the mark-to-market changes of certain debt securities. Net gain on other financial assets increased strongly as the Group recorded a higher gain from the disposal of certain debt securities investments in the first half of 2016.

Business Operations

Well-recognised development in the treasury business

Responding to the complex economic environment, the Group continued to meet customers' needs with time-to-market and innovative products and services. It also pushed forward its strategy of diversified customer segments and revenue resources to drive business development. As a result, foreign exchange trading volume and related revenue for customer transactions grew satisfactorily from the same period in 2015. In the bond underwriting business, the Group strengthened its professional competence in the underwriting of USD and other currency-denominated bonds despite a downtrend in the demand for offshore RMB assets. In recognition of its outstanding performance in the treasury business, BOCHK received the Hong Kong Domestic Foreign Exchange Bank of the Year award in the Asian Banking and Finance Wholesale Banking Awards 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 the ASEAN region

In line with its ASEAN development strategy, the Group set up closer cooperation mechanisms with BOC's entities in the region to promote further growth in their treasury business and support their funding needs. During the period, the Group visited several ASEAN countries and introduced treasury products to financial institutions and central banks in these countries to consolidate relationships. In the banknotes business, the Group strengthened relationships with banknotes suppliers and captured market opportunities in countries such as Thailand, Singapore and the Philippines.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Optimising RMB clearing services

The Group strengthened its clearing capabilities to ensure the stable development and continuous improvement of its RMB clearing services in Hong Kong and overseas. During the period, BOCHK received approval to join the CIPS, being the first overseas bank to join this system as a direct participant. The Group also completed the first cross-border RMB remittance transaction conducted by an offshore RMB clearing bank. Joining the CIPS will enable the Group to further enhance its overall RMB clearing capabilities.

A proactive but risk aware investment strategy

The Group managed its banking book investments proactively. It closely monitored changes in the market and actively looked for investment opportunities to enhance returns while remaining alert to risks. During the period, the Group increased its investments in certificates of deposits and bonds in anticipation of a moderate pace in US interest rate hike.

INSURANCE

Financial Results

Profit before taxation in the Group's Insurance segment was HK\$611 million in the first half of 2016, down 5.9% year-on-year. The decline was mainly caused by the trading loss in its equity investments portfolio, as compared to a trading gain in the first half of 2015, and 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 59.6% as the Group adjusted its product mix by reducing single premium business but increasing regular premium business to ensure a stable stream of renewal premium income for long-term growth.

Business Operations

Continued product enhancement and distribution channel diversification

The Group continued to broaden its product offerings to meet the needs of customers and diversify its distribution channels to reach different customer segments. During the period, it launched new products such as the MaxiWealth ULife Insurance Plan and the UltraReach

Insurance Plan for customers with insurance and savings needs. It also enhanced the Forever Glorious ULife Plan and the BestCare Critical Illness Plan. By expanding the broker channel, tied agency channel and e-Channel, the Group was able to capture more business opportunities.

Maintaining leadership in RMB insurance products

The Group maintained its leading position in the Hong Kong RMB insurance market by focusing on product optimisation and innovation. In addition, the Group launched a variety of promotional programmes, including premium discounts and the title sponsorship for an RMB currency exchange rates programme on a TV news channel, to reinforce its professional image in RMB insurance. In recognition of its business performance in the industry, BOC Life received all awards in the RMB Business Outstanding Awards – Outstanding Insurance Business, organised by Metro Finance, Metro Finance Digital and Hong Kong *Wen Wei Po* for the fifth consecutive year.

DIVERSIFIED BUSINESS PLATFORMS

Good progress in asset management

BOCHK Asset Management Limited ("BOCHK Asset Management") continued to expand its footprint in the first half of 2016. Under the Mainland-Hong Kong Mutual Recognition of Funds scheme, the BOCHK All Weather China High Yield Bond Fund was approved by the China Securities Regulatory Commission, and BOCHK Asset Management prepared for the launch of the fund in the Mainland in the second half of the year. Also during the review period, BOCHK Asset Management acted as the representative of Bank of China Investment Management Co., Ltd., a joint-venture company of BOC, to assist in the distribution of their southbound funds in Hong Kong. In addition, it continued to establish partnerships with BOC's overseas branches for promotion of its asset management services.

Steady development in trustee services

The Group engages in the provision of trustee, provident fund, retirement fund and unit trust administration services through its subsidiary company, BOCI-Prudential Trustee Limited ("BOCI-Prudential Trustee"). During the period, BOCI-Prudential Trustee collaborated with

MANAGEMENT'S DISCUSSION AND ANALYSIS

different units of the Group to enhance its sales, referrals and cross-selling capabilities. In line with the ongoing development of the Internet, a number of functional enhancements were made to the Group's online MPF administration platform and mobile application to improve the overall customer experience. In addition, significant progress was made in preparation for the launch of the Default Investment Strategy proposed by the Government and the Mandatory Provident Fund Schemes Authority.

Product diversification in securities and futures brokerage services

The Group engages in the provision of brokerage services for futures and options through its subsidiary company, Po Sang Futures Limited ("Po Sang Futures"). During the period, Po Sang Futures provided a wider range of products to meet the diverse needs of customers with the launch of trading services for Sector Index Futures Contracts and RMB Currency Futures Contracts. Through the promotional campaigns it launched during the period, Po Sang Futures enhanced its brand image.

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 first half of 2015 and the gain on disposal of NCB were as follows:

HK\$'m	Half-year ended 30 June 2016	Half-year ended 30 June 2015
Profit of discontinued operations for the period	961	1,301
Gain on disposal of discontinued operations	29,956	–

Acquisition Agreements in relation to the acquisitions of BOC Thailand and BOC Malaysia

On 30 June 2016, BOCHK entered into Share Purchase Agreements with BOC in relation to the acquisitions of the entire issued share capital of Bank of China (Thai) Public Company Limited ("BOC Thailand") and the entire issued share capital of Bank of China (Malaysia) Berhad ("BOC Malaysia"), respectively, as part of the restructuring exercise of the Group in the ASEAN region.

The ASEAN region is a high growth market and a key region for the Belt and Road initiative and RMB internationalisation. It has also been one of the core regions for the BOC Group's overseas business development over the years. The acquisition of certain ASEAN assets from BOC signifies the start of the transition of BOCHK from a local bank into a regional bank. The Group will leverage its geographic advantage and professionalism to fully implement the integrated strategy

MANAGEMENT'S DISCUSSION AND ANALYSIS

of BOC Group's domestic and overseas operations. By acquiring BOC Thailand and BOC Malaysia, the Group can ride on its status as the largest offshore RMB clearing bank and fully leverage its competitive edges in services, products and resources to build up business scale and strength. The Group will adopt a matrix management structure to oversee its ASEAN institutions. Meanwhile, a business supervisory committee has been set up to steer the overall business development in the region and a business integration team has been established to coordinate and manage the integration work, ensuring a smooth transition of business operations and management of the ASEAN institutions.

For further information on the acquisitions, please refer to the announcement made by the Group on 30 June 2016.

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.

Risk management governance structure

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 Risk Committee ("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.

MANAGEMENT'S DISCUSSION AND ANALYSIS

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 subsidiary, Chiyu, is 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.

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. 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.

For 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. The Group adopts loan grading criteria which divides credit assets into five categories with reference to the HKMA's guidelines. The Risk Management Department ("RMD") provides regular credit management information reports and ad hoc reports to the Management Committee ("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 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.

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

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.

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. 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.

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.

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 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.

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: mismatches in the maturity or repricing periods of assets and liabilities that may affect net interest income;

MANAGEMENT'S DISCUSSION AND ANALYSIS

- 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.

The Group's risk management framework applies also to interest rate risk management. The Asset and Liability Management Committee ("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.

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.

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

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 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.

In accordance with the requirements of Supervisory Policy Manual LM-2 "Sound Systems and controls for Liquidity Risk Management" issued by the HKMA in 2011, 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.

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

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haircut of interbank placement and marketable securities. As at 30 June 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. 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.

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.

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

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.

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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.

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 3.4 to the Interim Financial Information.

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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 in customers surrender. 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 control 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.

CONDENSED CONSOLIDATED INCOME STATEMENT

	Notes	(Unaudited) Half-year ended 30 June 2016 HK\$'m	(Restated) (Unaudited) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS			
Interest income		17,767	19,542
Interest expense		(5,595)	(6,250)
Net interest income	5	12,172	13,292
Fee and commission income		7,753	7,864
Fee and commission expense		(2,086)	(2,139)
Net fee and commission income	6	5,667	5,725
Gross earned premiums		9,303	15,507
Gross earned premiums ceded to reinsurers		(5,719)	(6,632)
Net insurance premium income		3,584	8,875
Net trading gain	7	2,305	705
Net gain/(loss) on financial instruments designated at fair value through profit or loss		1,032	(167)
Net gain on other financial assets	8	578	816
Other operating income	9	367	473
Total operating income		25,705	29,719
Gross insurance benefits and claims and movement in liabilities		(11,173)	(16,135)
Reinsurers' share of benefits and claims and movement in liabilities		6,213	7,146
Net insurance benefits and claims and movement in liabilities	10	(4,960)	(8,989)
Net operating income before impairment allowances		20,745	20,730
Net charge of impairment allowances	11	(526)	(468)
Net operating income		20,219	20,262
Operating expenses	12	(5,820)	(5,503)
Operating profit		14,399	14,759
Net gain from disposal of/fair value adjustments on investment properties	13	104	349
Net (loss)/gain from disposal/revaluation of properties, plant and equipment	14	(5)	85
Share of profits less losses after tax of associates and a joint venture		42	23
Profit before taxation		14,540	15,216
Taxation	15	(2,312)	(2,726)
Profit from continuing operations		12,228	12,490
DISCONTINUED OPERATIONS			
Profit from discontinued operations	34	30,917	1,301
Profit for the period		43,145	13,791
Profit attributable to:			
Equity holders of the Company			
– from continuing operations		11,814	12,086
– from discontinued operations		30,917	1,301
		42,731	13,387
Non-controlling interests		414	404
		43,145	13,791
Dividends	16	13,269	5,762
		HK\$	HK\$
Earnings per share for profit attributable to the equity holders of the Company			
Basic and diluted	17		
– profit for the period		4.0416	1.2662
– profit from continuing operations		1.1174	1.1431

The notes on pages 40 to 114 are an integral part of this interim financial information.

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Note	(Unaudited) Half-year ended 30 June 2016 HK\$'m	(Unaudited) Half-year ended 30 June 2015 HK\$'m
Profit for the period	43,145	13,791
Items that will not be reclassified subsequently to income statement:		
Premises:		
Revaluation of premises	(470)	1,832
Deferred tax	152	(228)
	(318)	1,604
Items that may be reclassified subsequently to income statement:		
Available-for-sale securities:		
Change in fair value of available-for-sale securities	2,225	434
Release upon disposal of available-for-sale securities reclassified to income statement	(630)	(826)
Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities reclassified to income statement	85	139
Deferred tax	(233)	187
	1,447	(66)
Change in fair value of hedging instruments under net investment hedges	–	(3)
Currency translation difference	(7)	20
Release upon disposal of discontinued operations reclassified to income statement	(370)	–
34	1,070	(49)
Other comprehensive income for the period, net of tax	752	1,555
Total comprehensive income for the period	43,897	15,346
Total comprehensive income attributable to:		
Equity holders of the Company	43,187	14,940
Non-controlling interests	710	406
	43,897	15,346

The notes on pages 40 to 114 are an integral part of this interim financial information.

CONDENSED CONSOLIDATED BALANCE SHEET

		(Unaudited) At 30 June 2016 HK\$'m	(Audited) At 31 December 2015 HK\$'m
	Notes		
ASSETS			
Cash and balances with banks and other financial institutions	19	362,789	230,730
Placements with banks and other financial institutions maturing between one and twelve months		63,980	64,208
Financial assets at fair value through profit or loss	20	72,252	57,777
Derivative financial instruments	21	44,066	43,207
Hong Kong SAR Government certificates of indebtedness		108,570	101,950
Advances and other accounts	22	1,014,095	920,214
Investment in securities	23	550,557	517,221
Interests in associates and a joint venture		416	376
Investment properties	24	15,910	15,262
Properties, plant and equipment	25	48,838	50,433
Deferred tax assets	31	56	58
Other assets	26	82,703	65,955
Assets held for sale	34	–	300,473
Total assets		2,364,232	2,367,864
LIABILITIES			
Hong Kong SAR currency notes in circulation		108,570	101,950
Deposits and balances from banks and other financial institutions		299,568	207,606
Financial liabilities at fair value through profit or loss	27	13,868	10,942
Derivative financial instruments	21	50,447	40,072
Deposits from customers	28	1,471,681	1,404,989
Debt securities and certificates of deposit in issue	29	8,649	6,976
Other accounts and provisions	30	63,406	34,225
Current tax liabilities		3,995	2,782
Deferred tax liabilities	31	6,409	6,457
Insurance contract liabilities	32	83,270	82,645
Subordinated liabilities	33	19,754	19,422
Liabilities associated with assets held for sale	34	–	251,805
Total liabilities		2,129,617	2,169,871
EQUITY			
Share capital	35	52,864	52,864
Reserves		175,722	139,714
Capital and reserves attributable to the equity holders of the Company		228,586	192,578
Non-controlling interests		6,029	5,415
Total equity		234,615	197,993
Total liabilities and equity		2,364,232	2,367,864

The notes on pages 40 to 114 are an integral part of this interim financial information.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	(Unaudited)								
	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	Retained earnings HK\$'m	Total HK\$'m	Non- controlling interests HK\$'m	Total equity HK\$'m
At 1 January 2015	52,864	37,510	1,930	10,011	778	73,621	176,714	4,758	181,472
Profit for the period	-	-	-	-	-	13,387	13,387	404	13,791
Other comprehensive income:									
Premises	-	1,589	-	-	-	-	1,589	15	1,604
Available-for-sale securities	-	-	(52)	-	-	-	(52)	(14)	(66)
Change in fair value of hedging instruments under net investment hedges	-	-	-	-	(3)	-	(3)	-	(3)
Currency translation difference	-	-	(4)	-	23	-	19	1	20
Total comprehensive income	-	1,589	(56)	-	20	13,387	14,940	406	15,346
Release upon disposal of premises	-	(351)	-	-	-	351	-	-	-
Transfer from retained earnings	-	-	-	675	-	(675)	-	-	-
Dividends	-	-	-	-	-	(6,080)	(6,080)	(108)	(6,188)
At 30 June 2015	52,864	38,748	1,874	10,686	798	80,604	185,574	5,056	190,630
At 1 July 2015	52,864	38,748	1,874	10,686	798	80,604	185,574	5,056	190,630
Profit for the period	-	-	-	-	-	13,409	13,409	295	13,704
Other comprehensive income:									
Premises	-	1,553	-	-	-	-	1,553	12	1,565
Available-for-sale securities	-	-	(1,580)	-	-	-	(1,580)	(32)	(1,612)
Change in fair value of hedging instruments under net investment hedges	-	-	-	-	52	-	52	2	54
Currency translation difference	-	(9)	-	-	(659)	-	(668)	(18)	(686)
Total comprehensive income	-	1,544	(1,580)	-	(607)	13,409	12,766	259	13,025
Release upon disposal of premises	-	(14)	-	-	-	14	-	-	-
Transfer from retained earnings	-	-	-	193	-	(193)	-	-	-
Dividends	-	-	-	-	-	(5,762)	(5,762)	(145)	(5,907)
Increase in non-controlling interests arising from capital issuance of a subsidiary	-	-	-	-	-	-	-	245	245
At 31 December 2015	52,864	40,278	294	10,879	191	88,072	192,578	5,415	197,993

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	(Unaudited)								
	Attributable to the equity holders of the Company								
	Reserves								
	Share capital	Premises revaluation reserve	Reserve for fair value changes of available-for-sale securities	Regulatory reserve*	Translation reserve	Retained earnings	Total	Non-controlling interests	Total equity
HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	
At 1 January 2016	52,864	40,278	294	10,879	191	88,072	192,578	5,415	197,993
Profit for the period	-	-	-	-	-	42,731	42,731	414	43,145
Other comprehensive income:									
Premises	-	(308)	-	-	-	-	(308)	(10)	(318)
Available-for-sale securities	-	-	1,136	-	-	-	1,136	311	1,447
Currency translation difference	-	-	(10)	-	8	-	(2)	(5)	(7)
Release upon disposal of discontinued operations reclassified to income statement	-	-	(167)	-	(203)	-	(370)	-	(370)
Total comprehensive income	-	(308)	959	-	(195)	42,731	43,187	710	43,897
Transfer from retained earnings	-	-	-	639	-	(639)	-	-	-
Release upon disposal of discontinued operations	-	(4,856)	-	(2,240)	-	7,096	-	-	-
Dividends	-	-	-	-	-	(7,179)	(7,179)	(96)	(7,275)
At 30 June 2016	52,864	35,114	1,253	9,278	(4)	130,081	228,586	6,029	234,615

* 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.

The notes on pages 40 to 114 are an integral part of this interim financial information.

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

	Notes	(Unaudited) Half-year ended 30 June 2016 HK\$'m	(Unaudited) Half-year ended 30 June 2015 HK\$'m
Cash flows from operating activities			
Operating cash inflow/(outflow) before taxation	36(a)	51,366	(44,747)
Hong Kong profits tax paid		(1,191)	(1,064)
Overseas profits tax paid		(223)	(340)
Net cash inflow/(outflow) from operating activities		49,952	(46,151)
Cash flows from investing activities			
Purchase of properties, plant and equipment		(355)	(530)
Proceeds from disposal of properties, plant and equipment		1	466
Purchase of investment properties		–	(35)
Dividend received from associates and a joint venture		2	2
Net cash inflow from disposal of discontinued operations	34	26,992	–
Net cash inflow/(outflow) from investing activities		26,640	(97)
Cash flows from financing activities			
Dividend paid to the equity holders of the Company		(7,179)	–
Dividend paid to non-controlling interests		(96)	(108)
Interest paid for subordinated liabilities		(210)	(204)
Net cash outflow from financing activities		(7,485)	(312)
Increase/(decrease) in cash and cash equivalents		69,107	(46,560)
Cash and cash equivalents at 1 January		308,456	403,828
Effect of exchange rate changes on cash and cash equivalents		(1,046)	(95)
Cash and cash equivalents at 30 June	36(b)	376,517	357,173

The notes on pages 40 to 114 are an integral part of this interim financial information.

NOTES TO THE INTERIM FINANCIAL INFORMATION

1. Basis of preparation and significant accounting policies

(a) Basis of preparation

The unaudited interim financial information has been prepared in accordance with HKAS 34 “Interim Financial Reporting” issued by the HKICPA.

(b) Significant accounting policies

The significant accounting policies adopted and methods of computation used in the preparation of the unaudited interim financial information are consistent with those adopted and used in the Group’s annual financial statements for the year ended 31 December 2015 and should be read in conjunction with the Group’s Annual Report for 2015.

Standards and amendments to standards that are relevant to the Group and mandatory for the first time for the financial year beginning on 1 January 2016

- 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 amendments are already effective for annual periods beginning on 1 January 2016. The adoption of these improvements does not have a material impact on the Group’s financial statements.

NOTES TO THE INTERIM FINANCIAL INFORMATION

1. Basis of preparation and significant accounting policies (continued)

(c) Standards and amendments issued that are relevant to the Group but not yet effective and have not been early adopted by the Group in 2016

Standards/ Amendments	Content	Applicable for financial years beginning on/after
HKAS 28 (2011) and HKFRS 10 (Amendments)	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	To be determined
HKFRS 9	Financial Instruments	1 January 2018
HKFRS 15	Revenue from Contracts with Customers	1 January 2018
HKFRS 16	Leases	1 January 2019

- 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.
- Please refer to Note 2.1(a) of the Group's Annual Report for 2015 for brief explanations of the rest of the above-mentioned standards and amendments.

2. Critical accounting estimates and judgements in applying accounting policies

The nature and assumptions related to the Group's accounting estimates are consistent with those used in the Group's financial statements for the year ended 31 December 2015.

3. 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.

3.1 Credit risk

(A) Gross advances and other accounts

(a) Impaired advances

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Gross advances and other accounts (continued)

(a) Impaired advances (continued)

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Gross impaired advances to customers	1,672	1,299
Impairment allowances made in respect of such advances	763	610
Current market value of collateral held against the covered portion of such advances to customers	1,410	987
Covered portion of such advances to customers	1,145	848
Uncovered portion of such advances to customers	527	451

The impairment allowances were made after taking into account the value of collateral in respect of such advances.

As at 30 June 2016, there were no impaired trade bills and advances to banks and other financial institutions (31 December 2015: Nil).

Classified or impaired advances to customers are analysed as follows:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Gross classified or impaired advances to customers	2,440	2,096
Gross classified or impaired advances to customers as a percentage of gross advances to customers	0.25%	0.24%
Individually assessed impairment allowances made in respect of such advances	711	564

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Gross advances and other accounts (continued)

(b) Advances overdue for more than three months

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.

The gross amount of advances overdue for more than three months is analysed as follows:

	At 30 June 2016		At 31 December 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	142	0.01%	128	0.02%
– one year or less but over six months	85	0.01%	169	0.02%
– over one year	163	0.02%	211	0.02%
Advances overdue for over three months	390	0.04%	508	0.06%
Individually assessed impairment allowances made in respect of such advances	144		161	

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Current market value of collateral held against the covered portion of such advances to customers	441	676
Covered portion of such advances to customers	197	339
Uncovered portion of such advances to customers	193	169

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Gross advances and other accounts (continued)

(b) Advances overdue for more than three months (continued)

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 30 June 2016, there were no trade bills and advances to banks and other financial institutions overdue for more than three months (31 December 2015: Nil).

(c) Rescheduled advances

	At 30 June 2016		At 31 December 2015	
	Amount HK\$'m	% of gross advances to customers	Amount HK\$'m	% of gross advances to customers
Rescheduled advances to customers net of amounts included in "Advances overdue for more than three months"	117	0.01%	–	–

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".

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Gross advances and other accounts (continued)

(d) 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.

	At 30 June 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	73,171	23.53%	–	–	–	240
– Property investment	60,390	80.72%	9	118	–	206
– Financial concerns	5,738	5.36%	–	–	–	46
– Stockbrokers	2,906	76.18%	–	–	–	11
– Wholesale and retail trade	29,491	51.96%	53	200	23	106
– Manufacturing	27,980	22.17%	22	108	6	108
– Transport and transport equipment	52,816	27.82%	1,680	2	438	181
– Recreational activities	2,642	2.37%	–	–	–	8
– Information technology	18,242	1.04%	–	–	–	56
– Others	111,173	21.94%	16	458	11	349
Individuals						
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	8,569	99.84%	13	149	–	5
– Loans for purchase of other residential properties	212,061	99.91%	84	1,320	1	97
– Credit card advances	12,935	–	44	485	–	112
– Others	42,229	74.51%	35	392	4	70
Total loans for use in Hong Kong	660,343	57.74%	1,956	3,232	483	1,595
Trade finance	84,578	12.27%	183	189	107	277
Loans for use outside Hong Kong	244,287	12.98%	301	53	121	787
Gross advances to customers	989,208	42.80%	2,440	3,474	711	2,659

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Gross advances and other accounts (continued)

(d) Concentration of advances to customers (continued)

(i) Sectoral analysis of gross advances to customers (continued)

	At 31 December 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	79,108	12.93%	195	255	103	280
Loans for use outside Hong Kong	239,648	15.71%	158	161	55	814
Gross advances to customers	890,243	47.58%	2,096	3,774	564	2,445

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Gross advances and other accounts (continued)

(d) 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

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Hong Kong	802,685	727,413
Mainland of China	125,492	118,546
Others	61,031	44,284
	989,208	890,243
Collectively assessed impairment allowances in respect of the gross advances to customers		
Hong Kong	2,073	1,911
Mainland of China	374	373
Others	212	161
	2,659	2,445

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Gross advances and other accounts (continued)

(d) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers (continued)

Overdue advances

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Hong Kong	3,260	3,289
Mainland of China	173	400
Others	41	85
	3,474	3,774
Individually assessed impairment allowances in respect of the overdue advances		
Hong Kong	133	126
Mainland of China	23	78
Others	–	–
	156	204
Collectively assessed impairment allowances in respect of the overdue advances		
Hong Kong	91	84
Mainland of China	4	5
Others	1	1
	96	90

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(A) Gross advances and other accounts (continued)

(d) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers (continued)

Classified or impaired advances

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Hong Kong	2,002	1,699
Mainland of China	387	393
Others	51	4
	2,440	2,096
Individually assessed impairment allowances in respect of the classified or impaired advances		
Hong Kong	520	407
Mainland of China	165	157
Others	26	–
	711	564
Collectively assessed impairment allowances in respect of the classified or impaired advances		
Hong Kong	52	45
Mainland of China	2	3
Others	–	–
	54	48

(B) Repossessed assets

The estimated market value of repossessed assets held by the Group as at 30 June 2016 amounted to HK\$101 million (31 December 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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(C) 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.

	At 30 June 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	59,242	127,685	233,037	36,634	21,949	478,547
Held-to-maturity securities	23,322	24,800	12,145	4,575	1,704	66,546
Loans and receivables	–	302	1,055	–	–	1,357
Financial assets at fair value through profit or loss	6,127	36,458	13,482	6,559	3,610	66,236
	88,691	189,245	259,719	47,768	27,263	612,686

	At 31 December 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	12,181	4,717	3,668	81,126
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	234,762	38,040	30,566	567,577

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.1 Credit risk (continued)

(C) 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.

	At 30 June 2016						
	Carrying values						Of which accumulated impairment allowances
	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	2	-	-	-	-	2	-
Of which accumulated impairment allowances	-	-	-	-	-	-	-

	At 31 December 2015						
	Carrying values						Of which accumulated impairment allowances
	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	-
Of which accumulated impairment allowances	-	-	-	-	-	-	-

As at 30 June 2016, there were no impaired certificates of deposit and no overdue debt securities and certificates of deposit (31 December 2015: Nil).

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk

(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 exposure¹ of the Group.

	Year	At 30 June HK\$'m	Minimum for the first half of year HK\$'m	Maximum for the first half of year HK\$'m	Average for the first half of year HK\$'m
VAR for all market risk	2016	30.3	30.1	58.6	42.9
	2015	21.9	17.9	38.4	28.3
VAR for foreign exchange risk	2016	26.8	25.5	42.1	33.3
	2015	10.0	9.8	18.4	12.5
VAR for interest rate risk	2016	20.0	15.3	57.4	26.5
	2015	21.7	15.3	37.6	24.8
VAR for equity risk	2016	3.1	0.0	3.1	0.9
	2015	0.3	0.1	0.4	0.3
VAR for commodity risk	2016	0.1	0.0	0.1	0.0
	2015	0.0	0.0	0.2	0.0

Note:

1. Structural FX positions have been excluded.

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk (continued)

(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.

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.

	At 30 June 2016							
	Equivalent in million of HK\$							
	US Dollars	Japanese Yen	Euro	Australian Dollars	Pound Sterling	Renminbi	Other foreign currencies	Total foreign currencies
Spot assets	690,494	95,766	37,426	22,468	13,111	469,744	10,399	1,339,408
Spot liabilities	(579,519)	(8,277)	(23,021)	(18,739)	(15,603)	(389,686)	(14,712)	(1,049,557)
Forward purchases	1,283,605	70,394	71,425	34,262	31,780	736,990	46,995	2,275,451
Forward sales	(1,381,626)	(157,901)	(85,896)	(38,081)	(29,063)	(815,793)	(42,479)	(2,550,839)
Net options position	2,051	(1)	1	6	(27)	(1,588)	(6)	436
Net long/(short) position	15,005	(19)	(65)	(84)	198	(333)	197	14,899
Net structural position	-	-	-	-	-	828	-	828

	At 31 December 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
Net structural position	293	-	-	-	-	9,355	-	9,648

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk (continued)

(C) Interest rate risk

The tables below summarise the Group's on-balance sheet exposure to interest rate risk as at 30 June 2016 and 31 December 2015. Included in the tables are the assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing date and maturity date.

	At 30 June 2016						Total 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	Non-interest bearing HK\$'m	
Assets							
Cash and balances with banks and other financial institutions	330,863	-	-	-	-	31,926	362,789
Placements with banks and other financial institutions maturing between one and twelve months	-	37,061	26,919	-	-	-	63,980
Financial assets at fair value through profit or loss	10,062	11,530	12,862	15,247	18,192	4,359	72,252
Derivative financial instruments	-	-	-	-	-	44,066	44,066
Hong Kong SAR Government certificates of indebtedness	-	-	-	-	-	108,570	108,570
Advances and other accounts	790,169	145,208	33,143	36,896	2,178	6,501	1,014,095
Investment in securities							
– Available-for-sale securities	30,727	95,411	129,796	139,071	83,542	4,107	482,654
– Held-to-maturity securities	2,927	1,946	12,139	35,021	14,513	-	66,546
– Loans and receivables	906	-	451	-	-	-	1,357
Interests in associates and a joint venture	-	-	-	-	-	416	416
Investment properties	-	-	-	-	-	15,910	15,910
Properties, plant and equipment	-	-	-	-	-	48,838	48,838
Other assets (including deferred tax assets)	20,877	-	-	-	-	61,882	82,759
Total assets	1,186,531	291,156	215,310	226,235	118,425	326,575	2,364,232
Liabilities							
Hong Kong SAR currency notes in circulation	-	-	-	-	-	108,570	108,570
Deposits and balances from banks and other financial institutions	267,268	1,444	533	-	-	30,323	299,568
Financial liabilities at fair value through profit or loss	1,943	4,976	4,841	1,071	1,037	-	13,868
Derivative financial instruments	-	-	-	-	-	50,447	50,447
Deposits from customers	1,082,371	168,868	121,854	516	-	98,072	1,471,681
Debt securities and certificates of deposit in issue	854	798	5,803	1,194	-	-	8,649
Other accounts and provisions (including current and deferred tax liabilities)	9,029	-	-	-	-	64,781	73,810
Insurance contract liabilities	-	-	-	-	-	83,270	83,270
Subordinated liabilities	-	-	-	19,754	-	-	19,754
Total liabilities	1,361,465	176,086	133,031	22,535	1,037	435,463	2,129,617
Interest sensitivity gap	(174,934)	115,070	82,279	203,700	117,388	(108,888)	234,615

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.2 Market risk (continued)

(C) Interest rate risk (continued)

	At 31 December 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	195,806	-	-	-	-	34,924	230,730
Placements with banks and other financial institutions maturing between one and twelve months	-	37,920	26,288	-	-	-	64,208
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	-	-	-	-	-	43,207	43,207
Hong Kong SAR Government certificates of indebtedness	-	-	-	-	-	101,950	101,950
Advances and other accounts	711,095	107,459	61,028	32,770	943	6,919	920,214
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	13,109	43,088	21,008	-	81,126
– Loans and receivables	-	1,005	2,161	-	-	-	3,166
Interests in associates and a joint venture	-	-	-	-	-	376	376
Investment properties	-	-	-	-	-	15,262	15,262
Properties, plant and equipment	-	-	-	-	-	50,433	50,433
Other assets (including deferred tax assets)	3,024	-	-	-	-	62,989	66,013
Assets held for sale	168,400	44,587	49,217	25,704	528	12,037	300,473
Total assets	1,119,988	326,377	247,818	240,017	98,326	335,338	2,367,864
Liabilities							
Hong Kong SAR currency notes in circulation	-	-	-	-	-	101,950	101,950
Deposits and balances from banks and other financial institutions	160,049	27,936	2,343	-	-	17,278	207,606
Financial liabilities at fair value through profit or loss	2,583	4,446	1,968	1,479	466	-	10,942
Derivative financial instruments	-	-	-	-	-	40,072	40,072
Deposits from customers	1,054,648	182,898	79,013	611	-	87,819	1,404,989
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)	8,782	-	-	-	-	34,682	43,464
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	1,375,166	256,197	129,686	28,668	485	379,669	2,169,871
Interest sensitivity gap	(255,178)	70,180	118,132	211,349	97,841	(44,331)	197,993

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 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%

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 Liquidity risk (continued)

(B) Maturity analysis

The tables below analyse the Group's assets and liabilities as at 30 June 2016 and 31 December 2015 into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

	At 30 June 2016							Total HK\$'m
	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	
Assets								
Cash and balances with banks and other financial institutions	260,694	81,708	-	-	-	-	20,387	362,789
Placements with banks and other financial institutions maturing between one and twelve months	-	-	37,061	26,919	-	-	-	63,980
Financial assets at fair value through profit or loss								
- Held for trading								
- Debt securities	-	8,668	9,856	9,246	11,669	2,919	-	42,358
- Certificates of deposit	-	22	138	1,264	253	-	-	1,677
- Designated at fair value through profit or loss								
- Debt securities	-	96	158	1,422	5,292	15,088	-	22,056
- Certificates of deposit	-	1	-	6	138	-	-	145
- Equity securities and fund	-	-	-	-	-	-	4,359	4,359
- Others	-	1,424	233	-	-	-	-	1,657
Derivative financial instruments	13,838	3,177	5,598	13,524	5,227	2,702	-	44,066
Hong Kong SAR Government certificates of indebtedness	108,570	-	-	-	-	-	-	108,570
Advances and other accounts								
- Advances to customers	117,408	18,275	48,954	165,852	417,798	215,388	2,163	985,838
- Trade bills	21	7,782	10,610	4,426	-	-	-	22,839
- Advances to banks and other financial institutions	-	2	2	-	5,414	-	-	5,418
Investment in securities								
- Available-for-sale								
- Debt securities	-	13,713	63,822	79,852	158,822	84,242	-	400,451
- Certificates of deposit	-	1,727	11,668	52,075	12,407	219	-	78,096
- Held-to-maturity								
- Debt securities	-	3,048	2,064	12,474	34,543	14,397	2	66,528
- Certificates of deposit	-	-	-	-	-	18	-	18
- Loans and receivables								
- Debt securities	-	906	-	451	-	-	-	1,357
- Equity securities and fund	-	-	-	-	-	-	4,107	4,107
Interests in associates and a joint venture	-	-	-	-	-	-	416	416
Investment properties	-	-	-	-	-	-	15,910	15,910
Properties, plant and equipment	-	-	-	-	-	-	48,838	48,838
Other assets (including deferred tax assets)	40,889	17,249	968	1,108	6,056	16,405	84	82,759
Total assets	541,420	157,798	191,132	368,619	657,619	351,378	96,266	2,364,232

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

	At 30 June 2016							Total HK\$'m
	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	
Liabilities								
Hong Kong SAR currency notes in circulation	108,570	-	-	-	-	-	-	108,570
Deposits and balances from banks and other financial institutions	214,211	83,380	1,444	533	-	-	-	299,568
Financial liabilities at fair value through profit or loss	-	1,943	4,978	4,843	1,069	1,035	-	13,868
Derivative financial instruments	10,008	6,690	6,234	16,585	5,019	5,911	-	50,447
Deposits from customers	943,015	237,428	168,868	121,854	516	-	-	1,471,681
Debt securities and certificates of deposit in issue – Debt securities	-	854	829	5,803	1,163	-	-	8,649
Other accounts and provisions (including current and deferred tax liabilities)	23,211	38,905	282	4,182	7,230	-	-	73,810
Insurance contract liabilities	23,840	350	921	1,306	12,610	44,243	-	83,270
Subordinated liabilities	-	-	419	-	19,335	-	-	19,754
Total liabilities	1,322,855	369,550	183,975	155,106	46,942	51,189	-	2,129,617
Net liquidity gap	(781,435)	(211,752)	7,157	213,513	610,677	300,189	96,266	234,615

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

	At 31 December 2015							Total HK\$'m
	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	
Assets								
Cash and balances with banks and other financial institutions	182,319	48,108	-	-	-	-	303	230,730
Placements with banks and other financial institutions maturing between one and twelve months	-	-	37,920	26,288	-	-	-	64,208
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	2,723	2,711	18,994	5,504	786	-	43,207
Hong Kong SAR Government certificates of indebtedness	101,950	-	-	-	-	-	-	101,950
Advances and other accounts								
- Advances to customers	104,814	25,975	44,039	135,015	360,990	214,384	2,017	887,234
- Trade bills	1	7,970	8,330	15,710	-	-	-	32,011
- 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	-	520	3,558	13,436	42,769	20,822	3	81,108
- 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 a joint venture	-	-	-	-	-	-	376	376
Investment properties	-	-	-	-	-	-	15,262	15,262
Properties, plant and equipment	-	-	-	-	-	-	50,433	50,433
Other assets (including deferred tax assets)	28,508	11,394	705	4,051	5,333	15,969	53	66,013
Assets held for sale	18,598	52,792	31,823	65,034	85,341	29,495	17,390	300,473
Total assets	448,679	173,555	242,816	384,945	666,552	358,239	93,078	2,367,864

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

	At 31 December 2015							Total HK\$m
	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	
Liabilities								
Hong Kong SAR currency notes in circulation	101,950	-	-	-	-	-	-	101,950
Deposits and balances from banks and other financial institutions	166,711	10,616	27,936	2,343	-	-	-	207,606
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	3,358	2,743	18,851	4,525	1,782	-	40,072
Deposits from customers	852,823	289,644	182,898	79,013	611	-	-	1,404,989
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)	20,246	11,751	1,479	2,663	7,322	3	-	43,464
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	1,265,679	387,091	261,270	157,184	53,607	45,040	-	2,169,871
Net liquidity gap	(817,000)	(213,536)	(18,454)	227,761	612,945	313,199	93,078	197,993

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.4 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. The Group conducted relevant experience studies. The results of the studies are considered in determining the assumptions of insurance liability which include appropriate level of prudential margins.

3.5 Capital management

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 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 the standardised (operational risk) ("STO") approach to calculate the operational risk capital charge.

(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".

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management (continued)

(A) Basis of regulatory consolidation (continued)

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	At 30 June 2016		At 31 December 2015	
	Total assets HK\$m	Total equity HK\$m	Total assets HK\$m	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.	300	203	220	199
BOCHK Information Technology Services (Shenzhen) Ltd.	323	281	314	270
BOCI-Prudential Trustee Limited	438	398	462	432
Che Hsing (Nominees) Limited	1	1	1	1
Chiyu Banking Corporation (Nominees) Limited	139	139	134	134
Grace Charter Limited	–	(11)	–	(11)
Kwong Li Nam Investment Agency Limited*	–	–	4	4
Nanyang Commercial Bank (Nominees) Limited*	–	–	1	1
Nanyang Commercial Bank Trustee Limited*	–	–	16	16
Po Sang Financial Investment Services Company Limited	366	346	363	345
Po Sang Futures Limited	673	460	496	454
Seng Sun Development Company, Limited	40	40	41	41
Sin Chiao Enterprises Corporation, Limited	7	7	7	7
Sin Hua Trustee Limited	5	5	5	5
Sino Information Services Company Limited	8	8	8	8

* 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.

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 30 June 2016 (31 December 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 30 June 2016 (31 December 2015: Nil).

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management (continued)

(B) Capital ratio

The capital ratios are analysed as follows:

	At 30 June 2016	At 31 December 2015
CET1 capital ratio	18.58%	12.83%
Tier 1 capital ratio	18.63%	12.89%
Total capital ratio	23.30%	17.86%

The consolidated capital base after deductions used in the calculation of the above capital ratios is analysed as follows:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
CET1 capital: instruments and reserves		
Directly issued qualifying CET1 capital instruments	43,043	43,043
Retained earnings	133,160	89,915
Disclosed reserves	43,081	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)	733	733
CET1 capital before regulatory deductions	220,017	183,129
CET1 capital: regulatory deductions		
Valuation adjustments	(36)	(20)
Deferred tax assets net of deferred tax liabilities	(56)	(69)
Gains and losses due to changes in own credit risk on fair valued liabilities	(208)	(198)
Cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties)	(45,637)	(50,874)
Regulatory reserve for general banking risks	(9,278)	(10,879)
Total regulatory deductions to CET1 capital	(55,215)	(62,040)
CET1 capital	164,802	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)	445	561
AT1 capital	445	561
Tier 1 capital	165,247	121,650

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management (continued)

(B) Capital ratio (continued)

	At 30 June 2016 HK\$'m	At 31 December 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)	224	226
Collective impairment allowances and regulatory reserve for general banking risks eligible for inclusion in Tier 2 capital	5,150	5,537
Tier 2 capital before regulatory deductions	20,809	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	20,537	22,893
Total regulatory deductions to Tier 2 capital	20,537	22,893
Tier 2 capital	41,346	46,886
Total capital	206,593	168,536

The capital buffer ratios are analysed as follows:

	At 30 June 2016
Capital conservation buffer ratio	0.625%
Higher loss absorbency ratio	0.375%
Countercyclical capital buffer ratio	0.491%

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

3. Financial risk management (continued)

3.5 Capital management (continued)

(C) Leverage ratio

The leverage ratio is analysed as follows:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Tier 1 capital	165,247	121,650
Leverage ratio exposure	2,208,301	2,268,203
Leverage ratio	7.48%	5.36%

The additional information of leverage ratio disclosures is available under section "Regulatory Disclosures" on the Bank's website at www.bochk.com.

4. Fair values of financial assets and liabilities

All financial instruments 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 and certain exchange-traded derivative contracts.
- 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 over-the-counter ("OTC") derivative contracts, debt securities and certificates of deposit with quote from pricing services vendors and issued structured deposits.
- 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.

For financial instruments 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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 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.

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy

	At 30 June 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 20)				
– Trading assets				
– Debt securities and certificates of deposit	1,526	42,509	–	44,035
– Equity securities	5	–	–	5
– Others	–	1,657	–	1,657
– Financial assets designated at fair value through profit or loss				
– Debt securities and certificates of deposit	–	19,716	2,485	22,201
– Equity securities	1,728	–	–	1,728
– Fund	2,626	–	–	2,626
Derivative financial instruments (Note 21)	13,861	30,196	9	44,066
Available-for-sale securities (Note 23)				
– Debt securities and certificates of deposit	96,483	380,337	1,727	478,547
– Equity securities	3,272	89	601	3,962
– Fund	145	–	–	145
Financial liabilities				
Financial liabilities at fair value through profit or loss (Note 27)				
– Trading liabilities	–	11,220	–	11,220
– Financial liabilities designated at fair value through profit or loss	–	2,648	–	2,648
Derivative financial instruments (Note 21)	10,038	40,409	–	50,447

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy (continued)

	At 31 December 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 20)				
– Trading assets				
– Debt securities and certificates of deposit	1	32,026	–	32,027
– 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 21)	12,493	30,714	–	43,207
Available-for-sale securities (Note 23)				
– Debt securities and certificates of deposit	95,982	333,106	1,095	430,183
– Equity securities	2,459	–	287	2,746
Financial liabilities				
Financial liabilities at fair value through profit or loss (Note 27)				
– Trading liabilities	–	8,371	–	8,371
– Financial liabilities designated at fair value through profit or loss	–	2,571	–	2,571
Derivative financial instruments (Note 21)	8,936	31,136	–	40,072

There were no financial asset and liability transfers between level 1 and level 2 for the Group during the period (31 December 2015: Nil).

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items

	At 30 June 2016			
	Financial assets			
	Financial assets designated at fair value through profit or loss		Available-for-sale securities	
	Debt securities and certificates of deposit HK\$'m	Derivative financial instruments HK\$'m	Debt securities and certificates of deposit HK\$'m	Equity securities HK\$'m
At 1 January 2016	1,829	–	1,095	287
Gains				
– Income statement				
– Net trading gain	–	9	–	–
– Net gain on financial instruments designated at fair value through profit or loss	255	–	–	–
– Other comprehensive income				
– Change in fair value of available-for-sale securities	–	–	70	24
Purchases	401	–	562	290
At 30 June 2016	2,485	9	1,727	601
Total unrealised gains for the period included in income statement for financial assets held as at 30 June 2016				
– Net trading gain	–	9	–	–
– Net gain on financial instruments designated at fair value through profit or loss	255	–	–	–

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

	At 31 December 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
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)	–	–

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

As at 30 June 2016 and 31 December 2015, financial instruments categorised as level 3 are mainly comprised of debt securities, certificates of deposit, certain OTC derivative contracts 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.

For certain OTC derivative contracts, the counterparty credit spreads used in valuation techniques are unobservable inputs with significant impact on valuation. Therefore, these OTC derivative contracts have been categorised by the Group as level 3.

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\$30 million (31 December 2015: HK\$14 million).

4.2 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 4.1.

NOTES TO THE INTERIM FINANCIAL INFORMATION

4. Fair values of financial assets and liabilities (continued)

4.2 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 4.1.

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.

	At 30 June 2016		At 31 December 2015	
	Carrying value HK\$m	Fair value HK\$m	Carrying value HK\$m	Fair value HK\$m
Financial assets				
Held-to-maturity securities (Note 23)	66,546	68,351	81,126	83,037
Loans and receivables (Note 23)	1,357	1,359	3,166	3,171
Financial liabilities				
Debt securities and certificates of deposit in issue (Note 29)	8,649	8,767	6,976	7,222
Subordinated liabilities (Note 33)	19,754	21,825	19,422	21,507

NOTES TO THE INTERIM FINANCIAL INFORMATION

5. Net interest income

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Interest income		
Due from banks and other financial institutions	2,402	4,902
Advances to customers	10,330	9,098
Investment in securities and financial assets at fair value through profit or loss	4,941	5,401
Others	94	141
	17,767	19,542
Interest expense		
Due to banks and other financial institutions	(925)	(714)
Deposits from customers	(4,115)	(5,087)
Debt securities and certificates of deposit in issue	(179)	(146)
Subordinated liabilities	(265)	(206)
Others	(111)	(97)
	(5,595)	(6,250)
Net interest income	12,172	13,292

Included within interest income is HK\$3 million (first half of 2015: HK\$10 million) of interest with respect to income accrued on advances classified as impaired for the first half of 2016. Interest income accrued on impaired investment in securities amounted to HK\$1 million (first half of 2015: HK\$1 million).

Included within interest income and interest expense are HK\$17,644 million (first half of 2015: HK\$19,467 million) and HK\$5,859 million (first half of 2015: HK\$6,532 million), before hedging effect, for financial assets and financial liabilities that are not recognised at fair value through profit or loss respectively.

NOTES TO THE INTERIM FINANCIAL INFORMATION

6. Net fee and commission income

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Fee and commission income		
Loan commissions	2,216	1,217
Credit card business	1,863	1,798
Insurance	896	740
Securities brokerage	887	2,144
Funds distribution	362	572
Bills commissions	310	254
Payment services	291	272
Trust and custody services	225	237
Currency exchange	167	149
Safe deposit box	151	127
Others	385	354
	7,753	7,864
Fee and commission expense		
Credit card business	(1,414)	(1,338)
Insurance	(132)	(159)
Securities brokerage	(119)	(251)
Others	(421)	(391)
	(2,086)	(2,139)
Net fee and commission income	5,667	5,725
Of which arise from:		
Financial assets or financial liabilities not at fair value through profit or loss		
– Fee and commission income	2,342	1,283
– Fee and commission expense	(14)	(10)
	2,328	1,273
Trust and other fiduciary activities		
– Fee and commission income	321	330
– Fee and commission expense	(11)	(14)
	310	316

NOTES TO THE INTERIM FINANCIAL INFORMATION

7. Net trading gain

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Net gain from:		
Foreign exchange and foreign exchange products	1,679	316
Interest rate instruments and items under fair value hedge	531	207
Commodities	63	29
Equity and credit derivative instruments	32	153
	2,305	705

8. Net gain on other financial assets

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Net gain on available-for-sale securities	570	796
Net gain on held-to-maturity securities	6	3
Others	2	17
	578	816

9. Other operating income

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Dividend income from investment in securities		
– Listed investments	51	58
– Unlisted investments	23	21
Gross rental income from investment properties	249	215
Less: Outgoings in respect of investment properties	(31)	(29)
Others	75	208
	367	473

Included in the "Outgoings in respect of investment properties" is HK\$1 million (first half of 2015: HK\$3 million) of direct operating expenses related to investment properties that were not let during the period.

NOTES TO THE INTERIM FINANCIAL INFORMATION

10. Net insurance benefits and claims and movement in liabilities

	Half-year ended 30 June 2016 HK\$'m	Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Gross insurance benefits and claims and movement in liabilities		
Claims, benefits and surrenders paid	(10,204)	(7,246)
Movement in liabilities	(969)	(8,889)
	(11,173)	(16,135)
Reinsurers' share of benefits and claims and movement in liabilities		
Reinsurers' share of claims, benefits and surrenders paid	7,495	2,506
Reinsurers' share of movement in liabilities	(1,282)	4,640
	6,213	7,146
Net insurance benefits and claims and movement in liabilities	(4,960)	(8,989)

11. Net charge of impairment allowances

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Advances to customers		
Individually assessed		
– New allowances	(206)	(319)
– Releases	21	80
– Recoveries	33	67
Net charge of individually assessed loan impairment allowances	(152)	(172)
Collectively assessed		
– New allowances	(416)	(314)
– Releases	1	–
– Recoveries	23	21
Net charge of collectively assessed loan impairment allowances	(392)	(293)
Net charge of loan impairment allowances	(544)	(465)
Others	18	(3)
Net charge of impairment allowances	(526)	(468)

NOTES TO THE INTERIM FINANCIAL INFORMATION

12. Operating expenses

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Staff costs (including directors' emoluments)		
– Salaries and other costs	2,981	2,861
– Pension cost	211	204
	3,192	3,065
Premises and equipment expenses (excluding depreciation)		
– Rental of premises	328	315
– Information technology	219	190
– Others	194	183
	741	688
Depreciation	903	851
Auditor's remuneration		
– Audit services	3	3
– Non-audit services	3	1
Other operating expenses	978	895
	5,820	5,503

13. Net gain from disposal of/fair value adjustments on investment properties

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Net gain from fair value adjustments on investment properties	104	349

14. Net (loss)/gain from disposal/revaluation of properties, plant and equipment

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Net gain from disposal of premises	–	95
Net loss from disposal of equipment, fixtures and fittings	(1)	(10)
Net loss from revaluation of premises	(4)	–
	(5)	85

NOTES TO THE INTERIM FINANCIAL INFORMATION

15. Taxation

Taxation in the income statement represents:

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Current tax		
Hong Kong profits tax		
– Current period taxation	2,262	2,409
– Over-provision in prior periods	(2)	(4)
	2,260	2,405
Overseas taxation		
– Current period taxation	195	446
– Over-provision in prior periods	–	(2)
	2,455	2,849
Deferred tax		
Origination and reversal of temporary differences and unused tax credits	(143)	(123)
	2,312	2,726

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 for the first half of 2016. Taxation on overseas profits has been calculated on the estimated assessable profits for the first half of 2016 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:

	Half-year ended 30 June 2016 HK\$'m	(Restated) Half-year ended 30 June 2015 HK\$'m
CONTINUING OPERATIONS		
Profit before taxation	14,540	15,216
Calculated at a taxation rate of 16.5% (2015: 16.5%)	2,399	2,511
Effect of different taxation rates in other countries	2	(19)
Income not subject to taxation	(65)	(238)
Expenses not deductible for taxation purposes	54	56
Over-provision in prior periods	(2)	(6)
Foreign withholding tax	(76)	422
Taxation charge	2,312	2,726
Effective tax rate	15.9%	17.9%

NOTES TO THE INTERIM FINANCIAL INFORMATION

16. Dividends

	Half-year ended 30 June 2016		Half-year ended 30 June 2015	
	Per share HK\$	Total HK\$m	Per share HK\$	Total HK\$m
Interim dividend	0.545	5,762	0.545	5,762
Special dividend	0.710	7,507	–	–
	1.255	13,269	0.545	5,762

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 a special dividend of HK\$0.710 per ordinary share amounting to approximately HK\$7,507 million. These declared dividends are not reflected as a dividend payable in this interim financial information, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2016.

17. Earnings per share for profit attributable to the equity holders of the Company

The calculation of basic earnings per share for the first half of 2016 is based on the consolidated profit for the period and profit from continuing operations attributable to the equity holders of the Company of approximately HK\$42,731 million and HK\$11,814 million (first half of 2015: HK\$13,387 million and HK\$12,086 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 first half of 2016 (first half of 2015: Nil).

18. Retirement benefit costs

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.

The Group's total contributions made to the ORSO schemes for the first half of 2016 amounted to approximately HK\$185 million (first half of 2015: approximately HK\$183 million), after a deduction of forfeited contributions of approximately HK\$4 million (first half of 2015: approximately HK\$4 million). For the MPF Scheme, the Group contributed approximately HK\$46 million (first half of 2015: approximately HK\$41 million) for the first half of 2016.

NOTES TO THE INTERIM FINANCIAL INFORMATION

19. Cash and balances with banks and other financial institutions

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Cash	7,221	7,923
Balances with central banks	157,592	110,225
Balances with banks and other financial institutions	116,268	64,474
Placements with banks and other financial institutions maturing within one month	81,708	48,108
	362,789	230,730

20. Financial assets at fair value through profit or loss

	Trading assets		Financial assets designated at fair value through profit or loss		Total	
	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
At fair value						
Treasury bills	16,972	9,504	–	–	16,972	9,504
Other debt securities	25,386	20,300	22,056	20,434	47,442	40,734
	42,358	29,804	22,056	20,434	64,414	50,238
Certificates of deposit	1,677	2,223	145	641	1,822	2,864
Total debt securities and certificates of deposit	44,035	32,027	22,201	21,075	66,236	53,102
Equity securities	5	–	1,728	1,995	1,733	1,995
Fund	–	–	2,626	2,500	2,626	2,500
Total securities	44,040	32,027	26,555	25,570	70,595	57,597
Others	1,657	180	–	–	1,657	180
	45,697	32,207	26,555	25,570	72,252	57,777

NOTES TO THE INTERIM FINANCIAL INFORMATION

20. 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	
	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Debt securities and certificates of deposit				
– Listed in Hong Kong	8,966	11,650	5,800	5,841
– Listed outside Hong Kong	2,914	3,993	9,840	8,570
	11,880	15,643	15,640	14,411
– Unlisted	32,155	16,384	6,561	6,664
	44,035	32,027	22,201	21,075
Equity securities				
– Listed in Hong Kong	5	–	1,352	1,436
– Listed outside Hong Kong	–	–	376	559
	5	–	1,728	1,995
Fund				
– Unlisted	–	–	2,626	2,500
Total securities	44,040	32,027	26,555	25,570

Total securities are analysed by type of issuer as follows:

	Trading assets		Financial assets designated at fair value through profit or loss	
	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Sovereigns	34,481	18,802	1,343	1,529
Public sector entities*	200	607	–	–
Banks and other financial institutions	5,226	6,914	16,107	15,447
Corporate entities	4,133	5,704	9,105	8,594
Total securities	44,040	32,027	26,555	25,570

* Included trading assets of HK\$200 million (31 December 2015: HK\$607 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

NOTES TO THE INTERIM FINANCIAL INFORMATION

21. Derivative financial instruments

The Group enters into the following exchange rate, interest rate, commodity and equity 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 precious metal 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 fair value 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, metal prices or equity prices relative to their terms. The aggregate fair values of derivative financial instruments can fluctuate significantly from time to time.

NOTES TO THE INTERIM FINANCIAL INFORMATION

21. Derivative financial instruments (continued)

The following tables summarise the contract/notional amounts of each class of derivative financial instrument as at 30 June 2016 and 31 December 2015:

	At 30 June 2016			
	Trading HK\$m	Hedging HK\$m	Not qualified for hedge accounting HK\$m	Total HK\$m
Exchange rate contracts				
Spot, forwards and futures	326,157	–	4,973	331,130
Swaps	2,243,855	–	15,219	2,259,074
Foreign currency options				
– Options purchased	34,035	–	–	34,035
– Options written	34,072	–	–	34,072
	2,638,119	–	20,192	2,658,311
Interest rate contracts				
Forwards and futures	2,306	–	–	2,306
Swaps	516,930	117,576	3,707	638,213
Interest rate options				
– Options written	1,113	–	–	1,113
	520,349	117,576	3,707	641,632
Commodity contracts	13,507	–	–	13,507
Equity contracts	3,757	–	–	3,757
Credit derivative contracts	970	–	–	970
	3,176,702	117,576	23,899	3,318,177

NOTES TO THE INTERIM FINANCIAL INFORMATION

21. Derivative financial instruments (continued)

	At 31 December 2015			
	Trading HK\$'m	Hedging HK\$'m	Not qualified for hedge accounting HK\$'m	Total HK\$'m
Exchange rate contracts				
Spot, forwards and futures	321,212	–	4,675	325,887
Swaps	2,063,424	–	15,863	2,079,287
Foreign currency options				
– Options purchased	31,947	–	–	31,947
– Options written	32,821	–	–	32,821
	2,449,404	–	20,538	2,469,942
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
	2,859,456	77,144	22,954	2,959,554

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

21. Derivative financial instruments (continued)

The following tables summarise the fair values of each class of derivative financial instrument as at 30 June 2016 and 31 December 2015:

	At 30 June 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	15,551	–	16	15,567	(10,696)	–	(7)	(10,703)
Swaps	21,178	–	26	21,204	(29,627)	–	(68)	(29,695)
Foreign currency options								
– Options purchased	271	–	–	271	–	–	–	–
– Options written	–	–	–	–	(320)	–	–	(320)
	37,000	–	42	37,042	(40,643)	–	(75)	(40,718)
Interest rate contracts								
Forwards and futures	2	–	–	2	(7)	–	–	(7)
Swaps	4,320	2,055	–	6,375	(4,758)	(4,473)	(29)	(9,260)
Interest rate options								
– Options written	–	–	–	–	(8)	–	–	(8)
	4,322	2,055	–	6,377	(4,773)	(4,473)	(29)	(9,275)
Commodity contracts	605	–	–	605	(411)	–	–	(411)
Equity contracts	31	–	–	31	(35)	–	–	(35)
Credit derivative contracts	11	–	–	11	(8)	–	–	(8)
	41,969	2,055	42	44,066	(45,870)	(4,473)	(104)	(50,447)

NOTES TO THE INTERIM FINANCIAL INFORMATION

21. Derivative financial instruments (continued)

	At 31 December 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	15,777	-	20	15,797	(9,687)	-	-	(9,687)
Swaps	22,817	-	87	22,904	(25,870)	-	-	(25,870)
Foreign currency options								
- Options purchased	513	-	-	513	-	-	-	-
- Options written	-	-	-	-	(487)	-	-	(487)
	39,107	-	107	39,214	(36,044)	-	-	(36,044)
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)
	41,223	1,877	107	43,207	(38,529)	(1,516)	(27)	(40,072)

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.

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Exchange rate contracts	12,141	13,212
Interest rate contracts	1,196	657
Commodity contracts	33	2
Equity contracts	174	181
Credit derivative contracts	32	-
	13,576	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\$27,138 million (31 December 2015: HK\$11,332 million) and the effect of valid bilateral netting agreements amounted to HK\$21,499 million (31 December 2015: HK\$9,682 million).

NOTES TO THE INTERIM FINANCIAL INFORMATION

22. Advances and other accounts

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Personal loans and advances	278,616	273,464
Corporate loans and advances	710,592	616,779
Advances to customers	989,208	890,243
Loan impairment allowances		
– Individually assessed	(711)	(564)
– Collectively assessed	(2,659)	(2,445)
	985,838	887,234
Trade bills	22,839	32,011
Advances to banks and other financial institutions	5,418	969
	1,014,095	920,214

As at 30 June 2016, advances to customers included accrued interest of HK\$1,306 million (31 December 2015: HK\$1,409 million).

As at 30 June 2016, no impairment allowance was made in respect of trade bills and advances to banks and other financial institutions (31 December 2015: Nil).

NOTES TO THE INTERIM FINANCIAL INFORMATION

23. Investment in securities

	At 30 June 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	108,065	–	–	108,065
Other debt securities	292,386	66,528	1,357	360,271
	400,451	66,528	1,357	468,336
Certificates of deposit	78,096	18	–	78,114
Total debt securities and certificates of deposit	478,547	66,546	1,357	546,450
Equity securities	3,962	–	–	3,962
Fund	145	–	–	145
	482,654	66,546	1,357	550,557

	At 31 December 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	81,108	3,166	320,285
	360,317	81,108	3,166	444,591
Certificates of deposit	69,866	18	–	69,884
Total debt securities and certificates of deposit	430,183	81,126	3,166	514,475
Equity securities	2,746	–	–	2,746
	432,929	81,126	3,166	517,221

NOTES TO THE INTERIM FINANCIAL INFORMATION

23. Investment in securities (continued)

Investment in securities is analysed by place of listing as follows:

	At 30 June 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	57,028	7,619	–
– Listed outside Hong Kong	157,966	28,005	–
	214,994	35,624	–
– Unlisted	263,553	30,922	1,357
	478,547	66,546	1,357
Equity securities			
– Listed in Hong Kong	3,001	–	–
– Listed outside Hong Kong	360	–	–
	3,361	–	–
– Unlisted	601	–	–
	3,962	–	–
Fund			
– Unlisted	145	–	–
	482,654	66,546	1,357
Market value of listed held-to-maturity securities		36,410	

	At 31 December 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	32,087	–
	151,853	39,061	–
– Unlisted	278,330	42,065	3,166
	430,183	81,126	3,166
Equity securities			
– Listed in Hong Kong	2,459	–	–
– Unlisted	287	–	–
	2,746	–	–
	432,929	81,126	3,166
Market value of listed held-to-maturity securities		39,299	

NOTES TO THE INTERIM FINANCIAL INFORMATION

23. Investment in securities (continued)

Investment in securities is analysed by type of issuer as follows:

	At 30 June 2016		
	Available- for-sale securities	Held-to- maturity securities	Loans and receivables
	HK\$'m	HK\$'m	HK\$'m
Sovereigns	149,594	267	–
Public sector entities*	23,938	14,164	–
Banks and other financial institutions	211,842	30,052	1,357
Corporate entities	97,280	22,063	–
	482,654	66,546	1,357

	At 31 December 2015		
	Available- for-sale securities	Held-to- maturity securities	Loans and receivables
	HK\$'m	HK\$'m	HK\$'m
Sovereigns	155,327	840	–
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	81,126	3,166

* Included available-for-sale securities of HK\$22,670 million (31 December 2015: HK\$17,491 million) and held-to-maturity securities of HK\$4,492 million (31 December 2015: HK\$4,614 million) which are eligible to be classified as public sector entities under the Banking (Capital) Rules.

24. Investment properties

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
At 1 January	15,262	14,559
Additions	–	47
Fair value gains	104	826
Reclassification from properties, plant and equipment (Note 25)	544	245
Exchange difference	–	(1)
Classified as assets held for sale	–	(414)
At period/year end	15,910	15,262

NOTES TO THE INTERIM FINANCIAL INFORMATION

25. Properties, plant and equipment

	Premises HK\$'m	Equipment, fixtures and fittings HK\$'m	Total HK\$'m
Net book value at 1 January 2016	48,187	2,246	50,433
Additions	109	219	328
Disposals	(1)	(1)	(2)
Revaluation	(474)	–	(474)
Depreciation for the period (Note 12)	(533)	(370)	(903)
Reclassification to investment properties (Note 24)	(544)	–	(544)
Net book value at 30 June 2016	46,744	2,094	48,838
At 30 June 2016			
Cost or valuation	46,744	7,699	54,443
Accumulated depreciation and impairment	–	(5,605)	(5,605)
Net book value at 30 June 2016	46,744	2,094	48,838
The analysis of cost or valuation of the above assets is as follows:			
At 30 June 2016			
At cost	–	7,699	7,699
At valuation	46,744	–	46,744
	46,744	7,699	54,443
Net book value at 1 January 2015	52,639	2,568	55,207
Additions	423	771	1,194
Disposals	(371)	(27)	(398)
Revaluation	3,516	–	3,516
Depreciation for the year	(1,070)	(773)	(1,843)
Reclassification to investment properties (Note 24)	(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	48,187	2,246	50,433
At 31 December 2015			
Cost or valuation	48,187	7,598	55,785
Accumulated depreciation and impairment	–	(5,352)	(5,352)
Net book value at 31 December 2015	48,187	2,246	50,433
The analysis of cost or valuation of the above assets is as follows:			
At 31 December 2015			
At cost	–	7,598	7,598
At valuation	48,187	–	48,187
	48,187	7,598	55,785

NOTES TO THE INTERIM FINANCIAL INFORMATION

26. Other assets

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Reposessed assets	74	44
Precious metals	3,515	3,673
Reinsurance assets	39,469	38,514
Accounts receivable and prepayments	39,645	23,724
	82,703	65,955

27. Financial liabilities at fair value through profit or loss

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Trading liabilities		
– Short positions in Exchange Fund Bills and Notes	11,213	8,371
– Others	7	–
	11,220	8,371
Financial liabilities designated at fair value through profit or loss		
– Structured deposits (Note 28)	2,648	2,571
	13,868	10,942

The carrying amount of financial liabilities designated at fair value through profit or loss as at 30 June 2016 was more than the amount that the Group would be contractually required to pay at maturity to the holders by HK\$1 million, and it was less than the amount that the Group would be contractually required to pay at maturity to the holders by HK\$5 million as at 31 December 2015. The amount of change in the fair values of financial liabilities at fair value through profit or loss, during the period and cumulatively, attributable to changes in own credit risk was insignificant.

NOTES TO THE INTERIM FINANCIAL INFORMATION

28. Deposits from customers

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Current, savings and other deposit accounts (per balance sheet)	1,471,681	1,404,989
Structured deposits reported as financial liabilities at fair value through profit or loss (Note 27)	2,648	2,571
	1,474,329	1,407,560
Analysed by:		
Demand deposits and current accounts		
– Corporate	108,634	99,951
– Personal	38,551	34,118
	147,185	134,069
Savings deposits		
– Corporate	348,771	304,593
– Personal	446,764	413,154
	795,535	717,747
Time, call and notice deposits		
– Corporate	330,539	344,205
– Personal	201,070	211,539
	531,609	555,744
	1,474,329	1,407,560

29. Debt securities and certificates of deposit in issue

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Debt securities, at amortised cost		
– Senior notes under the Medium Term Note Programme	5,803	5,728
– Other debt securities	2,846	1,248
	8,649	6,976

30. Other accounts and provisions

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Other accounts payable	63,138	33,957
Provisions	268	268
	63,406	34,225

NOTES TO THE INTERIM FINANCIAL INFORMATION

31. 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 this interim financial information 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 first half of 2016 and the year ended 31 December 2015 are as follows:

	At 30 June 2016					
	Accelerated tax depreciation	Property revaluation	Losses	Impairment allowances	Others	Total
	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m
At 1 January 2016	596	7,192	–	(459)	(930)	6,399
Credited to income statement (Note 15)	(12)	(67)	–	(32)	(32)	(143)
(Credited)/charged to other comprehensive income	–	(152)	–	–	248	96
Exchange difference	–	–	–	1	–	1
At 30 June 2016	584	6,973	–	(490)	(714)	6,353

	At 31 December 2015					
	Accelerated tax depreciation	Property revaluation	Losses	Impairment allowances	Others	Total
	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m	HK\$'m
At 1 January 2015	607	7,858	–	(645)	94	7,914
Charged/(credited) to income statement	7	(112)	(35)	40	(702)	(802)
Charged/(credited) to other comprehensive income	–	483	–	–	(416)	67
Exchange difference	–	(3)	2	9	–	8
Classified as assets held for sale	(18)	(1,034)	33	137	94	(788)
At 31 December 2015	596	7,192	–	(459)	(930)	6,399

NOTES TO THE INTERIM FINANCIAL INFORMATION

31. 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:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Deferred tax assets	(56)	(58)
Deferred tax liabilities	6,409	6,457
	6,353	6,399

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Deferred tax assets to be recovered after more than twelve months	(56)	(58)
Deferred tax liabilities to be settled after more than twelve months	7,072	7,284
	7,016	7,226

As at 30 June 2016, the Group has not recognised deferred tax assets in respect of tax losses amounting to HK\$8 million (31 December 2015: HK\$8 million). These tax losses do not expire under the current tax legislation.

32. Insurance contract liabilities

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
At 1 January	82,645	73,796
Benefits paid	(9,951)	(12,807)
Claims incurred and movement in liabilities	10,576	21,656
At period/year end	83,270	82,645

The insurance contract liabilities that are covered by reinsurance arrangements amounted to HK\$34,495 million (31 December 2015: HK\$36,071 million) and the associated reinsurance assets of HK\$39,469 million (31 December 2015: HK\$38,514 million) are included in "Other assets" (Note 26).

NOTES TO THE INTERIM FINANCIAL INFORMATION

33. Subordinated liabilities

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Subordinated notes, at amortised cost with fair value hedge adjustment USD2,500m*	19,754	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 3.5(B).

* Interest rate at 5.55% per annum payable semi-annually, due February 2020.

34. Discontinued operations and assets held for sale

According to the announcement made on 14 July 2015, BOC has 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 ("Cinda Financial") (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 is conditional upon the satisfaction of the conditions precedent set out in the Sale and Purchase Agreement.

On 30 May 2016, all the conditions precedent set out in the Sale and Purchase Agreement have been satisfied, and the disposal was completed in accordance with the terms and conditions of the Sale and Purchase Agreement. Upon completion, NCB ceased to be a subsidiary of BOCHK.

The comparative amounts of condensed consolidated income statement have been restated as if the discontinued operations had been discontinued at the beginning of year 2015.

NOTES TO THE INTERIM FINANCIAL INFORMATION

34. Discontinued operations and assets held for sale (continued)

The results of discontinued operations for the period are as follows:

	Half-year ended 30 June 2016* HK\$'m	Half-year ended 30 June 2015 HK\$'m
DISCONTINUED OPERATIONS		
Interest income	2,883	4,318
Interest expense	(1,090)	(1,938)
Net interest income	1,793	2,380
Fee and commission income	513	622
Fee and commission expense	(6)	(22)
Net fee and commission income	507	600
Net trading loss	(24)	(97)
Net loss on financial instruments designated at fair value through profit or loss	(1)	(1)
Net gain on other financial assets	95	63
Other operating income	3	13
Net operating income before impairment allowances	2,373	2,958
Net charge of impairment allowances	(356)	(341)
Net operating income	2,017	2,617
Operating expenses	(884)	(1,073)
Operating profit	1,133	1,544
Net gain from disposal of/fair value adjustments on investment properties	–	20
Net gain from disposal/revaluation of properties, plant and equipment	–	2
Profit before taxation	1,133	1,566
Taxation	(172)	(265)
Profit after taxation	961	1,301
Gain on disposal of discontinued operations	29,956	–
Profit from discontinued operations	30,917	1,301
	HK\$	HK\$
Earnings per share for profit attributable to the equity holders of the Company		
Basic and diluted		
– profit from discontinued operations	2.9242	0.1231

* Up to the date of disposal.

NOTES TO THE INTERIM FINANCIAL INFORMATION

34. Discontinued operations and assets held for sale (continued)

The net cash flows incurred by discontinued operations are as follows:

	Half-year ended 30 June 2016* HK\$'m	Half-year ended 30 June 2015 HK\$'m
Operating activities	(13,447)	(7,863)
Investing activities	(27)	(25)
Financing activities	–	(543)
Net cash outflow incurred by discontinued operations	(13,474)	(8,431)

* Up to the date of disposal.

The gain on disposal of discontinued operations is analysed as follows:

	Half-year ended 30 June 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

NOTES TO THE INTERIM FINANCIAL INFORMATION

34. 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:

	Half-year ended 30 June 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

NOTES TO THE INTERIM FINANCIAL INFORMATION

34. 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:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
ASSETS HELD FOR SALE		
Cash and balances with banks and other financial institutions	–	53,124
Placements with banks and other financial institutions maturing between one and twelve months	–	7,057
Financial assets at fair value through profit or loss	–	7,263
Derivative financial instruments	–	653
Advances and other accounts	–	168,924
Investment in securities	–	55,107
Investment properties	–	414
Properties, plant and equipment	–	6,960
Current tax assets	–	47
Deferred tax assets	–	11
Other assets	–	913
Total assets held for sale	–	300,473
LIABILITIES ASSOCIATED WITH ASSETS HELD FOR SALE		
Deposits and balances from banks and other financial institutions	–	18,040
Financial liabilities at fair value through profit or loss	–	4,576
Derivative financial instruments	–	284
Deposits from customers	–	215,311
Other accounts and provisions	–	12,607
Current tax liabilities	–	188
Deferred tax liabilities	–	799
Total liabilities associated with assets held for sale	–	251,805
	–	48,668

The cumulative income recognised in other comprehensive income relating to assets held for sale is as follows:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Cumulative income recognised in other comprehensive income	–	5,963

35. Share capital

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Issued and fully paid: 10,572,780,266 ordinary shares	52,864	52,864

NOTES TO THE INTERIM FINANCIAL INFORMATION

36. Notes to condensed consolidated cash flow statement

(a) Reconciliation of operating profit to operating cash inflow/(outflow) before taxation

	Half-year ended 30 June 2016 HK\$'m	Half-year ended 30 June 2015 HK\$'m
Operating profit		
– from continuing operations	14,399	14,759
– from discontinued operations	1,133	1,544
	15,532	16,303
Depreciation	903	961
Net charge of impairment allowances	882	809
Unwind of discount on impairment allowances	(6)	(10)
Advances written off net of recoveries	(256)	(963)
Change in subordinated liabilities	542	93
Change in balances with banks and other financial institutions with original maturity over three months	(20,793)	204
Change in placements with banks and other financial institutions with original maturity over three months	1,642	(4,871)
Change in financial assets at fair value through profit or loss	(8,896)	(10,989)
Change in derivative financial instruments	9,597	4,320
Change in advances and other accounts	(93,779)	(64,538)
Change in investment in securities	(32,652)	(124,668)
Change in other assets	(18,585)	(15,726)
Change in deposits and balances from banks and other financial institutions	92,417	(30,176)
Change in financial liabilities at fair value through profit or loss	2,929	8,926
Change in deposits from customers	66,634	132,218
Change in debt securities and certificates of deposit in issue	1,673	(4,830)
Change in other accounts and provisions	31,920	39,095
Change in insurance contract liabilities	625	8,983
Effect of changes in exchange rates	1,037	112
Operating cash inflow/(outflow) before taxation	51,366	(44,747)
Cash flows from operating activities included		
– interest received	21,280	23,934
– interest paid	6,440	8,253
– dividend received	75	80

NOTES TO THE INTERIM FINANCIAL INFORMATION

36. Notes to condensed consolidated cash flow statement (continued)

(b) Analysis of the balances of cash and cash equivalents

	At 30 June 2016 HK\$'m	At 30 June 2015 HK\$'m
Cash and balances with banks and other financial institutions with original maturity within three months	340,809	316,136
Placements with banks and other financial institutions with original maturity within three months	22,350	19,056
Treasury bills with original maturity within three months	13,327	21,698
Certificates of deposit with original maturity within three months	31	283
	376,517	357,173

37. 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.

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Direct credit substitutes	6,641	24,360
Transaction-related contingencies	7,545	7,600
Trade-related contingencies	24,462	31,713
Asset sales with recourse	–	5,419
Commitments that are unconditionally cancellable without prior notice	397,273	471,092
Other commitments with an original maturity of		
– up to one year	8,135	10,519
– over one year	110,108	114,376
	554,164	665,079
Credit risk-weighted amount	48,599	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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

38. Capital commitments

The Group has the following outstanding capital commitments not provided for in this interim financial information:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Authorised and contracted for but not provided for	654	223
Authorised but not contracted for	73	16
	727	239

The above capital commitments mainly relate to commitments to purchase computer equipment and software, and to renovate the Group's premises.

39. Operating lease commitments

(a) As lessee

The Group has commitments to make the following future minimum lease payments under non-cancellable operating leases:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Land and buildings		
– Not later than one year	562	787
– Later than one year but not later than five years	722	1,394
– Later than five years	13	112
	1,297	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:

	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Land and buildings		
– Not later than one year	442	421
– Later than one year but not later than five years	405	330
	847	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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

40. 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 a joint venture.

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.

NOTES TO THE INTERIM FINANCIAL INFORMATION

40. 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
Half-year ended 30 June 2016								
CONTINUING OPERATIONS								
Net interest income/(expense)								
– External	1,587	5,085	4,330	1,168	2	12,172	–	12,172
– Inter-segment	2,657	123	(2,421)	(3)	(356)	–	–	–
	4,244	5,208	1,909	1,165	(354)	12,172	–	12,172
Net fee and commission income/(expense)	2,685	2,860	57	(95)	323	5,830	(163)	5,667
Net insurance premium income	–	–	–	3,593	–	3,593	(9)	3,584
Net trading gain/(loss)	327	81	2,052	(176)	12	2,296	9	2,305
Net (loss)/gain on financial instruments designated at fair value through profit or loss	–	–	(7)	1,039	–	1,032	–	1,032
Net gain on other financial assets	–	2	429	147	–	578	–	578
Other operating income	6	2	–	63	956	1,027	(660)	367
Total operating income	7,262	8,153	4,440	5,736	937	26,528	(823)	25,705
Net insurance benefits and claims and movement in liabilities	–	–	–	(4,960)	–	(4,960)	–	(4,960)
Net operating income before impairment allowances	7,262	8,153	4,440	776	937	21,568	(823)	20,745
Net (charge)/reversal of impairment allowances	(196)	(353)	23	–	–	(526)	–	(526)
Net operating income	7,066	7,800	4,463	776	937	21,042	(823)	20,219
Operating expenses	(3,373)	(1,309)	(520)	(165)	(1,276)	(6,643)	823	(5,820)
Operating profit/(loss)	3,693	6,491	3,943	611	(339)	14,399	–	14,399
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	104	104	–	104
Net (loss)/gain from disposal/revaluation of properties, plant and equipment	(1)	(6)	–	–	2	(5)	–	(5)
Share of profits less losses after tax of associates and a joint venture	–	–	–	–	42	42	–	42
Profit/(loss) before taxation	3,692	6,485	3,943	611	(191)	14,540	–	14,540
At 30 June 2016								
ASSETS								
Segment assets	306,355	727,418	1,171,168	104,313	68,222	2,377,476	(13,660)	2,363,816
Interests in associates and a joint venture	–	–	–	–	416	416	–	416
	306,355	727,418	1,171,168	104,313	68,638	2,377,892	(13,660)	2,364,232
LIABILITIES								
Segment liabilities	783,402	715,132	536,111	96,519	12,113	2,143,277	(13,660)	2,129,617
Half-year ended 30 June 2016								
CONTINUING OPERATIONS								
Other information								
Capital expenditure	3	–	–	3	322	328	–	328
Depreciation	190	75	35	6	597	903	–	903
Amortisation of securities	–	–	(349)	15	–	(334)	–	(334)

NOTES TO THE INTERIM FINANCIAL INFORMATION

40. 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
Half-year ended 30 June 2015 (Restated)								
CONTINUING OPERATIONS								
Net interest income/(expense)								
– External	1,106	3,535	7,561	1,087	3	13,292	–	13,292
– Inter-segment	2,888	1,075	(3,641)	5	(327)	–	–	–
	3,994	4,610	3,920	1,092	(324)	13,292	–	13,292
Net fee and commission income/(expense)	3,861	1,848	56	(156)	255	5,864	(139)	5,725
Net insurance premium income	–	–	–	8,884	–	8,884	(9)	8,875
Net trading gain	336	115	211	33	2	697	8	705
Net loss on financial instruments designated at fair value through profit or loss	–	–	(11)	(156)	–	(167)	–	(167)
Net gain on other financial assets	641	17	45	113	–	816	–	816
Other operating income	13	3	–	10	959	985	(512)	473
Total operating income	8,845	6,593	4,221	9,820	892	30,371	(652)	29,719
Net insurance benefits and claims and movement in liabilities	–	–	–	(8,989)	–	(8,989)	–	(8,989)
Net operating income before impairment allowances	8,845	6,593	4,221	831	892	21,382	(652)	20,730
Net (charge)/reversal of impairment allowances	(98)	(372)	1	–	1	(468)	–	(468)
Net operating income	8,747	6,221	4,222	831	893	20,914	(652)	20,262
Operating expenses	(3,137)	(1,165)	(462)	(177)	(1,214)	(6,155)	652	(5,503)
Operating profit/(loss)	5,610	5,056	3,760	654	(321)	14,759	–	14,759
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	349	349	–	349
Net (loss)/gain from disposal/revaluation of properties, plant and equipment	(3)	–	(1)	(5)	94	85	–	85
Share of profits less losses after tax of associates and a joint venture	–	–	–	–	23	23	–	23
Profit before taxation	5,607	5,056	3,759	649	145	15,216	–	15,216
At 31 December 2015								
ASSETS								
Segment assets	301,551	638,386	985,051	98,282	68,425	2,091,695	(24,680)	2,067,015
Interests in associates and a joint venture	–	–	–	–	376	376	–	376
Assets held for sale	39,480	134,506	123,419	–	7,541	304,946	(4,473)	300,473
	341,031	772,892	1,108,470	98,282	76,342	2,397,017	(29,153)	2,367,864
LIABILITIES								
Segment liabilities	752,284	675,095	400,515	91,593	11,631	1,931,118	(13,052)	1,918,066
Liabilities associated with assets held for sale	91,705	138,603	35,993	–	1,605	267,906	(16,101)	251,805
	843,989	813,698	436,508	91,593	13,236	2,199,024	(29,153)	2,169,871
Half-year ended 30 June 2015 (Restated)								
CONTINUING OPERATIONS								
Other information								
Capital expenditure	9	–	–	22	504	535	–	535
Depreciation	182	70	35	5	559	851	–	851
Amortisation of securities	–	–	421	(48)	–	373	–	373

NOTES TO THE INTERIM FINANCIAL INFORMATION

41. Assets pledged as security

As at 30 June 2016, the liabilities of the Group amounting to HK\$9,905 million (31 December 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\$22,310 million (31 December 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\$32,730 million (31 December 2015: HK\$22,594 million) mainly included in "Trading assets", "Investment in securities" and "Trade bills".

42. 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.

(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 30 June 2016, the related aggregate amounts due from and to BOC of the Group were HK\$126,973 million (31 December 2015: HK\$102,324 million) and HK\$80,499 million (31 December 2015: HK\$55,448 million) respectively. The aggregate amounts of income and expenses of the Group arising from these transactions with BOC for the first half of 2016 were HK\$751 million (first half of 2015: HK\$2,074 million) and HK\$192 million (first half of 2015: HK\$287 million) respectively. Transactions with other companies controlled by BOC are not considered material.

NOTES TO THE INTERIM FINANCIAL INFORMATION

42. Significant related party transactions (continued)

(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.

(c) *Summary of transactions entered into during the ordinary course of business with associates, a joint venture and other related parties*

The aggregate income/expenses and balances arising from related party transactions with associates, a joint venture and other related parties of the Group are summarised as follows:

	Half-year ended 30 June 2016 HK\$'m	Half-year ended 30 June 2015 HK\$'m
Income statement items		
Associates		
– Other operating expenses	35	32
Other related parties		
– Administrative services fees received/receivable	5	5
	At 30 June 2016 HK\$'m	At 31 December 2015 HK\$'m
Balance sheet item		
Associates		
– Other accounts and provisions	9	–

NOTES TO THE INTERIM FINANCIAL INFORMATION

42. Significant related party transactions (continued)

(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, senior management and company secretary. 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 periods, 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 is detailed as follows:

	Half-year ended 30 June 2016 HK\$'m	Half-year ended 30 June 2015 HK\$'m
Salaries and other short-term employee benefits	17	17
Post-employment benefits	–	1
	17	18

NOTES TO THE INTERIM FINANCIAL INFORMATION

43. 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:

	At 30 June 2016				
	Non-bank private sector				Total HK\$'m
	Banks HK\$'m	Official sector HK\$'m	Non-bank financial institutions	Non-financial private sector	
			HK\$'m	HK\$'m	
Mainland of China	399,269	178,059	11,595	137,461	726,384
Hong Kong	5,689	466	14,971	274,183	295,309

	At 31 December 2015				
	Non-bank private sector				Total HK\$'m
	Banks HK\$'m	Official sector HK\$'m	Non-bank financial institutions	Non-financial private sector	
			HK\$'m	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

NOTES TO THE INTERIM FINANCIAL INFORMATION

44. 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 banking subsidiaries.

		At 30 June 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	268,994	34,084	303,078
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	73,338	11,751	85,089
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	50,085	8,946	59,031
Other entities of central government not reported in item 1 above	4	25,217	171	25,388
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	54,318	12,113	66,431
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	5,142	298	5,440
Total	8	477,094	67,363	544,457
Total assets after provision	9	2,228,365		
On-balance sheet exposures as percentage of total assets	10	21.41%		

NOTES TO THE INTERIM FINANCIAL INFORMATION

44. Non-bank Mainland exposures (continued)

	Items in the HKMA return	At 31 December 2015		
		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	<u>2,282,058</u>		
On-balance sheet exposures as percentage of total assets	10	<u>22.91%</u>		

45. Compliance with HKAS 34

The unaudited interim financial information for the first half of 2016 complies with HKAS 34 “Interim Financial Reporting” issued by the HKICPA.

NOTES TO THE INTERIM FINANCIAL INFORMATION

46. Statutory accounts

The financial information relating to the year ended 31 December 2015 that is included in this Interim Report as comparative information does not constitute the Company's statutory annual consolidated financial statements for that year but is derived from those financial statements. Further information relating to these statutory financial statements required to be disclosed in accordance with section 436 of the Hong Kong Companies Ordinance is as follows:

The Company has delivered the financial statements for the year ended 31 December 2015 to the Registrar of Companies as required by section 662(3) of, and Part 3 of Schedule 6 to, the Hong Kong Companies Ordinance.

The Company's auditor has reported on those financial statements. The auditors' report was unqualified; did not include a reference to any matters to which the auditor drew attention by way of emphasis without qualifying its report; and did not contain a statement under sections 406(2), 407(2) or (3) of the Hong Kong Companies Ordinance.

ADDITIONAL INFORMATION

1. 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

CHAN Chun Ying

Registered Office

52nd 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 Depository Bank

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

Credit Ratings (Long Term)

Standard & Poor's	A+
Moody's	Aa3
Fitch	A

Index Constituent

The Company is a constituent of the following indices:

Hang Seng Index Series
Hang Seng Corporate Sustainability Index Series
MSCI Index Series
FTSE Index Series

Stock Codes

Ordinary shares: The Stock Exchange of Hong Kong Limited	2388
Reuters	2388.HK
Bloomberg	2388 HK

Level 1 ADR Programme: CUSIP No.	096813209
OTC Symbol	BHKLY

Website

www.bochk.com

ADDITIONAL INFORMATION

2. Interim dividend, special dividend and closure of register of members

The Board has declared an interim dividend of HK\$0.545 per share (2015: HK\$0.545) and special dividend of HK\$0.710 per share (2015: Nil), payable on Monday, 3 October 2016 to shareholders whose names appear on the Register of Members of the Company on Monday, 26 September 2016.

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to the interim dividend and special dividend, from Wednesday, 21 September 2016 to Monday, 26 September 2016 (both days inclusive), during which period no transfer of shares will be registered. In order to qualify for the interim dividend and special 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 Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, not later than 4:30 p.m. on Tuesday, 20 September 2016. Shares of the Company will be traded ex-dividend as from Monday, 19 September 2016.

3. Interest of substantial shareholders

The register maintained by the Company pursuant to section 336 of the SFO recorded that, as at 30 June 2016, the following parties had the following interests (as defined in the SFO) in the Company set opposite their respective names:

Name of Corporation	Number of shares held in the Company	Approximate % of the 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 30 June 2016.

ADDITIONAL INFORMATION

4. Directors' and Chief Executive's interests in shares, underlying shares and debentures

As at 30 June 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. The 40,000 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 30 June 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.

ADDITIONAL INFORMATION

5. Changes of information in respect of Directors

In accordance with Rule 13.51B(1) of the Listing Rules, the changes in information required to be disclosed by Directors pursuant to paragraphs (a) to (e) and (g) of Rule 13.51(2) of the Listing Rules after the publication of the Company's Annual Report 2015 on 30 March 2016 up to 30 August 2016 (being the approval date of this Interim Report) are set out below:

- (a) Mr CHEN Siqing, Vice Chairman and Non-executive Director of the Company, has been serving as the Chairman of the Board of Directors and Non-executive Director of BOC Aviation Limited (formerly known as BOC Aviation Private Limited) since December 2011 which has been listed on the Stock Exchange on 1 June 2016.
- (b) Mr YUE Yi, Vice Chairman, Executive Director and Chief Executive of the Company, has been appointed as President and ceased to be the Honorary President of Hong Kong Chinese Enterprises Association since 7 April 2016, and concurrently has been appointed as Chairman of The Hong Kong Chinese Enterprises Charitable Foundation Limited. He has been appointed as Committee Member of The Hong Kong General Chamber of Commerce on 10 May 2016 and the Chairman of Chinese Banking Association of Hong Kong Company Limited on 20 June 2016. Mr Yue resigned as the Chairman of NCB as well as the Chairman of NCB (China) on 30 May 2016 and 5 July 2016 respectively.
- (c) Mr LI Jiuzhong, Executive Director of the Company, resigned as a Director of NCB and a Director of NCB (China) on 30 May 2016 and 5 July 2016 respectively.
- (d) Mr TUNG Savio Wai-Hok, Independent Non-executive Director of the Company, was appointed as the Chairman of Audit Committee with effect from 6 June 2016.

The biographies of Directors are available under the sub-section "Organisation – Board of Directors" of the section headed "About Us" on the Company's website at www.bochk.com.

6. Purchase, sale or redemption of the Company's shares

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

ADDITIONAL INFORMATION

7. Audit Committee

The Audit Committee consists of Independent Non-executive Directors only. It is chaired by Mr TUNG Savio Wai-Hok¹. Other members include Madam CHENG Eva, Dr CHOI Koon Shum² and Mr KOH Beng Seng. Mr SHAN Weijian retired as an Independent Non-executive Director and ceased to be the Chairman of Audit Committee with effect from the immediate conclusion of the annual general meeting held on 6 June 2016.

Based on the principle of independence, the Audit Committee assists the Board in monitoring the financial reports, internal control, internal audit and external audit of the Group.

At the request of the Audit Committee of the Company, the Group's external auditor has carried out a review of the interim financial information in accordance with the Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the HKICPA. The Audit Committee has reviewed with the Management the accounting principles and practices adopted by the Group and discussed auditing, internal control and financial reporting matters including the review of the unaudited interim reports.

Notes:

1. Mr TUNG Savio Wai-Hok was appointed as the Chairman of Audit Committee with effect from 6 June 2016.
2. Dr CHOI Koon Shum was appointed as an Independent Non-executive Director and a member of Audit Committee with effect from the immediate conclusion of the annual general meeting held on 6 June 2016.

8. Compliance with the "Corporate Governance Code and Corporate Governance Report"

The Company is committed to embracing and enhancing good corporate governance principles and practices. During the period under review, the Company has been in full compliance with all code provisions of the Corporate Governance Code and Corporate Governance Report as contained in Appendix 14 of the Listing Rules (the "Corporate Governance Code") 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. The Company has also complied with nearly all the recommended best practices set out in the Corporate Governance Code throughout the period. For further details, please refer to the section titled "Corporate Governance" contained in the Annual Report 2015 of the Company.

9. Compliance with the Codes for Securities Transactions by Directors

The Company has established and implemented the "Code for Securities Transactions by Directors" (the "Company's Code") to govern the Directors' dealing 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. Apart from the securities of the Company, the Company's Code also applies to the Director's dealings in the securities of BOC and BOC Aviation Limited which have been listed on the Hong Kong Stock Exchange in June 2006 and June 2016 respectively. In this connection, the Company had made specific enquiry of all Directors, who confirmed that they had strictly complied with the provisions set out in both the Company's Code and the Model Code throughout the period under review. The Company had undertaken a review of the Company's Code in October 2015. There were no fundamental amendments to the Company's Code and changes were in adaptive nature mainly to refine the Company's Code.

ADDITIONAL INFORMATION

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

The unaudited interim 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.

11. Interim Report

This Interim 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 Interim 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 Interim Report and other 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.

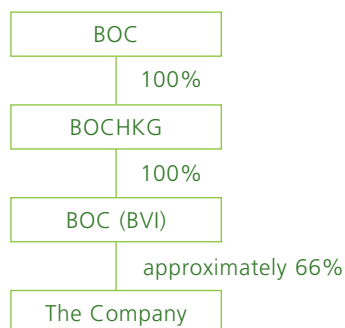
If you have any queries about how to obtain copies of this Interim Report or how to access those corporate communications on the Company's website, please call the Company's hotline at (852) 2846 2700.

12. 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 interim financial information. 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 interim financial information 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.



ADDITIONAL INFORMATION

12. Reconciliation between HKFRSs vs IFRS/CAS (continued)

Second, the Group has prepared its interim financial information 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 interim financial information 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.

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 period.

(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	
	Half-year ended 30 June 2016 HK\$m	Half-year ended 30 June 2015 HK\$m	At 30 June 2016 HK\$m	At 31 December 2015 HK\$m
Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under HKFRSs	43,145	13,791	234,615	197,993
Add: IFRS/CAS adjustments				
Restatement of carrying value of bank premises	5,814	740	(35,667)	(42,389)
Deferred tax adjustments	(965)	(43)	5,978	7,104
Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under IFRS/CAS	47,994	14,488	204,926	162,708

INDEPENDENT REVIEW REPORT



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

Report on review of interim financial information

To the board of directors of BOC Hong Kong (Holdings) Limited

(Incorporated in Hong Kong with limited liability)

Introduction

We have reviewed the interim financial information set out on pages 34 to 114, which comprises the condensed consolidated balance sheet of BOC Hong Kong (Holdings) Limited (the “Company”) and its subsidiaries (together, the “Group”) as at 30 June 2016 and the related condensed consolidated income statement, the condensed consolidated statement of comprehensive income, the condensed consolidated statement of changes in equity and the condensed consolidated cash flow statement for the six-month period then ended, and other explanatory notes. The Main Board Listing Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and Hong Kong Accounting Standard 34 “Interim Financial Reporting” (“HKAS 34”) issued by the Hong Kong Institute of Certified Public Accountants. The directors of the Company are responsible for the preparation and presentation of this interim financial information in accordance with HKAS 34. Our responsibility is to express a conclusion on this interim financial information based on our review. Our report is made solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Scope of review

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410, “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Hong Kong Institute of Certified Public Accountants. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the interim financial information is not prepared, in all material respects, in accordance with HKAS 34.

A stylized, handwritten signature of 'Ernst & Young' in green ink.

Ernst & Young

Certified Public Accountants

Hong Kong, 30 August 2016

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
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) Limited	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) Ltd.	PRC 26 May 1993	Registered capital HK\$40,000,000	100.00%	Information technology services

APPENDIX

Subsidiaries of the Company (continued)

Name	Place and date of incorporation/operation	Issued share capital/ registered capital	Interest held	Principal activities
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
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
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 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.

Sino Information Services Company Limited commenced members' voluntary winding up on 26 October 2015.

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.

DEFINITIONS

In this Interim 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
"ALCO"	the Asset and Liability Management Committee
"AT1"	Additional Tier 1
"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
"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
"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

DEFINITIONS

Terms	Meanings
"CFO"	Chief Financial Officer
"CIC"	China Investment Corporation
"CRO"	Chief Risk Officer
"CVA"	Credit Valuation Adjustment
"Central Huijin"	Central Huijin Investment Ltd.
"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
"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
"IT"	Information Technology
"LCO"	the Legal & Compliance and Operational Risk Management Department
"LCR"	Liquidity Coverage Ratio
"LIBOR"	London Interbank Offered Rate

DEFINITIONS

Terms	Meanings
"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
"ORSO schemes"	the Occupational Retirement Schemes under Occupational Retirement Schemes Ordinance, Chapter 426 of the Laws of Hong Kong
"OTC"	Over-the-counter
"PRC"	the People's Republic of China
"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)

DEFINITIONS

Terms	Meanings
"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



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