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

Stock Code: 2388

Annual Report 2017

A Century of Heritage
A New Era of Excellence

Due to size limit, this electronic copy of the Annual Report contains certain photographs with lower resolution. The 2017 Annual Report with higher resolution is available on the Company's website at www.bochk.com.

This version of the 2017 Annual Report will be replaced by the printed version available around mid April 2018.

Our Vision is to be

Your Premier Bank

Our Mission is to

Build customer satisfaction and provide quality and professional service

Offer rewarding career opportunities and cultivate staff commitment

Create values and deliver superior returns to shareholders

Our Core Values are

Social Responsibility We care for and contribute to our communities

Performance We measure results and reward achievement

Integrity We uphold trustworthiness and business ethics

Respect We cherish every individual

Innovation We encourage creativity

Teamwork We work together to succeed

Combining the initials of mission and core values, we have

BOC SPIRIT

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

BOC Hong Kong (Holdings) Limited ("the Company") was established by combining the businesses of the member banks in Hong Kong belonged to the Bank of China Group after their restructuring. The Company was incorporated in Hong Kong on 12 September 2001 to hold the entire equity interest of Bank of China (Hong Kong) Limited ("BOCHK"), its principal operating subsidiary. Bank of China Limited ("BOC") holds approximately 66.06% of the equity interest in the Company through BOC Hong Kong (BVI) Limited, an indirect wholly-owned subsidiary of BOC. The Company began trading on the main board of the Stock Exchange of Hong Kong on 25 July 2002 and is one of the largest listed companies and commercial banking groups in Hong Kong, with stock code "2388" and ADR OTC Symbol: "BHKLY".

BOCHK has strong market positions in all major businesses. We have the most extensive local branch network and diverse service platforms in Hong Kong, including approximately 200 branches, more than 250 automated banking centres, efficient e-channels of over 1,000 self-service machines, as well as Internet and Mobile Banking services. We offer a comprehensive range of financial, investment and wealth management services to personal, corporate and institutional customers. To implement the overseas development strategy of BOC Group, we strive to drive our regional development by expanding our business in the Southeast Asian region. Our branches and subsidiaries have been extended to Southeast Asian countries such as Malaysia, Thailand, Indonesia, Cambodia, Brunei, Vietnam and the Philippines, with the provision of professional and high-quality financial services to local customers. We will also expedite our development into a top-class, full-service and internationalised regional bank.

BOCHK is one of the three note-issuing banks and the sole clearing bank for Renminbi ("RMB") business in Hong Kong. With our strong RMB franchise, we are the first choice for customers in this business. Through the deep collaboration with our parent bank, BOC, we provide a full range of high-quality cross-border services to multinationals, cross-border customers, mainland enterprises going global, central banks and super-sovereign organisations.

As a major commercial banking group and an internationalised regional financial group with roots firmly planted in Hong Kong for 100 years, we are committed to fulfilling our corporate social responsibility to promote sustainable development and deliver greater value to our customers, shareholders, employees and the community.

Contents

Financial Highlights

	2017	2016
For the year	**HK$'m**	HK$'m
Net operating income before impairment allowances[1]	**48,769**	42,595
Operating profit[1]	**33,990**	29,482
Profit before taxation[1]	**35,262**	29,971
Profit for the year[1]	**29,214**	25,203
Profit attributable to equity holders of the Company[1]	**28,481**	24,574
Per share	**HK$**	HK$
Basic earnings per share[1]	**2.6938**	2.3243
Dividend per share	**1.398**	1.8800
At year-end	**HK$'m**	HK$'m
Total assets	**2,645,753**	2,354,740
Issued and fully paid up share capital	**52,864**	52,864
Capital and reserves attributable to equity holders of the Company	**242,739**	228,647
Financial ratios	**%**	%
Return on average total assets[2]	**1.24**	2.36
Return on average shareholders' equity[3]	**13.18**	26.17
Cost to income ratio[1]	**28.10**	29.37
Loan to deposit ratio[4]	**64.50**	64.87
Average value of liquidity coverage ratio[5]		
First quarter	**121.41**	112.92
Second quarter	**123.88**	109.70
Third quarter	**121.12**	118.69
Fourth quarter	**135.64**	107.02
Total capital ratio[6]	**20.39**	22.35

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

$$= \frac{\text{Profit attributable to equity holders of the Company}}{\text{Average of the beginning and ending balance of capital and reserves attributable to equity holders of the Company}}$$

4. Loan to deposit ratio is calculated as at year end. Loan represents gross advances to customers. Deposit represents deposits from customers including structured deposits reported as "Financial liabilities at fair value through profit or loss".
5. 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.
6. 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.
7. The Group has applied the merger accounting method in the preparation of financial statements for the combination with entities under common control in 2017. The comparative information for the year 2016 has been restated accordingly.

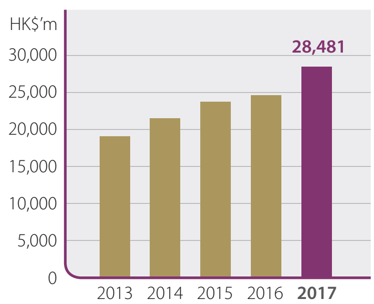
Five-Year Financial Summary

The financial information of the Group for the last five years commencing from 1 January 2013 is summarised below:

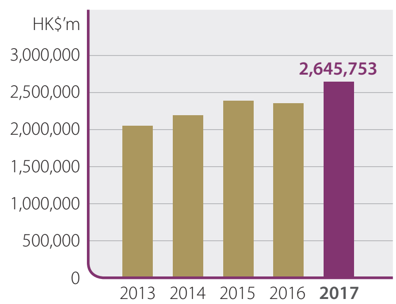
	2017	2016	2015	2014	2013
For the year	**HK$'m**	HK$'m	HK$'m	HK$'m	HK$'m
Net operating income before impairment allowances[1]	**48,769**	42,595	40,181	36,794	33,545
Operating profit[1]	**33,990**	29,482	27,815	26,261	23,571
Profit before taxation[1]	**35,262**	29,971	28,575	26,612	23,797
Profit for the year[1]	**29,214**	25,203	24,289	21,823	19,726
Profit attributable to equity holders of the Company[1]	**28,481**	24,574	23,757	21,482	19,095
Per share	**HK$**	HK$	HK$	HK$	HK$
Basic earnings per share[1]	**2.6938**	2.3243	2.2470	2.0318	1.8061
At year-end	**HK$'m**	HK$'m	HK$'m	HK$'m	HK$'m
Advances and other accounts	**1,189,609**	1,008,025	928,871	1,014,129	924,943
Total assets	**2,645,753**	2,354,740	2,382,815	2,189,367	2,046,936
Daily average balance of total assets	**2,565,562**	2,398,318	2,327,436	2,112,622	1,890,403
Deposits from customers[2]	**1,774,297**	1,523,292	1,418,058	1,483,224	1,327,980
Total liabilities	**2,398,409**	2,120,186	2,182,650	2,007,895	1,883,928
Issued and fully paid up share capital	**52,864**	52,864	52,864	52,864	52,864
Capital and reserves attributable to equity holders of the Company	**242,739**	228,647	194,750	176,714	158,813
Financial ratios	**%**	%	%	%	%
Return on average total assets	**1.24**	2.36	1.19	1.19	1.22
Cost to income ratio[1]	**28.10**	29.37	28.90	28.21	28.76
Loan to deposit ratio	**64.50**	64.87	63.37	64.79	64.63

1. The financial information is from continuing operations and the comparative information has been restated accordingly.
2. Deposits from customers include structured deposits reported as "Financial liabilities at fair value through profit or loss".
3. The Group has applied the merger accounting method in the preparation of financial statements for the combination with entities under common control in 2017. The comparative information for the year 2016 has been restated accordingly. However, the financial information prior to year 2016 had not been restated as the difference before and after restatement is insignificant.

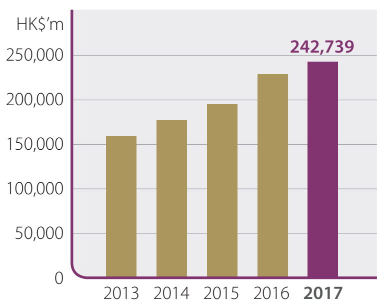
Profit attributable to equity holders of the Company



Total assets



Capital and reserves attributable to equity holders of the Company




Hong Kong
Thailand
Cambodia
Vietnam
The Philippines
Brunei
Malaysia
Indonesia

Regional Development

Message from the Chairman

2017 was an extraordinary year. The 19th National Congress of the Communist Party of China was successfully convened and attracted wide attention around the world. The Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era was affirmed, calling on the country and its people to advance along the triumphant path. The year also marked the 20th anniversary of Hong Kong's return to the motherland. During this time, Hong Kong continued its stable social and economic development. Seizing the opportune moment of the 100th anniversary of BOC's service to the city, BOCHK strictly implemented the Group's strategy as well as the decisions and plans set out by the Board. We actively supported Hong Kong economically and socially and expedited our transformation into an internationalised regional bank. We continuously increased our operating earnings while at the same time making new contributions to the long-term prosperity and stability of Hong Kong.

I am pleased to report that profit attributable to equity holders of the Company from our continuing operations hit a new high, increasing by 15.9% year-on-year to HK$28,481 million. We achieved steady growth in total assets, further improved on our financial performance indicators, and maintained a stable risk profile. The Board has recommended a final dividend of HK$0.758 per share. Together with the interim dividend and the special dividend, the full-year total dividend will be HK$1.398 per share. Excluding the special dividend, the Company's total dividend payout as a percentage of profit attributable to equity holders will be 48.4%.

Capturing the opportunities arising from national strategic initiatives, we have accelerated our regional business development and completed the disposal of our equity stake in Chiyu Bank, as well as a series of acquisitions including subsidiaries and branches in Thailand, Indonesia, Cambodia, the Philippines and Vietnam. At this point, BOCHK has already expanded its business footprint in Southeast Asia to seven countries, making substantial progress in its regional expansion strategy. We sought to deepen consolidation with those institutions with regard to business, management and corporate culture as the integration advanced. We capitalised on the important national initiatives of the Belt and Road, the "Going Global" strategy of mainland enterprises and RMB internationalisation, through which we realised collaborative synergies and promoted the growth of the lending and deposit-taking businesses of our Southeast Asia institutions. We made steady progress in the building of a regional risk management system to strengthen our risk management, compliance and internal controls. The asset quality of our Southeast Asia institutions stood at a stronger level compared with their respective domestic market averages. In order to promote the development of our corporate culture, we vigorously enhanced talent exchange and training programmes, which supported our growth by providing a stream of high-calibre employees and fostering healthy staff spirit.

Riding on the development of the Guangdong-Hong Kong-Macao Greater Bay Area, we seized the initiative to drive forward integral collaboration. To this end, BOC Group has established a committee and authorised BOCHK to spearhead its work. It will strengthen regional collaboration by harnessing the power and resources of the institutions and diverse range of business operating entities under BOC Group in the region. Its objective is to cement BOC Group's leading advantages and enhance the contributions of its institutions in Guangdong Province, Hong Kong and Macao.

Our leading position was further expanded by our proactive efforts to promote RMB internationalisation. BOCHK fully leveraged its status as the sole RMB clearing bank in Hong Kong and continuously enhanced its clearing facilities. We accomplished several revamps and upgrades of our RMB payment and settlement system. This allows us to provide liquidity support to overseas institutions that participate in RMB business in a more convenient fashion. We provided exclusive cross-border settlement services for the funds under Bond Connect following our appointment as the sole designated bank for Central Moneymarkets Unit (CMU) under the programme. We also successfully completed the issuance of RMB9 billion of Panda Bonds, the largest issuance in a single tranche thus far in that market.

We remained deeply committed to the local market and stepped up Fintech innovation, solidifying and enhancing our market position further. Our customer deposits and loans grew by 16.5% and 15.8% respectively from the end of the previous year. The total amount of new mortgage loans underwritten by us reached its highest level in recent years, while our leading position in the reverse mortgage market remained solid. We witnessed continuous customer growth in the mid- and high-end personal banking, cross-border and SME segments. I am pleased to note that BOCHK succeeded in keeping its top ranking as an arranger in the Hong Kong-Macao syndicated loan market for the 13th consecutive year, as we proactively captured business opportunities from the Belt and Road Initiative and mainland enterprises' "Going Global" strategy. Our IPO receiving bank business retained its market leadership in Hong Kong for the 7th consecutive year. We deepened our branch network transformation programme and earnestly drove Fintech innovation and the intelligent service development of our bank branches, resulting in marked enhancement in the overall productivity of our branch outlets, as well as rapid growth in the number of customers and transaction volumes through our electronic service channels. In order to provide increasingly comprehensive financial services and effectively expand our sources of income, we continued to promote the development of our key business platforms including credit card, private banking, life insurance, asset management, cash management, custody and trust services as well as securities and futures.

To celebrate the 20th anniversary of Hong Kong's return to the motherland and the 100th anniversary of BOC's service to the city, BOCHK successfully held a series of centenary celebration activities. Through these, we evoked our memories of the past while embracing a positive future, focusing on local development while promoting patriotism for the country and Hong Kong. We successfully issued Bank of China (Hong Kong) Centenary Commemorative Banknotes, which received a warm market response. We took care to improve people's livelihood and boosted our charitable giving as an initiative to promote the prosperity and stability of Hong Kong.

The favourable performance of BOCHK was widely recognised by the industry. In 2017, we earned such important awards as Strongest Bank in Asia Pacific and Hong Kong from various well-known magazines, including *The Asian Banker*, *The Banker* and *Asian Banking and Finance*. We received the Best Fintech (Emerging Solutions/Payment Innovation) Gold Award in the 2017 Hong Kong ICT Awards and, for the 10th year in a row, the Best SME's Partner Award from the Hong Kong General Chamber of Small and Medium Business. We were also granted the Best SME's Partner Gold Award 2017.

In 2017, Mr TIAN Guoli resigned as Chairman of the Company due to change of job. During his tenure, Mr TIAN has endeavoured to perform his duties and responsibilities diligently and effectively. Under his leadership, the Company earnestly delivered progress in accordance with the decisions and plans of the Central Government in the fields of economics and finance. It strongly supported the implementation of the nation's important strategic initiatives and effectively served the demands of the real economy. While persistently pursuing the strategic goal of "Serving Society, Delivering Excellence", Mr TIAN proactively promoted the internationalisation and regional transformation strategy of BOCHK and thus wrote a brand new chapter of the Company's development. On behalf of the Board, I would like to take this opportunity to express our heartfelt appreciation for the excellent contributions made by Mr TIAN. Our sincere thanks also go to Mr XU Luode, who has resigned as Non-executive Director of the Company due to change of job, for his contribution to BOCHK.

Due to reason of age, Mr YUE Yi ceased to be Vice Chairman, Executive Director and Chief Executive of the Company as of 1 January 2018, being succeeded by Mr GAO Yingxin. On behalf of the Board, I would like to express our deep gratitude and high praise for the outstanding contribution made by Mr YUE to the Company during his tenure, and offer a warm welcome to Mr GAO, who returns to BOCHK where he previously served for many years. We believe that with his broad international exposure and abundant practical experience, Mr GAO will definitely lead BOCHK to make new and even greater achievements.

Looking into 2018, we expect the global economic recovery to continue. The mainland economy will transit from a stage of rapid growth to a stage of high-quality development. Hong Kong's economy, meanwhile, will maintain its positive growth momentum. The Southeast Asia region will also sustain a steady growth trajectory. BOCHK will be guided by the Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, closely follow BOC Group's strategic goal of "Build a World-class Bank in the New Era" and forge ahead to build a top-class, full-service and internationalised regional bank. Capitalising on the important national opportunities of the Belt and Road Initiative, RMB internationalisation and the development of the Guangdong-Hong Kong-Macao Greater Bay Area, we will capture the promising business prospects brought about by the mutual connectivity of financial markets between the mainland and Hong Kong and give full play to Fintech trends in order to further enhance the competitiveness, scale and market position of our businesses. BOCHK will write a new chapter of its development for the new era, while making a greater contribution to the long-term prosperity and stability of Hong Kong and creating superior returns for our shareholders.

CHEN Siqing
Chairman
Hong Kong, 29 March 2018

Message from the Chief Executive

2017 witnessed the continued recovery of the global economy. The mainland economy remained stable with good growth momentum, while Hong Kong's economy grew at its fastest pace in recent years. The operating environment for the banking industry in Hong Kong improved, though market competition remained intense. With 2017 marking the centenary of BOC's service to Hong Kong, we earnestly adhered to the Group's strategies and carried out the Board of Directors' decisions. We strived for steady advancement in our operations and management by capturing business opportunities and introducing reforms and innovations. As a result, we effectively implemented our strategy and further enhanced the reputation of our century-old brand. In 2017, we were awarded Bank of the Year in Hong Kong for the third time by *The Banker* in the UK and the Strongest Bank in Asia Pacific and Hong Kong for the fourth consecutive year by *The Asian Banker*.

Time flies like an arrow. I assumed the position of Vice Chairman and Chief Executive of BOCHK in March 2015. Now, as I retired from my position, those last three years seem to have passed very quickly.

During the past three years, thanks to the leadership of the Board of Directors, the clear development strategies of the Group, the devoted efforts of all of our employees and the support received from various sectors in Hong Kong, the Group experienced healthy and rapid development, sustained growth in asset size, successively recorded new highs in profitability and increased the market share of its major businesses. As of the end of 2017, the total deposits and advances of the Group had increased by more than 40% compared with the end of 2014, while our asset quality outperformed the market. Our market influence continued to increase and our operating results and development strategies were highly recognised by the market. Total shareholder return and market capitalisation recorded an accumulated growth of over 70% and 50%, respectively.

During the past three years, we grasped market opportunities and underwent transformation. By pushing forward the share transfers of NCB and Chiyu and restructuring the Southeast Asian institutions of our parent bank, we steadily transformed from a local bank into an internationalised regional bank. Leveraging our competitive advantages, we deepened local market penetration, promoted Fintech innovation, and implemented our branch network transformation which increased the overall service capabilities of our branches and enhanced customer experience.

During the past three years, we made every endeavour to support the national Belt and Road Initiative and the development of the Guangdong-Hong Kong-Macao Greater Bay Area, support SMEs and the real economy in Hong Kong, and use Fintech to provide residents from remote areas and the underprivileged with greater access to convenient and high-quality banking services. Capitalising on our advantages as Hong Kong's RMB clearing bank, we reinforced and enhanced Hong Kong's status as an international financial centre and global offshore RMB business hub. Furthermore, we strictly abided by the law and took the initiative to prevent various risks. We also devoted ourselves to charitable causes and youth development. With 2017 marking the centenary of BOC's service to Hong Kong, we organised a series of celebration activities and donated a sum of HK$200 million to various charitable projects. We remained committed to contributing to Hong Kong's economic development, well-being improvement and long-term prosperity and stability.

I am fortunate enough to have my 38-year career at BOC draw to a close at the outset of BOCHK's new centenary journey, and in such a vibrant city as Hong Kong. I am also fortunate to have taken part in the implementation of "One Country, Two Systems". Looking back at my career development in BOC, where I started as a junior employee and was gradually promoted up the ranks, I have always found myself in the embrace of the Bank's care and nurture, as well as the help and support of my dear colleagues. I would like to take this opportunity to extend my sincere gratitude for the teaching and advice given by BOC's predecessors, former management and former colleagues, the dedication shown by the staff, the guidance provided by the Board of Directors, and the trust and support I have received from investors and our friends in various sectors. In my gratitude, I will always care about BOC's business development and wish it every success.

Mr GAO Yingxin, the new Chief Executive, has been serving at BOC for more than 30 years. He has recorded significant achievements in the operations and management of various banking businesses. In addition, he has worked in Hong Kong for 10 years, and so is familiar with both the city and BOCHK. He will surely be able to lead BOCHK to greater success and a new era of excellence.

At the outset of this new centenary journey, under the leadership of the parent bank, BOCHK is committed to developing into a top-class, full-service and internationalised regional bank. I believe that BOCHK will open up new horizons for its development and enjoy an even brighter future.

YUE Yi
Hong Kong, 29 March 2018

Message from the Chief Executive

In 2017, the Group earnestly carried out the Board of Director's decisions and strived for steady advancement in its operations and management. We again achieved a record high profit from continuing operations, further expanded our asset size and recorded solid performance in our financial indicators. Profit attributable to equity holders reached HK$31,070 million, and profit from continuing operations rose by 15.9% from 2016 to HK$28,481 million. As of 31 December 2017, total assets increased 12.4% from the end of 2016 to HK$2,645,753 million. Return on average shareholders' equity ("ROE") on continuing operations and return on average total assets ("ROA") on continuing operations stood at 13.49% and 1.14% respectively, both higher than in 2016. The asset-liability structure was optimised, with net interest margin (adjusted) rising 5 basis points from 2016 to 1.44%. Net interest income and net fee and commission income grew by 33.4% and 7.8% year-on-year respectively. Commission income from securities brokerage and funds distribution increased significantly by 34.3% and 34.0% year-on-year respectively.

The Group continued to seize opportunities, leverage its professional service capabilities and proactively develop its businesses, with satisfactory growth in major businesses. As of the end of 2017, deposits from customers and advances to customers grew to HK$1,774,297 million and HK$1,144,459 million respectively, up 16.5% and 15.8% from the end of 2016. The amount of new mortgage loans was the highest in recent years, and we secured the largest market share of the Reverse Mortgage Programme. Moreover, we ranked first as mandated lead arranger in the Hong Kong and Macao syndicated loan market for the 13th consecutive year, and maintained the largest market share in the initial public offering ("IPO") receiving bank business for the 7th consecutive year. We supported the implementation of Bond Connect and acted as the sole designated bank of the Hong Kong Central Moneymarkets Unit, as well as becoming Bond Connect's sole channel for the settlement of cross-border funds. In 2017, the total transaction volume processed via the RMB RTGS system exceeded a total value of RMB210 trillion, well ahead of the world's other offshore RMB markets.

The Group's strategy has been well implemented and all major initiatives were carried out effectively. We completed the share transfer of Chiyu and pushed forward the restructuring of our Southeast Asian institutions in an orderly manner. The branches and subsidiaries in Malaysia, Thailand, Indonesia, Cambodia, Vietnam and the Philippines have been integrated into the Group, while our self-established Brunei Branch runs smoothly. Regional management started to bear fruit, as the institutions that have joined us achieved laudable performance in terms of overall profitability, total assets, deposits from customers and advances to customers. Capitalising on the opportunities arising from the Belt and Road Initiative and the Guangdong-Hong Kong-Macao Greater Bay Area development, we promoted synergistic development and enhanced cross-border collaboration among Guangdong, Hong Kong and Macao. We acted as the Chairman of a committee within BOC for promoting such collaborative development and progress has been made. We introduced the Guangdong-Hong Kong-Macao Business Registration and Banking Services Connect, in cooperation with BOC Guangdong Branch and the Guangdong Province Administration for Industry & Commerce. The Group increased resources for Fintech innovation and advocated financial inclusion for the general public. Constant breakthroughs in the application of innovative technologies such as blockchain, biometric authentication and big data have been made. We actively promoted the development of smart branches and launched a new official BOCHK WeChat account and a mobile application for BOC Life. Both the number of customers using e-channels and the number of transactions recorded satisfactory growth. We continued to optimise the BOCHK iService 24-hour video banking service and introduced payment services such as WeChat Pay to further enhance customer experience.

The Group diligently performs its duties in accordance with relevant laws and regulations. Continuous efforts are made in enhancing standards and practices in respect of risk management, internal control and anti-money laundering ("AML"). We strictly adhered to regulatory requirements by introducing reforms to our banking culture, promoting a sound corporate culture in order to facilitate the implementation of our development strategy. Liquidity remained sound and asset quality was further improved. Classified or impaired advances to customers decreased by 8.9% from the end of 2016, and the classified or impaired loan ratio stood at 0.18%, well below the market average, representing a decrease of 0.05 percentage points from the end of 2016. We further enhanced the Group's AML measures so as to achieve more effective control. The Group is building a regional risk management system to enhance the risk management and internal control capabilities of its Southeast Asian institutions.

In celebration of the 20th anniversary of Hong Kong's return to the motherland and the centenary of Bank of China's service to Hong Kong, the Group gave back to society and carried on its tradition of promoting patriotism and love of Hong Kong. We successfully held a series of centenary celebration activities that attracted wide participation and support from across society, further promoting our brand reputation. We successfully issued the Bank of China (Hong Kong) Centenary Commemorative Banknote, and will use the net proceeds generated from the banknote sales for local community projects and charitable causes. Upholding the principle of caring for our community, we increased resources for community and charitable activities. In 2017, we participated in a total of 28 charitable programmes and donated a sum of HK$200 million. During the year, the Group acted as the Chairman Bank of the Hong Kong Association of Banks and the Chairman of both the Hong Kong Chinese Enterprises Association and the Chinese Banking Association of Hong Kong, seeking development opportunities for the banking industry with its peers, and to develop the economy and improve people's livelihood together with Chinese enterprises in Hong Kong.

In 2018, the global economy is expected to maintain steady growth. China and the countries and regions along the Belt and Road route will be the key drivers of economic development. Based on the lofty blueprint outlined by the 19th National Congress, the country is currently developing a modernised economy and setting the stage for opening up on all fronts. This will generate impetus and create growth opportunities for the world as well as promising opportunities for Hong Kong. The new HKSAR Government has focused on improving the economy and people's livelihood, and playing an active role in promoting the Belt and Road Initiative and the development of the Guangdong-Hong Kong-Macao Greater Bay Area. Its continued efforts in enhancing Hong Kong's traditional advantages and identifying new economic growth drivers will bring enormous business opportunities to the Hong Kong banking industry.

We aim to "Build a Top-class, Full-service and Internationalised Regional Bank". We will uphold our beliefs, strive to tackle problems, drive our growth through technology and innovation, ensure compliance with laws and regulations, embrace our corporate culture and adopt a people-oriented and steadfast management approach in the design and implementation of our diverse business strategies and measures. These strategies include stepping up the restructuring of our Southeast Asian institutions to promote regional development, speeding up technological innovation and product development to promote digital development, and accelerating the building of diversified platforms and the integration of the commercial banking and investment banking businesses to promote development on all fronts. In addition, we will deepen market penetration in Hong Kong, promote financial inclusion, focus on Guangdong-Hong Kong-Macao interconnectivity for Bank of China Group and step up cross-border business development. We will ensure sustainable and steady development by strengthening risk management as well as compliance and internal control. More efforts will be made to improve management fundamentals and staff team building, so as to enhance our governance capability. We will proactively fulfil our social responsibility and promote our brand image. With the goal of making a greater contribution to enhancing Hong Kong's status as an international financial centre and promoting its long-term stability and prosperity, the Group will continue to provide practical support to the HKSAR Government in governing and executing its policies in accordance with the law.

Last but not least, I would like to take this opportunity to report changes in the Group's senior management. Mr YUE Yi ceased to be Vice Chairman and Chief Executive of the Group from 1 January 2018 due to reason of age. In the past three years, under the leadership of Mr YUE, together with guidance from the Board of Directors and support from various sectors, the Management and staff delivered good operating results and laid a solid foundation for future development. Moreover, due to reassignment, Mr LIN Jingzhen resigned as Deputy Chief Executive (Corporate Banking) in February this year. On behalf of the staff, I would like to extend our gratitude for Mr YUE's and Mr LIN's contributions to the Group's business development.

I am honoured to be appointed as Vice Chairman and Chief Executive at the outset of the Group's new centenary journey. I would like to take this opportunity to thank our customers, shareholders and various sectors for their long-standing support, the Board of Directors for its wise guidance and the staff for their diligence and endeavour. This new era calls for new achievements. We believe that, by virtue of the Group's century-old foundations, the great strength of our brand and the concerted efforts made by our staff, we will gradually develop into a top-class, full-service and internationalised regional bank, and continue to deliver greater value for our stakeholders.

GAO Yingxin
Vice Chairman & Chief Executive
Hong Kong, 29 March 2018

A Century of Services, Always with You

2017 marked the 20th anniversary of Hong Kong's return to the motherland and the centenary of BOC's service to Hong Kong. On 24 September 1917, BOC set up a sub-branch in Hong Kong, which was also its first institution outside the Chinese mainland. Through a century of continuous effort, BOCHK has transformed from a small sub-branch with fewer than 10 staff members into a leading commercial banking group. It is also one of Hong Kong's three note-issuing banks, one of the city's largest listed companies and the sole clearing bank for RMB business in Hong Kong. Nowadays, BOCHK not only plays a significant role in Hong Kong's economic development, but also makes important contributions to the prosperity and stability of Hong Kong society. To mark this special occasion, BOCHK organised a series of events to celebrate Hong Kong's return to the motherland and our centenary with Hong Kong citizens. At the same time, we actively fulfilled our corporate social responsibility by inviting underprivileged communities and grassroots families to join in with some of the events and share the joy with us.

In June, BOCHK organised the "A Century of Services, Always with You - Exhibition of Bank of China's Centenary of Service to Hong Kong". At the same time, we joined hands with Hong Kong Chinese Enterprises Association to hold the "Exhibition of Chinese Enterprises' Services to Hong Kong". More than 50 major Chinese enterprises participated in this exhibition. Through pictures and text, the exhibition showcased the continuous effort and contributions made by Chinese enterprises in terms of promoting Hong Kong's economic development, securing people's livelihood and supporting philanthropy.

"A Century of Services, Always with You - Exhibition of Bank of China's Centenary of Service to Hong Kong" reviewed the century-long history of BOCHK's service to the city through a wide variety of pictures and text, exhibits and videos. It also highlighted the bright prospects of BOCHK, which has continuously deepened its local market penetration, driven forward regional development and created greater value for stakeholders.

A Glorious Century

In July, we held a grand event to celebrate the centenary of BOC's service to Hong Kong at the Hong Kong Convention and Exhibition Centre, which was attended by more than 3,000 guests. These included Mr Tung Chee-hwa, Vice Chairman of the National Committee of the Chinese People's Political Consultative Conference; Mr Leung Chun-ying, Vice Chairman of the National Committee of the Chinese People's Political Consultative Conference; Mrs Carrie Lam Cheng Yuet-ngor, Chief Executive of HKSAR, heads of the central authorities based in Hong Kong, renowned representatives from different local sectors, senior management of our parent bank, BOCHK's honorary retirees and staff representatives.

The grand celebration reviewed our centenary of progress and glorious achievements, while unveiling a new chapter of our development. The wonderful performance of our staff during this special occasion demonstrated the quality of employee and corporate culture of BOCHK, further strengthening the theme of "A Century of Services, Always with You".


中国银行(香港)
BANK OF CHINA
百年中銀 與您同行
A CENTURY OF SERVICES, ALWAYS WITH YOU
2016年度中銀之星

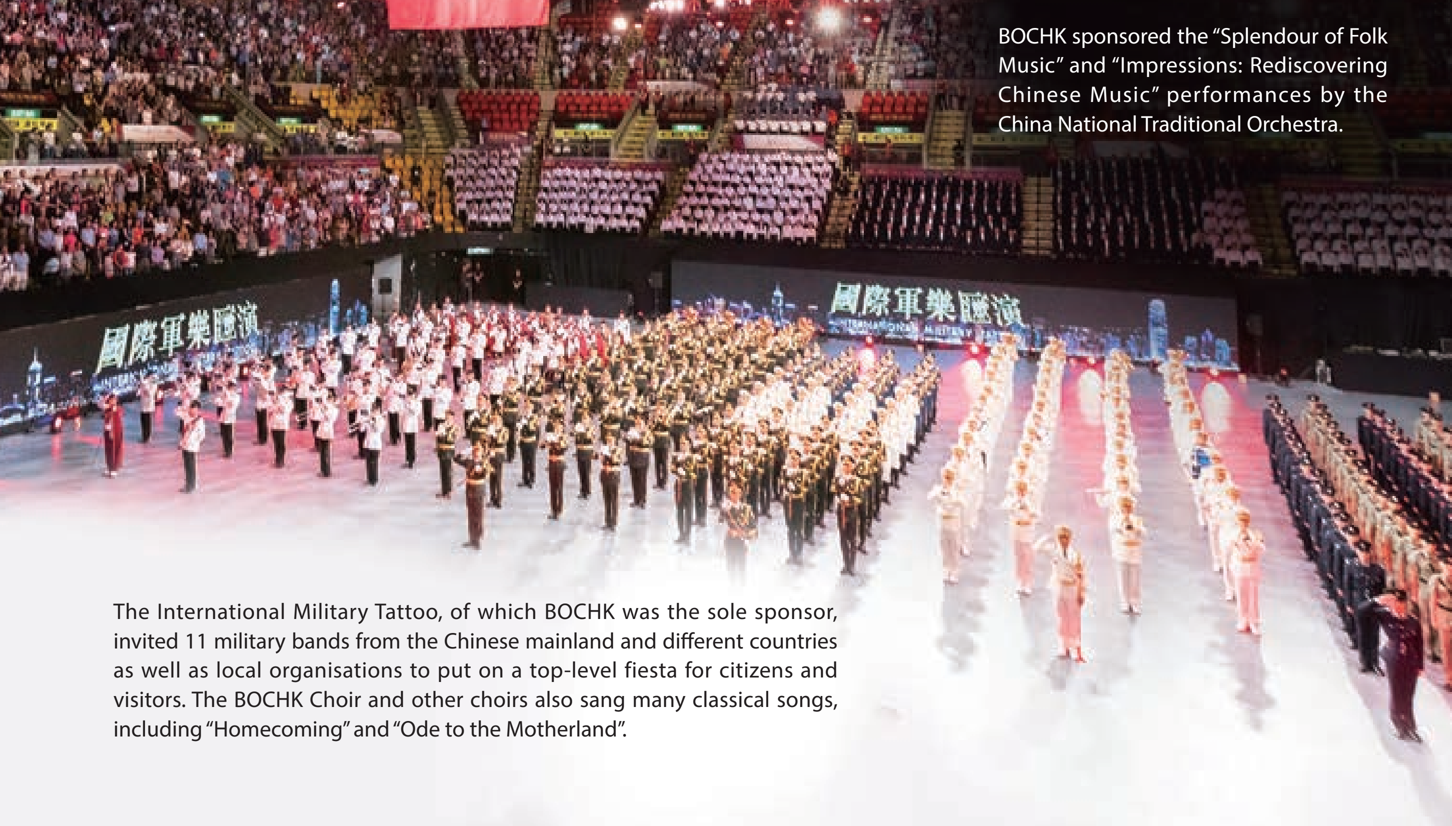
In 2017, BOCHK issued the “Bank of China (Hong Kong) Centenary Commemorative Banknote” in celebration of the 100th anniversary of BOC’s presence in Hong Kong. The front side of the Banknote features a famous local landmark, Bank of China Tower, superimposed on an image of the Bank of China Building, with the old Bank of China Hong Kong Branch and Bank of China Head Office in Beijing pictured on the side. These buildings symbolise the glorious history of BOC’s centenary of service to Hong Kong. The reverse side of the Commemorative Banknote features an image of a newspaper advertisement for the grand opening of Bank of China Hong Kong Branch, which was upgraded from sub-branch status in 1919, and the logos of the 12 member banks of Bank of China Group in Hong Kong in 1983. There is also an image of the first HKD banknote issued by BOC in 1994, superimposed on the centre of the Commemorative Banknote. This special design tells the long and illustrious history of BOC’s Hong Kong presence and its service to the city over the past century.

In special honour of the centenary of BOCHK, net proceeds generated from the sale of the Commemorative Banknote, after deducting all relevant costs, will be used for local community projects and charitable causes.

Joint Celebration

BOCHK was the title sponsor of the "BOCHK 2017 Hong Kong New Year Countdown", which attracted over 330,000 citizens and visitors to enjoy a pyro-musical show together at Victoria Harbour. This event also unveiled the start of the celebrations of our centenary of service to Hong Kong.

BOCHK sponsored the "Splendour of Folk Music" and "Impressions: Rediscovering Chinese Music" performances by the China National Traditional Orchestra.



The International Military Tattoo, of which BOCHK was the sole sponsor, invited 11 military bands from the Chinese mainland and different countries as well as local organisations to put on a top-level fiesta for citizens and visitors. The BOCHK Choir and other choirs also sang many classical songs, including "Homecoming" and "Ode to the Motherland".

BOCHK joined hands with Hong Kong Chinese Enterprises Association to hold a forum on "China's Outward Investment Trends and Hong Kong's Role", to celebrate the 20th anniversary of Hong Kong's return to the motherland. The forum aimed to facilitate the exchanges on strengthening Hong Kong's position as a "super-connector" and capitalising on national strategies such as the Belt and Road Initiative. Over 2,000 guests from the mainland, Hong Kong, Southeast Asia and other countries and regions attended the forum.

In celebration of BOC's centenary of service to Hong Kong, a book titled *The Era of RMB SDR and the Offshore RMB Centre in Hong Kong* was published by BOCHK in June. The book analyses the development and prospects of offshore RMB business. BOCHK has been Hong Kong's sole RMB clearing bank since 2003, proactively developed various RMB businesses and made contributions to RMB internationalisation and promoting the development of Hong Kong as an offshore RMB centre.

A Century-long Branding

BOCHK produced a TV commercial, "A Century of Services, Always with You", which tells the history of BOCHK's development into an internationalised regional bank over the past century. It also reflects on the precious moments that BOCHK has shared together with the country and Hong Kong in both hard times and prosperity.

BOCHK joined hands with various organisations to hold the "New Era - Chinese Paintings 2017 Hong Kong Exhibition". The exhibition, which featured more than 100 ink paintings by contemporary artists active in the mainland, Hong Kong and Taiwan, aimed to pass on the inheritance and promote the excellence of Chinese traditional culture.

Caring for Employees

BOCHK held a "Staff and Family Members Carnival" at Hong Kong Disneyland Resort to celebrate its centenary of service to Hong Kong. The Carnival attracted more than 28,000 people, including BOC staff and their family members, BOC retirees, families and seniors from grassroots communities. This demonstrated BOCHK's fulfilment of corporate social responsibility for employee care and its dedication to charitable activities.

Innovation

Management Discussion and Analysis

As a result of the disposal of Chiyu, the financial results of Chiyu are reported as profit from discontinued operations in the Group's consolidated income statement, with comparative information restated. Meanwhile, the assets and liabilities of Chiyu are presented separately as assets held for sale and liabilities associated with assets held for sale in the consolidated balance sheet as at 31 December 2016. Certain comparative figures in this Management Discussion and Analysis have been restated to conform to the current year's presentation.

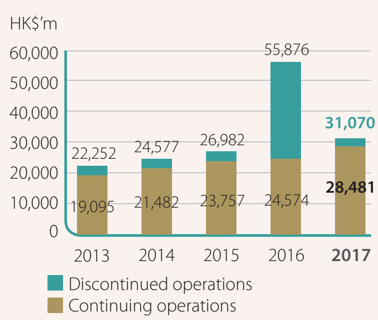
Following the completion of the share acquisition of Bank of China (Malaysia) Berhad ("BOC Malaysia") and Bank of China (Thai) Public Company Limited ("BOC Thailand") on 17 October 2016 and 9 January 2017 respectively, and the completion of the acquisition of the Indonesia Business and Cambodia Business of BOC on 10 July 2017 and 6 November 2017 respectively, the Group has applied the merger accounting method in the preparation of financial statements for the combination of entities under common control. The comparative information for 2016 has been restated accordingly.

The above transactions are collectively referred as the "disposal and acquisitions" in this Management Discussion and Analysis.

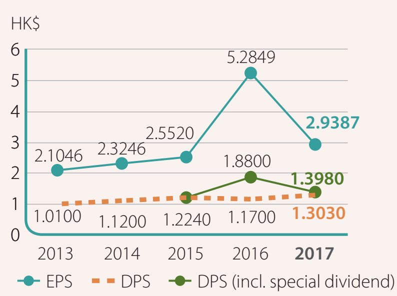
Financial Performance and Conditions at a Glance

The following table is a summary of the Group's key financial results for 2017 in comparison with the previous four years. The average value of liquidity coverage ratio is reported on a quarterly basis.

Profit Attributable to Equity Holders[1]



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

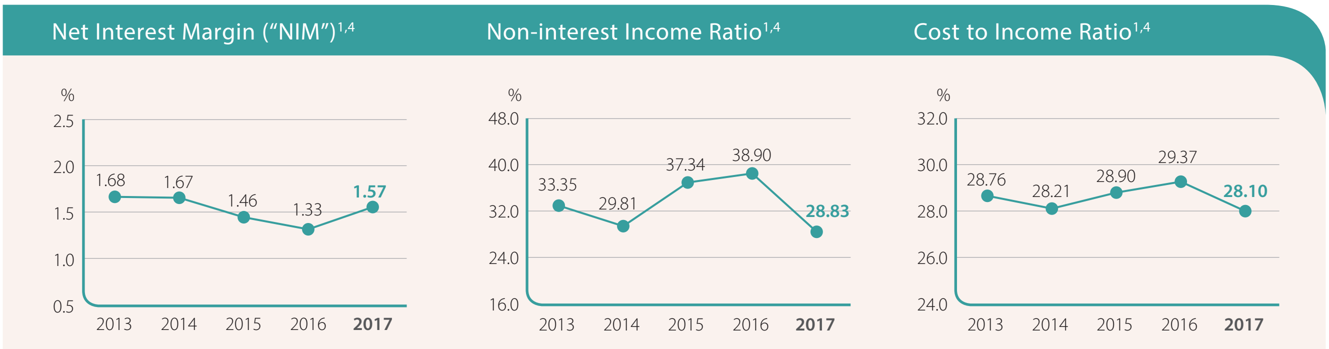


Profit attributable to equity holders

- Profit attributable to equity holders amounted to HK$31,070 million. Profit attributable to equity holders from continuing operations increased by 15.9% year-on-year to HK$28,481 million. Profit attributable to equity holders from discontinued operations was HK$2,589 million, accounted for mainly by the gain on the disposal of Chiyu. ROE was 13.18%. ROE on continuing operations[2] was 13.49%, up 1.30 percentage points year-on-year. ROA was 1.24%. ROA on continuing operations[3] was 1.14%, up 0.01 percentage point year-on-year.

Solid returns to shareholders

- EPS was HK$2.9387. Dividend per share was HK$1.303 and the special dividend was HK$0.095 per share.



Improvement in net interest margin ("NIM"), along with expanded asset size

- NIM was 1.57%, up 24 basis points year-on-year. The Group continued to be proactive in managing its assets and liabilities, recording both an increased average balance and an enhanced average yield of advances to customers and debt securities investments. The Group also captured opportunities from the interbank market to improve the average yield of balances and placements with banks. If the funding income or cost of foreign currency swap contracts[5] were included, NIM would have been 1.44%, up 5 basis points.

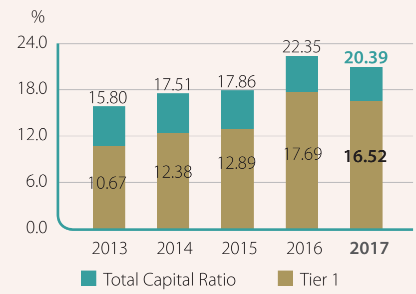
Fall in non-interest income ratio

- Non-interest income ratio was 28.83%, down 10.07 percentage points year-on-year. If the funding income or cost of foreign currency swap contracts were excluded, non-interest income ratio would have been 34.45%, down 1.99 percentage points.

Cautious cost control with high operational efficiency

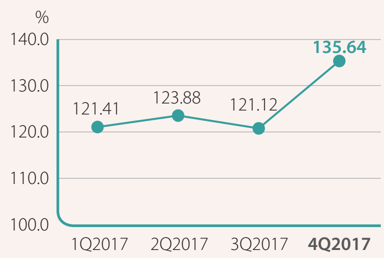
- The Group's cost to income ratio was 28.10% in 2017, down 1.27 percentage points year-on-year, putting cost efficiency at a solid level relative to the industry peers.

Capital Ratio

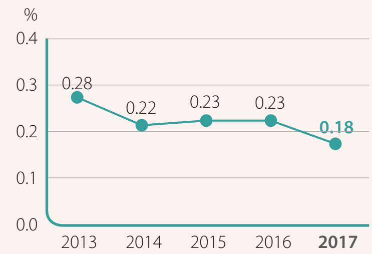


as at 31 December

Average Value of Liquidity Coverage Ratio



Classified or Impaired Loan Ratio[1,4,6]



as at 31 December

Strong capital position to support business growth

- Total capital ratio was 20.39%. Tier 1 capital ratio was 16.52%, down 1.17 percentage points from that at the end of 2016.

Sound liquidity position

- The average value of liquidity coverage ratio was above the regulatory requirement throughout the four quarters of 2017.

Stable asset quality with classified or impaired loan ratio well below market average

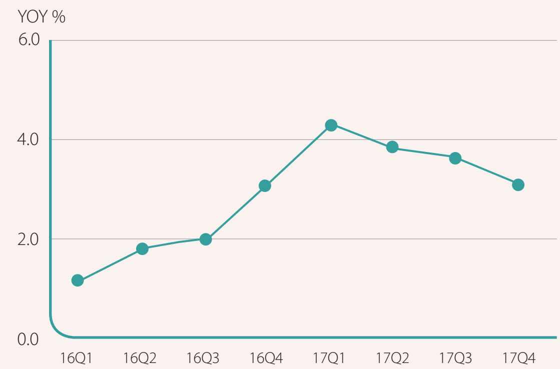
- The classified or impaired loan ratio was 0.18%, well below the market average.

1. The Group has applied the merger accounting method in the preparation of financial statements for the combination of entities under common control in 2017. The comparative information for 2016 has been restated accordingly. However, financial information prior to 2016 has not been restated as the difference before and after restatement is insignificant.
2. ROE on continuing operations is calculated by dividing profit attributable to equity holders from continuing operations by the average of the beginning and ending balance of capital and reserves attributable to equity holders, excluding the impact of profit attributable to equity holders from discontinued operations and special dividend paid.
3. ROA on continuing operations is calculated by dividing profit for the year from continuing operations by the daily average balance of total assets excluding those of discontinued operations.
4. The financial information is from continuing operations and excludes assets held for sale and liabilities associated with assets held for sale.
5. Foreign exchange swap contracts are normally used for the Group's liquidity management and funding activities. In foreign exchange swap contracts, the Group exchanges one currency (original currency) for another (swapped currency) at the spot exchange rate (spot transaction) and commits to reverse the spot transaction by exchanging the same currency pair at a future maturity date at a predetermined rate (forward transaction). In this way, surplus funds in the original currency are swapped into another currency for liquidity and funding purposes with minimal foreign exchange risk. The exchange difference (funding income or cost) 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.
6. Classified or impaired loans represent advances that are either classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

Economic Background and Operating Environment

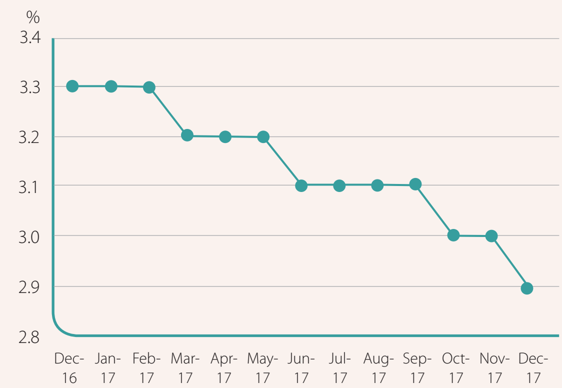
In 2017, the global economy continued to recover. The US economy maintained stable growth with improving financial and labour markets and stable property market performance, despite the combination of the Federal Reserve's balance sheet normalisation programme and three interest rate hikes. The Eurozone economy continued to improve amid the European Central Bank's highly accommodative monetary policy and a continuous improvement in global economic conditions. The ASEAN region's solid economic growth remained on track, supported by accelerated global economic growth, stable commodity prices and increased infrastructure investments by some ASEAN countries. Growth in the mainland of China continued to stabilise and China's economic structure further improved with the high-tech and equipment manufacturing sector, and the service sector both gathering pace and emerging as significant new economic growth drivers.

Hong Kong Real GDP Growth Rate



Source: HKSAR Census and Statistics Department

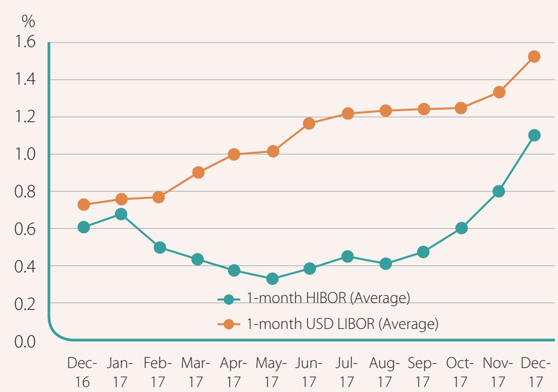
Hong Kong Unemployment Rate



Source: HKSAR Census and Statistics Department

In Hong Kong, real GDP growth in 2017 was 3.8% over the previous year, the highest since 2011. The synchronous recovery of the world's major economies helped to boost Hong Kong's trade performance, while tourism and retail sales also gradually improved. Stock and property markets remained buoyant amid prevailing low interest rates, leading to higher demand for financial and related services. These factors, coupled with positive consumer confidence driven by a consistently low unemployment rate, supported the overall economic performance of Hong Kong.

HIBOR and USD LIBOR



Source: Bloomberg

The liquidity of the Hong Kong banking sector remained ample in 2017, although market interest rates rose in line with US interest rate hikes. The average 1-month HIBOR and 1-month LIBOR rose from 0.30% and 0.50% respectively in 2016 to 0.55% and 1.11% respectively in 2017.

Hong Kong's stock market staged a strong rally, underpinned by improved macroeconomic conditions, strong corporate earnings and capital inflows from the mainland into Hong Kong's stock market. The Hang Seng Index surged by 36.0% over the year, recording its highest growth since 2009 and outpacing major international markets. Transaction volumes picked up significantly, with those on the Shenzhen-Hong Kong Stock Connect and Shanghai-Hong Kong Stock Connect registering substantial increases.

Management Discussion and Analysis

During the year, local private residential property prices hit new highs and the number of residential property transactions increased from that of 2016. The Government continued to implement demand management measures and announced a new round of measures for residential mortgage loans in order to strengthen banks' risk management on mortgage business.

The offshore RMB business in Hong Kong continued to grow steadily in 2017. A number of initiatives were introduced to promote capital account convertibility and the internationalisation of the RMB. These included expanding the free trade zones ("FTZs") in seven provinces of the mainland, including Henan, Hubei, Sichuan, Zhejiang, Liaoning, Shaanxi and Chongqing, and allowing offshore institutional investors to engage with eligible onshore financial institutions to undertake derivative business in RMB against foreign currencies. Also, Bond Connect was successfully launched and become an important channel for offshore institutions to invest in bonds in the mainland market, thus achieving breakthroughs in the establishment of mutual capital market access between Hong Kong and the mainland. As a result of these initiatives, development opportunities opened up for the financial industry in Hong Kong, further promoting the healthy development of the offshore RMB market.

In 2017, banks in Hong Kong operated in a highly challenging environment. These challenges included changes in global monetary policies, heightened geopolitical risks, rising trade protectionism and intensified market competition. Nevertheless, new growth drivers for banks in Hong Kong included the enormous demand for financial services arising from steady progress in the implementation of the Belt and Road Initiative, the launch of a development framework for the Guangdong-Hong Kong-Macao Greater Bay Area and the further implementation of mutual capital market access between Hong Kong and the mainland.

Consolidated Financial Review

The comparative information for 2016 has been restated as a result of the Group's disposal and acquisitions.

Financial Highlights

HK$'m, except percentages	2017	(Restated) 2016	Change (%)
FROM CONTINUING OPERATIONS			
Net operating income before impairment allowances	**48,769**	42,595	14.5
Operating expenses	**(13,703)**	(12,512)	9.5
Operating profit before impairment allowances	**35,066**	30,083	16.6
Operating profit after impairment allowances	**33,990**	29,482	15.3
Profit before taxation	**35,262**	29,971	17.7
Profit attributable to equity holders of the Company	**31,070**	55,876	(44.4)
– from continuing operations	**28,481**	24,574	15.9
– from discontinued operations	**2,589**	31,302	(91.7)

In 2017, the Group seized market opportunities for development, leveraged its competitive advantages and responded positively to a complex and uncertain operating environment. As a result, the Group's core businesses realised satisfactory growth. Key business areas achieved good results, with key financial indicators remaining at solid levels. During the year, the Group proactively pushed forward business restructuring in Southeast Asia and further optimised its regional operations. Regional synergies began to emerge as the Group made notable progress towards its building into an internationalised regional bank. The Group continued to develop the local market in Hong Kong, enhanced market penetration among local customers and continued to refine its business structure to become more customer-centric. It deepened collaboration with BOC to expand its cross-border business development. The development of its diversified business platforms gathered pace and it achieved solid growth in income from its diversified business operations. At the same time, it strengthened innovation in financial technology ("Fintech") so as to upgrade the smart service levels of its products and services as well as its overall service capabilities. It also reinforced its strong RMB clearing business franchise by broadening its scope of services and enhancing its trading capabilities so as to consolidate its leading market position. To ensure its sustainable and healthy development, the Group further strengthened its risk management, internal controls and compliance management.

In 2017, profit attributable to equity holders of the Group amounted to HK$31,070 million. Profit attributable to equity holders from continuing operations amounted to HK$28,481 million, an increase of HK$3,907 million, or 15.9%, year-on-year. Net operating income before impairment allowances was HK$48,769 million, an increase of HK$6,174 million, or 14.5%, year-on-year. Net interest income increased, due to the growth of the Group's average interest-earning assets and a rise in net interest margin. The Group captured opportunities arising from improved investor sentiment in the market and focused on providing diversified investment services. As a result, net fee and commission income rose year-on-year. During the year, the funding cost of foreign currency swap contracts resulted in a decrease in the net trading gain of the banking business, which partially offset the above-mentioned income growth. Operating expenses rose to support the Group's long-term business expansion. Meanwhile, the net charge of loan impairment allowances increased year-on-year. A higher net gain from fair-value adjustments on investment properties was recorded. Profit attributable to equity holders from discontinued operations amounted to HK$2,589 million, which included a gain on the disposal of Chiyu of HK$2,504 million. This represented a drop of HK$28,713 million from the previous year's figure, which had included a gain on the disposal of NCB of HK$29,956 million.

Second Half Performance

As compared with the first half of 2017, the Group's net operating income before impairment allowances increased by HK$1,415 million, or 6.0% half-on-half. This was mainly attributable to an increase in net interest income arising from the continuous expansion in the Group's average interest-earning assets. The banking business recorded an increase in net trading gain, arising from a half-on-half decrease in the funding cost of foreign currency swap contracts. Operating expenses increased by HK$1,343 million, or 21.7% from the first half of the year, while the net charge of loan impairment allowances rose by HK$373 million, or 107.5%. Meanwhile, the net gain from fair-value adjustments on investment properties decreased notably by HK$577 million, or 65.1%. As a result, profit attributable to equity holders from continuing operations decreased by HK$1,185 million or 8.0%, 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 as a result of the Group's disposal and acquisitions.

Net Interest Income and Net Interest Margin

HK$'m, except percentages	2017	(Restated) 2016	Change (%)
Interest income	**48,951**	36,776	33.1
Interest expense	**(14,243)**	(10,752)	32.5
Net interest income	**34,708**	26,024	33.4
Average interest-earning assets	**2,216,623**	1,946,172	13.9
Net interest spread	**1.44%**	1.23%	
Net interest margin*	**1.57%**	1.33%	

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

The Group's net interest income increased by HK$8,684 million, or 33.4%, year-on-year. The increase was driven by growth in average interest-earning assets and an increase in net interest margin.

Average interest-earning assets expanded by HK$270,451 million, or 13.9%. The increase in deposits from customers led to an increase in advances to customers, balances and placements with banks as well as debt securities investments.

Net interest margin was 1.57%, up 24 basis points. The Group continued to proactively manage its assets and liabilities, enhancing the average yield of advances to customers and debt securities investments. In addition, the Group captured opportunities from the interbank market to improve the average yield of balances and placements with banks, which also resulted in a rise in net interest margin. If the funding income or cost of foreign currency swap contracts* were included, net interest margin would have been 1.44%, up 5 basis points.

* Foreign exchange swap contracts are normally used for the Group's liquidity management and funding activities. In foreign exchange swap contracts, the Group exchanges one currency (original currency) for another (swapped currency) at the spot exchange rate (spot transaction) and commits to reverse the spot transaction by exchanging the same currency pair at a future maturity date at a predetermined rate (forward transaction). In this way, surplus funds in the original currency are swapped into another currency for liquidity and funding purposes with minimal foreign exchange risk. The exchange difference (funding income or cost) 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.

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

	2017		(Restated) 2016	
ASSETS	Average balance HK$'m	Average yield %	Average balance HK$'m	Average yield %
Balances and placements with banks and other financial institutions	**438,113**	**2.18**	332,802	1.36
Debt securities investments	**670,159**	**1.98**	634,504	1.62
Advances to customers	**1,091,645**	**2.38**	956,915	2.26
Other interest-earning assets	**16,706**	**1.29**	21,951	0.89
Total interest-earning assets	**2,216,623**	**2.21**	1,946,172	1.88
Non interest-earning assets[1]	**348,939**	**–**	452,146	–
Total assets	**2,565,562**	**1.91**	2,398,318	1.53

LIABILITIES	Average balance HK$'m	Average rate %	Average balance HK$'m	Average rate %
Deposits and balances from banks and other financial institutions	**226,074**	**0.92**	233,899	0.79
Current, savings and time deposits	**1,558,918**	**0.68**	1,348,081	0.57
Subordinated liabilities	**19,312**	**4.82**	19,513	3.04
Other interest-bearing liabilities	**47,705**	**1.41**	36,012	1.51
Total interest-bearing liabilities	**1,852,009**	**0.77**	1,637,505	0.65
Shareholders' funds[2] and other non interest-bearing deposits and liabilities[1]	**713,553**	**–**	760,813	–
Total liabilities	**2,565,562**	**0.56**	2,398,318	0.45

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

Second Half Performance

In the second half of the year, net interest income recorded a half-on-half increase of HK$466 million, or 2.7%, to reach HK$17,587 million. This was due to growth in average interest-earning assets, and was partially offset by a decrease in net interest margin. Average interest-earning assets grew by HK$192,405 million, or 9.1%, which was supported by an increase in deposits from customers. Net interest margin was 1.51%, down 12 basis points, as loan pricing and deposit costs came under pressure from intensified market competition. In addition, a drop in RMB market interest rates lowered the average yield of RMB assets. Nevertheless, an increase in advances to customers and a rise in the average yield of debt securities investments partially offset this negative impact. If the funding cost of foreign currency swap contracts were included, net interest margin would have been 1.43%, down 3 basis points.

Net Fee and Commission Income

HK$'m, except percentages	2017	(Restated) 2016	Change (%)
Loan commissions	**3,559**	3,522	1.1
Credit card business	**3,202**	3,703	(13.5)
Securities brokerage	**2,624**	1,954	34.3
Insurance	**1,326**	1,630	(18.7)
Funds distribution	**985**	735	34.0
Bills commissions	**802**	724	10.8
Payment services	**629**	631	(0.3)
Trust and custody services	**555**	470	18.1
Currency exchange	**433**	336	28.9
Safe deposit box	**291**	277	5.1
Others	**999**	950	5.2
Fee and commission income	**15,405**	14,932	3.2
Fee and commission expense	**(3,889)**	(4,248)	(8.5)
Net fee and commission income	**11,516**	10,684	7.8

In 2017, net fee and commission income amounted to HK$11,516 million in 2017, up HK$832 million or 7.8% year-on-year. The Group captured opportunities arising from improved investor sentiment in the market and focused on delivering promotional campaigns to mid- to high-end and cross-border customers. As a result, commission income from securities brokerage and funds distribution grew 34.3% and 34.0% year-on-year, respectively. The Group also leveraged its diversified business platforms to record healthy growth in a number of areas. Income from currency exchange rose by 28.9% year-on-year, as the Group captured market opportunities to achieve satisfactory growth of its banknote business in Asia. The Group was effective in expanding its trust and custody services, resulting in a year-on-year increase of 18.1% in related income. Bills and loan commissions also recorded solid growth. Income from its credit card business dropped 13.5% year-on-year, as the 10.5% growth in commission income from credit card business in Hong Kong was more than offset by the drop in fee income from merchant acquiring business in Hong Kong, which was affected by cardholder spending from mainland visitors to Hong Kong. In addition, commission income from insurance and payment services also dropped. The decrease in fee and commission expense was mainly due to lower credit card related expenses.

Second Half Performance

Net fee and commission income in the second half of the year increased by HK$36 million, or 0.6%, compared to the previous half-year. Commission income from securities brokerage and funds distribution increased significantly. Commission income from credit cards, insurance, trust and custody services, currency exchange and payment services also increased. However, a drop in loan commissions largely offset the aforesaid increases. Fee and commission expense rose from the first half of the year, mainly attributable to higher credit card and securities brokerage related expenses.

Net Trading Gain

HK$'m, except percentages	2017	(Restated) 2016	Change (%)
Foreign exchange and foreign exchange products	**157**	3,719	(95.8)
Interest rate instruments and items under fair value hedge	**739**	867	(14.8)
Commodities	**205**	32	540.6
Equity and credit derivative instruments	**225**	88	155.7
Net trading gain	**1,326**	4,706	(71.8)

Net trading gain decreased by HK$3,380 million, or 71.8% year-on-year, to HK$1,326 million. If the funding income or cost of foreign currency swap contracts were excluded, net trading gain would have risen by 11.2%, primarily due to higher gains from foreign exchange and bullion transactions and an increase in income from equity-linked products. These gains were partially offset by lower mark-to-market gains of certain debt securities investments and interest rate instruments, caused by interest rate movements.

Second Half Performance

Compared with the first half of 2017, net trading gain decreased by HK$18 million or 2.7%. If the funding cost of foreign currency swap contracts were excluded, net trading gain would have decreased by 34.3%, primarily due to the decrease in mark-to-market gain on certain foreign exchange products.

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

HK$'m, except percentages	2017	(Restated) 2016	Change (%)
Net gain on financial instruments designated at fair value through profit or loss	**2,181**	101	2059.4

The Group recorded a net gain of HK$2,181 million on financial instruments designated at FVTPL in 2017, compared with a net gain of HK$101 million in 2016. The change was mainly attributable to an increased gain arising from the equity securities and bond fund investments of BOC Life, as well as an increase in the mark-to-market gain of its debt securities investments, caused by market interest rate movements. Changes in BOC Life's policy reserves, as reflected in changes in net insurance benefits and claims and movement in liabilities, were also attributable to the movement of market interest rates.

Second Half Performance

A net gain of HK$993 million was recorded in the second half of the year, down HK$195 million or 16.4% compared with the first half of the year. The change was mainly attributable to a half-on-half decrease in the mark-to-market gain of BOC Life's debt securities investments. This decrease was partially offset by an increased gain from its equity securities investments.

Operating Expenses

HK$'m, except percentages	2017	(Restated) 2016	Change (%)
Staff costs	**7,813**	6,939	12.6
Premises and equipment expenses (excluding depreciation)	**1,704**	1,591	7.1
Depreciation	**1,949**	1,805	8.0
Other operating expenses	**2,237**	2,177	2.8
Total operating expenses	**13,703**	12,512	9.5

	At 31 December 2017	(Restated) At 31 December 2016	Change (%)
Staff headcount measured in full-time equivalents*	**13,049**	12,738	2.4

* The comparative information of staff headcounts measured in full-time equivalents at 31 December 2016 has been restated to enable analysis on a comparable basis.

Total operating expenses increased by HK$1,191 million, or 9.5% year-on-year, as a result of the Group's ongoing investment in the service capabilities, business systems and platforms needed to support long-term business growth. The Group remained focused on disciplined cost control, its cost to income ratio remained low at 28.10%, with cost efficiency at a solid level relative to the wider industry.

Staff costs increased by 12.6% year-on-year, mainly due to annual salary increment, increased headcount, and an increase in performance-related remuneration.

Premises and equipment expenses were up 7.1%, reflecting higher expenses related to the enhancement of business systems and platforms, and an increase in rental costs.

Depreciation rose by 8.0%, largely due to a larger depreciation charge on information technology ("IT") infrastructure. The depreciation charge on the fixtures and fittings of rented premises also increased.

Other operating expenses increased by 2.8%, mainly due to higher business promotional and advertising expenses.

Second Half Performance

Compared with the first half of 2017, total operating expenses increased by HK$1,343 million, or 21.7%. The increase was due to higher staff costs and business promotional and advertising expenses.

Net Charge of Loan Impairment Allowances

HK$'m, except percentages	2017	(Restated) 2016	Change (%)
Net charge of allowances before recoveries			
– individually assessed	**(2)**	(84)	(97.6)
– collectively assessed	**(1,196)**	(667)	79.3
Recoveries	**131**	137	(4.4)
Net charge of loan impairment allowances	**(1,067)**	(614)	73.8

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

	At 31 December 2017	(Restated) At 31 December 2016
Loan impairment allowances		
– individually assessed	**0.04%**	0.07%
– collectively assessed	**0.32%**	0.28%
Total loan impairment allowances	**0.36%**	0.35%

The net charge of loan impairment allowances in 2017 was HK$1,067 million, an increase of HK$453 million, or 73.8%, from 2016. Net charge of collectively assessed impairment allowances increased by HK$529 million, or 79.3%, attributable to growth in advances to customers and the Group has taken a prudent and stable approach to increase impairment allowances for a certain loan portfolio.

As at 31 December 2017, total loan impairment allowances as a percentage of gross advances to customers was 0.36%, up slightly from the end of 2016.

Second Half Performance

Compared with the first half of 2017, the net charge of loan impairment allowances increased by HK$373 million, or 107.5%. The Group recorded a net charge of individually assessed impairment allowances in the second half of 2017. Meanwhile, there was a net reversal in the first half, mainly due to loan repayments by certain corporate customers. Net charge of collectively assessed impairment allowances increased, as the Group has taken a prudent and stable approach to increase impairment allowances for a certain loan portfolio. This increase was partly offset by the lower net charge owing to lower loan growth in the second half of the year.

Balance Sheet Analysis

The comparative figures as of 31 December 2016 have been restated to conform to the current year's presentation.

Asset Composition

	At 31 December 2017		(Restated) At 31 December 2016		
HK$'m, except percentages	Amount	% of total	Amount	% of total	Change (%)
Cash and balances with banks and other financial institutions	**364,205**	**13.8**	236,306	10.0	54.1
Placements with banks and other financial institutions maturing between one and twelve months	**59,056**	**2.2**	72,610	3.1	(18.7)
Hong Kong SAR Government certificates of indebtedness	**146,200**	**5.5**	123,390	5.3	18.5
Securities investments[1]	**704,507**	**26.6**	655,231	27.8	7.5
Advances and other accounts	**1,189,609**	**45.0**	1,008,025	42.8	18.0
Fixed assets and investment properties	**66,930**	**2.5**	64,039	2.7	4.5
Other assets[2]	**115,246**	**4.4**	141,846	6.0	(18.8)
Assets held for sale	**–**	**–**	53,293	2.3	(100.0)
Total assets	**2,645,753**	**100.0**	2,354,740	100.0	12.4

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

As at 31 December 2017, total assets of the Group amounted to HK$2,645,753 million, an increase of HK$291,013 million, or 12.4%, from the end of 2016. The Group continued to enhance the management of its assets and liabilities in order to ensure sustainable growth in business and profitability.

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

- Cash and balances with banks and other financial institutions increased by HK$127,899 million, or 54.1%, mainly due to an increase in balances with banks and central banks;
- Advances and other accounts rose by HK$181,584 million, or 18.0%, with growth in advances to customers rising by HK$156,266 million, or 15.8%;
- Other assets decreased by HK$26,600 million, or 18.8%, mainly due to a decrease in derivative financial instruments;
- Assets held for sale dropped to zero as the Group completed the disposal of Chiyu.

Advances to Customers

HK$'m, except percentages	At 31 December 2017 Amount	At 31 December 2017 % of total	(Restated) At 31 December 2016 Amount	(Restated) At 31 December 2016 % of total	Change (%)
Loans for use in Hong Kong	**759,038**	**66.3**	664,030	67.2	14.3
Industrial, commercial and financial	**436,754**	**38.2**	375,506	38.0	16.3
Individuals	**322,284**	**28.1**	288,524	29.2	11.7
Trade finance	**78,182**	**6.8**	72,210	7.3	8.3
Loans for use outside Hong Kong	**307,239**	**26.9**	251,953	25.5	21.9
Total advances to customers	**1,144,459**	**100.0**	988,193	100.0	15.8

In 2017, the Group captured opportunities arising from national strategies including the Belt and Road Initiative, the Going Global strategy, the development of the Guangdong-Hong Kong-Macao Greater Bay Area and Southeast Asia. It strengthened its collaboration with the BOC Group in order to provide a diversified range of financial services to mainland enterprises going global as well as corporates in Southeast Asia. The Group also continued to develop the local market in Hong Kong with a focus on family-owned businesses, chambers of commerce and listed companies, along with business development related to government and public sector entities. In addition, it enhanced its services to customers in the SME, residential mortgage and other retail loan businesses by leveraging the competitive edge arising from its branch transformation and its diversified business platforms. Advances to customers grew by HK$156,266 million, or 15.8%, to HK$1,144,459 million in 2017.

Loans for use in Hong Kong grew by HK$95,008 million or 14.3%:

- Lending to the industrial, commercial and financial sectors increased by HK$61,248 million or 16.3%, reflecting growth in the property development, manufacturing, transport and transport equipment, financial concerns and information technology industries;

- Lending to individuals increased by HK$33,760 million or 11.7%. Residential mortgage loans (excluding those under Government-sponsored home purchasing schemes) grew by 7.3% while other individual loans increased by 32.8%, mainly driven by the increase in property refinancing.

Trade finance rose by HK$5,972 million or 8.3%. Loans for use outside Hong Kong grew by HK$55,286 million or 21.9%, mainly driven by growth in loans for use in the Asia-Pacific region.

Loan Quality

HK$'m, except percentages	At 31 December 2017	(Restated) At 31 December 2016
Advances to customers	**1,144,459**	988,193
Classified or impaired loan ratio	**0.18%**	0.23%
Total impairment allowances	**4,084**	3,429
Total impairment allowances as a percentage of advances to customers	**0.36%**	0.35%
Residential mortgage loans[1] – delinquency and rescheduled loan ratio[2]	**0.01%**	0.02%
Card advances – delinquency ratio[2]	**0.21%**	0.24%

	2017	2016
Card advances – charge-off ratio[3]	**1.51%**	1.51%

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

To maintain stable asset quality, the Group adhered to a prudent credit strategy for the year. The classified or impaired loan ratio was 0.18% as at 31 December 2017, down 0.05 percentage point from the end of last year. Classified or impaired advances to customers decreased by HK$203 million, or 8.9%, to HK$2,079 million.

The credit quality of the Group's residential mortgage loans and card advances remained sound. The combined delinquency and rescheduled loan ratio of residential mortgage loans was 0.01% as at 31 December 2017. The charge-off ratio of card advances was 1.51%, unchanged from that of 2016.

Deposits from Customers*

HK$'m, except percentages	At 31 December 2017 Amount	At 31 December 2017 % of total	(Restated) At 31 December 2016 Amount	(Restated) At 31 December 2016 % of total	Change (%)
Demand deposits and current accounts	**203,831**	**11.5**	173,988	11.4	17.2
Savings deposits	**910,184**	**51.3**	805,831	52.9	12.9
Time, call and notice deposits	**657,498**	**37.0**	540,048	35.5	21.7
	1,771,513	**99.8**	1,519,867	99.8	16.6
Structured deposits	**2,784**	**0.2**	3,425	0.2	(18.7)
Deposits from customers	**1,774,297**	**100.0**	1,523,292	100.0	16.5

* Including structured deposits.

The Group implemented a number of strategic initiatives in its deposits business in 2017, including the development of payroll account services, receiving bank business for IPOs, cash management, settlement and custody business, with the aim of retaining deposits from customers. As at 31 December 2017, total deposits from customers amounted to HK$1,774,297 million, up HK$251,005 million, or 16.5%, from the end of last year. Demand deposits and current accounts grew by 17.2%, saving deposits increased by 12.9%, and time, call and notice deposits were up 21.7%.

Capital and Reserves Attributable to Equity Holders of the Company

HK$'m, except percentages	At 31 December 2017	(Restated) At 31 December 2016	Change (%)
Share capital	**52,864**	52,864	–
Premises revaluation reserve	**36,689**	35,608	3.0
Reserve for fair value changes of available-for-sale securities	**42**	(592)	N/A
Regulatory reserve	**10,224**	9,227	10.8
Translation reserve	**(669)**	(1,217)	(45.0)
Merger reserve	**–**	3,455	(100.0)
Retained earnings	**143,589**	129,302	11.0
Reserves	**189,875**	175,783	8.0
Capital and reserves attributable to equity holders of the Company	**242,739**	228,647	6.2

Capital and reserves attributable to equity holders of the Company amounted to HK$242,739 million as at 31 December 2017, an increase of HK$14,092 million, or 6.2%, from the end of 2016. Retained earnings rose by 11.0%, mainly reflecting the profit for 2017 after the distribution of dividends. The premises revaluation reserve increased by 3.0%, which was attributable to an increase in the valuation of premises in 2017. The reserve for fair value changes of available-for-sale securities moved from a deficit to a surplus, driven by market interest rate movements. The regulatory reserve rose by 10.8%, mainly driven by growth in advances to customers. The merger reserve arose from the Group's application of the merger accounting method in relation to its combination with BOC Thailand and BOC's Indonesia Business and Cambodia Business.

Capital Ratio and Liquidity Coverage Ratio

HK$'m, except percentages	At 31 December 2017	At 31 December 2016
Consolidated capital after deductions		
Common Equity Tier 1 capital	**170,012**	158,828
Additional Tier 1 capital	**–**	458
Tier 1 capital	**170,012**	159,286
Tier 2 capital	**39,816**	41,926
Total capital	**209,828**	201,212
Total risk-weighted assets	**1,029,152**	900,288
Common Equity Tier 1 capital ratio	**16.52%**	17.64%
Tier 1 capital ratio	**16.52%**	17.69%
Total capital ratio	**20.39%**	22.35%

	2017	2016
Average value of liquidity coverage ratio		
First quarter	**121.41%**	112.92%
Second quarter	**123.88%**	109.70%
Third quarter	**121.12%**	118.69%
Fourth quarter	**135.64%**	107.02%

The minimum capital requirements under the Basel III phase-in arrangements came into effect on 1 January 2013 and will become fully effective on 1 January 2019. The Group's capital level was further enhanced by the gain from the disposal of Chiyu. In the course of formulating its internal capital management targets, the Group took into consideration not only the regulatory requirements but also its rapid business development and short- and long-term capital requirements, including support from capital replenishment solutions, with the ultimate aim of ensuring the long-term stability of its capital level. The Group also continued to refine measures for monitoring changes in the risk-weight of its assets. At the same time, the Group made use of stringent and forward-looking stress testing to assess the demand and supply of capital under different stress scenarios, examined management targets for capital adequacy and formulated a capital adjustment solution to ensure the Group's ability to comply with capital requirements under stressed conditions.

At 31 December 2017, both the common equity tier 1 ("CET1") capital ratio and tier 1 capital ratio were 16.52%, down 1.12 and 1.17 percentage points respectively from the end of 2016. Profits net of dividends for 2017 drove up CET1 capital and tier 1 capital by 7.0% and 6.7% respectively. Total risk-weighted assets ("RWAs") were up 14.3%, driven by an increase in credit RWAs due to growth in advances to customers in 2017, which was partially offset by a reduction in RWAs following the disposal of Chiyu. The total capital ratio of the Group was 20.39%.

The Group's liquidity position remained sound with the average value of liquidity coverage ratio for all four quarters of 2017 above the regulatory requirement.

Business Review

Business Segment Performance

Profit/(loss) before Taxation by Business Segments

HK$'m, except percentages	2017	% of total	2016	(Restated) % of total	Change (%)
CONTINUING OPERATIONS					
Personal Banking	**8,055**	**22.8**	7,486	25.0	7.6
Corporate Banking	**14,813**	**42.0**	13,238	44.1	11.9
Treasury	**10,227**	**29.0**	8,625	28.8	18.6
Insurance	**1,401**	**4.0**	1,230	4.1	13.9
Others	**766**	**2.2**	(608)	(2.0)	N/A
Total profit before taxation	**35,262**	**100.0**	29,971	100.0	17.7

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

Personal Banking

Financial Results

Personal Banking achieved a profit before tax of HK$8,055 million in 2017, an increase of HK$569 million, or 7.6% year-on-year, mainly driven by an increase in net interest income and non-interest income.

Net interest income increased by 14.3%. This was mainly driven by an improvement in the deposit spread along with an increase in the average balance of deposits and loans. Net fee and commission income increased by 11.9% as the Group achieved satisfactory performance in its securities brokerage and funds distribution business with encouraging year-on-year growth in commission income. Net trading gain rose by 31.1%, owing to growth in income from the bond business and equity-linked structured products. Operating expenses were up 18.2%, mainly due to an increase in staff costs and business-related expenses. Net charge of impairment allowances increased by 77.6%, as the Group has taken a prudent and stable approach to increase impairment allowances for a certain loan portfolio.

Business Operations

Optimising wealth management services

The Group seized market opportunities and actively deepened its business relationships with customers. It continued to refine its wealth management system and widen the range of upgraded wealth management services. The Group offered exclusive private banking products, including bonds and equity-linked notes, to enrich the privileged product spectrum for high-end customers, and redesigned its Wealth Management Centre to strengthen its professional brand image. It organised the Worldwide Wealth Management Expo 2017, hosted investment strategy seminars and sponsored a series of Hong Kong Jockey Club Cup activities, so as to provide more value-added services for mid- to high-end customers. The total number of mid- to high-end customers increased by 24% year-on-year.

Private Banking business maintained satisfactory growth and acquired high net-worth clients from local, mainland and overseas. In line with its people-oriented culture, the Group strengthened its private banking team and accelerated development in cross-border business. It optimised the private banking open platform and launched a brand new and exclusive internet banking service so as to enhance customer experience. It actively participated in the development of the private banking industry by supporting The Pilot Apprenticeship Programme for Private Wealth Management, which is jointly organised by the HKMA and the Private Wealth Management Association, to provide training to wealth management talent. In September 2017, BOCHK's Private Banking Headquarter was established at the Bank of China Building, a Grade 1 historic building in Hong Kong, to signify its status as the Overseas Private Banking Centre of BOC Group and to enhance its brand reputation. Both the total number of private banking clients and related assets under management grew satisfactorily from the end of last year.

Faster growth in deposit and loan business

The Group achieved promising growth in its deposit business by pursuing a targeted strategy for different customer segments, providing differentiated pricing to customer groups, driving customer upgrades and strengthening cross-selling. The Group also made a concerted effort to acquire employee payroll business from government entities and large corporates so as to grow current and savings deposits and continuously optimise its deposit structure. In its loan business, the Group integrated its internal resources to enhance the mortgage approval process and introduced digital sales to enhance customer experience. It developed partnerships with property agencies and law firms with a view to deepening cooperative relationships through joint sales activities. At the same time, the Group strengthened its product innovation and integrated service capabilities to boost loan growth. In 2017, both the balance of deposits and the amount of new loan drawdown of the personal banking reached record highs, with customer deposits increasing by 21% from the prior year-end and the number of new residential mortgage loan transactions rising by 43% year-on-year.

Enhancing cross-border service capabilities

Capturing the opportunities arising from the development of the Guangdong-Hong Kong-Macao Greater Bay Area, the Group cooperated with BOC to drive forward the implementation of major cross-border projects, with the aim of achieving mutual brand recognition for personal customers and promoting service sharing and joint sales in the area. Both the total number of cross-border customers and related total relationship balance recorded satisfactory growth from the end of last year. The Group established additional cross-border financial services centres and introduced the BOCHK WeChat cross-border official account so as to enhance its integrated cross-border service capabilities through online and offline collaboration. In addition, the Group coordinated with a number of BOC branches to launch joint marketing activities promoting account opening attestation and employee payroll services to well-known large and medium-sized Chinese enterprises, which helped to boost the number of potential high-end customers and establish the Group as the first-choice bank for cross-border customers. During the year, the total number of cross-border customers grew 24% year-on-year.

Deepening branch transformation

During the year, the Group completed the optimisation of its personal banking business structure. This included refining frontline unit management and strengthening professional support from the headquarters to the frontlines. This was effective in boosting the productivity of its branches. The Group also completed the design of a new branch model and further optimised its branch network by setting up large-scale integrated branches. Leveraging its extensive branch network, the Group transformed its retail-focused branch service coverage to a more comprehensive service model. This shift was integrated with the implementation of the Group's SME "personal + business" all-in-one model, with the overall aim of becoming customers' primary bank. The Group actively participated in the SME Financing Guarantee Scheme launched by the government to facilitate the growth of the real economy and to contribute to the development of SMEs. In line with the HKMA's call to encourage overseas enterprises to conduct business in Hong Kong, the Group launched a series of seminars and exhibitions to enhance the integrated servicing capabilities of small enterprises. During the year, the total number of business integrated accounts increased by 15%.

Stepping up the smart service development

The Group bolstered its omni-channel infrastructure by promoting full-function enhancement projects, including Smart Counter and iService. Together with innovative projects including mobile banking, biometric identification and a customer labelling database, the Group broadened its online payment channels by promoting the Small Value Transfer service in mobile banking, Smart Account and blockchain cross-border e-wallet. The Group also strived to become a smart green bank by enhancing paperless operations and digitising customer information, so as to promote the centralisation and reconstruction of the digital processes of its core businesses and to accelerate the shift from counter transactions to e-channel transactions.

Innovation in credit card business

Retail consumption in Hong Kong was stagnant in the first half of 2017 but regained momentum in the second half. The Group capitalised on such market conditions and changes in customer consumption patterns by launching a series of promotions in order to maintain continuous growth in cardholder spending volume. During the year, the Group actively promoted e-payment services to provide customers with convenient day-to-day payments. Following the launch of Apple Pay with VISA and MasterCard last year, the Group pioneered the launch of Apple Pay with UnionPay credit card and debit card, as well as introducing Samsung Pay and Android Pay with VISA and MasterCard. In addition, the Group cooperated with WeChat Pay Hong Kong and Alipay Hong Kong to introduce a binding local wallet service, thus creating a differentiated competitive edge and successfully achieving growth in online cardholder spending volume. It also issued several co-branded cards, including the BOC CMHK Dual Currency Diamond Card with China Mobile Hong Kong and UnionPay International, to target cross-border customers and to enhance the competitive advantages of all parties. During the year, the Group maintained its leadership in the UnionPay merchant acquiring and card issuing business in Hong Kong.

Corporate Banking

Financial Results

Corporate Banking achieved a profit before tax of HK$14,813 million, an increase of HK$1,575 million, or 11.9%, year-on-year. The growth was mainly driven by an increase in net interest income and net fee and commission income.

Net interest income increased by 15.7%, owing to the increase in the average balance of loans and deposits, coupled with improvement in the deposit spread. Net fee and commission income rose by 3.8%, mainly driven by commission income from the trust, insurance, securities brokerage and bills services. Operating expenses were up 12.1%, owing to an increase in staff costs and business-related expenses. Net charge of impairment allowances increased by 60.7%, due to the higher net charge of collectively assessed impairment allowances, attributable to growth in advances to customers.

Business Operations

Continuous expansion of customer base

Amid intense market competition, the Group strengthened its business contacts with existing customers while actively acquiring new customers. Faced with increased market uncertainty and fierce competition, the Group made a concerted effort to expand its syndicated loan business, arranging a number of syndicated loans with significant market influence during the year. The Group's total loan arrangement volume amounted to US$15 billion for the year, making it the top mandated arranger in the Hong Kong and Macao syndicated loan market for the 13th consecutive year. The total amount of funds raised from IPOs in which the Group served as the main receiving bank reached HK$79.2 billion, representing a market share of 64.9%. The Group obtained several major service tenders from the HKSAR government and related entities, which effectively strengthened its business relationships with the government. It successfully established business relationships with a number of major central banks, national treasuries and sovereign wealth funds. Deposits growth from institutions was satisfactory, providing a stable funding source for the Group's USD loans. The Group grasped opportunities arising from policies such as the establishment of treasury centres in Hong Kong and mainland corporates going global to expedite the development of its cash pooling and treasury centre businesses, with the aim of becoming the first-choice bank for cross-border pooling services. The Group also made breakthroughs in regionalisation and globalisation by providing support to mainland corporates going global, and helping leading enterprises in Hong Kong and Southeast Asia to manage their local, regional and global funding activities.

Proactive development in local commercial SME business

The Group continued to improve its services to local commercial customers by deepening business relationships with local family-owned businesses, chambers of commerce and listed companies in Hong Kong, helping them by establishing a convenient and effective financial service platform so as to mutually enhance market competitiveness and growth. The Group helped customers to access business opportunities in the mainland and overseas countries by inviting them to participate in the Cross-border Investment Matching Service held by BOC branches around the world. In addition, by leveraging the competitive advantages arising from its branch network, the Group continued to enhance its service capabilities to local corporate customers. BOCHK won the Best SME's Partner Gold Award 2017 from the Hong Kong General Chamber of Small and Medium Business in recognition of its acquisition of the Best SME's Partner Award for ten consecutive years.

Solid progress of business development in Southeast Asia

The corporate banking business collaborated with the Group's Southeast Asian institutions to acquire major projects and customers, with the aim of advancing those institutions' business development. It focused on cultivating the Southeast Asian institutions' marketing capabilities and stimulating their internal growth drivers through full product and service coverage. Guided by its long-term strategic vision, the Group made a concerted effort to develop business opportunities with leading Southeast Asian enterprises. The Group also expedited the establishment of a regional management mechanism and expanded its regional businesses with these institutions to create an effective, integrated system for sales, products and management. Capturing opportunities arising from the Guangdong-Hong Kong-Macao Greater Bay Area and FTZs in the mainland, the Group expanded its business model by continuously strengthening regional collaboration, optimising its service model for cross-border products and enriching the variety of its bilateral trading products. The Group also met regulatory requirements by setting up a cross-border financial infrastructure for mutual access.

Enhancing competitiveness of transaction banking products

The Group accelerated business transformation and product innovation in its corporate banking business by capturing opportunities in Hong Kong, the mainland and Southeast Asia. It continued to improve its competitive advantages in products and services, which was in turn effective in supporting the expansion of its customer segments. This attracted lower-cost funding, enhanced customer retention within the Group and drove profitability. It also strengthened the innovation and integration of its transaction banking products, so as to provide customers with a one-stop, scenario-based and comprehensive product solution that can be applied across different industry segments, including the real estate and aviation industry. Moreover, it introduced the new "1+N" supply chain service model. The Group led the market in terms of technological innovation. It completed the first application using blockchain technology for trade finance in Hong Kong and continued to improve the level of its e-banking services. Through the establishment of ASEAN regional product centres, the Group was able to seize business opportunities within the region, upgrade its service systems and enrich its products, thereby uplifting its regional service capabilities in transaction banking. BOCHK received the Achievement Award for Best Trade Finance Bank in Hong Kong and Best Corporate Trade Finance Deal in Thailand from *The Asian Banker*. Furthermore, BOCHK was named Hong Kong Domestic Cash Management Bank of the Year for the fourth consecutive year by *Asian Banking and Finance*.

Proactive credit risk management

In 2017, the Group continued to adhere to a prudent credit policy. In view of the uncertain economic environment, the Group adopted close credit monitoring on a more frequent and proactive basis. This included enhancing the analysis of industries and countries that could be negatively affected by market volatility, so as to identify risks and weaknesses. Moreover, it closely monitored emerging risks in the mainland and any related impacts on customers, reinforced its supervision of customers in segments under threat of overcapacity and in highly concerned industries, and put prompt precautionary measures in place. The Group also formulated risk control guidelines for its business strategies relating to the Belt and Road Initiative and mainland enterprises going global, thus supporting the healthy development of its credit business.

Treasury

Financial Results

Treasury recorded a profit before tax of HK$10,227 million, an increase of HK$1,602 million, or 18.6%, year-on-year. The growth was driven by an increase in net interest income, which was partially offset by the funding cost of foreign currency swap contracts recorded in 2017.

Net interest income surged by 119.5%, mainly attributable to an increase in the average balance of debt securities investments and balances and placements with banks, and an increase in the average yield of related assets caused by a rise in market interest rates. Net trading gain decreased by 98.5%, owing to the funding cost of foreign currency swap contracts, which was partially offset by an increased gain from currency exchange business and commodities trading. Operating expenses were up 24.9%, owing to higher staff costs.

Business Operations

Enhancing trading and service capabilities

During the year, the Group responded to a number of market changes and enhanced its capability in G10 currency trading. By applying in-depth fundamental research and capturing market opportunities, while at the same time cautiously controlling its risk exposure, the Group achieved notable growth in its trading business. It offered professional services and a diversified range of innovative products to meet customer needs. The Group also launched a series of structured derivatives products and strengthened the price quotation function of its electronic trading platforms. In celebration of the centenary of BOC's service to Hong Kong, the Group introduced the limited edition 9999 Commemorative Gold Plate, which was well received by customers. In recognition of its treasury business performance, BOCHK received the Hong Kong Domestic Foreign Exchange Bank of the Year award from *Asian Banking and Finance* and the Outstanding Treasury Business – Dim Sum Bond Market Maker award at the 2017 RMB Business Outstanding Awards, jointly organised by Metro Finance and Hong Kong Ta Kung Wen Wei Media Group. BOCHK also won the Key Business Partner in FIC Market award in the 4th Annual RMB Fixed Income and Currency Conference 2017, organised by HKEX.

Proactive expansion in banknote business

In 2017, the Group became the first bank in Hong Kong to provide Brunei dollar and South African rand banknote withdrawal and deposit services. This took the total number of listed currencies available for note exchange at the Group's retail counters to 24, further reinforcing its market leadership in local retail note exchange. In the wholesale banknote business, the Group established a more flexible and efficient operating framework to enhance its service capabilities in the mainland of China. It supported BOC Guangxi Branch's establishment as the ASEAN Banknote Centre in order to improve its service capabilities to customers. Moreover, the Group achieved further milestones in the internationalisation of its banknote business. Drawing on its expertise in supporting the Southeast Asia banknote business, BOCHK became the world's sole overseas operating bank of EURO Extended Custodial Inventory.

Consolidating competitive advantages in RMB clearing business

The Group further consolidated its competitive edge in offshore RMB business. Following the launch of Bond Connect in July 2017, BOCHK has acted as the sole designated bank for the Hong Kong Central Moneymarkets Unit and Bond Connect Company Limited for providing cross-border fund settlement services for institutions in both Hong Kong and the mainland, thus providing institutions with comprehensive services related to Bond Connect. In October, the Group successfully connected with the bilateral transformation function of the securities settlement system of China's Cross-border Interbank Payment System ("CIPS"), thus joining the first batch of direct participating banks to support bilateral business and provide delivery versus payment settlement for Bond Connect, and reinforcing its unique position as Bond Connect's sole overseas CIPS direct participating bank.

A proactive but risk-aware investment strategy

The Group continued to take a cautious approach in managing its banking book investments by closely monitoring market changes and seeking investment opportunities to enhance return, while remaining alert to risk. During the year, the Group adjusted its investment portfolio to respond to changes in interest rates and to enhance its returns from the allocation of funds.

Insurance

Financial Results

In 2017, profit before tax in the Group's Insurance segment was HK$1,401 million, up 13.9% year-on-year. The growth was mainly attributable to the improved performance of its equity securities and bond fund investments, as well as a rise of 37.9% in net insurance premium income, which was mainly attributable to the increase in renewal premium income. Operating expenses were up 16.3%, mainly due to higher staff costs.

Business Operations

Product innovation and channel expansion

The Group capitalised on its diversified distribution channels. In its bancassurance channels, it focused on developing its commercial, high-net-worth and private banking customer segments, in addition to the retail market. In terms of non-banking channels, it served non-bank customers through tied agency, brokerage, and third party affiliates. Cross-channel synergy enhanced business momentum. The Group remained committed to developing the local market and maintained its leading positions in the Hong Kong life insurance market and RMB insurance market. The Group also actively enriched its product range and supported the development of each distribution channel. Innovative products and value-added services were introduced to meet the differentiated needs of high-net-worth customers and visitors to Hong Kong. The Group's newly-launched and innovative annuity product, SmartRetire Annuity Insurance Plan, attracted the younger customer segment and captured extensive attention from the market, owing to its unique and flexible features, including the Retirement Fund Payout Option and Premium Payment Term Options. In order to support cross-border business, BOC Life deepened collaboration within the Group's business units, promoted the BOC Life brand to enhance awareness in overseas markets, and improved operational support and facilities to offshore customers.

Providing one-stop life insurance services

During the year, the Group established customer service centres providing both life insurance and diversified wealth management services in order to offer one-stop professional life insurance services to visitors to Hong Kong and high-net-worth customers. These centres are equipped with special features, including the first-of-its-kind Predictive-underwriting Engine, so as to provide services such as instant underwriting approval, mobile verification and medical examination. Service ambassadors with underwriting and claims authority are also stationed at the centres to provide customers with meticulous and efficient one-stop services and solutions. In recognition of its outstanding claims services, BOC Life received the Claims Innovation of the Year award at the Claims Awards Asia-Pacific 2017, organised by the Claims Club Asia-Pacific of *Insurance Post*.

Proactive application of innovative technology

The Group launched a number of InsurTech services, the first of their kind in the market, to enhance operational efficiency and customer experience. These included Easy Claims, the first online hospital cash claims platform to provide real-time approval in Hong Kong; the Electronic Bill Presentment and Payment service for premium payment; Apple Pay and Android Pay payment gateways; ecConnect for customers to store policies of other insurance companies and enjoy superior claim services, and e-signature, all of which offer new experiences to customers.

Recognition of outstanding services

BOC Life's outstanding services and professional reputation were recognised by the industry. During the year, it received a number of awards locally and internationally, including the Brand of the Year and Cross Border Insurance Service Excellence awards from *Bloomberg Businessweek*; the 2017 RMB Business Outstanding Awards, jointly organised by Metro Finance and Hong Kong Ta Kung Wen Wei Media Group; and the High Net Worth Team of the Year, Client Engagement – Best-In-Class and Outstanding Customer Support Team awards from *Benchmark*. In terms of credit rating, BOC Life's solid financial strength was affirmed by a financial strength rating from Moody's Investors Service of A2, with its outlook revised from stable to positive, reflecting BOC Life's excellent asset and liability management and solvency.

Diversified Business Platforms

In keeping with its goal of business diversification, the Group achieved satisfactory performance in enhancing its diversified business platforms. Business related to credit cards, private banking, cash management and life insurance are discussed under the Personal Banking, Corporate Banking and Insurance segments above. The Group's asset management, custody, trust and securities and futures businesses are discussed below.

A wider range of asset management products

In 2017, BOCHK Asset Management Limited ("BOCHK AM") rapidly developed its business. Its assets under management ("AUM") grew by over 25% from the end of 2016. During the year, its investment performance outperformed the market, with both bond and equity investment portfolios outperforming their corresponding benchmark indices. Products and services were further enriched, thus expanding the coverage of underlying assets. A total of two new public funds and five new private funds were launched during the year. Apart from traditional bond funds and equity funds, newly-launched funds included a fixed-maturity bond fund, a commercial real estate fund and a multi-asset strategy fund. The number and diversity of institutional clients further expanded, gradually transforming BOCHK AM's client structure from serving mainly local institutional clients to also serving mainland financial institutions and state-owned enterprises. BOCHK AM also expanded its client base among large-scale institutional clients in Europe and the US. By strengthening its collaboration with BOC and Bank of China Investment Management Co., Ltd., it boosted sales of its northbound fund (BOCHK All Weather China High Yield Bond Fund), with strong growth in related AUM from the end of 2016. Moreover, BOCHK AM successfully transferred its undertakings for collective investment in transferable securities ("UCITS") fund to BOC Luxembourg's new fund platform, also recording notable growth in related AUM.

Rapid expansion in custody business

In 2017, the Group's custody business achieved rapid growth in all major aspects. Its consistent focus on the insurance and pension sectors yielded outstanding results, as these client segments delivered remarkable growth amid robust equity and bond markets. During the year, the Group established a business relationship with a major insurance-type QDII client and successfully implemented large-scale custody asset transfers. The Group further attended to the needs of institutional clients going out of and coming into the mainland, focused on product diversification and nurtured local and overseas clients of different types in order to achieve a record high in new mandate numbers and a further enhancement in client diversity. The Group captured opportunities arising from various mergers and acquisitions ("M&A"), listed company activities, financing arrangements and the Belt and Road Initiative to proactively offer escrow services. At the same time, the Group leveraged its market expertise in RMB to promote active sales for Bond Connect and maintain its leading market position. At the end of 2017, total assets under custody reached HK$1,162.4 billion, reflecting a substantial rise in custody business volume and support to low- to non-interest customer deposits.

Trustee business recording remarkable growth

The Group provides trustee and fund administration services for occupational retirement schemes and mandatory provident fund ("MPF") schemes as well as trustee and custodian services for unit trusts through its subsidiary company, BOCI-Prudential Trustee Limited ("BOCI-Prudential Trustee"). BOCI-Prudential Trustee strives to deliver a holistic retirement planning solution by generating corporate synergy, actively broadening diversified distribution channels, optimising referral and incentive mechanisms, and promoting technological innovations and system function upgrades. In 2017, it continued to acquire large institutional clients and increase new business volume. During the year, BOCI-Prudential Trustee secured a further tenure of an MPF administration service contract from a governmental institution and was successfully awarded with new tenders from several large corporates. As of the end of 2017, the MPF asset size of BOCI-Prudential Trustee reached a record high, representing an increase of over 28% from the end of 2016. In respect of unit trust funds, BOCI-Prudential Trustee acted as the Transfer Agency for the approved northbound fund (BOCHK All Weather China High Yield Bond Fund) managed by BOCHK AM, processing daily cross-border transactions. In addition, it added two renowned asset management companies to the client base of its trustee services; a subsidiary of a time-honoured insurance brand in the mainland, and an institution with excellent financial strength in an ASEAN country.

BOCI-Prudential Trustee received a total of 29 awards from independent rating agencies, the market, the industry and the innovation and technology sector in recognition of its outstanding performance and strength. BOCI-Prudential Trustee's My Choice MPF Scheme and BOC-Prudential Easy-Choice MPF Scheme received multiple accolades at the MPF Awards 2017, organised by MPF Ratings. It was awarded the Excellent Brand of MPF Online Platform award for the second consecutive year in the Hong Kong Leaders' Choice Brand Awards 2017, organised by Metro Finance; and the Best of MPF App Service Provider award for the third consecutive year at e-Brand Awards 2017, organised by *e-zone* of *Hong Kong Economic Times*. Furthermore, it also received a number of fund awards at the 2017 Lipper Hong Kong Fund Awards, organised by Lipper, and the Top Fund Awards 2017, organised by *Bloomberg Businessweek*.

Steady growth in securities and futures brokerage services

The Group engages in the provision of brokerage services for futures and options trading through its subsidiary company, Po Sang Securities and Futures Limited ("Po Sang Securities and Futures"). In 2017, Po Sang Securities and Futures reached a new milestone following the completed restructuring of its organisational structure and business model. In addition to existing futures and options contract trading services, it introduced a range of market-oriented investment services, including securities trading services and securities financing services for individual and corporate clients. It also established its first account executive team and developed its institutional sales services. With a new securities trading platform in operation, Po Sang Securities and Futures also introduced a number of core services including securities margin trading, IPO subscription and IPO financing services. It now has a total of five branches, located in Central, Mongkok, Mei Foo, Tai Po and Yuen Long, thus strengthening its marketing capabilities in those respective Hong Kong regions.

Southeast Asia Business

BOCHK's overall development strategy in Southeast Asia

Southeast Asia has remarkable development potential, both as a core focus of China's Belt and Road Initiative, a key market for RMB internationalisation and as a target region for Chinese enterprises going global. Hong Kong, serving as a testing ground for China's new opening-up initiatives, is an essential conduit connecting the mainland and Southeast Asia. It also assumes the role of a super-connector between China and countries along the Belt and Road. BOCHK has actively pushed forward the restructuring of its assets in Southeast Asia. This move is important not only in terms of supporting China's Belt and Road Initiative and consolidating Hong Kong's status as an international financial centre, but also in terms of strategically aligning with BOC Group's efforts to build a financial artery along the Belt and Road and accelerating the Group's own development to build a top-class, full-service and internationalised regional bank. Aiming to achieving mainstream bank status in local Southeast Asia areas, the Group's Southeast Asian institutions made a concerted effort to integrate into local society and serve mainstream clients, including Chinese enterprises operating in Belt and Road areas, mainland enterprises going global and leading local corporates, overseas Chinese and high-net-worth customers. They also focused on local mainstream projects and business areas such as RMB business, commodities and supply chain financing, as well as high-end private banking services.

Accelerating business development in Southeast Asia and promoting its regional transformation strategy

In 2017, the Group's asset integration in Southeast Asia was conducted in an orderly manner. Synergies began to emerge, facilitating a leap forward in the Group's building into an internationalised regional bank. Following the acquisition of BOC Thailand on 9 January 2017, the Group completed the acquisition of the Indonesia Business and Cambodia Business of BOC on 10 July 2017 and 6 November 2017 respectively. The acquisition of the Vietnam Business and Philippines Business of BOC was completed on 29 January 2018. As a result, the Jakarta Branch, Phnom Penh Branch, Ho Chi Minh City Branch and Manila Branch became branches of BOCHK. For further information on these acquisitions, please refer to the announcements issued by the Group on 28 February, 6 July, 3 November, 6 November and 29 December 2017. During 2017, the Group also completed the preparation work for the opening of BOC Malaysia's Melaka Branch.

Strengthening regional business collaboration and developing local mainstream markets

Since 2017, the Group's Hong Kong operations have proactively supported business development in Southeast Asia and recorded great achievements through cooperation with its Southeast Asian institutions. In corporate banking business, the Group achieved regional synergy through internal collaboration, expanding business cooperation with leading enterprises in Southeast Asia and participating in major infrastructure projects related to the construction of railway and communication equipment, oil and optical cables. In addition, BOCHK's competitive edge was extended to its Southeast Asian institutions through enriched product offerings such as cash management, structured financing, syndicated loan arrangement and customised trade products tailored to clients' needs, providing more comprehensive services for local customers. BOCHK collaborated with its Southeast Asian institutions in jointly undertaking cross-border loans for Hong Kong enterprises while actively expanding its institutional and RMB banknote businesses.

In personal banking business, the Group reinforced local sales teams to better serve personal customers by stationing account executives at its Southeast Asian institutions and conducting team building and staff training. BOC Malaysia launched its medical insurance plan in 2017 and received positive feedback, and introduced eight products from four fund houses after obtaining a licence for funds distribution from the local regulatory authority. With respect to bancassurance business, BOCHK Jakarta Branch worked closely with life insurance companies on product referral.

Maintaining prudent risk management policies and achieving sustainable and healthy development

The Group adhered to a prudent credit strategy in order to achieve sustainable and healthy development in its credit business. It formulated guidelines to facilitate risk control and sustainable expansion in its credit business with regard to business strategies relating to Chinese enterprises going global and the Belt and Road initiative.

In order to refine its regional management system and mechanism, the Group gave guidance to its Southeast Asian institutions regarding management structure, internal control, policies and procedures, as well as approval authority and limits pertaining to credit risk, thus ensuring that they act in accordance with BOCHK's credit risk management principles and standards as well as related regulatory requirements. Moreover, the Group extended its credit risk management system and standards to its Southeast Asian institutions as part of its compliance supervision, and focused on enhancing Southeast Asian institutions' management of credit and anti-money laundering risk.

The Group is committed to adopting consistent and prudent risk management policies, and as such all Southeast Asian institutions must comply with its risk appetite and credit risk policies. It has established a regional credit risk management system that provides full guidance and support to its Southeast Asian institutions in terms of their organisational structure, policies and procedures, approval processes and staff allocation and system techniques, in order to ensure that they operate in accordance with the Group's standards and the requirements of the HKMA and local regulators in Southeast Asia.

Technology and Operations

The Group attached a high level of importance to Fintech innovation. It proactively introduced customer-oriented Fintech services and continuously enhanced its competitive edge in e-Finance, driving business development forward in a number of domains. During the year, the Group achieved breakthroughs in the application of technological innovation, including blockchain, biometric authentication and big data. Development of blockchain technology applications for property valuation made good progress, with more than 80% of the Group's valuation cases conducted using this technology. The application was also extended to trade finance services, enhancing transaction efficiency. The use of biometric authentication technology was expanded to different business scenarios. The Group became the first bank in Hong Kong to introduce finger vein authentication on ATMs. It also adopted fingerprint and voiceprint authentication for mobile banking and call centres respectively, providing customers with safer and more convenient authentication options. It continued to develop its big data platform, enhancing insight analysis on individual customers and customer segmentation for more effective marketing. Meanwhile, the Group strived to promote the development of e-channel facilities. BOCHK iService, a 24-hour video banking service, was optimised and the brand new BOCHK WeChat account and BOC Life mobile application were launched. Payment services including Apple Pay, Samsung Pay, Android Pay and WeChat Pay were introduced to improve customer experience. As a result of the initiatives mentioned above, the total number of customers using e-channels including internet and mobile banking services continued to rise during the year, together with a year-on-year increase in the total number of related transactions.

As part of its commitment to driving innovation and promoting Fintech development in Hong Kong, the Group signed a strategic cooperation agreement with China Mobile International and China Mobile Hong Kong. The partnership enables all parties to develop diversified service platforms, create a core customer base, accelerate regional development and jointly develop business in Southeast Asia. In addition, the Group strived to strengthen its strategic cooperation with several large internet companies in order to expand its cross-border business and improve overall competitiveness. During the year, the Group set up the Innovation Laboratory and Innovation Workshop as a platform to strengthen cooperation and idea exchanges with industry regarding innovation.

The Group continued to strengthen development in its IT infrastructure in order to maintain stable business growth. During the year, the Group proactively pushed forward information systems integration as part of the deployment of BOC Group's global IT strategy. The relocation of the Group's disaster recovery centre was completed in order to improve the operational efficiency and stability of its application systems during disaster recovery. In line with its regional development strategy, the Group expedited regional system architecture planning and implementation, and established regional IT governance and procedures. With respect to technology risk management and other security issues, the Group has adopted international best practices and launched a series of cyber security awareness programmes to increase the sophistication of technology risk management.

In recognition of its innovations in technology and IT development, BOCHK was recognised as Excellent Brand of Fintech-Banking in the Hong Kong Leaders' Choice Brand Award 2017, hosted by Metro Finance and Metro Finance Digital. In recognition of its efforts to develop and apply blockchain technology in the local banking and finance industry, BOCHK won the Best FinTech (Emerging Solutions/Payment Innovation) Gold Award at the Hong Kong ICT Awards 2017. Its finger vein authentication function also won the Best Smart Hong Kong (Digital Inclusion Application) Certificate of Merit in the same awards. In the 12th Retail Banking Awards, organised by *Asian Banking and Finance*, BOCHK received the Mobile Banking Initiative of the Year – Hong Kong award for the third consecutive year, the Digital Banking Initiative of the Year – Hong Kong award for the second consecutive year, and the Online Securities Platform of the Year – Hong Kong award, reflecting BOCHK's outstanding performance in e-banking services. As a commendation to BOCHK's IT governance, it was awarded a Gold Medal in the IT Governance Achievement Award in Private Sector presented by the ISACA China Hong Kong Chapter.

Disposal of Chiyu Banking Corporation Limited

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

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

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

Profit attributable to equity holders from discontinued operations amounted to HK$2,589 million, including a gain on the disposal of Chiyu of HK$2,504 million. This represented a decrease of HK$28,713 million from the previous year's figure, which included a gain on the disposal of NCB of HK$29,956 million.

HK$'m	2017	2016
Profit of discontinued operations	**85**	1,346
Gain on disposal of discontinued operations	**2,504**	29,956
Profit attributable to equity holders of the Company from discontinued operations	**2,589**	31,302

Outlook and Business Focus for 2018

The global economy will continue to recover in 2018. The International Monetary Fund expects global output to grow by 3.9% in 2018, slightly faster than the previous year's 3.7%. The US economy will maintain stable growth as it benefits from tax reform implementation. The Chinese economy is expected to realise mid- to high-speed growth, having entered a stage of high-quality development rather than high-speed expansion. The Hong Kong economy is expected to maintain a positive outlook and satisfactory performance in 2018 amid an improved external environment, full employment and the policies of the new Government administration. The ASEAN region will continue to experience solid economic growth, supported by accelerated infrastructure development, an improving business environment and a rise in foreign investment.

2018 will be a year of both opportunities and challenges. More opportunities will be created for Hong Kong banks by major national strategic initiatives and policies (such as the Belt and Road Initiative and the Guangdong-Hong Kong-Macao Greater Bay Area Plan), strengthened connections between financial markets in Hong Kong and the mainland, a bullish outlook for Hong Kong's capital markets, robust investment and M&A flows in Southeast Asia and the drawing of the RMB internationalisation 2.0 era. At the same time, uncertainties in the global political and economic environment, intensifying market competition and a more stringent regulatory environment for business development will continue to create challenges for the operation and development of banks. The Group will aim to "Build a Top-class, Full-service and Internationalised Regional Bank", proactively respond to market changes and reinforce the development of its core businesses. It will accelerate regional expansion and business transformation, enhance its product innovation and service capabilities while remaining committed to prudent risk management, so as to achieve sustainable development in all areas.

The Group will accelerate the integration of its Southeast Asian institutions in order to push forward its regional development. It will further refine its regional management mechanism, reinforce support to its Southeast Asian institutions, tailor their business development to local conditions and enrich its product offering, with the aim of achieving sustainable and balanced development and establishing itself as a mainstream bank in local Southeast Asia markets, as well as a major bank for enterprises along the Belt and Road and enterprises going global. The Group will focus on RMB business and step up the development of the RMB market in local Southeast Asia. For corporate banking business, the Group will develop relationships with mainstream clients and industries in Southeast Asia areas, focusing on Chinese family-owned businesses to establish a target client base. For personal banking business, it will focus on credit cards, mobile banking and payroll account services, striving to become the main bank for mid- to high-end and cross-border Chinese clients and clients of payroll account services. It will also optimise the risk management system of its Southeast Asian institutions, cultivate a solid compliance culture and optimise the "Three Lines of Defence" mechanism in order to meet both Group and local regulatory requirements.

The Group will accelerate technological innovation and product R&D in order to achieve digital development. It will apply internet thinking and digital technology to its business model restructuring and product upgrading and development, and refine its innovation mechanism in order to become a leading digitalised bank. Aiming at enhancing customer experience and enlarging its customer base in local areas, the Guangdong-Hong Kong-Macao Greater Bay Area and Southeast Asia, the Group will innovate a diversified range of featured services, integrate its online and offline channels and provide systematic, automatic, intelligent and timely one-stop services.

In pursuit of full-function development, the Group will speed up the construction of its diversified business platforms and the integration of its commercial banking and investment banking businesses. Focusing on clients' varied financial needs, the Group will accelerate the integration of its investment banking, diversified businesses and traditional commercial banking businesses, leverage the competitive advantages arising from its distribution channels and customer segments and enhance its overall service capabilities, in order to expand its customer base and business coverage.

The Group will remain committed to developing the local market and further enhancing its competitive edge. It will lend its weight to Hong Kong's economic development, support major projects, acquire more customers from local market SMEs, listed companies and family-owned businesses, and deepen business cooperation with the Government and public sector entities. It will also step up innovations in livelihood finance in order to serve customers more comprehensively and efficiently. In addition, it will actively expand its RMB business and strengthen its trading capacity, thus supporting Hong Kong in consolidating and enhancing its role as a hub for global offshore RMB business.

The Group will proactively expand its cross-border business with a focus on the regional integration of Guangdong, Hong Kong and Macao. Leveraging opportunities arising from the Belt and Road Initiative, the regional integration of Guangdong, Hong Kong and Macao and the relaxation of China's FTZ policies, the Group will work more closely with BOC institutions in the mainland and overseas countries, provide support to key industrial sectors and major projects and upgrade its one-stop products and services, thus enhancing its regional competitiveness. It will also strengthen innovation in its cross-border RMB business in order to become the first-choice bank for cross-border personal banking clients.

The Group will reinforce general management and team building in order to enhance its corporate governance. It will accelerate the establishment of intensified, intelligent and regionalised operations and leverage economies of scale so as to further enhance operational efficiency. The Group's asset yield and net interest margin will improve due to strengthened asset and liability management. Moreover, with the aim of establishing the BOC Group training centre for international professional talent, the Group will step up staff allocation and training for key business areas and set up an education and training system tailored to its development needs.

Credit Ratings

As at 31 December 2017	Long-term	Short-term
Standard & Poor's	A+	A-1
Moody's	Aa3	P-1
Fitch	A	F1

RISK MANAGEMENT

Banking Group

Overview

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

Credit risk management

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

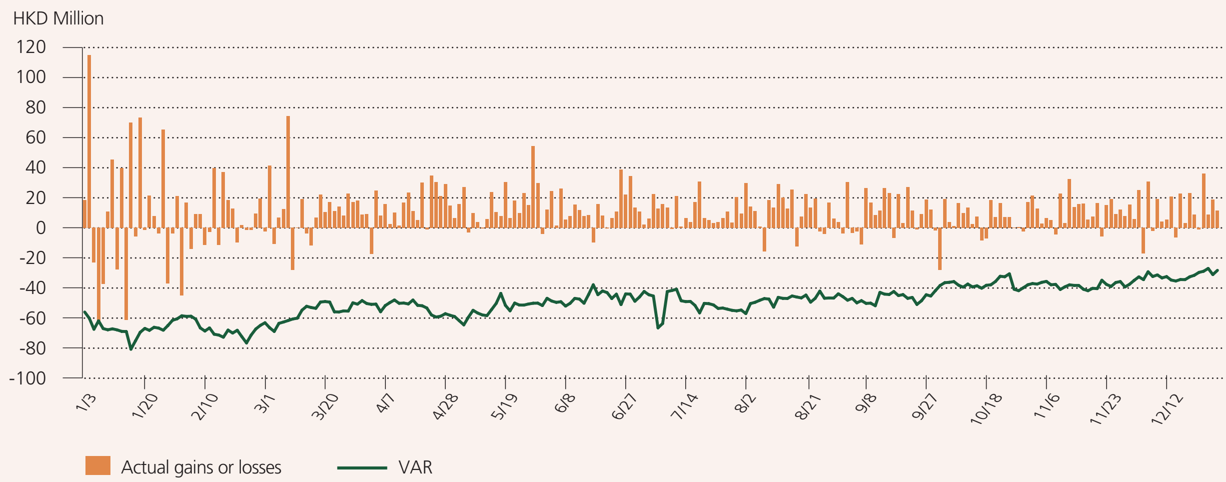
Market risk management

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

The Group uses the VAR to measure and report general market risks to the Risk Committee ("RMC") 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 gains or losses arising from those positions on the next business day. Generally speaking, the number of back-testing exceptions in a rolling 12-month period will not exceed four times, given a 99% confidence level. The graph below shows the back-testing result of the VAR against actual gains or losses of the Group.

Daily Back-testing in 2017



There was one actual loss exceeding the VAR for the Group in 2017 as shown in the back-testing results.

Interest rate risk management

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

Liquidity risk management

Liquidity risk is the risk that banks may not be able to obtain sufficient and timely funding at reasonable cost to meet their obligations as they fall due. The Group maintains sound liquidity risk appetite to provide stable, reliable and adequate sources of cash to meet liquidity needs under normal circumstances or stressed scenarios; and to survive with net positive cumulative cash flow in extreme scenarios, without requesting the HKMA to act as the lender of last resort. For details of the Group's Liquidity Risk Management, please refer to Note 4.3 to the Financial Statements.

Operational risk management

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

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

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

Reputation risk management

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

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

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

Legal and compliance risk management

Legal risk is the risk that unenforceable contracts, lawsuits or adverse judgments may disrupt or otherwise negatively affect the operations or financial conditions of the Group. Compliance risk is the risk of legal or regulatory sanctions, financial losses or losses in reputation the Group may suffer as a result of its failure to comply with applicable laws and regulations. Legal and compliance risks are managed by the LCO, while the risks related to money laundering, terrorist financing and financial crime are independently managed and controlled by the Financial Crime Compliance Department ("FCC"). Both LCO and FCC report directly to the CRO. As part of the Group's corporate governance framework, the policies for the management of legal and compliance risks, and money laundering, terrorist financing and financial crime compliance risks are approved by the RMC as delegated by the Board.

Strategic risk management

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

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

Capital management

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

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

Stress testing

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

BOC Life

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

Insurance risk management

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

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

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

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

Interest rate risk management

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

Liquidity risk management

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

Credit risk management

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

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

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

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

Equity price risk management

BOC Life's equity price risk refers to the risk of loss due to volatility of market price in equity securities, equity funds, private equity and real asset. 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

BOC Life's 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.

Greater Bay Area Development

Corporate Information

Board of Directors

Chairman

CHEN Siqing#	(appointment as Chairman effective from 30 August 2017)
TIAN Guoli#	(resignation effective from 16 August 2017)

Vice Chairman

GAO Yingxin	(re-designation as Executive Director and appointment as Vice Chairman effective from 1 January 2018)
YUE Yi	(resignation effective from 1 January 2018)

Directors

REN Deqi#
LI Jiuzhong
CHENG Eva*
CHOI Koon Shum*
KOH Beng Seng*
TUNG Savio Wai-Hok*
XU Luode# (resignation effective from 11 June 2017)

Non-executive Directors
* Independent Non-executive Directors

Senior Management

Chief Executive

GAO Yingxin	(appointment effective from 1 January 2018)
YUE Yi	(resignation effective from 1 January 2018)

Chief Risk Officer

LI Jiuzhong

Deputy Chief Executives

YUAN Shu
LIN Jingzhen (resignation effective from 1 February 2018)

Chief Operating Officer

ZHONG Xiangqun

Chief Financial Officer

SUI Yang

Deputy Chief Executive

KUNG YEUNG Ann Yun Chi

Company Secretary

LUO Nan

Registered Office

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

Auditor

Ernst & Young

Share Registrar

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

ADR Depositary Bank

Citibank, N.A.
388 Greenwich Street
23rd Floor
New York, NY 10013
United States of America

Website

www.bochk.com

Board of Directors and Senior Management

DIRECTORS

Mr CHEN Siqing
Chairman

Aged 57, is currently the Chairman of the Board, the Chairman of the Nomination Committee and a member of the Remuneration Committee of the Company and BOCHK. He has been appointed as Non-executive Director of the Company and BOCHK since December 2011, Vice Chairman of the Company and BOCHK from March 2014 to August 2017 and Chairman of the Company and BOCHK since August 2017. He has also been appointed as the Chairman of BOC since August 2017 and was the Vice Chairman of BOC from April 2014 to August 2017. Mr CHEN was the President of BOC from February 2014 to August 2017. He is also a Director of BOC (BVI) and BOCHKG. Mr CHEN joined BOC in 1990 and worked in the Hunan Branch before he was seconded to the Hong Kong Branch of China and South Sea Bank Ltd. as Assistant General Manager. Mr CHEN held various positions in BOC from June 2000 to May 2008, including Assistant General Manager, Vice General Manager of the Fujian Branch, General Manager of the Risk Management Department of BOC and General Manager of the Guangdong Branch. He served as Executive Vice President of BOC from June 2008 to February 2014. Mr CHEN also served as the Chairman of the Board of Directors of BOC Aviation Limited from December 2011 to March 2018, which has been listed on Hong Kong Stock Exchange on 1 June 2016. Mr CHEN graduated from Hubei Institute of Finance and Economics in 1982 and obtained an MBA from Murdoch University, Australia in 1999. He is a Certified Public Accountant and holds the title of Senior Economist.

Mr GAO Yingxin

Vice Chairman and Chief Executive

Aged 55, has been re-designated as Executive Director and appointed as the Vice Chairman and Chief Executive of the Company and BOCHK since January 2018. He is also a member of the Strategy and Budget Committee. Mr GAO was a Non-executive Director and a member of the Risk Committee of the Company and BOCHK from March 2015 to December 2017. He was Executive Director of BOC from December 2016 to January 2018 and Executive Vice President of BOC from May 2015 to January 2018. Mr GAO was also the Deputy Chief Executive (Corporate Banking) of the Company and BOCHK from February 2005 to March 2015 and an Executive Director of the Company and BOCHK from May 2007 to March 2015. He has been appointed as Chairman of BOCHK Charitable Foundation, and Chairman of BOC Insurance (International) Holdings Company Limited with effect from 1 January 2018 and Chairman of BOC Life effective from 9 February 2018. On 1 January 2018, Mr GAO has been appointed as the designated representative of BOCHK to Hong Kong Association of Banks, member of Risk Management Committee of Hong Kong Exchanges and Clearing Limited, member of each of Banking Advisory Committee and Bank Notes Issue Advisory Committee, Chairman of Hong Kong Interbank Clearing Limited, as well as Vice Chairman of Board of Trustees of Ho Leung Ho Lee Foundation. He has been appointed as Chairman of Chinese Banking Association of Hong Kong since 15 January 2018, Chairman of Hong Kong Chinese Enterprises Association and Chairman of The Hong Kong Chinese Enterprises Charitable Foundation Limited since 19 January 2018, Vice President of The Hong Kong Institute of Bankers since 12 February 2018, member of Exchange Fund Advisory Committee since 20 February 2018, and member of General Committee of Hong Kong General Chamber of Commerce since 22 March 2018. He has been serving as Chairman of the board of directors of China Cultural Industrial Investment Fund Co., Ltd. in May 2015, Chairman of BOCI and Chairman of Bank of China (Luxembourg) S.A. in August 2015, Chairman of Bank of China (UK) Limited in October 2015 and Chairman of BOC International (China) Limited in September 2016. He is also Chairman of BOC Poverty Relief and Education Charity Fund Limited. Mr GAO was Chairman of NCB, Vice Chairman of NCB (China) and a Director of BOCG Insurance and resigned all the positions in March 2015. Before joining BOCHK, he was President and Chief Operating Officer of BOCI. Mr GAO joined BOC Group in 1986 where he began working on financing projects for various industries at BOC's Head Office in Beijing. In 1999, he became the General Manager of Corporate Banking at BOC Head Office where he was responsible for managing and building BOC Group's customer relationships with and global financing for multinational corporations and premium domestic clients in the Mainland of China. He was also in charge of BOC's major financing projects. Mr GAO graduated from the East China University of Science and Technology with a Master's Degree in Engineering in 1986. He holds the title of Senior Economist.

Mr REN Deqi

Non-executive Director

Aged 54, is a Non-executive Director, the Chairman of the Strategy and Budget Committee and a member of the Risk Committee of the Company and BOCHK. He is the Chairman of BOCCC since August 2017. He is also the President of Shanghai RMB Trading Unit of BOC. He has been serving as Executive Director of BOC since December 2016 and Executive Vice President of BOC since July 2014. Mr REN joined BOC in 2014. He worked in China Construction Bank ("CCB") for many years and held various positions. From October 2013 to May 2014, he served as General Manager of Risk Management Department of CCB. From August 2003 to October 2013, he successively served as Deputy General Manager of Credit Approval Department, General Manager of Risk Control Department, General Manager of Credit Management Department, and General Manager of the Hubei Branch of CCB. Mr REN received a Master's Degree in Engineering from Tsinghua University in 1988. He holds the title of Senior Economist.

Mr LI Jiuzhong

Executive Director

Aged 55, is an Executive Director of the Company and BOCHK. He has been the Chief Risk Officer of the Group since March 2010. He is in charge of the Group's overall risk management function, overseeing BOCHK's Risk Management Department, Legal & Compliance and Operational Risk Management Department, and Financial Crime Compliance Department. He is also the Chairman of BOC Thailand and a Director of BOCCC, BOC Insurance (International) Holdings Company Limited and BOC Life. He was a Director of NCB and NCB (China). Mr LI has over 30 years' experience in the banking industry. Mr LI joined BOC in 1983 and, since then, he has assumed various positions at BOC Head Office and overseas branch. He served as Assistant General Manager and became Deputy General Manager of BOC London Branch from 1996 to 2002, Deputy General Manager of Corporate Banking Department of BOC Head Office from 2002 to 2004, and also General Manager of Corporate Banking Department, Risk Management Department, and Global Markets Department of BOC Head Office from 2004 to 2009. Mr LI graduated from Northeast Petroleum University in 1983 with a Bachelor's Degree in Science in Oilfield Development and Management and obtained a Master's Degree in Science in International Banking and Financial Studies from Heriot-Watt University (UK) in 1993.

Mdm CHENG Eva

Independent Non-executive Director

Aged 57, is an Independent Non-executive Director and member of each of the Audit Committee and the Strategy and Budget Committee of the Company and BOCHK. She was the former Secretary for Transport and Housing of the Government of the HKSAR. She joined the government's Administrative Service in August 1983 and was posted to various bureaux and departments, including serving as the Permanent Secretary for Economic Development and Labour (Economic Development) and Commissioner for Tourism. She retired from the Government of the HKSAR on 30 June 2012. Mdm CHENG holds a Bachelor's Degree in Social Sciences from University of Hong Kong.

Dr CHOI Koon Shum

Independent Non-executive Director

Aged 60, is an Independent Non-executive Director, the Chairman of the Remuneration Committee, member of each of the Audit Committee and the Nomination Committee of the Company and BOCHK. Dr CHOI is the Chairman of Sunwah Group, Sunwah International Limited (listed in Toronto), Sunwah Kingsway Capital Holdings Limited (listed in Hong Kong) and Vietnam VinaCapital. He is also an Independent Non-executive Director of Hui Xian Asset Management Limited, the Manager of Hui Xian Real Estate Investment Trust (listed in Hong Kong). Dr CHOI has extensive experience in food industry, real estate development, international trade as well as technology and finance related business.

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

Mr KOH Beng Seng

Independent Non-executive Director

Aged 67, is an Independent Non-executive Director, the Chairman of the Risk Committee and member of each of the Audit Committee, the Remuneration Committee and the Nomination Committee of the Company and BOCHK. Mr KOH is currently the Chief Executive Officer of Octagon Advisors Pte Ltd, a business and management consulting company based in Singapore. He is also the Non-executive Chairman of Great Eastern Holdings Limited, a company listed in Singapore, and a Director of Hon Sui Sen Endowment CLG Limited. He was formerly a Director of Sing Han International Financial Services Limited, and was also an Independent Non-executive Director of Singapore Technologies Engineering Ltd and United Engineers Limited, companies listed in Singapore. Mr KOH was Deputy President of United Overseas Bank ("UOB") and a member of UOB's Executive Committee from 2000 to 2004. During this period, he was in charge of UOB's operations, delivery channels, information technology, corporate services, risk management and compliance functions. Prior to that, Mr KOH has spent over 24 years at the Monetary Authority of Singapore where he made significant contributions to the development and supervision of the Singapore financial sector in his capacity as Deputy Managing Director, Banking & Financial Institutions Group. He has also served as a Director of Chartered Semiconductor Manufacturing and as a part-time adviser to the International Monetary Fund. Mr KOH holds a Bachelor's Degree in Commerce from Nanyang University in Singapore and a Master's Degree in Business Administration from Columbia University in the United States.

Mr TUNG Savio Wai-Hok

Independent Non-executive Director

Aged 66, is an Independent Non-executive Director, the Chairman of the Audit Committee and member of each of the Remuneration Committee, the Nomination Committee, the Risk Committee and the Strategy and Budget Committee of the Company and BOCHK. Mr TUNG is currently the Chairman of Investcorp Technology Partners and Senior Advisor of Investcorp, he was the Chief Investment Officer and one of the founding partners of Investcorp. Mr TUNG was appointed a Director, a member of the Compensation Committee and the Cybersecurity Committee of Tech Data Corporation, a company listed on NASDAQ. Before joining Investcorp in 1984, he worked for Chase Manhattan Bank for about 11 years, holding various positions in its front, middle and back offices and served in its offices in New York, Bahrain, Abu Dhabi and London. Mr TUNG has served on the boards of many of Investcorp portfolio companies, including Club Car, Circle K, Saks Fifth Avenue, Simmons Mattresses, Star Market, and Stratus Computer. He is also a board member and treasurer of the Aaron Diamond AIDS Research Center, an affiliate of Rockefeller University. Mr TUNG holds a BSc in Chemical Engineering from Columbia University of New York, where he is also a trustee emeritus and a member of the Columbia University Medical Center Board of Visitors.

SENIOR MANAGEMENT

Mr YUAN Shu
Deputy Chief Executive

Aged 55, is the Deputy Chief Executive of the Group in charge of the financial market business, including Global Markets, Investment Management, Global Transaction Banking, Asset Management and other capital market-related businesses. He is a Director and Chairman of BOCI-Prudential Trustee, BOC Group Trustee Company Limited and Po Sang Securities and Futures Limited as well as a Director of BOC Insurance (International) Holdings Company Limited. He was also a Director of BOC Life. Mr YUAN has over 30 years of experience in the industry with solid professional expertise and management experience. He has held different positions in the financial market businesses at Head Office and in various overseas branches of BOC. Mr YUAN joined the Trading Department of BOC in 1983, then held positions in the Paris and Tokyo branches, as well as the Trading Department and Global Financial Markets Department of BOC Head Office. Mr YUAN was a Director (Trading) of the Global Financial Markets Department in 2006 and was promoted to General Manager (Trading) of the Financial Markets Unit in 2010. Prior to joining the Group as Deputy Chief Executive (Financial Markets), he served as the General Manager of the Hong Kong Branch, BOC, from December 2014. Mr YUAN graduated from Renmin University of China majoring in International Finance.

Mr ZHONG Xiangqun
Chief Operating Officer

Aged 48, is the Chief Operating Officer of the Group, overseeing the Bank-wide Operation Department, Information Technology Department, E-Finance Centre and Corporate Services Department. He is also a Director of BOCCC. Prior to joining the Group, Mr ZHONG served as General Manager of E-Finance Department of BOC in charge of the development of e-finance business, covering mobile payment, e-business, e-financing and big data application. Joining BOC in 1994, Mr ZHONG has held management positions in Information Technology Department, Personal Banking Unit, Card Centre and Innovation & Development Department, etc. He was a Director of China UnionPay and a Member of China Financial Standardization Technical Committee. Mr ZHONG has solid expertise in information technology and cyber security as well as practical business experience. Mr ZHONG graduated from Peking University with a Bachelor's Degree in Information Science specialised in Software and a Master's Degree in Applied Mathematics.

Mdm SUI Yang

Chief Financial Officer

Aged 44, is the Chief Financial Officer of the Group, overseeing Financial Management Department, General Accounting and Accounting Policy Department and Treasury. Mdm SUI is the Chairman of BOCHK Asset Management Limited. She was also a Director of NCB. Prior to joining the Group in August 2014, Mdm SUI served as Deputy General Manager of Financial Management Department of BOC. She joined BOC in April 1997 and assumed various positions in Finance & Accounting Department of BOC including Deputy General Manager of Management Information System ("MIS") Centre of BOC from September 2008 to March 2011, Assistant General Manager of MIS Centre of BOC from March 2007 to September 2008 and Assistant General Manager of MIS Centre and Finance & Accounting Department of BOC from August 2006 to March 2007. Mdm SUI possesses extensive knowledge and experience in financial management. She obtained a Master's Degree and a Bachelor's Degree in Economics from the Central University of Finance & Economics (formerly the Central Institute of Finance and Banking). Mdm SUI is a member of the Chinese Institute of Certified Public Accountants.

Mrs KUNG YEUNG Ann Yun Chi

Deputy Chief Executive

Aged 55, is the Deputy Chief Executive of the Group in charge of Personal Banking and Wealth Management Department, Personal Banking Risk and Integrated Management Department, Channel Management Department, Private Banking, BOCCC and BOC Life. She is also the Vice Chairman of BOCCC and a Director of BOC Insurance (International) Holdings Company Limited and BOC Life. Mrs KUNG joined BOCHK in August 2007 as Head of Channel Management. She was appointed as the Head of Personal Banking in April 2011, and was promoted to her current role in March 2015. Prior to joining the Group, Mrs KUNG had held various senior positions in Standard Chartered Bank (Hong Kong) Limited. With over 25 years of experience in the industry, Mrs KUNG possesses extensive knowledge in personal banking and a strong background in financial services. Mrs KUNG graduated from the University of Southern California in the United States of America where she obtained her Bachelor of Science Degree in Business Administration with a concentration in Accounting. In addition to business pursuits, Mrs Kung plays an active role in the business community and in public service in Hong Kong.

Report of the Directors

The Directors are pleased to present their report together with the audited consolidated financial statements of the Group for the year ended 31 December 2017.

Principal Activities

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

Business Review

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

Results and Appropriations

The results of the Group for the year are set out in the consolidated income statement on pages 127 to 128.

The Board has recommended a final dividend of HK$0.758 per share, amounting to approximately HK$8,014 million, subject to the approval of shareholders at the forthcoming annual general meeting to be held on Wednesday, 27 June 2018. If approved, the final dividend will be paid on Monday, 16 July 2018 to shareholders whose names appear on the Register of Members of the Company on Monday, 9 July 2018. Together with the interim dividend of HK$0.545 per share and the special dividend of HK$0.095 per share declared in August 2017, the total dividend payout for 2017 would be HK$1.398 per share.

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

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to attend and vote at the Annual General Meeting of the Company, from Thursday, 21 June 2018 to Wednesday, 27 June 2018 (both days inclusive), during which period no transfer of shares will be registered. In order to attend and vote at the Annual General Meeting of the Company, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, not later than 4:30 p.m. on Wednesday, 20 June 2018. The Annual General Meeting of the Company will be held at 2:00 p.m. on Wednesday, 27 June 2018.

Closure of Register of Members for Entitlement to Final Dividend

The Register of Members of the Company will be closed, for the purpose of determining shareholders' entitlement to the proposed final dividend, from Wednesday, 4 July 2018 to Monday, 9 July 2018 (both days inclusive), during which period no transfer of shares will be registered. In order to qualify for the proposed final dividend, shareholders should ensure that all transfer documents, accompanied by the relevant share certificates, are lodged with the Company's Share Registrar, Computershare Hong Kong Investor Services Limited, at Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, not later than 4:30 p.m. on Tuesday, 3 July 2018. Shares of the Company will be traded ex-dividend as from Friday, 29 June 2018.

Donations

Charitable and other donations made by the Group during the year amounted to approximately HK$20 million.

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

Shares Issued

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

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

Debentures Issued

During the year, BOCHK issued the following debentures to raise funds for general working capital purpose.

Class	Amount issued	Consideration received
Senior notes	RMB9,000,000,000	RMB9,000,000,000

Distributable Reserves

Distributable reserves of the Company as at 31 December 2017, calculated under Part 6 of the Hong Kong Companies Ordinance, amounted to approximately HK$9,341 million.

Five-year Financial Summary

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

Directors

The list of Directors of the Company is set out on page 58. The biographical details of the Directors and senior management are set out on pages 59 to 65. The term of office for each Non-executive Director is approximately three years.

Mr CHEN Siqing was appointed as the Chairman effective from 30 August 2017. Mr GAO Yingxin has been re-designated from the Non-executive Director to the Executive Director and appointed as the Vice Chairman and Chief Executive effective from 1 January 2018. Mr XU Luode resigned as the Non-executive Director effective from 11 June 2017. Mr TIAN Guoli resigned as the Chairman and Non-executive Director effective from 16 August 2017. Mr YUE Yi resigned as the Vice Chairman, Executive Director and Chief Executive effective from 1 January 2018. The Board would like to express its sincere gratitude and the highest respect to Mr TIAN, Mr YUE and Mr XU for their valuable contributions during their tenure of office.

In accordance with Article 98 of the Articles of Association and pursuant to Code provision A.4.2 of the Corporate Governance Code, the terms of office of Mr REN Deqi, Mr KOH Beng Seng and Mr TUNG Savio Wai-Hok will expire at the forthcoming annual general meeting. All the retiring Directors being eligible, will offer themselves for re-election at the forthcoming annual general meeting.

Save for the list of Directors of the Company as set out on page 58, other directors of the Company's subsidiaries during the year ended 31 December 2017 are as follows:

ZHANG Qingsong*	YUAN Shu	ZHONG Xiangqun	SUI Yang
KUNG YEUNG Ann Yun Chi	CHAI Woon Chew	Chaiyuth SUDTHITANAKORN	CHAN Chi Fai
CHAN Hing Wah	CHAN Ka Pui	CHAN Lap Bong	CHAN Siu Ping Chordio
Chatchai VIRAMETEEKUL	CHENG Po Kee	CHEUNG Wing Shing Vincent	CHEW Lee Lin
CHU Wing Yiu	DATO' LOW Kian Chuan	DU Qiang	Eugene KHOO Kong Hooi
FUNG Pui Cheung	GUAN Xuefei	GWEE Siew Ping	HAN Jianchiu
HUANG Jinyue	KAN Wai Mun Carmen	Krish FOLLETT	KWONG Shu Ming
LAU Hon Chuen	LAU Tim	LEUNG Yuen Hong	LI Feng
LI Jun	LI Siu Ling	LIU Guizhen	LIU Hui Jun
LIU Min	LIU Yalin	LO Kin Wing Terry	LO Ping Wa
LO Wai Man Mary	MOK Chung Man	Neil Anthony TORPEY	NG Chor Chu
NG Leung Sing	QIU Hengchang	SHEN Hua	SHING Sze Yee
SUN Dawei	SZE Ying Tat	TANG Fong Chai Francis	TSANG Kam Yin Wendy
WANG Hongwei	WANG Jian	WANG Tong	WANG Yunchao
WONG Chun Keung	WONG Kine Yuen	WONG Man Chiu	WONG Man Yee
WU Lin	WU Shiqiang	YIP Kwun Hung	ZHANG Zhao
DATUK TER Leong Yap*	HU Haozhong*	SHUM Wai Chun*	SO Pui Sheung*
YANG Ruhai*	ZENG Xiaoping*	ZHANG Lei*	CHAN Yiu Fai#
CHEN Zhong Xin#	CHEUNG Wai Hing#	FAN Wing Yu Winnie#	FU Kim#
FUNG Chi Lap#	HUANG Ling#	LEE Hoi Yin, Stephen#	SO Shing Shun#
TAN Wan Chye#	TSE Siu Ling#	WONG Chek Ming#	WONG Siu Man#
WOO Chia Wei#	YIP Man Kai#	YU Kwok Chun#	

* Resigned/ceased as a director of the relevant subsidiary(ies) during the year.
# Directors of the subsidiaries that were disposed/dissolved during the year.

Directors' Service Contracts

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

Directors' Interests in Transactions, Arrangements or Contracts

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

Directors' Interests in Competing Business

Mr CHEN Siqing and Mr REN Deqi are Executive Directors of BOC. Mr GAO Yingxin was the Executive Director of BOC (he resigned such position with effect from 24 January 2018). During the year, Mr TIAN Guoli was the Executive Director of BOC and Mr XU Luode was Executive Vice President of BOC.

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

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

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

Directors' Rights to Acquire Shares

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

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

As at 31 December 2017, the interests and short position of the 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)

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

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

All the interests stated above represented long positions. Save as disclosed above, as at 31 December 2017, none of the Directors, Chief Executive or their respective associates had any interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register required to be kept by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

Interest of Substantial Shareholders

The register maintained by the Company pursuant to section 336 of the SFO recorded that, as at 31 December 2017, the following parties had the following interests (as defined in the SFO) in the Company set opposite their respective names:

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

Notes:

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

All the interests stated above represented long positions. Apart from the disclosure above, according to the register maintained by the Company pursuant to section 336 of the SFO, BOCI Financial Products Limited had an interest in 143,522 shares which represented short positions. BOC and Central Huijin are deemed to be interested in such number of shares for the purpose of the SFO. Save as disclosed, no other interests or short positions were recorded in the register maintained by the Company under section 336 of the SFO as at 31 December 2017.

Management Contracts

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

Equity-linked Agreements

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

Permitted Indemnity Provision

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

Purchase, Sale or Redemption of the Company's Shares

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

Major Customers

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

Connected Transactions

The Independent Non-executive Directors have reviewed the transactions which the Company disclosed in a public announcement on 14 December 2016 and confirmed that these transactions were:

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

(ii) conducted on normal commercial terms or better; and

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

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

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

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

Auditor

The financial statements for the year 2017 have been audited by Ernst & Young who will retire and offer themselves for re-appointment at the 2018 annual general meeting.

On behalf of the Board

CHEN Siqing
Chairman
Hong Kong, 29 March 2018

Corporate Governance

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

The Company has been in full compliance with all code provisions as set out in the Corporate Governance Code contained in Appendix 14 of the Listing Rules except for Code provision E.1.2. Due to other business arrangement, Mr TIAN Guoli, the former Chairman of the Board who resigned on 16 August 2017, was unable to attend the annual general meeting held on 28 June 2017 and delegated Mr YUE Yi, the former Vice Chairman and Chief Executive of the Company who resigned on 1 January 2018, to chair the meeting of the Company. Due to other business arrangement, Mr TUNG Savio Wai-Hok, the Chairman of the Independent Board Committee, was unable to attend the extraordinary general meeting held on 28 June 2017 for approval of the continuing connected transactions and the new caps, which was attended by Mdm CHENG Eva and Mr KOH Beng Seng, other members of the Independent Board Committee. The Company also complies with nearly all the recommended best practices set out in the Corporate Governance Code. In particular, the Company publishes quarterly financial and business reviews so that shareholders and investors can be kept up to date of the performance, financial positions and prospects of the Company on a timely basis. BOCHK, the Company's wholly-owned and principal operating subsidiary, has followed the guidelines as set out in the Supervisory Policy Manual module CG-1 entitled "Corporate Governance of Locally Incorporated Authorised Institutions" ("SPM CG-1") issued by the HKMA. To further enhance corporate governance standard, the Company will revamp its corporate governance system and strengthen relevant measures by referencing to market trend as well as guidelines and requirements issued by regulatory authorities. The Company will continue to maintain sound corporate governance standards and procedures to ensure the completeness, transparency and quality of our information disclosure.

Corporate Governance Policy

Policy Statement

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

Essential Principles

(1) Eminent Board

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

(2) Prudent Risk Management

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

(3) Fair Remuneration System

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

(4) Effective Disclosure Mechanism

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

(5) Upholding Shareholders' Rights

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

(6) Safeguarding Stakeholders' Interests

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

(7) Sustainable Corporate Social Responsibility

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

(8) Pursuit of "Good to Great"

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

Policy Goal

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

Corporate Governance Framework

Responsibilities of the Board and Management

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

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

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

Roles of the Chairman and the Chief Executive

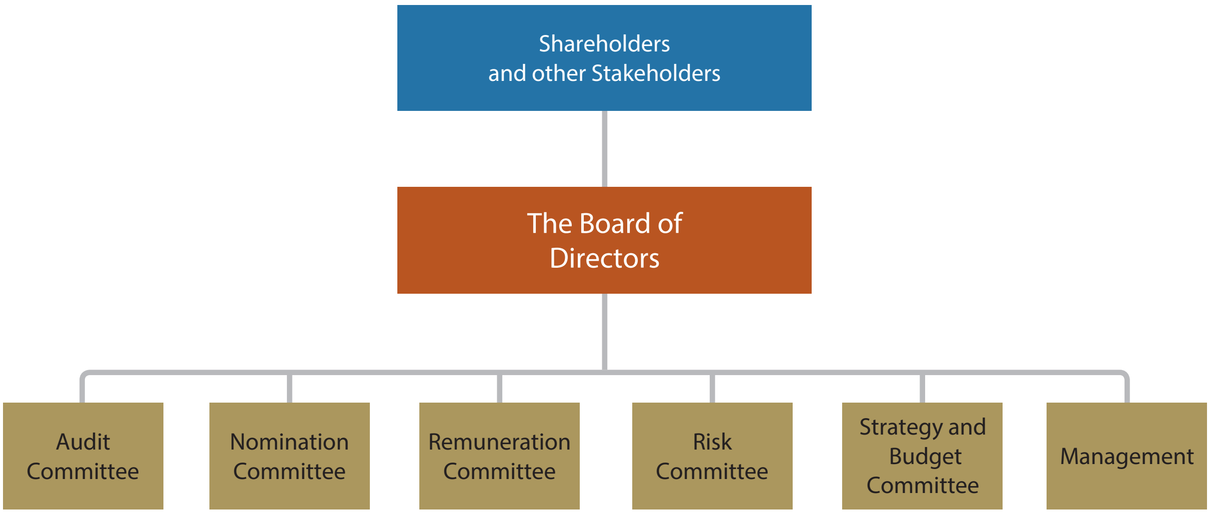
To avoid concentration of power in any single individual, the positions of the Chairman and the Chief Executive of the Company are held by two different individuals. Their roles are distinct, clearly established and stipulated in the Board's Mandate. In short, the Chairman is responsible for ensuring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

Board Committees

Based on the latest regulatory requirements, guidelines as well as market practices, the Board has established five standing Board Committees to assist in performing its responsibilities, namely the Audit Committee, the Nomination Committee, the Remuneration Committee, the Risk Committee, and the Strategy and Budget Committee. In addition, the Board will authorise an Independent Board Committee comprising all the Independent Non-executive Directors as and when required to review, approve and monitor connected transactions (including continuing connected transactions) in accordance with relevant rules and regulations that should be approved by the Board.

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

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



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

Board of Directors

Composition and Terms of Office of the Board

During the year and up to the date of this Annual report, the Board is composed of eight Directors, of whom two are the Executive Directors, two are the Non-executive Directors and four are the Independent Non-executive Directors. The Board maintains an appropriate level of checks and balances to ensure independence and objectivity of the decisions of the Board, as well as the impartial oversight of the Management. The Board acts honestly and in good faith so that decisions are made objectively with a view to delivering long-term and maximum shareholder value and fulfilling its corporate responsibility to other stakeholders of the Group.

Dr CHOI Koon Shum had been appointed as the Chairman of the Remuneration Committee effective from 1 April 2017; Mr TUNG Savio Wai-Hok ceased to be the Chairman of the Remuneration Committee, but remained as its member effective from 1 April 2017. Mr XU Luode resigned as the Non-executive Director and ceased to be a member of each of the Remuneration Committee and the Strategy and Budget Committee effective from 11 June 2017. Mr TIAN Guoli resigned as the Chairman of the Board and Non-executive Director and ceased to be the Chairman of the Nomination Committee effective from 16 August 2017; Mr CHEN Siqing had been appointed as the Chairman of the Board as well as the Chairman of the Nomination Committee effective from 30 August 2017. Mr YUE Yi resigned as the Vice Chairman, Executive Director and Chief Executive and ceased to be a member of the Strategy and Budget Committee effective from 1 January 2018; Mr GAO Yingxin had been re-designated from the Non-executive Director to the Executive Director, appointed as the Vice Chairman and Chief Executive and ceased to be a member of the Risk Committee effective from 1 January 2018, but remained as a member of the Strategy and Budget Committee. Save as disclosed above, there are no other changes to the composition of the Board and Board Committees during the year and up to the date of this Annual Report.

All the existing Non-executive Directors and Independent Non-executive Directors of the Company have been appointed for a fixed term of approximately 3 years, with formal letters of appointment setting out the key terms and conditions of their appointment. In accordance with Article 98 of the Articles of Association and pursuant to Code provision A.4.2 of the Corporate Governance Code, the terms of office of Mr REN Deqi, Mr KOH Beng Seng and Mr TUNG Savio Wai-Hok will expire at the forthcoming annual general meeting, and being eligible, offer themselves for re-election. Further details regarding the proposed re-election of Directors are set out in the section headed "Report of the Directors". In addition, the Company has also established a written and formal process for the appointment of the Independent Non-executive Directors to ensure that the appointment procedures are standardised, thorough and transparent.

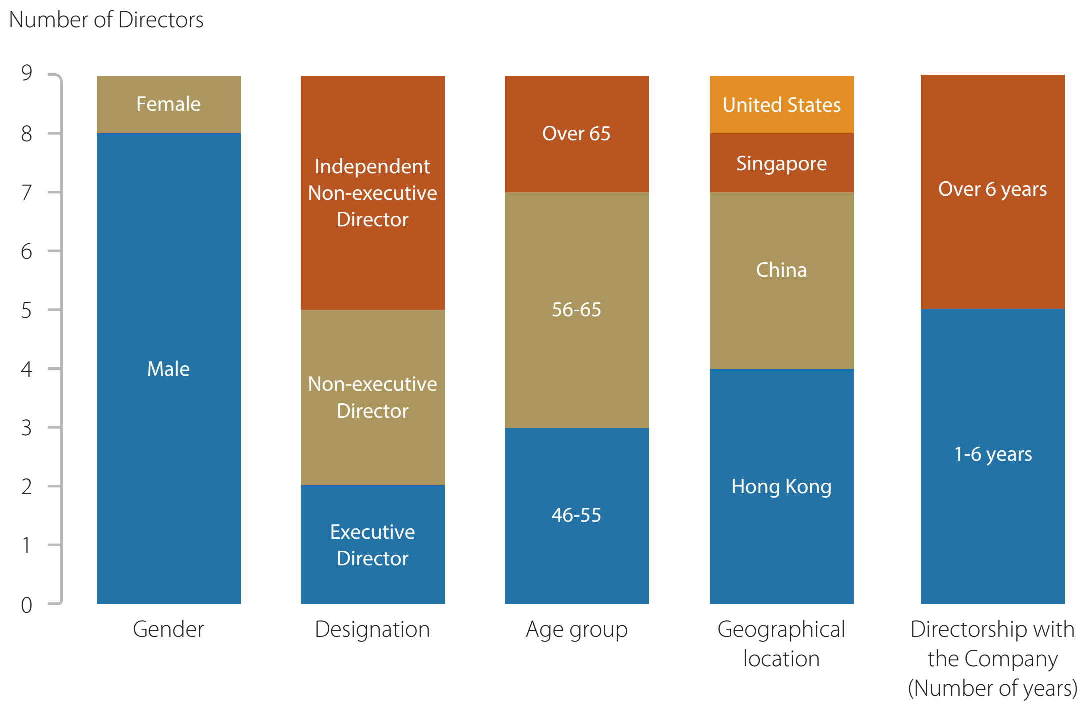
Selection, Diversity and Independence of the Board Members

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

The Nomination Committee shall be responsible for the identification, nomination and selection of Directors. Potential candidates of Executive Directors could be sourced and selected amongst the senior management. Potential candidates of Independent Non-executive Directors could be recruited through global selection. Pursuant to the provisions of the Company's Articles of Association and relevant regulations, shareholders could also nominate a person other than a retiring Director for election as a Director (including Non-executive Director) at a general meeting. Where necessary, the Nomination Committee may appoint external advisors to assist in recruiting appropriate individuals. The appointment of Directors shall be eventually approved by the Board and/or shareholders at general meetings.

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

An analysis of the Board Composition as at the year end is set out below:



Mr CHEN Siqing and Mr REN Deqi are the Executive Directors of BOC. Mr GAO Yingxin was the former Executive Director of BOC (he resigned such position with effect from 24 January 2018). During the year, Mr XU Luode was the Executive Vice President of BOC and Mr TIAN Guoli was the Executive Director of BOC (they resigned such positions with effect from 11 June 2017 and 16 August 2017 respectively). Save as disclosed above, there are no other relationships between the Board members, including financial, business, family or other material relationships.

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

Directors' Liability Insurance Policy

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

Directors' Training and Professional Development

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

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

During the year, all Directors have participated in continuous professional development to develop and refresh their knowledge and skills in accordance with Code provision A.6.5 of the Corporate Governance Code contained in Appendix 14 to the Listing Rules. In 2017, the Company invited experts to deliver seminars to the Directors and senior management with regard to introduction and implementation of risk adjusted return on capital, new requirements on bank culture reform, and case studies on anti-money laundering. Furthermore, each of the Directors has received a series of training locally or overseas as he/she thought fit, hosted or attended briefings, meetings, seminars, forums and conferences organised by the Company or various regulatory authorities, including a conference for independent non-executive directors and Fintech Day organised by the HKMA, a regulator's dialogue on the empowerment of independent non-executive directors in banking industry and cultivating bank culture organised by the HKMA and The Hong Kong Institute of Bankers as well as anti-corruption seminar for directors in banking industry presented by Independent Commission Against Corruption. Areas of relevant training included, among others:

- national policy outlook;
- risk management and internal control, environmental, social and governance reporting;
- business conduct, anti-corruption and ethical standards;
- anti-money laundering and sanctions case studies;
- functions of a board and roles, duties and liabilities of directors;
- corporate governance and bank culture reform;
- developments of financial technology;
- regulatory updates; and
- banking industry development trend, etc.

The Directors' records of annual training information have been entered in the register of directors' training records maintained and updated by the Company from time to time. As at year end, the participation of all Directors on continuous professional development is summarised as follows:

Directors Note	Business Conduct, Anti-Corruption and Ethical Standards/Corporate Governance	Risk Management and Internal Control/ Regulatory Updates	Banking Industry Development Trend and Global/National Economy
Non-executive Directors			
Mr CHEN Siqing	✔	✔	✔
Mr REN Deqi	✔	✔	✔
Independent Non-executive Directors			
Mdm CHENG Eva	✔	✔	✔
Dr CHOI Koon Shum	✔	✔	✔
Mr KOH Beng Seng	✔	✔	✔
Mr TUNG Savio Wai-Hok	✔	✔	✔
Executive Directors			
Mr GAO Yingxin *(re-designation from Non-executive Director to Executive Director effective from 1 January 2018)*	✔	✔	✔
Mr LI Jiuzhong	✔	✔	✔
Mr YUE Yi *(resignation as Executive Director effective from 1 January 2018)*	✔	✔	✔

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

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

Six Board meetings were held during 2017 with an average attendance rate of 92%. Regular meeting schedule for the year was prepared and approved by the Board in the preceding year. Formal notices of regular Board meetings were sent to all Directors at least 14 days before the date of the scheduled meetings and Board agenda and meeting materials were despatched to all Board members for review at least 7 days prior to the scheduled meetings. Board agendas were approved by the Chairman following consultation with other Board members and the senior management. In addition, in order to facilitate open discussion with all the Non-executive Directors and on their requests, the Chairman met with all the Non-executive Directors (including the Independent Non-executive Directors), in the absence of the Executive Directors and the senior management, during the discussion session before each Board meeting. Relevant practice has been incorporated in the Working Rules of the Board.

Details of respective Directors' attendance at the Board meetings, Board Committee meetings, annual general meeting and extraordinary general meeting in 2017 are set out as follows:

	Number of meetings attended/Number of meetings convened during Directors' term of office							
		Board Committees					General Meeting	
Directors Note	Board	Audit Committee	Nomination Committee	Remuneration Committee	Risk Committee	Strategy and Budget Committee	Annual General Meeting	Extraordinary General Meeting
Number of meetings held during the year	6	5	2	2	6	5	1	1
Non-executive Directors								
CHEN Siqing *(Chairman)*	5/6	–	2/2	2/2	–	–	1/1	1/1
GAO Yingxin *(re-designated as Executive Director and appointed as Vice Chairman and Chief Executive effective from 1 January 2018)*	5/6	–	–	–	5/6	3/5	1/1	1/1
REN Deqi	5/6	–	–	–	6/6	5/5	1/1	1/1
TIAN Guoli *(resigned effective from 16 August 2017)*	2/3	–	1/1	–	–	–	0/1	0/1
XU Luode *(resigned effective from 11 June 2017)*	2/2	–	–	1/1	–	2/2	–	–
Independent Non-executive Directors								
CHENG Eva	5/6	5/5	–	–	–	3/5	1/1	1/1
CHOI Koon Shum	6/6	3/5	2/2	2/2	–	–	0/1	0/1
KOH Beng Seng	6/6	5/5	2/2	2/2	6/6	–	1/1	1/1
TUNG Savio Wai-Hok	6/6	5/5	2/2	2/2	6/6	5/5	0/1	0/1
Executive Directors								
YUE Yi *(resigned effective from 1 January 2018)*	6/6	–	–	–	–	5/5	1/1	1/1
LI Jiuzhong	6/6	–	–	–	–	–	0/1	0/1
Average Attendance Rate	92%	92%	100%	100%	96%	86%	60%	60%

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

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

Board Committees

Audit Committee

The Audit Committee comprised 4 members at the end of the year, all of which are Independent Non-executive Directors. Its composition, main duties and major works performed during the year are as follows:

Composition

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

Main duties

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

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

- the Company's financial statements for the year ended 31 December 2016 and the annual results announcement that were recommended to the Board for approval
- the Company's interim financial statements for the six months ended 30 June 2017 and the interim results announcement that were recommended to the Board for approval
- the Company's announcements on quarterly financial and business review for the period ended 31 March 2017 and 30 September 2017 that were recommended to the Board for approval
- the audit reports and report on internal control recommendations submitted by external auditor, and the on-site examination reports issued by regulators
- the appointment of external auditor, the fees payable to external auditor for the annual audit, interim review and other non-audit services
- the Group's audit plan for next year and key areas identified
- the organisation structure, deployment of human resources and pay level of the Internal Audit, its budget for next year
- annual review of the effectiveness of the internal audit function
- the 2016 performance appraisal and key performance indicators for the General Manager of Group Audit and the Group Audit for next year
- the annual review of the effectiveness of the Group's risk control and internal control systems
- annual review of the "Policy on External Auditor Management", the "Policy on Staff Reporting of Irregularities" and the "Internal Audit Charter"

Nomination Committee

The Nomination Committee comprised 4 members at the end of the year, including 1 Non-executive Director and 3 Independent Non-executive Directors. Its composition, main duties and major works performed during the year are as follows:

Composition	Main duties
Mr CHEN Siqing[1] (Chairman) Dr CHOI Koon Shum[2] Mr KOH Beng Seng[2] Mr TUNG Savio Wai-Hok[2]	• review of overall human resources strategies of the Group • selection and nomination of Directors, Board Committee members and Senior Management • regular monitoring and review of structure, size and composition (including but not limited to gender, age, cultural and educational background, ethnicity, geographical location, professional experience, skills and knowledge, etc.) of the Board and Board Committees • review of the effectiveness of the Board and Board Committees • ensuring the participation in training and continuous professional development of Directors and Senior Management • regular review of code of conduct applicable to employees **Major works performed during the year (included the approval, review and proposal to the Board)** • consideration of the matters relating to the adjustment and appointment of Directors and Senior Management • consolidation of self-evaluation results of the Board and Board Committees, and putting forward recommendations to the Board to further enhance the functions and effectiveness of the Board and Board Committees • annual review on the "Policy on Independence of Directors"

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

Remuneration Committee

The Remuneration Committee comprised 4 members at the end of the year, including 1 Non-executive Director and 3 Independent Non-executive Directors. Its composition, main duties and major works performed during the year are as follows:

Composition

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

Main duties

- review and recommendation of remuneration strategy and incentive framework of the Group
- setting of the remuneration of Directors, Board Committee members, Senior Management and Key Personnel
- oversight of corporate culture of the Group

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

- formulation, review and amendment on the major human resources and remuneration policies
- review on Directors' remuneration
- performance appraisal result of the Executive Directors and Senior Management for year 2016
- proposal on staff bonus for year 2016 and salary adjustment for year 2017 for the Group, including the Senior Management
- remuneration relating to the appointment of the Senior Management
- key performance indicators of the Group and the Senior Management for year 2018
- proposal on human resources budget of the Group for year 2018
- annual review on the "Policy on Directors' Remuneration"
- implementation of the HKMA bank culture reform

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

Risk Committee

The Risk Committee comprised 4 members at the end of the year, including 2 Non-executive Directors and 2 Independent Non-executive Directors. Its composition, main duties and major accomplishments during the year are as follows:

Composition

Mr KOH Beng Seng[2] (Chairman)
Mr REN Deqi[1]
Mr GAO Yingxin[3]
Mr TUNG Savio Wai-Hok[2]

Main duties

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

Major works performed during the year

- review and approval of key risk management policies, including the Group's Risk Appetite, the "BOCHK Group Operating Principles", the "Risk Management Policy Statement of BOCHK Group", the "Capital Management Policy of BOCHK", the "BOCHK Group Financial Instruments Valuation Policy", the "Staff Code of Conduct", the "Policy for Validating Internal Rating Systems", the "Anti-Money Laundering and Counter-Terrorist Financing Policy of BOCHK Group", the "Product Development and Risk Monitoring Management Policy", the "Connected Transactions Management Policy", the "Sharing and Use of Credit Data Management Policy", the "Stress Test Policy of BOCHK" and stress test scenarios, and a range of risk management policies covering credit risk, market risk, liquidity risk, interest rate risk, operational risk, technology risk, legal, compliance and reputation risk, strategic risk, etc.
- review of the risk adjustment method for group bonus funding mechanics and the approval of the results of risk adjustment of BOCHK Group for 2016
- review and approval of the Group's operating plans, including the Group's target balance sheets, the BOCHK's banking book investment plans and portfolio key risk indicators, as well as risk management limits
- review and monitoring of Basel Accord implementation, including review of model validation reports, model performance reports, and receiving the status reports of the allocation of risk-weighted assets and update
- review of various risk management reports, including the Group's risk management reports and report on changes in interest rate and its impact on investment portfolio, etc.
- review and approval of significant high risk exposures or transactions

Notes:
1. Non-executive Director
2. Independent Non-executive Director
3. Non-executive Director during the year and re-designated as Executive Director with effect from 1 January 2018

Strategy and Budget Committee

The Strategy and Budget Committee comprised 5 members at the end of the year, including 2 Non-executive Directors, 2 Independent Non-executive Directors as well as the Chief Executive and Executive Director of the Company. Its composition, main duties and major works performed during the year are as follows:

Composition

Mr REN Deqi[1] (Chairman)
Mr YUE Yi[4]
Mr GAO Yingxin[3]
Mdm CHENG Eva[2]
Mr TUNG Savio Wai-Hok[2]

Main duties

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

Major works performed during the year

- review of the Group's capital injection to Southeast Asian institutions, including some key financial and risk indicators and capital provision methods for Board's approval
- review of the Group's proposal of setting up a branch in a country, focusing on the discussion of the feasibility and business development strategies for Board's approval
- review of the proposal of setting up subsidiaries and restructuring of the Group according to the strategy of overseas business development of the Group for Board's approval
- review of the proposals for acquisition of a targeted company in order to facilitate the restructurings of the Group's business segment for Board's approval
- review and monitoring of the implementation of 2017 Financial Budget and Business Plan of the Group, and also review and endorsement of the Financial Budget and Business Plan of the Group submitted by the Management for the year 2018 and recommendation of the same to the Board

Notes:
1. Non-executive Director
2. Independent Non-executive Director
3. Non-executive Director during the year and re-designated as Executive Director with effect from 1 January 2018
4. Executive Director during the year and resigned with effect from 1 January 2018

Directors' Securities Transactions

The Company has established and implemented the "Code for Securities Transactions by Directors" (the "Company's Code") to govern the Directors' dealings in securities transactions of the Company. Terms of the Company's Code are more stringent than the mandatory standards set out in the "Model Code for Securities Transactions by Directors of Listed Issuers" as contained in Appendix 10 of the Listing Rules. Apart from the securities of the Company, the Company's Code also applies to the Director's dealings in the securities of BOC and its subsidiary, BOC Aviation Limited, which have been listed on the Stock Exchange of Hong Kong since June 2006 and June 2016 respectively. Upon specific enquiry by the Company, all Directors confirmed that they had strictly complied with the provisions as set out in both the Company's Code and the said Model Code throughout year 2017.

Directors' Remuneration

Pursuant to the "Policy on Directors' Remuneration" adopted by the Company, when recommending the remuneration of Directors, the Remuneration Committee should benchmark against companies of comparable business type or scale, the role (chairmanship or membership) they played, job nature and workload at both the Board and Board Committee levels (including frequency of meetings and nature of agenda items) in order to compensate Directors fairly. The remuneration of Directors is subject to regular review based on market practices, regulatory requirements and inflation, etc. No individual Director is allowed to participate in the procedures for deciding his/her individual remuneration package. The remuneration of the Independent Non-executive Directors is not linked with the performance of the Company. Information relating to the remuneration of each Director for 2017 is set out in Note 20 to the Financial Statements. With the approval from the Annual General Meeting held on 28 June 2017, the basic Director's fee had increased to HK$400,000 p.a. The present scale of Director's fees, including additional fees for membership of Board Committees, is given below:

Board of Directors:	
All Directors	HK$400,000 p.a.
Board Committees:	
Chairman	HK$100,000 p.a.
Other Committee members	HK$50,000 p.a.

Note: For the year ended 31 December 2017, all Non-executive Directors (excluding Independent Non-executive Directors) have not received their Directors' fees as mentioned above and Executive Directors did not receive any fees for being members of the Board and its Committees.

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

Remuneration and Incentive Mechanism

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

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

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

  The Remuneration and Incentive Policy of the Group defines "Senior Management" and "Key Personnel" as follows:

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

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

- **Determination of the Remuneration Policy**

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

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

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

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

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

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

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

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

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

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

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

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

- **Annual Review of Remuneration Policy**

  The Remuneration Policy of the Group is subject to annual review with reference to changes on external regulatory requirements, market conditions, organisational structure and risk management requirements, etc. The "Policy on Directors' Remuneration" was reviewed and the Director's fee was adjusted in 2017 in response to regulatory requirements.

  Also, due to regional development needs, the Group reviewed the "BOCHK Group Remuneration and Incentive Policy", "BOCHK Group Variable Pay Deferral Policy", "BOCHK Group Bonus Funding Policy" and the identification criteria and position lists of "Key Personnel", "Risk Control Personnel" and etc. as delineated in the "BOCHK Group Remuneration and Incentive Policy" and the four regulated employee categories would be managed from a Group perspective. The reviewed policies would be implemented in all members of the Group in 2018.

- **External Remuneration Consultant**

  To ensure the suitability and competitiveness of the remuneration and incentive mechanism, the Group appointed Willis Towers Watson for independent consultation in areas of pay management of the Independent Non-executive Directors, Senior Management and key positions, regional remuneration management mechanics and market remuneration data, etc.

- **Disclosure on Remuneration**

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

External Auditor

Pursuant to the "Policy on External Auditor Management" adopted by the Board, the Audit Committee reviewed and monitored and was satisfied with the independence and objectivity of Ernst & Young, the Group's external auditor, and the effectiveness of its audit procedures, based on the principles and standards set out in the said Policy that were in line with international best practices. Upon the recommendation of the Audit Committee, the Board will propose that Ernst & Young be re-appointed as auditor of the Group at the Company's 2018 annual general meeting. Subject to shareholders' authorisation, the Board will authorise the Audit Committee to determine the remuneration of Ernst & Young. For 2017, the fee paid or payable by the Group to Ernst & Young was HK$39 million (2016: HK$44 million), of which HK$28 million (2016: HK$28 million) was for audit services and HK$11 million (2016: HK$16 million) related to other services (mainly including tax-related and advisory services). The Audit Committee was satisfied that the non-audit services in 2017 did not affect the independence of Ernst & Young.

Risk Management and Internal Control

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

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

The Group conducts an annual review of the effectiveness of its risk management and internal control systems covering all material controls, including financial, operational and compliance controls as well as risk management. The review is conducted by reference to the guidelines and definitions given by the regulatory and professional bodies for the purpose of assessing five different internal control elements, namely, the control environment, risk assessment, control activities, information and communication, and monitoring.

The assessment covers all the major internal controls and measures, including financial, operational and compliance controls as well as risk management functions. The review also considers the adequacy of resources, staff qualifications and experience and training of the Group's accounting, financial reporting and internal audit functions. The review is coordinated by the Group's internal audit which, after the Management and various business departments have performed their self-assessment and the Management has confirmed the effectiveness of the relevant systems, then carries out an independent examination and other post-assessment work on the review process and results. The results of the 2017 review, which have been reported to the Audit Committee and the Board, revealed that the Group's risk management and internal control systems were effective and adequate.

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

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

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

- the Group has various risk management and human resources policies. There are specific units and personnel that are responsible for handling reputation, strategic, legal, compliance, credit, market, operational, liquidity and interest rate risks. There are also procedures and internal controls for the handling and dissemination of inside information. The Group has set up mechanisms to identify, evaluate and manage all the major risks, and has established corresponding internal control procedures as well as processes for resolving internal control defects. (The Group's risk management is given on pages 50 to 55);

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

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

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

The Group is committed to upholding good corporate governance practices and the internal control system of all subsidiaries are reviewed regularly. During the year of 2017, continuous improvements on the organisation structure and segregation of duty, the risk management policy and procedure, and the enhancement of disclosure transparency have been undertaken by the Group. In response to internal and external changes in global economic condition, operating environment, regulatory requirement and business development, the Group has implemented a series of measures and undertaken an on-going review on the effectiveness of the internal control mechanism. In 2017, areas for improvement have been identified and appropriate measures have been implemented.

Communication with Shareholders

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

Mr YUE Yi (the Chairman of annual general meeting and extraordinary general meeting), Mr KOH Beng Seng (the Chairman of the Risk Committee) and Mr REN Deqi (the Chairman of the Strategy and Budget Committee) were present at the Company's 2017 annual general meeting and extraordinary general meeting held on 28 June 2017 at Four Seasons Grand Ballroom, Level 2, Four Seasons Hotel Hong Kong, 8 Finance Street, Central, Hong Kong, as well as Ernst & Young, the auditor, and Investec Capital Asia Limited, the independent financial adviser in connection with the continuing connected transactions, were also present at the Company's 2017 annual general meeting and extraordinary general meeting respectively, to respond to enquiries raised by shareholders. Mr TIAN Guoli (the former Chairman), Mr LI Jiuzhong, Dr CHOI Koon Shum and Mr TUNG Savio Wai-Hok were unable to attend the meetings due to other business engagements. Save as disclosed above, all other Directors including Mr CHEN Siqing, Mr GAO Yingxin and Mdm CHENG Eva were also present at the meetings. Resolutions passed at the Company's 2017 annual general meeting included: adoption of the Company's 2016 financial statements, declaration of 2016 final dividend, fixing of Directors' fees, re-election of Directors, re-appointment of auditor, the grant of general mandates to the Board to issue and buy back shares of the Company, and resolution was passed at the extraordinary general meeting to approve the continuing connected transactions and the new caps. Relevant voting results are available under the sub-section "Stock Exchange Announcements" of the section headed "Investor Relations" on the Company's website at www.bochk.com.

As disclosed in the 2016 Annual Report of the Company, in view of the investors' concern regarding the potential dilution of the shareholder value arising from the exercise of power pursuant to the grant of a general mandate to issue shares to the Board, the Board has voluntarily reduced the general mandate to issue shares of up to 5% of the total number of shares in issue as compared to the 20% limit permitted under the Listing Rules in the event that the issue of shares is for cash and not related to any acquisition of assets for approval by the shareholders at the 2017 annual general meeting. The Board would also recommend the threshold of up to 5% of the total number of shares in issue (subject to adjustment in case of any subdivision and consolidation of shares after the passing of the relevant resolution) at the 2018 annual general meeting for approval by shareholders. Further, given its commitment to high standards of corporate governance, the Board also adopted certain internal policies for the exercise of the powers granted to the Board under the general mandates to issue shares solely for cash and buy back shares. The relevant policies are summarised as follows:

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

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

All the resolutions to be proposed at the Company's 2018 annual general meeting will be voted on by poll. Accordingly, the Company will engage Computershare Hong Kong Investor Services Limited, the Company's Share Registrar, to act as the scrutineer for such purpose. The results of the poll voting will be posted on the Stock Exchange's website and the Company's website as soon as practicable following conclusion of the vote-counting for shareholders' information.

Besides, in order that shareholders can have a better understanding of the agenda items to be discussed at the 2018 annual general meeting and to encourage their active participation so that exchange of views and communication can be further enhanced, the Company has provided detailed information on the 2018 annual general meeting in a circular to shareholders which includes introduction to the proposed resolutions to be approved at the annual general meeting, information on the retiring Directors who are eligible for re-election, information on voting and other issues relating to the 2018 annual general meeting in the form of "Frequently Asked Questions".

Shareholders' Rights

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

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

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

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

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

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

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

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

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

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

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

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

Disclosure of Information

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

Directors' Responsibility Statement in relation to Financial Statements

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

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

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

Investor Relations

Investor Relations Policy and Guidelines

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

Investor Relations Programmes

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

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

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

Information Disclosure Policy

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

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

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

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

Access to Corporate Information

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

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

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

Overview of Investor Relations Activities in 2017

In 2017, the Company continued its efforts to provide effective channels for communication with the investment community.

Annual General Meeting

At the Annual General Meeting held in June 2017, the Vice Chairmen of the Board, the Chairmen and members of the Risk Committee and the Strategy and Budget Committee, members of the Audit Committee, the Nomination Committee and the Remuneration Committee respectively, the Company's senior management and external auditor were present to respond to questions and comments from shareholders. A total of 1,720 registered shareholders, 663 authorised corporate representatives and 740 authorised proxies holding an aggregate of 8,539,812,151 shares, representing 80.77% of the Company's total number of shares in issue, were present. Minutes of the 2017 Annual General Meeting were made available to shareholders on the Company's website.

Extraordinary General Meeting

At the Extraordinary General Meeting held in June 2017, the Vice Chairmen of the Board, the Chairmen and members of the Risk Committee and the Strategy and Budget Committee, members of the Audit Committee, the Nomination Committee and the Remuneration Committee respectively, the Company's senior management and the independent financial adviser in connection with the continuing connected transactions and the new caps were present to respond to questions and comments from shareholders. A total of 1,734 registered shareholders, 474 authorised corporate representatives and 631 authorised proxies holding an aggregate of 1,596,506,036 shares, representing 15.10% of the Company's total number of shares in issue, were present. All relevant connected persons abstained from voting on the resolution at the said meeting. Minutes of the Extraordinary General Meeting were made available to shareholders on the Company's website.

Results Announcements

At the Company's 2016 annual results announcement and 2017 interim results announcement, the senior management led by the Chief Executive conducted briefings with analysts and the press to apprise them of the Company's operating and financial results, business strategies and outlook. The presentation materials, announcements and webcasts were available to the public on the Company's website.

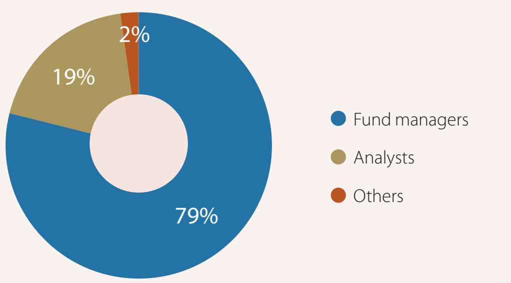
In addition to the interim and annual results announcements, the Company published quarterly financial and business reviews to keep shareholders up to date about the Company's performance and financial position.

Communication with the Investment Community

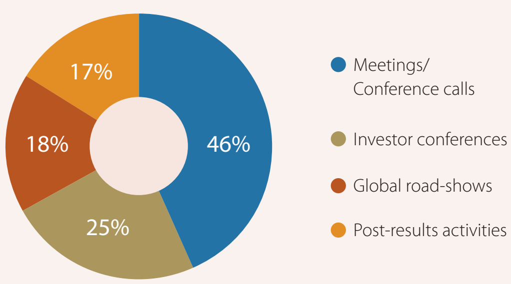
In 2017, the Company held approximately 190 meetings with investors and analysts across the world, with a total attendance of over 550. These meetings, which were conducted to give investors a better understanding of the Company's strategies and new business initiatives, were held during global road-shows, investor conferences, company visits and conference calls. The Company is widely covered by more than 15 securities research institutions. In order to expand investor base, optimise its geographical distribution and capture the increasing popularity of the Mutual Market Access programme between mainland and Hong Kong, the Company proactively conducted visits to institutional investors in the cities of China including Beijing, Shanghai and Shenzhen in addition to those based in New York, Boston, Tokyo and Singapore. These efforts were conducive to a higher institutional shareholding among mainland investors. As to promote market understanding of our regional development strategy, the Company also facilitated an investor group visit to our subsidiary in Malaysia which helped investors acquire a deeper knowledge about the implementation of the Company's strategy and its domestic subsidiary's operations.

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

Investor Meetings by Category



Investors Met by Event



Investor Relations

Going Forward

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

Investor Relations Contact

Enquiries can be directed to:

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

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

Shareholder Information

Financial Calendar 2018

Major Events	Dates
Announcement of 2017 annual results	29 March (Thursday)
Latest time for lodging transfers for entitlement to attend and vote at the 2018 Annual General Meeting	20 June (Wednesday) 4:30 p.m.
Book closure period (both days inclusive)	21 June (Thursday) to 27 June (Wednesday)
Latest time for lodging proxy forms for the 2018 Annual General Meeting	25 June (Monday) 2:00 p.m.
2018 Annual General Meeting	27 June (Wednesday) 2:00 p.m.
Last day in Hong Kong for dealing in the Company's shares with entitlement to final dividend	28 June (Thursday)
Ex-dividend date	29 June (Friday)
Latest time for lodging transfers for entitlement to final dividend	3 July (Tuesday) 4:30 p.m.
Book closure period (both days inclusive)	4 July (Wednesday) to 9 July (Monday)
Record date for final dividend	9 July (Monday)
Final dividend payment date	16 July (Monday)
Announcement of 2018 interim results	Mid to late August

Annual General Meeting

The 2018 Annual General Meeting will be held at 2:00 p.m. on Wednesday, 27 June 2018 at Grand Ballroom, The Lobby Floor, Grand Hyatt Hong Kong, 1 Harbour Road, Wan Chai, Hong Kong.

Share Information

Listing and Stock Codes

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

Market Capitalisation and Index Recognition

As at 29 December 2017, the Company's market capitalisation was HK$418.7 billion, among the top 20 leading stocks on the Main Board of Hong Kong Stock Exchange in terms of market capitalisation. Given the Company's market capitalisation and liquidity, its shares are a constituent of Hang Seng Index, MSCI Index and FTSE Index series. In addition, the Company is a constituent of Hang Seng Corporate Sustainability Index Series and Hang Seng High Dividend Yield Index, which recognises its performance in related areas.

Debt Securities

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

Subordinated Notes

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

Share Price and Trading Information

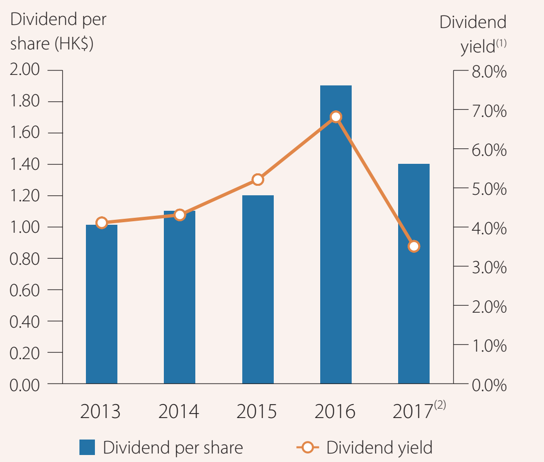
Share price (HK$)	2017	2016	2015
Closing price at year end	39.60	27.75	23.70
Highest trading price during the year	40.50	29.85	33.70
Lowest trading price during the year	27.65	18.82	22.30
Average daily trading volume (m shares)	11.63	11.55	12.75
Number of ordinary shares issued (shares)	10,572,780,266		
Public float	Approximately 34%		

Investor Relations

Dividends

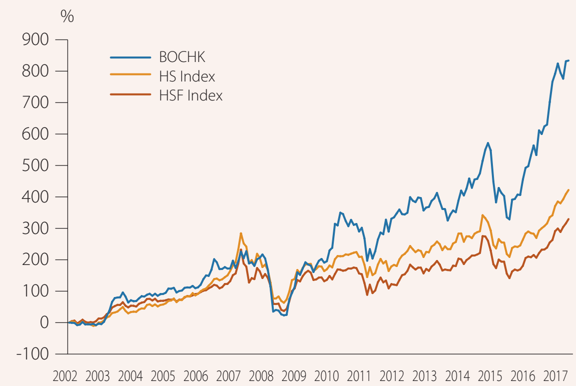
The Board of Directors has recommended a final dividend of HK$0.758 per share, which is subject to the approval of shareholders at the 2018 Annual General Meeting. With the interim dividend per share of HK$0.545 and the special dividend per share of HK$0.095 paid during 2017, the total dividend per share will amount to HK$1.398 for the full year.

Dividend Per Share and Dividend Yield[1]



(1) Annual dividend yield is calculated based on dividends of the year (i.e. interim dividend, special dividend and proposed final dividend of the year) and closing share price at that year-end.
(2) 2017 proposed final dividend will be subject to shareholders' approval at the Company's forthcoming Annual General Meeting.

Total Shareholder Return since Initial Public Offering



Source: Bloomberg

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

Credit Ratings (long-term)

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

Shareholding Structure and Shareholder Base

As at 31 December 2017, the Company had 10,572,780,266 shares in issue of which approximately 34% was held by the public and 0.35% was held in the form of ADSs. The Company's 75,554 registered shareholders were distributed in various parts of the world, including Asia, Europe, North America and Australia. Apart from BOC, the Company is not aware of any major shareholders with a shareholding of more than 5% which has to be reported under the SFO.

During the year, the shareholder structure of the Company remained stable. The following table shows the distribution of ownership according to the register of members which includes registered shareholders and shareholders recorded in the participant shareholding report generated from the Central Clearing and Settlement System as at 31 December 2017:

Category	Number of registered shareholders	% of registered shareholders	Number of shares held by registered shareholders	Approximate % of total issued shares
Individuals	75,426	99.83	225,405,334	2.13
Institutions, corporates and nominees Note	127	0.17	3,406,297,176	32.22
Bank of China Group Note	1	0.00	6,941,077,756	65.65
Total	75,554	100.00	10,572,780,266	100.00

Note:
As recorded in the register maintained by the Company pursuant to section 336 of the SFO, the total number of shares held by Bank of China Group was 6,984,274,213 shares, representing approximately 66.06% of the total number of shares in issue of the Company as at 31 December 2017. This figure included certain numbers of shares held for Bank of China Group in the securities account opened with BOCI Securities Limited, a participant of the Central Clearing and Settlement System. Accordingly, these shares are included under the category of 'Institutions, corporates and nominees'.

Shareholder Enquiries

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

Hong Kong	Computershare Hong Kong Investor Services Limited 17M Floor, Hopewell Centre 183 Queen's Road East, Wan Chai, Hong Kong	
	Telephone:	(852) 2862 8555
	Facsimile:	(852) 2865 0990
	E-mail:	hkinfo@computershare.com.hk
USA	Citibank, N.A. Shareholder Services P.O. Box 43077, Providence, Rhode Island 02940-3077, USA	
	Telephone:	1-877-248-4237 (toll free) 1-781-575-4555 (outside USA)
	E-mail:	citibank@shareholders-online.com

Other Information

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

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

People Centrism

CORPORATE SOCIAL RESPONSIBILITY

As a leading commercial banking group firmly rooted in Hong Kong for a century, we fully understand our responsibility for contributing to Hong Kong's long-term development, enhancing its status as an international financial centre and supporting the sustainable development of society. The Group attaches great importance to the needs and opinions of its various stakeholders and strives to deliver greater value to them. As the Group's regional development has deepened, we have extended our efforts to fulfil our corporate social responsibility (CSR) to where we operate, implementing a number of CSR initiatives that have been widely recognised by different sectors of the community.

The Company has been a constituent of the Hang Seng Corporate Sustainability Index for eight consecutive years and has been selected as a Top 20 Company in the Hong Kong Business Sustainability Index for three consecutive years, in recognition of the Group's performance in upholding the principles of sustainability and CSR initiatives. The Group has also been named a Caring Company by the Hong Kong Council of Social Service for 15 consecutive years since 2003.

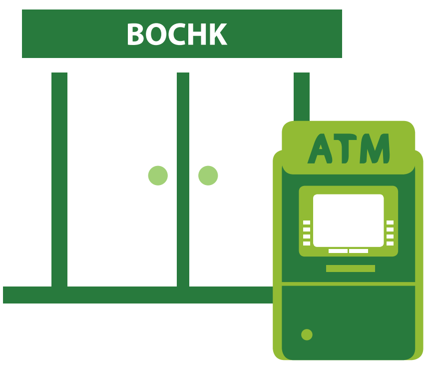
This section gives an overview of the Group's CSR initiatives during 2017. For details, please refer to the Group's CSR Report 2017.

Promoting Economic Development and Financial Inclusion

Leveraging our competitive business advantages, we strive to provide customers with comprehensive, professional and high-quality services. We are expanding our business in Southeast Asia so as to transform ourselves into an internationalised regional bank. We also actively support the country's Belt and Road Initiative and the Guangdong-Hong Kong-Macao Greater Bay Area development. In doing so, we give full play to Hong Kong's unique role as a "super-connector", firmly grasp the opportunities arising from "Leveraging Hong Kong's Advantages, Meeting the Country's Needs", thereby supporting the country's development while contributing to the reinforcement and enhancement of Hong Kong's status as an international financial centre.

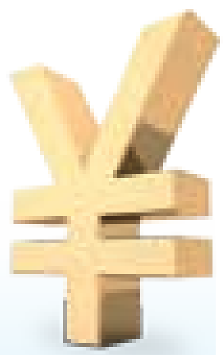
In addition, by adhering to the Group's customer-centric philosophy, we are committed to providing convenient banking and financing services to people from all walks of life through our service network that is the largest and most extensive in Hong Kong. This includes approximately 200 branches and over 1,000 self-service banking machines in more than 250 automated banking centres covering different districts of Hong Kong. At the same time, we are actively promoting the financial inclusion advocated by the HKMA.

approximately **200** branches and **>1,000** self-service banking machines in **>250** automated banking centres



To better serve the national Belt and Road Initiative, the Group organised and sponsored relevant seminars and meetings. This photo shows the second Belt and Road Summit co-organised by the Hong Kong Special Administrative Region (HKSAR) Government and the Hong Kong Trade Development Council and sponsored by the Group.

To support the development of the Guangdong-Hong Kong-Macao Greater Bay Area, we launched several convenient cross-border services, such as Cross-boundary Electronic Bill Presentment for Payment between Hong Kong and Guangdong Province, Cross-boundary Electronic Cheque and Tax Payment between Hong Kong and Shenzhen, the Guangdong-Hong Kong Business Registration and Banking Services Connect, and BOCHK Guangdong-Hong Kong Business Service Connect. This photo shows the launch ceremony of Guangdong-Hong Kong Business Registration and Banking Services Connect.



As the sole clearing bank for Hong Kong's RMB business, we organised training seminars for local RMB participating banks to facilitate communication and exchanges.

We provided special loan schemes for SMEs in line with the HKSAR Government's policies in supporting SMEs. We have received the Best SME's Partner Award from the Hong Kong General Chamber of Small and Medium Business for 10 consecutive years, thus enabling us to receive the Best SME's Partner Gold Award 2017 as well.

During the year, we launched an account bundling service with WeChat that allows customers to set their own mobile payment limits, providing them with a new mobile payment experience.

Our blockchain application on property valuation won the Gold Award of the Best Fintech (Emerging Solutions/ Payment Innovation) Award from the Office of the HKSAR Government Chief Information Officer and the Hong Kong Institute of Bankers.

We are a pioneer in providing "finger vein authentication" service at our branches and extended its use to ATMs for cash withdrawal, transfer and account balance inquiry, so as to provide customers with a safe and convenient experience.

We launched the BOC Caring Debit Card with the New Home Association and the Hong Kong Chinese Enterprises Association to provide services with preferential offers to the grassroots community.

Caring for Our People with People-oriented Philosophy

Guided by its people-oriented philosophy, the Group constantly strives to enhance its human resources management system and introduces various caring initiatives. We provide a competitive incentive and remuneration scheme as well as a harmonious, diverse and friendly working environment to our staff. In doing so, we continuously attract and nurture talent, and support our staff to realise their potential. As of the end of 2017, our diverse workforce had a total of 13,050 employees, with different experience and skills.

total of
13,050
employees

The Group is widely recognised for its human resources management. During the year, we won Gold Awards for Excellence in Talent Acquisition and Graduate Recruitment/Development from *Human Resources* magazine, the Best Employer Branding Award from *CTgoodjobs*, a subsidiary of the *Hong Kong Economic Times*, and a Silver Award from *LinkedIn* at the Transformation Awards 2017.

As part of our initiatives to nurture internationalised talent for the Group, management and key staff of our Southeast Asian institutions conducted exchanges in Hong Kong to learn about the best practices of its financial system.

To facilitate the growth and development of our staff, we arranged various training courses to enhance their professional skills.

We organised various recreational activities for our staff.

CORPORATE SOCIAL RESPONSIBILITY

Conserving Resources and Protecting the Environment

The Group encourages environmentally responsible business practices. Through energy reduction and the adoption of more energy-efficient use of resources, we aim to reduce the adverse environmental impact and related risks generated by the Group's operations, thereby promoting sustainable development. We also support the low-carbon economy and adhere to our green banking strategy. Through our management initiatives and active engagement in environmental protection activities of the Group, commercial and industrial sectors and the community, we endeavour to contribute to the reduction of the impact brought about by climate change.

approximately
1.1 million
customers opted to receive consolidated e-statements

As of the end of 2017, approximately 1.1 million customers opted to receive consolidated e-statements. The number of customers choosing e-statements increased by 27% compared with 2016.

The Group signed up to the *Charter on External Lighting* organised by the Environment Bureau (ENB) of the HKSAR Government for the second consecutive year in support of minimising energy wastage and light pollution, and received a Platinum Award from the ENB.

Since 2009, we have supported the WWF's Earth Hour initiative by turning off non-essential lighting in our main office buildings for one hour, helping to raise public awareness of energy saving.

Reduce Annual Electricity Consumption

↓194
gigawatt hours

= the electricity consumed by 21,555 average four-member households in one year

Annual Water Usage

↓730,000
tonnes

= the volume of 386 standard 50-metre swimming pools

Annual Waste

↓4 million
tonnes

= the weight of 14,285 Airbus A380s

Recycled Materials

>460,000
tonnes

= the weight of 30,666 double-decker buses

We jointly organised the BOCHK Corporate Environmental Leadership Awards Programme with the Federation of Hong Kong Industries. In 2017, corporate participants of the programme completed 1,388 green projects, collectively reducing the annual electricity consumption by more than 194 gigawatt hours (equivalent to the electricity consumed by 21,555 average four-member households in one year). Other collective achievements included lowering annual water usage by 730,000 tonnes (equivalent to the volume of 386 standard 50-metre swimming pools) and reducing annual waste by 4 million tonnes (equivalent to the weight of 14,285 Airbus A380s). In addition, almost 460,000 tonnes of materials were recycled (equivalent to the weight of 30,666 double-decker buses).

approximately
4,000 Kilograms
of recycled red packets

We sponsored the Red Packets Recycling Campaign, which received wide support from the public and our staff. During the year, we received an estimated weight of approximately 4,000 kilograms of recycled red packets.

Sharing and Caring

donated a sum of

HK$200million

to a total of 28 projects

Firmly rooted in Hong Kong, the Group is committed to caring for the community and building harmonious society, as well as providing assistance to those in need. We support a diverse range of community activities that promote the steady development of the community and bring positive energy to society. We place great value on community investment and are dedicated to giving back to society. By collaborating with various charitable organisations and industry associations, as well as encouraging our staff and their families and friends to participate in volunteer activities, we share the success of our corporate development with the community.

2017 marks the 20th anniversary of Hong Kong's return to the motherland and Bank of China's centenary of service to Hong Kong. BOCHK continued to uphold its mission of caring for society and stepped up its investment in charitable causes. During the year, BOCHK and BOCHK Charitable Foundation donated a sum of HK$200 million to a total of 28 projects.

As the Chairman Bank of the Hong Kong Association of Banks (HKAB), we fully supported HKAB in launching the Food for Love Project. This project offered job opportunities to people with disabilities to prepare nutritious and various kinds of food packs that were delivered by volunteers to the elderly and to low-income families. More than 10,000 people benefitted from the project.

For this special occasion, we launched four large-scale charitable projects that are influential to society:

We donated HK$100 million to the City University of Hong Kong to support the development of veterinary medicine and to promote the development of public health, animal disease research and food safety in Hong Kong. We also supported the university in hiring visiting professors in Veterinary Medicine and Life Sciences and set up scholarships for students participating in overseas exchange and internship programmes.

We donated HK$50 million to the Hong Kong Football Association to set up a community football fund and promote the BOCHK Community Football Partnership Programme, with the aim of encouraging participation in football by the youth at the grassroots level, thereby promoting local football development.

>400,000

hot meals were delivered

We supported Food Angel in setting up Food Station. During the year, over 400,000 hot meals and 510,000 food packages were delivered, benefitting some 1.58 million people in need.

Since 1990, the Group has been providing scholarships and bursaries amounting to HK$20 million to 10 tertiary institutions in Hong Kong, benefitting over 2,200 students.

We, together with other renowned organisations and philanthropists, donated a total of HK$20 million to set up the BOC Xianyang Four-county Education Fund. The Fund supports educational development by subsidising and encouraging students and teachers in four national-level poverty-stricken counties in Xianyang City of Shaanxi Province, namely Changwu, Yongshou, Xunyi and Chunhua.

A total of MYR5 million was donated to support the reconstruction of the school campus of Kuen Cheng High School in Kuala Lumpur, Malaysia, so as to provide students with a modernised learning environment and promote Chinese culture and the use of Chinese as a medium of instruction in school.

CORPORATE SOCIAL RESPONSIBILITY

We sponsored the Endeavour Education Centre to establish the Excellence Scholarship in Chinese History with an aim to encourage students to deepen their understanding of Chinese history. Furthermore, we supported a series of educational activities organised by the centre to facilitate a more comprehensive, accurate and thorough understanding of the country's development by the youth, thereby helping them establish correct understanding of history and the nation.

We organised visits to our branches for children participating in the Child Development Fund Scheme of the Labour and Welfare Bureau of the HKSAR Government, helping them to understand the banking facilities and services.

We sponsored the Hong Kong Island & Kowloon Regional Inter-school Sports Competitions. During the year, about 80,000 student enrolments in over 8,000 matches of 20 sports events were recorded.

about **80,000**
student enrolments in
> 8,000 matches

During the year, 615 students received training in the BOCHK Sports Volunteer Programme and contributed over 13,000 hours of volunteer service.

For eight consecutive years, we have sponsored the Hong Kong Corporate Citizenship Programme organised by the Hong Kong Productivity Council to encourage enterprises to fulfil their social responsibility. A total of 277 enterprises participated in the programme in 2017.

We encourage employees and their families and friends to serve the community and contribute to building socially inclusive society. In 2017, the BOCHK volunteer team spent nearly 50,000 hours on community service. The number of participation in community activities increased to 14,085, a 19% rise compared with 2016. Our volunteer service has been awarded the Gold Award for Volunteer Service by the Social Welfare Department of the HKSAR Government for eight consecutive years.

Awards and Recognition

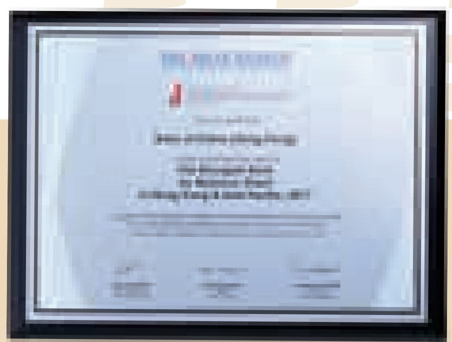
Given our solid financial strength and outstanding performance of our major businesses, we were granted various industry awards which have further reinforced our leading market positions. We were named the Bank of the Year in Hong Kong by *The Banker* in the UK and the Strongest Bank in Asia Pacific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

Financial Strength and Corporate Governance

- Bank of the Year in Hong Kong ***(The Banker)***
- Strongest Bank in Asia Pacific and Strongest Bank in Hong Kong ***(The Asian Banker)***
- Listed Company Award of Excellence (Blue Chip) ***(Hong Kong Economic Journal)***

The Banker
Bank of the Year 2017
HONG KONG

THE ASIAN BANKER
STRONGEST BANK
IN HONG KONG AND
ASIA PACIFIC 2014-2017
by balance sheet



Service Excellence

- Achievement Award for Best Trade Finance Bank in Hong Kong and Best Corporate Trade Finance Deal in Thailand ***(The Asian Banker)***
- Hong Kong Domestic Cash Management Bank of the Year, Hong Kong Mobile Banking Initiative of the Year, Hong Kong Digital Banking Initiative of the Year, Hong Kong Online Securities Platform of the Year and Hong Kong Domestic Foreign Exchange Bank of the Year ***(Asian Banking & Finance)***
- Rank No. 1 as mandated lead arranger in the Hong Kong and Macao syndicated loan market for 13 consecutive years ***(Basis Point)***
- Syndicated Corporate Deal of the Year ***(Asia Pacific Loan Market Association)***
- The Best SME's Partner Gold Award ***(The Hong Kong General Chamber of Small and Medium Business)***
- Outstanding Import & Export Industry Partner Award ***(The Hong Kong Chinese Importers' and Exporters' Association)***
- IT Governance Achievement Awards (Non-Public Sector) – Gold Award ***(Information Systems Audit and Control Association)***
- Best FinTech Gold Award (Emerging Solutions/Payment Innovation) and Best Smart Hong Kong (Digital Inclusion Application) – Certificate of Merit ***(Office of the Government Chief Information Officer)***
- Ten honours in the Outstanding Financial Management Planner Awards ***(The Hong Kong Institute of Bankers)***
- The Mystery Caller Assessment Gold Award and Banking – Best-in-Class Award ***(Hong Kong Call Centre Association)***
- Key Business Partner in FIC Market ***(Hong Kong Exchanges and Clearing Limited)***
- Offshore Investor Excellence Award ***(China Foreign Exchange Trading System)***
- Malaysian e-Payment Excellent Award 2017: Best Emerging IBG Bank ***(MyClear**, a subsidiary of Bank Negara Malaysia**)***
- Best Acquisition Financing Thailand of the Year ***(The Asset)***
- 2017 Claims Awards Asia-Pacific (Claims Innovation of the Year) – Winner ***(Insurance Post)***
- Cross Border Insurance Service – Excellence and Brand of the Year – Excellence ***(Bloomberg Businessweek)***
- The Hong Kong Leaders' Choice Brand Awards ***(Metro Finance)***:
  Excellent Brand of FinTech – Banking
  Excellent Brand of Corporate Banking Services
  Excellent Brand of Mobile Payment Services
  Excellent Brand of Mortgage Services – Banking
  Excellent Brand of Securities Services – Banking
  Excellent Brand of Personal Credit Card
  Excellent Brand of MPF Online Platform

Awards and Recognition

- Fund of the Year Awards 2017 ***(Benchmark)***:
  China Fixed Income of House Award – Best-In-Class
- Wealth Management Awards 2017 ***(Benchmark)***:
  The High Net Worth Team of the Year
  Client Engagement – Best-In-Class
  Outstanding Customer Support Team
- Wealth & Money Management Awards – Best China Financial Institutions 2017 ***(Wealth & Finance International)***
- Cross-border Banking Services Award ***(Sing Tao Daily)***
- Outstanding Wealth Management Service (Banking), Excellence Award for Dual Currency Credit Card Product and Excellence Award for Overseas Spending ***(Sky Post)***
- Outstanding Intelligent Personal Banking Services ***(ET Net)***
- My Favourite Travelling Credit Card Award ***(U Magazine)***
- ***MasterCard Worldwide:***
  The Highest Market Share of Cross-border Cardholder Spending Volume In Macau
  The Highest Market Share of Cardholder Spending In Macau
  The Highest Growth of Open Cards In Hong Kong - 1st Runner Up
  The Highest Market Share of Open Cards In Hong Kong - 1st Runner Up
- The Best Travel Prepaid Card in Malaysia ***(UnionPay International)***

RMB Business

- RMB Business Outstanding Awards ***(Metro Finance and Hong Kong Ta Kung Wen Wei Media Group)***:
  Outstanding Treasury Business – Dim Sum Bond Market Maker
  Outstanding Retail Banking – Cross-border Wealth Management Service
  Outstanding Retail Banking – Cross-border Mobile Payment Service
  Outstanding Corporate/Commercial Banking – Cross-border All-round Services
  Outstanding Retail Banking – Credit Card
  Outstanding Insurance – Universal Life
  Outstanding Insurance – Customer Service
- The Hong Kong Leaders' Choice Brand Awards ***(Metro Finance)***:
  Excellent Brand of RMB Banking Services
- Fund of the Year Awards 2017 ***(Benchmark)***: RMB Fixed Income of House Award – Outstanding Achiever

Social Responsibility

- Included as a constituent of the ***Hang Seng Corporate Sustainability Index*** and ***Hang Seng (Mainland and HK) Corporate Sustainability Index*** respectively, and a constituent of the ***Hang Seng Corporate Sustainability Benchmark Index***
- A top 20 constituent stock of the ***Hong Kong Business Sustainability Index***
- 15 Years Plus Caring Company Logo ***(The Hong Kong Council of Social Service)***
- Outstanding Corporate Social Responsibility Award ***(The Mirror)***
- Selected as a Junzi Corporation 2017 ***(Hang Seng Management College)***
- Platinum Award in the Charter on External Lighting Programme ***(Environment Bureau)***
- Excellence of Environmental Contribution ***(U Magazine)***

BOC Life:

- Social Capital Builder ***(Community Investment and Inclusion Fund of the Labour and Welfare Bureau)***
- Indoor Air Quality Certificate – Excellent Class ***(Environmental Protection Department)***

BOCCC:

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

Talent Development Management

- Excellence in Talent Acquisition Gold Award and Excellence in Graduate Recruitment/Development Gold Award ***(Human Resources)***
- Best Employer Branding Award ***(CTgoodjobs)***
- Transformation Award 2017 – Silver Award ***(LinkedIn HK)***
- The Top 20 Global General Counsel ***(Financial Times)***

BOC Life:

- Employer of Choice Award 2017 ***(JobMarket)***

Contact Us

Bank of China (Hong Kong)

Enquiry Hotline

Contents	Telephone
Personal Customer Service Hotline	(852) 3988 2388
24-hour *Wealth Management* Service Hotline	(852) 3988 2888
24-hour *Enrich Banking* Service Hotline	(852) 3988 2988
Corporate Customer Service Hotline	(852) 3988 2288

Contents	Telephone
BOC Credit Card Hotline	(852) 2853 8828
BOC Credit Card Loss Card Hotline	(852) 2544 2222
ATM Card Hotline	(852) 2691 2323
BOC Express Cash Customer Service Hotline	(852) 2108 3611

Branch Locator

www.bochk.com/en/branch.html

Internet Banking and Mobile Banking

Internet Banking:
www.bochk.com

Mobile Banking:

Social Media

BOCHK_Banking

BOCHK_CC

中銀香港BOCHK

www.youtube.com/user/bankofchinahk

Independent Auditor's Report

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

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

Opinion

We have audited the consolidated financial statements of BOC Hong Kong (Holdings) Limited (the "Company") and its subsidiaries (the "Group") set out on pages 127 to 281, which comprise the consolidated balance sheet as at 31 December 2017, and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2017, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and have been properly prepared in compliance with the Hong Kong Companies Ordinance.

Basis for opinion

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

Key audit matters

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

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

Key audit matters:	How our audit addressed the key audit matters:
Impairment assessment of advances to customers Refer to significant accounting policies in Note 2.14, critical accounting estimates and judgements in applying accounting policies in Note 3.1, and disclosures on credit risk and loan impairment allowances in Note 4.1 and Note 26 to the financial statements. As at 31 December 2017, gross advances to customers amounted to HK$1,144,459 million, representing 43.26% of total assets; and the impairment allowance for advances to customers amounted to HK$4,084 million. The assessment of impairment for advances to customers involved significant management judgements and estimates of the losses incurred within the loan portfolios at the reporting date. The Group adopted an individual impairment assessment approach in respect of individually significant loans or impaired loans; and a collective impairment assessment approach in respect of loans not individually significant or not individually impaired. Under the collective approach, the assessment of future cash flows for loan portfolios was based on the historical loss experience of loans with similar credit risk characteristics, with adjustments based on economic factors and judgemental overlays. Parameters associated with the historical loss experience included probability of default, loss given default and loss identification period.	We obtained an understanding of the Group's credit policy and evaluated and tested the design and the operating effectiveness of the key controls over the processes of credit assessment, loan classification and loan impairment assessment. Our control testing on the loan impairment process included the identification of impairment indicators and assessment of the assumptions used in the individual and collective impairment models. In assessing the individually assessed impairment allowances made by the Group, we adopted a risk-based sampling approach for our loan review procedures. We selected samples based on risk characteristics of individual items including the industry and geographic location of the operations of borrowers, internal loan grading and past due history. We formed an independent view on the classification of the loans and the level of provisions recognised by the Group through reviewing the borrowers' detailed information about their financial performance, recoverable cash flows and valuation of collaterals, as well as re-calculating samples of discounted cash flows for the impaired loans. We assessed the collective impairment model, data input and related management's assumptions on the impact of macro-economic trends and judgemental overlays for the various types of loan portfolios. We evaluated these assumptions by considering various factors including the period of historical data used in the model, observable economic data, market information and specific industry trends. We also performed testing on the relevant data quality by sample checking to the relevant data source and re-computed management's calculation of the collective impairment. Furthermore, we evaluated and tested the design and operating effectiveness of the Group's key controls related to disclosures on credit risk in Note 4.1 to the financial statements.

Key audit matters:	How our audit addressed the key audit matters:
Valuation of financial instruments Refer to significant accounting policies in Note 2.12, critical accounting estimates and judgements in applying accounting policies in Note 3.3, and disclosures on fair values of financial instruments in Notes 5.1 and 5.2 to the financial statements. The Group has applied valuation techniques to determine the fair value of financial instruments that are not quoted in active markets. These valuation techniques, in particular those that include significant unobservable inputs, involve management using subjective judgements and assumptions. With different valuation techniques and assumptions applied, the valuation results can vary significantly. As at 31 December 2017, the Group's financial assets and liabilities measured at fair value amounted to HK$693,849 million and HK$50,764 million respectively, representing 26.23% and 2.12% of total assets and total liabilities respectively. Financial instruments which had significant unobservable inputs in the valuation, and hence were categorised within level 3 of the fair value hierarchy, involved a higher degree of uncertainty in their valuation. As at 31 December 2017, 79.16% and 0.78% of the Group's financial assets measured at fair value were categorised within level 2 and level 3, respectively.	We evaluated and tested the design and operating effectiveness of key controls related to the valuation of financial instruments, including independent price verification, independent model validation and approval. We focused on the valuation methodologies and assumptions of financial instruments that were classified as level 2 and level 3 in the fair value hierarchy. We involved our valuation specialists in evaluating the valuation techniques, inputs and assumptions through comparison with the valuation techniques that are commonly used in the market, the validation of observable inputs using external market data, and comparison with valuation outcomes obtained from various pricing sources. We also evaluated and tested the design and operating effectiveness of the Group's key controls related to the fair value disclosures in Notes 5.1 and 5.2 to the financial statements.

Key audit matters:	How our audit addressed the key audit matters:
Recognition of deferred tax assets Refer to significant accounting policies in Note 2.23, critical accounting estimates and judgements in applying accounting policies in Note 3.6, and disclosures on deferred taxation in Note 37 to the financial statements. As at 31 December 2017, the Group recognised deferred tax assets of HK$549 million relating to temporary differences arising from impairment allowances and HK$1,147 million relating to other temporary differences and tax credits. The majority of other temporary differences and tax credits related to tax credits recoverable from the tax authorities in Hong Kong under double tax treaty arrangements, arising from withholding income taxes payable in other jurisdictions on certain income. Application on such tax credits will be made to the tax authorities in Hong Kong after the corresponding withholding income taxes payable is settled and evidenced by respective payment receipts issued from the corresponding tax authorities. These deferred tax assets, where required by accounting standards, were offset against and included within deferred tax liabilities as shown in Note 37 to the financial statements. The recognition of the deferred tax assets involved significant management judgements and assumptions, based upon the estimation of available tax credits and the possibility to recover such deferred tax assets recognised.	Our audit procedures included, amongst others, the involvement of our tax specialists to assist in evaluating the judgements and assumptions adopted by management to determine the recognition and recoverability of the deferred tax assets, in light of current tax laws. We also assessed management's estimates of the Group's entitlement to the tax credits and examined correspondences between the Group and relevant tax authorities. In addition, we also assessed the adequacy of disclosures in Note 37 to the financial statements with respect to compliance with HKAS 12 – Income Taxes.

Key audit matters:	How our audit addressed the key audit matters:
Valuation of insurance contract liabilities Refer to significant accounting policies in Note 2.19, critical accounting estimates and judgements in applying accounting policies in Note 3.5, and disclosures on insurance contract liabilities in Note 38 to the financial statements. As at 31 December 2017, the Group, through its consolidated subsidiary BOC Group Life Assurance Company Limited, had insurance contract liabilities amounting to HK$103,229 million, representing 4.30% of the Group's total liabilities. The measurement of insurance contract liabilities involved significant judgements over uncertain future outcomes, mainly the estimated ultimate total settlement value of insurance contract liabilities, including any guarantees provided to policyholders. Economic assumptions, such as investment return and associated discount rates, and operating assumptions, such as mortality and morbidity, were the key inputs used to estimate these insurance contract liabilities as reported in the consolidated balance sheet.	We used our actuarial specialists to assist in the performance of our audit procedures. These included a review of the product features and the methodology used in valuing the insurance contract liabilities in accordance with the relevant regulations and accounting requirements. We also tested the internal controls performed by management over the valuation process. We also assessed the economic assumptions and operating assumptions used in the insurance contract liabilities valuation with reference to market data and policyholder experience and assessed the accuracy of the calculation of policy reserves through performing independent recalculation. In addition, we assessed the validity of the Group's liability adequacy test under HKFRS 4 – Insurance Contracts. Our assessment included an evaluation of management's projected cash flows based on relevant product features. We tested the associated assumptions by comparing with industry experience data.

Other information included in the Annual Report

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

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

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

Responsibilities of the directors for the consolidated financial statements

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

The engagement partner on the audit resulting in this independent auditor's report is LEE Shun Yi, Jasmine.

Ernst & Young
Certified Public Accountants
Hong Kong, 29 March 2018

Consolidated Income Statement

For the year ended 31 December	Notes	2017 HK$'m	(Restated) 2016 HK$'m
CONTINUING OPERATIONS			
Interest income		**48,951**	36,776
Interest expense		**(14,243)**	(10,752)
Net interest income	6	**34,708**	26,024
Fee and commission income		**15,405**	14,932
Fee and commission expense		**(3,889)**	(4,248)
Net fee and commission income	7	**11,516**	10,684
Gross earned premiums		**21,792**	19,339
Gross earned premiums ceded to reinsurers		**(7,127)**	(8,705)
Net insurance premium income		**14,665**	10,634
Net trading gain	8	**1,326**	4,706
Net gain on financial instruments designated at fair value through profit or loss		**2,181**	101
Net gain on other financial assets	9	**1,163**	1,006
Other operating income	10	**931**	815
Total operating income		**66,490**	53,970
Gross insurance benefits and claims and movement in liabilities		**(25,881)**	(21,140)
Reinsurers' share of benefits and claims and movement in liabilities		**8,160**	9,765
Net insurance benefits and claims and movement in liabilities	11	**(17,721)**	(11,375)
Net operating income before impairment allowances		**48,769**	42,595
Net charge of impairment allowances	12	**(1,076)**	(601)
Net operating income		**47,693**	41,994
Operating expenses	13	**(13,703)**	(12,512)
Operating profit		**33,990**	29,482
Net gain from disposal of/fair value adjustments on investment properties	14	**1,197**	429
Net loss from disposal/revaluation of properties, plant and equipment	15	**(25)**	(14)
Share of profits less losses after tax of associates and joint ventures	28	**100**	74
Profit before taxation		**35,262**	29,971
Taxation	16	**(6,048)**	(4,768)
Profit from continuing operations		**29,214**	25,203
DISCONTINUED OPERATIONS			
Profit from discontinued operations	40	**2,623**	31,493
Profit for the year		**31,837**	56,696

Consolidated Income Statement

For the year ended 31 December	Notes	2017 HK$'m	(Restated) 2016 HK$'m
Profit attributable to:			
Equity holders of the Company			
– from continuing operations		**28,481**	24,574
– from discontinued operations	40	**2,589**	31,302
		31,070	55,876
Non-controlling interests			
– from continuing operations		**733**	629
– from discontinued operations	40	**34**	191
		767	820
		31,837	56,696
Dividends	17	**14,781**	19,877
		HK$	HK$
Earnings per share for profit attributable to equity holders of the Company			
Basic and diluted	18		
– profit for the year		**2.9387**	5.2849
– profit from continuing operations		**2.6938**	2.3243

The notes on pages 134 to 281 are an integral part of these financial statements.

Consolidated Statement of Comprehensive Income

For the year ended 31 December	Notes	2017 HK$'m	(Restated) 2016 HK$'m
Profit for the year		**31,837**	56,696
Items that will not be reclassified subsequently to income statement:			
Premises:			
Revaluation of premises	30	**2,129**	(135)
Deferred tax	37	**(298)**	311
		1,831	176
Items that may be reclassified subsequently to income statement:			
Available-for-sale securities:			
Change in fair value of available-for-sale securities		**1,967**	(104)
Release upon disposal of available-for-sale securities reclassified to income statement		**(1,107)**	(1,072)
Amortisation with respect to available-for-sale securities transferred to held-to-maturity securities reclassified to income statement		**63**	134
Deferred tax		**(85)**	179
		838	(863)
Currency translation difference		**459**	(210)
Release upon disposal of discontinued operations reclassified to income statement	40	**48**	(370)
		1,345	(1,443)
Other comprehensive income for the year, net of tax		**3,176**	(1,267)
Total comprehensive income for the year		**35,013**	55,429
Total comprehensive income attributable to:			
Equity holders of the Company		**34,085**	54,798
Non-controlling interests		**928**	631
		35,013	55,429

The notes on pages 134 to 281 are an integral part of these financial statements.

Consolidated Balance Sheet

As at 31 December	Notes	2017 HK$'m	(Restated) 2016 HK$'m
ASSETS			
Cash and balances with banks and other financial institutions	21	**364,205**	236,306
Placements with banks and other financial institutions maturing between one and twelve months	22	**59,056**	72,610
Financial assets at fair value through profit or loss	23	**93,194**	67,358
Derivative financial instruments	24	**33,541**	64,332
Hong Kong SAR Government certificates of indebtedness		**146,200**	123,390
Advances and other accounts	25	**1,189,609**	1,008,025
Investment in securities	27	**618,172**	593,650
Interests in associates and joint ventures	28	**417**	319
Investment properties	29	**19,669**	18,227
Properties, plant and equipment	30	**47,261**	45,812
Deferred tax assets	37	**58**	85
Other assets	31	**74,371**	71,333
Assets held for sale	40	**–**	53,293
Total assets		**2,645,753**	2,354,740
LIABILITIES			
Hong Kong SAR currency notes in circulation	32	**146,200**	123,390
Deposits and balances from banks and other financial institutions		**223,074**	198,933
Financial liabilities at fair value through profit or loss	33	**19,720**	13,371
Derivative financial instruments	24	**31,044**	49,304
Deposits from customers	34	**1,771,513**	1,519,867
Debt securities and certificates of deposit in issue	35	**21,641**	1,121
Other accounts and provisions	36	**52,967**	52,867
Current tax liabilities		**4,337**	3,095
Deferred tax liabilities	37	**5,704**	5,598
Insurance contract liabilities	38	**103,229**	86,534
Subordinated liabilities	39	**18,980**	19,093
Liabilities associated with assets held for sale	40	**–**	47,013
Total liabilities		**2,398,409**	2,120,186

As at 31 December	Notes	2017 HK$'m	(Restated) 2016 HK$'m
EQUITY			
Share capital	41	**52,864**	52,864
Reserves		**189,875**	175,783
Capital and reserves attributable to equity holders of the Company		**242,739**	228,647
Non-controlling interests		**4,605**	5,907
Total equity		**247,344**	234,554
Total liabilities and equity		**2,645,753**	2,354,740

The notes on pages 134 to 281 are an integral part of these financial statements.

Approved by the Board of Directors on 29 March 2018 and signed on behalf of the Board by:

CHEN Siqing

Director

GAO Yingxin

Director

Consolidated Statement of Changes in Equity

	Attributable to equity holders of the Company									
		Reserves								
	Share capital HK$'m	Premises revaluation reserve HK$'m	Reserve for fair value changes of available-for-sale securities HK$'m	Regulatory reserve* HK$'m	Translation reserve HK$'m	Merger reserve** HK$'m	Retained earnings HK$'m	Total HK$'m	Non-controlling interests HK$'m	Total equity HK$'m
At 1 January 2016, as previously reported	52,864	40,278	294	10,928	(346)	1,789	88,943	194,750	5,415	200,165
Effect of merger of entities under common control	–	–	2	–	(495)	3,455	661	3,623	–	3,623
At 1 January 2016, as restated	52,864	40,278	296	10,928	(841)	5,244	89,604	198,373	5,415	203,788
Profit for the year	–	–	–	–	–	–	55,876	55,876	820	56,696
Other comprehensive income:										
Premises	–	186	–	–	–	–	–	186	(10)	176
Available-for-sale securities	–	–	(705)	–	–	–	–	(705)	(158)	(863)
Currency translation difference	–	–	(16)	–	(173)	–	–	(189)	(21)	(210)
Release upon disposal of discontinued operations reclassified to income statement	–	–	(167)	–	(203)	–	–	(370)	–	(370)
Total comprehensive income	–	186	(888)	–	(376)	–	55,876	54,798	631	55,429
Acquisition of entities under common control	–	–	–	–	–	(4,076)	–	(4,076)	–	(4,076)
Transfer from retained earnings	–	–	–	539	–	2,287	(2,826)	–	–	–
Release upon disposal of discontinued operations	–	(4,856)	–	(2,240)	–	–	7,096	–	–	–
Dividends	–	–	–	–	–	–	(20,448)	(20,448)	(139)	(20,587)
At 31 December 2016	52,864	35,608	(592)	9,227	(1,217)	3,455	129,302	228,647	5,907	234,554
At 1 January 2017, as previously reported	**52,864**	**35,608**	**(592)**	**9,227**	**(722)**	**–**	**128,268**	**224,653**	**5,907**	**230,560**
Effect of merger of entities under common control	**–**	**–**	**–**	**–**	**(495)**	**3,455**	**1,034**	**3,994**	**–**	**3,994**
At 1 January 2017, as restated	**52,864**	**35,608**	**(592)**	**9,227**	**(1,217)**	**3,455**	**129,302**	**228,647**	**5,907**	**234,554**
Profit for the year	**–**	**–**	**–**	**–**	**–**	**–**	**31,070**	**31,070**	**767**	**31,837**
Other comprehensive income:										
Premises	**–**	**1,831**	**–**	**–**	**–**	**–**	**–**	**1,831**	**–**	**1,831**
Available-for-sale securities	**–**	**–**	**682**	**–**	**–**	**–**	**–**	**682**	**156**	**838**
Currency translation difference	**–**	**2**	**(58)**	**–**	**510**	**–**	**–**	**454**	**5**	**459**
Release upon disposal of discontinued operations reclassified to income statement	**–**	**–**	**10**	**–**	**38**	**–**	**–**	**48**	**–**	**48**
Total comprehensive income	**–**	**1,833**	**634**	**–**	**548**	**–**	**31,070**	**34,085**	**928**	**35,013**
Acquisition of entities under common control	**–**	**–**	**–**	**–**	**–**	**(6,618)**	**–**	**(6,618)**	**–**	**(6,618)**
Transfer from retained earnings	**–**	**–**	**–**	**1,156**	**–**	**3,163**	**(4,319)**	**–**	**–**	**–**
Release upon disposal of discontinued operations	**–**	**(752)**	**–**	**(159)**	**–**	**–**	**911**	**–**	**(2,078)**	**(2,078)**
Dividends	**–**	**–**	**–**	**–**	**–**	**–**	**(13,375)**	**(13,375)**	**(152)**	**(13,527)**
At 31 December 2017	**52,864**	**36,689**	**42**	**10,224**	**(669)**	**–**	**143,589**	**242,739**	**4,605**	**247,344**

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

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

The notes on pages 134 to 281 are an integral part of these financial statements.

Consolidated Cash Flow Statement

For the year ended 31 December	Notes	2017 HK$'m	(Restated) 2016 HK$'m
Cash flows from operating activities			
Operating cash inflow/(outflow) before taxation	42(a)	**138,522**	(68,917)
Hong Kong profits tax paid		**(4,703)**	(4,497)
Overseas profits tax paid		**(383)**	(531)
Net cash inflow/(outflow) from operating activities		**133,436**	(73,945)
Cash flows from investing activities			
Additions of properties, plant and equipment		**(1,523)**	(1,545)
Proceeds from disposal of properties, plant and equipment		**13**	2
Additions of investment properties	29	**(13)**	(6)
Proceeds from disposal of investment properties		**2**	–
Dividend received from associates and joint ventures	28	**2**	2
Acquisition of entities under common control		**(6,618)**	(4,076)
Net cash inflow from disposal of discontinued operations	40	**810**	26,992
Net cash (outflow)/inflow from investing activities		**(7,327)**	21,369
Cash flows from financing activities			
Dividend paid to equity holders of the Company		**(13,375)**	(20,448)
Dividend paid to non-controlling interests		**(152)**	(139)
Repayment of subordinated liabilities	42(b)	**(16)**	–
Interest paid for subordinated liabilities	42(b)	**(595)**	(478)
Net cash outflow from financing activities		**(14,138)**	(21,065)
Increase/(decrease) in cash and cash equivalents		**111,971**	(73,641)
Cash and cash equivalents at 1 January		**249,574**	322,083
Effect of exchange rate changes on cash and cash equivalents		**16,399**	1,132
Cash and cash equivalents at 31 December	42(c)	**377,944**	249,574

The notes on pages 134 to 281 are an integral part of these financial statements.

Notes to the Financial Statements

1. Principal activities

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

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

2. Significant accounting policies

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

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

2.1 Basis of preparation

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

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

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

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(a) Standards and amendments issued that are already mandatorily effective for accounting periods beginning on 1 January 2017

Standards/ Amendments	Content	Applicable for financial years beginning on/after	Currently relevant to the Group
HKAS 7 (Amendment)	Statement of Cash Flows: Disclosure Initiative	1 January 2017	Yes
HKAS 12 (Amendment)	Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses	1 January 2017	No

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

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2017

Standards/ Amendments/ Interpretations	Content	Applicable for financial years beginning on/after	Currently relevant to the Group
HKAS 28 (2011) and HKFRS 10 (Amendments)	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	To be determined	Yes
HKAS 28 (2011) (Amendment)	Long-term Interests in Associates and Joint Ventures	1 January 2019	Yes
HKAS 40 (Amendments)	Transfer of Investment Property	1 January 2018	Yes
HKFRS 2 (Amendment)	Share-Based Payment: Classification and Measurement of Share-Based Payment Transactions	1 January 2018	No
HKFRS 4 (Amendments)	Applying HKFRS 9 Financial Instruments with HKFRS 4 Insurance Contracts	1 January 2018	No
HKFRS 9	Financial Instruments	1 January 2018	Yes
HKFRS 9 (Amendments)	Financial Instruments: Prepayment Features with Negative Compensation	1 January 2019	Yes
HKFRS 15	Revenue from Contracts with Customers	1 January 2018	Yes
HKFRS 16	Leases	1 January 2019	Yes
HKFRS 17	Insurance contracts	1 January 2021	Yes
HK(IFRIC) – Int 22	Foreign Currency Transactions and Advance Consideration	1 January 2018	Yes
HK(IFRIC) – Int 23	Uncertainty over Income Tax Treatments	1 January 2019	Yes

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

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

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2017 (continued)

- HKAS 28 (2011) (Amendment), "Long-term Interests in Associates and Joint Ventures". The amendment clarifies that long-term interests such as preference shares or shareholder's loans, to which the equity method shall not be applied, are in the scope of both HKFRS 9 and HKAS 28 and explains that HKFRS 9 is applied independently before the allocation of losses under equity method. The amendments are to be applied retrospectively, early application is permitted. The application of this amendment will not have a material impact on the Group's financial statements.

- HKAS 40 (Amendments), "Transfer of Investment Property". The amendments clarify that there must be a change in use when a property is transferred to or from investment properties. A change in use would involve an assessment of whether a property meets, or has ceased to meet, the definition of investment property; and supporting evidence that a change in use has occurred. The amendments are to be applied retrospectively or prospectively, early application is permitted. The requirements of these amendments are consistent with the Group's current practice and will not have a material impact on the Group's financial statements.

- HKFRS 4 (Amendments), "Applying HKFRS 9 Financial Instruments with HKFRS 4 Insurance Contracts". The amendments address concerns arising from the different effective dates of HKFRS 9 and the forthcoming insurance contracts standard, early application is permitted. The amendments introduce the following two approaches:

  - **Deferral approach – Temporary exemption from HKFRS 9**

    Entities whose activities are predominantly connected with insurance may choose to defer the application of HKFRS 9 until 2021. Entities that defer the application of HKFRS 9 will continue to apply HKAS 39.

  - **Overlay approach**

    All entities that issue insurance contracts may choose to recognise in other comprehensive income, rather than income statement, the volatility that could arise when HKFRS 9 is applied before the new insurance contracts standard is issued.

  The Group assessed the financial impact and decided to apply HKFRS 9 consistently to all entities in the Group.

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2017 (continued)

- HKFRS 9, "Financial Instruments". The issuance of IFRS 9 "Financial Instruments" completes the International Accounting Standards Board's comprehensive response to the financial crisis. HKFRS 9, the equivalent standard of IFRS 9 under HKFRS, includes a logical model for classification and measurement, a single, forward-looking "expected loss" impairment model and a tighter linkage of risk management to hedge accounting. Except for hedging accounting, which is generally applied prospectively, retrospective application is required but with no compulsory requirement to provide comparative information.

  The Group adopts the new standard from 1 January 2018 onward and will not restate comparative information. The Group also early adopts the amendments related to "Prepayment Features with Negative Compensation", together with the Group's first time application of the core part of HKFRS 9 as a whole, which is mandatorily effective for reporting periods beginning on or after 1 January 2019 with earlier application permitted. The amendments specify that a financial asset containing prepayment features with negative compensation can be measured at amortised cost or at fair value through other comprehensive income if they meet the other relevant requirements of HKFRS 9. Moreover, the amendments clarify, for financial liabilities that are modified or exchanged that do not lead to derecognition, the accounting treatment is consistent with that required for modifications of financial assets.

  Steering Committee has been established to oversee the implementation of the standard. Groupwide project team has also been formed to assess the impact, formulate the work plan, and implement the below all three aspects of the standard. The development of expected credit losses (ECL) models has been completed and parallel run was performed during the second half of 2017 to enable the Group a better understanding of the potential effect of HKFRS 9 and to be familiar with the new governance and operational processes. The adoption of HKFRS 9 is expected to reduce net assets at 1 January 2018 by HK$2.5 billion, with changes in classification and measurement requirements reducing net assets by HK$1.5 billion and changes in impairment requirements reducing net assets by HK$1.0 billion, all net of tax. After applying regulatory transitional arrangement, the Group's total capital ratio is expected to decrease by around 10 basis points. The above overall financial impact is subject to change of assumptions, judgement and estimates to be finalised in the accounts of 2018. The changes introduced in HKFRS 9 for each of the aspects are highlighted as follows:

  (i) Classification and Measurement

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

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2017 (continued)

(i) Classification and Measurement (continued)

The classification and measurement requirements of financial liabilities have been basically carried forward with minimal amendments from HKAS 39.

The accounting for fair value option of financial liabilities were changed to address own credit risk. The amount of change in fair value attributable to change in credit risk of financial liabilities will be presented in other comprehensive income while the remaining amount of change in fair value will be included in the income statement. The amount recognised in other comprehensive income will not be subsequently reclassified to the income statement but may be transferred within equity.

There is no change in HKFRS 9 to allow designation of financial instruments at fair value through profit or loss to eliminate or significantly reduce measurement or recognition inconsistencies upon initial application.

The Group has performed a detailed analysis on financial assets and financial liabilities. As a result, the Group has reclassified its financial assets based on its business model and the contractual cash flow characteristics of financial assets. The Group has also decided to apply the fair value option to reclassify the subordinated notes issued from measured at amortised cost to measured at fair value through profit or loss. The related fair value hedge will be ceased accordingly. The difference arising from the initial application of new classification and measurement requirements will be recognised in retained earnings.

(ii) Impairment

The standard introduces a new, expected-loss impairment model that will require more timely recognition of expected credit losses. The impairment for financial instruments that are subsequently measured at amortised cost, fair value through other comprehensive income (debt instruments), irrevocable loan commitments and financial guarantee contracts will be governed by this standard. Specifically, it requires entities to assess credit risk and estimate ECL with an unbiased and probability-weighted approach. Not only information about past events, but all available information including current conditions and forecast of future economic conditions should be considered with discounting for time value of money. The Group will account for expected credit losses within the next 12 months as Stage 1 when those financial instruments are first recognised; and to recognise full lifetime expected credit losses as Stage 2 on a more timely basis when there have been significant increases in credit risk since initial recognition. Full lifetime expected credit losses will also be recognised as Stage 3 if objective evidence of impairment occurred and interest accrual will then be net of the impairment amount of associated Stage 3 financial assets. The resulting impairment under HKFRS 9 would be more forward-looking than that under HKAS 39.

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2017 (continued)

(iii) Hedge accounting

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

The Group has chosen to prospectively apply HKFRS 9 on transition. As HKFRS 9 does not change the general principles of accounting for effective hedges, applying the hedging accounting requirements of HKFRS 9 will not have a significant impact on the Group's financial statements.

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

  The new standard will replace the separate models for goods, services and construction contracts stipulated in different standards under the current HKFRS. The application of this new standard from 1 January 2018 onward will not have a material impact on the Group's financial statements.

- 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 assessing the financial impact of the standard.

2. Significant accounting policies (continued)

2.1 Basis of preparation (continued)

(b) Standards, amendments and interpretations issued that are not yet mandatorily effective and have not been early adopted by the Group in 2017 (continued)

- HKFRS 17, "Insurance contracts". HKFRS 17 aims at replacing the current insurance contracts standard HKFRS 4, an interim standard that leads to highly divergent accounting practices that exist in the insurers' local jurisdictions. The new standard establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts, with an objective to ensure that an entity provides relevant information that faithfully represents insurance contracts. Early application of the standard is permitted but only if the entity also applies HKFRS 9 and HKFRS 15. The Group is considering the financial impact of the standard and the timing of its application.

- HK(IFRIC) – Int 22, "Foreign Currency Transactions and Advance Consideration". The interpretation specifies that the exchange rate on the date of cash payment or receipt is used for transactions that involve advance consideration paid or received in a foreign currency. The interpretation can either be applied retrospectively or prospectively to all assets, expenses and income. Earlier application is permitted. The application of this interpretation will not have a material impact on the Group's financial statements.

- HK(IFRIC) – Int 23, "Uncertainty over Income Tax Treatments". The interpretation specifies how an entity should reflect and measure the effects of uncertainty in accounting for income taxes by determining how probable that a taxation authority will accept an uncertain tax treatment. The interpretation can either be applied on a fully retrospective basis or on a modified retrospective basis. Earlier application is permitted. The application of this interpretation will not have a material impact on the Group's financial statements.

(c) Improvements to HKFRSs

- "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. These improvements do not have a material impact on the Group's financial statements.

2. Significant accounting policies (continued)

2.2 Consolidation

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

(1) Subsidiaries

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

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

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

(i) Business combinations not under common control

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

2. Significant accounting policies (continued)

2.2 Consolidation (continued)

(1) Subsidiaries (continued)

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

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

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

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

(ii) Business combinations under common control

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

2. Significant accounting policies (continued)

2.2 Consolidation (continued)

(1) Subsidiaries (continued)

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

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

(2) Transactions with non-controlling interests

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

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

(3) Associates and joint ventures

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

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

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

2. Significant accounting policies (continued)

2.2 Consolidation (continued)

(3) Associates and joint ventures (continued)

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

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

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

2.3 Segmental reporting

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

2.4 Foreign currency translation

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

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

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

2. Significant accounting policies (continued)

2.4 Foreign currency translation (continued)

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

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

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

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

2.5 Derivative financial instruments and hedge accounting

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

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

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

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

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

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

2. Significant accounting policies (continued)

2.5 Derivative financial instruments and hedge accounting (continued)

Hedge accounting is used for derivatives designated in this way.

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

(a) Fair value hedge

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

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

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

(b) Cash flow hedge

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

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

2. Significant accounting policies (continued)

2.5 Derivative financial instruments and hedge accounting (continued)

(c) Net investment hedge

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

2.6 Offsetting financial instruments

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

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

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

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

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

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

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

2. Significant accounting policies (continued)

2.8 Financial assets

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

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

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

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

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

- eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mismatch") that would otherwise arise from measuring the financial assets or recognising the gains and losses on them on different bases; or
- applies to a group of financial assets, financial liabilities or both that is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the key management; or
- relates to financial assets containing one or more embedded derivative that significantly modifies the cash flow resulting from those financial assets.

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

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

2. Significant accounting policies (continued)

2.8 Financial assets (continued)

(2) Loans and receivables

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

(3) Held-to-maturity

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

(4) Available-for-sale

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

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

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

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

2. Significant accounting policies (continued)

2.9 Financial liabilities

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

(1) Trading liabilities

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

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

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

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

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

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

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

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

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

2. Significant accounting policies (continued)

2.10 Financial guarantee contracts

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

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

2.11 Recognition and derecognition of financial instruments

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

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

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

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

2. Significant accounting policies (continued)

2.12 Fair value measurement

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

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

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

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

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

2.13 Precious metals

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

2.14 Impairment of financial assets

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

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

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

2. Significant accounting policies (continued)

2.14 Impairment of financial assets (continued)

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

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

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

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

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

(1) Assets carried at amortised cost

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

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

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

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

2. Significant accounting policies (continued)

2.14 Impairment of financial assets (continued)

(1) Assets carried at amortised cost (continued)

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

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

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

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

(2) Assets classified as available-for-sale

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

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

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

2. Significant accounting policies (continued)

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

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

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

2.16 Investment properties

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

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

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

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

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

2. Significant accounting policies (continued)

2.17 Properties, plant and equipment

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

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

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

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

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

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

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

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

2. Significant accounting policies (continued)

2.17 Properties, plant and equipment (continued)

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

2.18 Leases

(1) Operating leases

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

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

(2) Finance leases

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

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

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

2.19 Insurance and investment contracts

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

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

2. Significant accounting policies (continued)

2.19 Insurance and investment contracts (continued)

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

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

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

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

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

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

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

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

2. Significant accounting policies (continued)

2.19 Insurance and investment contracts (continued)

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

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

(2) Liability adequacy test

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

2.20 Cash and cash equivalents

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

2.21 Provisions

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

2.22 Employee benefits

(1) Retirement benefit costs

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

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

2. Significant accounting policies (continued)

2.22 Employee benefits (continued)

(2) Leave entitlements

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

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

(3) Bonus plans

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

2.23 Current and deferred income taxes

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

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

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

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

Deferred income tax liabilities are provided in full on all taxable temporary differences. Deferred income tax assets are recognised on deductible temporary differences, the carry forward of any unused tax credits and unused tax losses to the extent that it is probable that future taxable profit will be available against which the deductible temporary differences, the carry forward of unused tax credits and unused tax losses can be utilised.

2. Significant accounting policies (continued)

2.23 Current and deferred income taxes (continued)

Deferred income tax is charged or credited in the income statement except for deferred income tax relating to fair value re-measurement of available-for-sale securities and revaluation of premises which are charged or credited to other comprehensive income, in which case the deferred income tax is also credited or charged to other comprehensive income and is subsequently recognised in the income statement together with the realisation of the deferred gain and loss.

Deferred tax liability or deferred tax asset arising from investment property is determined based on the presumption that the revaluation amount of such investment property will be recovered through sale with the relevant tax rate applied.

2.24 Repossessed assets

Repossessed assets are initially recognised at the lower of their fair value less costs to sell and the amortised cost of the related outstanding loans on the date of repossession, and the related loans and advances together with the related impairment allowances are derecognised from the balance sheet. Subsequently, repossessed assets are measured at the lower of their cost and fair values less costs to sell and are reported as "non-current assets held for sale" included in "Other assets".

2.25 Fiduciary activities

The Group commonly acts as a trustee, or in other fiduciary capacities, that result in its holding or managing assets on behalf of individuals, trusts and other institutions. These assets and any gains or losses arising thereon are excluded from these financial statements, as they are not assets of the Group.

2.26 Contingent liabilities and contingent assets

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that an outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised as a provision but is disclosed in the notes to the financial statements. When a change in the probability of an outflow occurs so that outflow is probable, it will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group.

Contingent assets are not recognised but are disclosed in the notes to the financial statements when an inflow of economic benefits is probable. When the inflow is virtually certain, it will be recognised as an asset.

2. Significant accounting policies (continued)

2.27 Related parties

For the purposes of these financial statements, a party is considered to be related to the Group if that party (i) controls, jointly controls or has significant influence over the Group; (ii) is a member of the same financial reporting group, such as parents, subsidiaries and fellow subsidiaries; (iii) is an associate or a joint venture of the Group or parent reporting group; (iv) is a key management personnel of the Group or parents; (v) is subject to common control with the Group; (vi) is an entity in which a person identified in (iv) controls; and (vii) provides key management personnel services to the Group or its parent. Related parties may be individuals or entities.

3. Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the carrying amounts of assets and liabilities within the next reporting period. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Areas susceptible to changes in essential estimates and judgements, which affect the carrying amount of assets and liabilities, are set out below. The effect of changes to either the key assumptions or other estimation uncertainties will be presented below if it is practicable to determine. It is possible that actual results may require material adjustments to the estimates referred to below.

3.1 Impairment allowances on loans and advances

The Group reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and advances before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group (e.g. payment delinquency or default), or economic conditions that correlate with defaults on assets in the group. The Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when estimating expected future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly.

Carrying amounts of loans and advances as at 31 December 2017 are shown in Note 25.

3.2 Impairment of held-to-maturity and available-for-sale securities

The Group reviews its held-to-maturity and available-for-sale investment portfolios to assess impairment at least on a quarterly basis. In determining whether any of these investments is impaired, risk characteristics and performance such as external credit rating and market price, will be assessed. The Group makes estimates on the default rate and loss severity of each investment with reference to market performance of the portfolios, current payment status of the issuers or performance of the underlying assets, or economic conditions that correlate with defaults on the collateralised assets. The methodology and assumptions used for impairment assessments are reviewed regularly.

Carrying amounts of investment in securities as at 31 December 2017 are shown in Note 27.

3. Critical accounting estimates and judgements in applying accounting policies (continued)

3.3 Fair values of derivative financial instruments

The fair values of derivative financial instruments that are not quoted in active markets are determined by using valuation techniques. Valuation techniques used include discounted cash flows analysis and models with built-in functions available in externally acquired financial analysis or risk management systems widely used by the industry such as option pricing models. To the extent practical, the models use observable data. In addition, valuation adjustments may be adopted if factors such as credit risk are not considered in the valuation models. Management judgement and estimates are required for the selection of appropriate valuation parameters, assumptions and modeling techniques. Further details will be discussed in Note 5.

Carrying amounts of derivative financial instruments as at 31 December 2017 are shown in Note 24.

3.4 Held-to-maturity securities

The Group follows the guidance of HKAS 39 in classifying certain non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity securities. This classification requires significant management judgement to evaluate the Group's intention and ability to hold such investments to maturity. If the Group fails to hold these investments to maturity other than for specific circumstances defined in HKAS 39, such as selling an insignificant amount, selling close to maturity or due to significant credit deterioration of such investments, it will be required to reclassify the entire portfolio of financial assets as available-for-sale securities. The investments would then be measured at fair value and not amortised cost.

Carrying amounts of held-to-maturity securities as at 31 December 2017 are shown in Note 27.

3.5 Estimate of future benefit payments and premiums arising from long term insurance contracts

In determining the Group's long term business fund liabilities (a component of insurance contract liabilities), the Group follows the Insurance (Determination of Long Term Liabilities) Rules and makes prudent assumptions which include appropriate margins for adverse deviation of the relevant factors. Estimates are made as to the expected number of deaths for each of the years in which the Group is exposed to risk. The Group bases these estimates on population statistics or reinsurance information, adjusted where appropriate to reflect the Group's own experience and relevant reinsurance arrangements. For contracts that insure the risk of longevity, appropriate prudent allowances are made for expected mortality improvements. The estimated number of deaths determines the value of the benefit payments and the value of the valuation premiums. The main source of uncertainty is that epidemics such as AIDS, SARS, avian flu and wide-ranging lifestyle changes, such as in eating, smoking and exercise habits, could result in future mortality being significantly worse than in the past for the age groups in which the Group has significant exposure to mortality risk. However, continuing improvements in medical care and social conditions could result in improvements in longevity in excess of those allowed for in the estimates used to determine the liability for contracts where the Group is exposed to longevity risk.

3. Critical accounting estimates and judgements in applying accounting policies (continued)

3.5 Estimate of future benefit payments and premiums arising from long term insurance contracts (continued)

Were the number of deaths and morbidity in future years to differ by 10% (2016: 10%) from the Management's estimate, the long term business fund liability would increase by approximately HK$193 million (2016: approximately HK$131 million), which accounts for 0.29% (2016: 0.22%) of the liability. In this case, it is assumed there is no relief arising from reinsurance contracts held.

For linked long term insurance contracts with a life cover component, it is assumed that the Group will be able to increase mortality risk charges in future years in line with emerging mortality experience.

Estimates are also made as to future investment income arising from the assets backing long term insurance contracts. These estimates are based on current market returns as well as expectations about future economic and financial developments. Were the average future investment returns to decrease by 50 basis points (2016: 50 basis points) from the Management's estimates, the long term business fund liability would increase by approximately HK$1,660 million (2016: approximately HK$1,225 million). In this case, it is assumed there is no relief arising from reinsurance contracts held.

The Group has also assessed whether a provision for expense is necessary in accordance with the Insurance Ordinance. A provision for expense is the amount required to meet the total net cost that would likely be incurred in fulfilling contracts if the Group were to cease to transact new business 12 months after the valuation date. As of 31 December 2017, no provision for maintenance expenses was provided (2016: Nil).

A resilience reserve was set up and included in long term business fund liabilities in accordance with the Insurance (Determination of Long Term Liabilities) Rules to provide a prudent provision against the effects of possible future changes to the value of the assets to meet the liabilities. The resilience reserve was set up based on the appointed actuary's advice of a 30 basis points (2016: 30 basis points) change in market yield of the underlying assets and valuation interest rates. The amount of resilience reserve set up depends on the degree of change in interest rate assumed.

3.6 Deferred tax assets

Deferred tax assets on unused tax losses are recognised to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits.

Deferred tax assets on unused tax credits are recognised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the estimation of available tax credits and the possibility to recover such deferred tax assets recognised.

4. Financial risk management

The Group is exposed to financial risks as a result of engaging in a variety of business activities. The principal financial risks are credit risk, market risk (including currency risk and interest rate risk) and liquidity risk. This note summarises the Group's exposures to these risks, as well as its objectives, risk management governance structure, policies and processes for managing and the methods used to measure these risks.

Financial risk management framework

The Group's risk management governance structure is designed to cover all business processes and ensures various risks are properly managed and controlled in the course of conducting business. The Group has a robust risk management organisational structure with a comprehensive set of policies and procedures to identify, measure, monitor and control various risks that may arise. These risk management policies and procedures are regularly reviewed and updated to reflect changes in markets and business strategies. Various groups of risk takers assume their respective responsibilities for risk management.

The Board of Directors, representing the interests of shareholders, is the highest decision-making authority of the Group and has the ultimate responsibility for risk management. The Board, with the assistance of its committees, has the primary responsibility for the formulation of risk management strategies and ensuring that the Group has an effective risk management system to implement these strategies.

The RMC, 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 approving 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 any risks that may arise from time to time from new businesses, products and changes in the operating environment. The CRO is also responsible for reviewing material risk exposures or transactions within his delegated authority. In accordance with the principle of setting the hierarchy of risk management policies approved by the Board, senior management are also responsible for approving the detailed risk management policies of their responsible areas.

Various units of the Group have their respective risk management responsibilities. Business units act as the first line of defence while risk management units, which are independent from the business units, are responsible for the day-to-day management of different kinds of risks. Risk management units have the primary responsibilities for drafting, reviewing and updating various risk management policies and procedures.

The Group's principal banking subsidiaries are subject to risk management policies that are consistent with those of the Group. Moreover, the Group's non-banking subsidiaries, such as BOC Life, are subject to the Group's risk management requirements. These subsidiaries are required to formulate their respective risk management policies based on the characteristics of their own industries, perform daily risk management responsibilities and report to BOCHK on a regular basis. Risk management units of BOCHK monitor the risk management status of these subsidiaries.

4. Financial risk management (continued)

Financial risk management framework (continued)

The Group has put in place appropriate internal control systems, including establishment of an organisation structure that sets clear lines of authority and responsibility for monitoring compliance with policies, procedures and limits. Proper reporting lines also provide sufficient independence of the control functions from the business areas, as well as adequate segregation of duties throughout the organisation which helps to promote an appropriate internal control environment.

Product development and risk monitoring

To ensure the effectiveness of risk assessment and monitoring, the Group has a comprehensive product development and risk monitoring system where roles and responsibilities of all related units are clearly defined and proper due diligence processes on product development are in place.

In accordance with the strategic objectives set by the Board and the Management, respective product management units are responsible for formulating business and product development plans, and proceeding to specific product development activities. The department of strategic development shall ensure the plans are aligned with the Group's overall strategies. Departments that are responsible for risk management, legal, compliance and finance, etc. are accountable for risk assessment and review.

Apart from product development, respective product management units shall work closely with relevant risk evaluating departments to identify and assess the risks of new products. Risk evaluating departments shall conduct independent review on the risk assessment results and the corresponding risk management measures. Products can only be launched upon completion of the product due diligence process to the satisfaction of all risk evaluating departments.

A prudent approach is adopted in offering treasury products to our clients. All new treasury products require approval from a special committee before launching.

4.1 Credit risk

Credit risk is the risk of loss that a customer or counterparty is unable to or unwilling to meet its contractual obligations. Credit risk exists in the trading book and banking book, as well as from on- and off-balance sheet transactions of the Group. It arises principally from lending, trade finance and treasury businesses.

Credit risk management framework

The Group has formulated a comprehensive set of credit risk management policies and procedures, and appropriate credit risk limits to manage and control credit risk that may arise. These policies, procedures and credit risk limits are regularly reviewed and updated to cope with changes in market conditions and business strategies.

The Group's organisation structure establishes a clear set of authority and responsibility for monitoring compliance with policies, procedures and limits.

4. Financial risk management (continued)

4.1 Credit risk (continued)

Credit risk management framework (continued)

The Chief Credit Officer, who reports directly to the CRO, takes charge of credit risk management and is also responsible for the control of credit risk exposures of subsidiaries in line with the credit risk management principles and requirements set by the Group. Various units of the Group have their respective credit risk management responsibilities. Business units act as the first line of defence. The Risk Management Department ("RMD"), which is independent from the business units, is responsible for the day-to-day management of credit risks and has the primary responsibility for providing an independent due diligence through identifying, measuring, monitoring and controlling credit risk to ensure an effective checks and balances, as well as drafting, reviewing and updating credit risk management policies and procedures. It is also responsible for the design, development and maintenance of the Group's internal rating system and ensures the system complies with the relevant regulatory requirements. Back offices are responsible for credit administration, providing operations support and supervision on the implementation of prerequisite terms and conditions of credit facilities.

In accordance with the Group's operating principle, the Group's principal subsidiaries have to formulate their own credit risk policies that are consistent with those of the Group's core principles. These subsidiaries are required to submit their risk management reports to the Group's Management on a regular basis.

The Board of Directors delegates credit approval authority to the CE. The CE can further delegate to the subordinates within his limit authorised by the Board of Directors. The Group sets the limits of credit approval authority according to the credit business nature, rating, the level of transaction risk, and the extent of the credit exposure.

Credit risk measurement and control

In view of the rapidly changing market conditions, the Group has been continuously revisiting its credit strategies and conducting rigorous reviews on the concerned portfolios.

Advances

Different credit approval and control procedures are adopted according to the level of risk associated with the customer, counterparty or transaction. The Credit Risk Assessment Committee, comprising experts from credit and other functions, is responsible for making an independent assessment of material credit applications which require the approval of DCEs or above. Credit applications for non-retail exposures are independently reviewed and objectively assessed by risk management units. Obligor ratings (in terms of probability of default) and facility ratings (in terms of loss given default) are assigned to these portfolios to support credit approval. Retail internal rating systems are deployed in the risk assessment of retail credit transactions, including small business retail exposures, residential mortgage loans, personal loans and credit cards. Loan grades, obligor and facility ratings as well as loss estimates (if applicable) are used to support credit approval.

The Group also uses loan grades, obligor ratings and loss estimates (if applicable) to support credit monitoring, reporting and analysis of credit risk information. For non-retail exposures, more frequent rating review and closer monitoring are required for higher-risk customers. For retail exposures, monthly updated internal ratings and loss estimates are used for credit monitoring on a portfolio basis. More comprehensive review is required for obligors being identified under high-risk pools.

4. Financial risk management (continued)

4.1 Credit risk (continued)

Credit risk measurement and control (continued)

Advances (continued)

The Group employs an internal master rating scale that can be mapped to Standard & Poor's external credit ratings. The structure of internal master rating scale is in compliance with the requirement of the Banking (Capital) Rules under the Hong Kong Banking Ordinance.

RMD provides regular credit management information reports and ad hoc reports to the MC, RMC and Board of Directors to facilitate their continuous monitoring of credit risk.

In addition, the Group identifies credit concentration risk by industry, geography, customer and counterparty. The Group monitors changes to counterparty credit risk, quality of the credit portfolio and credit risk concentrations, and reports regularly to the Group's Management.

The Group adopts loan grading criteria which divides credit assets into five categories with reference to the HKMA's guidelines, as below:

"Pass" represents loans where the borrower is current in meeting its repayment obligations and full repayment of interest and principal is not in doubt.

"Special Mention" represents loans where the borrower is experiencing difficulties which may threaten the Group's position. Ultimate loss is not expected at this stage but could occur if adverse conditions persist.

"Substandard" represents loans where the borrower displays a definable weakness that is likely to jeopardise repayment.

"Doubtful" represents loans where collection in full is improbable and the Group expects to sustain a loss of principal and/or interest, taking into account the net realisable value of the collateral.

"Loss" represents loans which are considered uncollectible after all collection options (such as the realisation of collateral or the institution of legal proceedings) have been exhausted.

4. Financial risk management (continued)

4.1 Credit risk (continued)

Credit risk measurement and control (continued)

Debt securities and derivatives

For investments in debt securities and securitisation assets, the obligor ratings or external credit ratings, assessment of the underlying assets and credit limits setting on customer/security issuer basis are used for managing credit risk associated with the investment. For derivatives, the Group sets customer limits to manage the credit risk involved and follows the same approval and control processes as applied for advances. On-going monitoring and stop-loss procedures are established.

The methodology and assumptions used for impairment assessments are reviewed regularly. In evaluating impairment of asset backed securities ("ABS") and mortgage backed securities ("MBS"), the Group continues 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 considers other objective evidence of impairment, taking into account the impact of liquidity on market prices and the movement in loss coverage ratios of individual ABS and MBS held by the Group.

Settlement risk arises mainly from foreign exchange transactions with counterparties and also from derivatives transactions in any situation where a payment in cash, securities or equities is made in the expectation of a corresponding receipt in cash, securities or equities. Daily settlement limits are established for each counterparty or customer to cover all settlement risk arising from the Group's market transactions on any single day.

Collateral held as security and other credit enhancements

The valuation and management of collateral have been documented in the credit risk management policies and procedures which cover acceptance criteria, validity of collateral, loan-to-value ratio, haircut ratio, valuation and insurance, etc. The collateral is revalued on a regular basis, though the frequency and the method used varies with the type of collateral involved and the nature and the risk of the underlying credit. The Group has established a mechanism to update the value of its main type of collateral, property collateral including the use of public indices on a portfolio basis. Collateral is insured with the Group as the beneficiary. In the personal sector, the main types of collateral are real estate, cash deposits and securities. In the commercial and industrial sector, the types of collateral include real estate, securities, cash deposits, vessels, etc.

For loans guaranteed by a third party, the Group will assess the guarantor's financial condition, credit history and ability to meet obligations.

As at 31 December 2017, the fair value of collateral held by the Group that was permitted to sell or re-pledge in the absence of default by the borrower amounted to HK$11,826 million (2016: HK$7,013 million). The Group had not sold or re-pledged such collateral (2016: Nil). These transactions are conducted under terms that are usual and customary to reverse repurchase and securities borrowing agreements.

4. Financial risk management (continued)

4.1 Credit risk (continued)

(A) Credit exposures

The maximum credit exposure is the worst case scenario of exposure to the Group without taking into account any collateral held or other credit enhancements. For on-balance sheet assets, the maximum exposure to credit risk equals their carrying amount. For letters of guarantee issued, the maximum exposure to credit risk is the maximum amount that the Group could be required to pay if the guarantees are called upon. For loan commitment and other credit related liabilities, the maximum exposure to credit risk is the full amount of the committed facilities.

The nature of the collateral held and other credit enhancements and their financial effect to the different classes of the Group's financial assets are as follows.

Balances and placements with banks and other financial institutions

These exposures are generally considered to be low risk due to the nature of the counterparties. Collateral is generally not sought on these assets.

Financial assets at fair value through profit or loss and investment in securities

Collateral is generally not sought on debt securities.

Derivative financial instruments

The Master Agreement published by the International Swaps and Derivatives Association, Inc. ("ISDA Master Agreement") is the preferred agreement for documenting derivatives activities of the Group. It provides the contractual framework under which dealing activities of over-the-counter ("OTC") transactions are conducted, and sets out close-out netting provisions upon termination following the occurrence of an event of default or a termination event. In addition, if deemed necessary, Credit Support Annex ("CSA") will be included to form part of the Schedule to the ISDA Master Agreement. Under a CSA, collateral is passed from one counterparty to another, as appropriate, to mitigate the credit exposures.

Advances and other accounts, contingent liabilities and commitments

The general types of collateral are disclosed on page 170. Advances and other accounts, contingent liabilities and commitments are collateralised to the extent considered appropriate by the Group taking account of the risk assessment of individual exposures. The collateral coverage of advances to customers is analysed on pages 179 to 180. The components and nature of contingent liabilities and commitments are disclosed in Note 43. Regarding the commitments that are unconditionally cancellable without prior notice, the Group would assess the necessity to withdraw the credit line in case where the credit quality of a borrower deteriorates. For contingent liabilities and commitments, 12.77% (2016: 10.91%) was covered by collateral as at 31 December 2017.

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts

Gross advances and other accounts before impairment allowances are summarised by product type as follows:

	2017 HK$'m	2016 HK$'m
Advances to customers		
Personal		
– Mortgages	**245,908**	228,266
– Credit cards	**14,648**	13,849
– Others	**67,227**	50,595
Corporate		
– Commercial loans	**738,494**	623,273
– Trade finance	**78,182**	72,210
	1,144,459	988,193
Trade bills	**42,975**	17,245
Advances to banks and other financial institutions	**6,259**	6,016
	1,193,693	1,011,454

Advances with a specific repayment date are classified as overdue when the principal or interest is past due and remains unpaid. Advances repayable by regular instalments are classified as overdue when an instalment payment is past due and remains unpaid. Advances repayable on demand are classified as overdue either when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instruction or when the advances have remained continuously exceeded the approved limit that was advised to the borrower.

Advances are impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred and that loss event(s) has an impact on the estimated future cash flows of the advances that can be reliably estimated.

If there is objective evidence that an impairment loss on advances has been incurred, the amount of loss is measured as the difference between the carrying amount and the present value of estimated future cash flows generated by the advances. Objective evidence that advances are impaired includes observable data that comes to the attention of the Group about the loss events.

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include:

– Significant financial difficulty incurred by the borrower;

– A breach of contract, such as a default or delinquency in principal or interest payment;

– For economic or legal reasons related to the borrower's financial difficulty, the Group has granted to the borrower a concession that it would not otherwise consider;

– Probable that the borrower will become bankrupt or undergo other financial reorganisation; or

– Other observable data indicating that there is a measurable decrease in the estimated future cash flows from such advances.

(a) Advances neither overdue nor impaired

Advances that were neither overdue nor impaired are analysed by internal credit grade as follows:

	2017			
	Pass HK$'m	Special mention HK$'m	Substandard or below HK$'m	Total HK$'m
Advances to customers				
Personal				
– Mortgages	243,575	223	62	243,860
– Credit cards	14,286	–	–	14,286
– Others	66,181	688	10	66,879
Corporate				
– Commercial loans	735,126	1,044	597	736,767
– Trade finance	78,077	49	–	78,126
	1,137,245	2,004	669	1,139,918
Trade bills	42,975	–	–	42,975
Advances to banks and other financial institutions	6,259	–	–	6,259
	1,186,479	2,004	669	1,189,152

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(a) Advances neither overdue nor impaired (continued)

	2016			
	Pass HK$'m	Special mention HK$'m	Substandard or below HK$'m	Total HK$'m
Advances to customers				
Personal				
– Mortgages	226,039	181	41	226,261
– Credit cards	13,496	–	–	13,496
– Others	50,185	78	5	50,268
Corporate				
– Commercial loans	619,542	740	650	620,932
– Trade finance	72,070	51	10	72,131
	981,332	1,050	706	983,088
Trade bills	17,245	–	–	17,245
Advances to banks and other financial institutions	6,016	–	–	6,016
	1,004,593	1,050	706	1,006,349

The occurrence of loss event(s) may not necessarily result in impairment loss where the advances are fully collateralised. While such advances are of "substandard" or lower grades, they are regarded as not being impaired and have been included in the above tables.

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(b) Advances overdue but not impaired

The gross amount of advances overdue but not impaired is analysed as follows:

	2017				
	Overdue for three months or less HK$'m	Overdue for six months or less but over three months HK$'m	Overdue for one year or less but over six months HK$'m	Overdue for over one year HK$'m	Total HK$'m
Advances to customers					
Personal					
– Mortgages	2,016	3	3	9	2,031
– Credit cards	321	–	–	–	321
– Others	301	2	–	–	303
Corporate					
– Commercial loans	500	10	–	4	514
– Trade finance	1	–	–	–	1
	3,139	15	3	13	3,170

	2016				
	Overdue for three months or less HK$'m	Overdue for six months or less but over three months HK$'m	Overdue for one year or less but over six months HK$'m	Overdue for over one year HK$'m	Total HK$'m
Advances to customers					
Personal					
– Mortgages	1,957	18	17	7	1,999
– Credit cards	310	–	–	–	310
– Others	284	2	3	3	292
Corporate					
– Commercial loans	1,001	–	–	5	1,006
– Trade finance	3	–	–	2	5
	3,555	20	20	17	3,612

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(c) Impaired advances

Advances individually identified to be impaired are analysed by product type as follows:

	2017		2016	
	Gross advances HK$'m	Market value of collateral HK$'m	Gross advances HK$'m	Market value of collateral HK$'m
Advances to customers				
Personal				
– Mortgages	**17**	**22**	6	9
– Credit cards	**41**	**–**	43	–
– Others	**45**	**6**	35	25
Corporate				
– Commercial loans	**1,213**	**1,426**	1,335	1,050
– Trade finance	**55**	**69**	74	14
	1,371	**1,523**	1,493	1,098
Impairment allowances made in respect of such advances	**538**		703	

	2017 HK$'m	2016 HK$'m
Current market value of collateral held against the covered portion of such advances to customers	**1,523**	1,098
Covered portion of such advances to customers	**1,083**	921
Uncovered portion of such advances to customers	**288**	572

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

As at 31 December 2017, there were no impaired trade bills and advances to banks and other financial institutions (2016: Nil).

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(c) Impaired advances (continued)

Classified or impaired advances to customers are analysed as follows:

	2017 HK$'m	2016 HK$'m
Gross classified or impaired advances to customers	**2,079**	2,282
Gross classified or impaired advances to customers as a percentage of gross advances to customers	**0.18%**	0.23%
Individually assessed impairment allowances made in respect of such advances	**491**	650

Classified or impaired advances to customers represent advances which are either classified as "substandard", "doubtful" or "loss" under the Group's classification of loan quality, or individually assessed to be impaired.

(d) Advances overdue for more than three months

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

	2017		2016	
	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	**117**	**0.01%**	94	0.01%
– one year or less but over six months	**123**	**0.01%**	81	0.01%
– over one year	**313**	**0.03%**	328	0.03%
Advances overdue for over three months	**553**	**0.05%**	503	0.05%
Individually assessed impairment allowances made in respect of such advances	**309**		250	

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

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

	2017 HK$'m	2016 HK$'m
Current market value of collateral held against the covered portion of such advances to customers	**520**	428
Covered portion of such advances to customers	**289**	224
Uncovered portion of such advances to customers	**264**	279

Collateral held against overdue or impaired loans is principally represented by charges over business assets such as commercial, residential premises and vessels for corporate loans and mortgages over residential properties for personal loans.

As at 31 December 2017, there were no trade bills and advances to banks and other financial institutions overdue for more than three months (2016: Nil).

(e) Rescheduled advances

	2017		2016	
	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"	**238**	**0.02%**	–	–

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".

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers

(i) Sectoral analysis of gross advances to customers

The following analysis of the gross advances to customers by industry sector is based on the categories with reference to the completion instructions for the HKMA return of loans and advances.

	2017					
	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	99,987	24.22%	–	5	–	336
– Property investment	53,581	78.47%	19	68	–	180
– Financial concerns	13,461	2.42%	–	–	–	68
– Stockbrokers	1,027	89.86%	–	1	–	3
– Wholesale and retail trade	34,931	38.23%	26	160	20	131
– Manufacturing	45,075	13.93%	32	25	4	159
– Transport and transport equipment	61,786	28.44%	1,062	27	44	213
– Recreational activities	2,040	1.47%	–	–	–	6
– Information technology	23,900	1.07%	–	–	–	79
– Others	100,966	41.99%	18	132	5	336
Individuals						
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	9,874	99.75%	12	147	–	6
– Loans for purchase of other residential properties	234,434	99.93%	75	1,520	1	128
– Credit card advances	14,620	–	39	549	–	124
– Others	63,356	80.57%	53	508	20	429
Total loans for use in Hong Kong	759,038	58.31%	1,336	3,142	94	2,198
Trade finance	78,182	14.13%	55	25	32	287
Loans for use outside Hong Kong	307,239	9.23%	688	1,003	365	1,108
Gross advances to customers	1,144,459	42.11%	2,079	4,170	491	3,593

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

	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	73,637	22.82%	–	1	–	248
– Property investment	53,908	81.58%	27	133	–	180
– Financial concerns	5,438	3.53%	–	–	–	45
– Stockbrokers	2,647	95.17%	–	–	–	9
– Wholesale and retail trade	35,091	37.14%	42	186	29	127
– Manufacturing	26,136	17.49%	49	51	7	100
– Transport and transport equipment	53,074	31.31%	1,239	17	289	186
– Recreational activities	2,510	1.59%	–	–	–	8
– Information technology	17,938	1.30%	–	–	–	58
– Others	105,127	24.95%	15	89	10	341
Individuals						
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	8,562	99.84%	10	170	–	5
– Loans for purchase of other residential properties	218,426	99.93%	89	1,812	2	101
– Credit card advances	13,819	–	41	524	–	123
– Others	47,717	71.08%	36	495	3	68
Total loans for use in Hong Kong	664,030	57.97%	1,548	3,478	340	1,599
Trade finance	72,210	13.99%	87	52	28	256
Loans for use outside Hong Kong	251,953	13.22%	647	1,021	282	924
Gross advances to customers	988,193	43.35%	2,282	4,551	650	2,779

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

The amounts of new impairment allowances charged to the income statement, and classified or impaired loans written off during the year are shown below:

	2017		2016	
	New impairment allowances HK$'m	Classified or impaired loans written off HK$'m	New impairment allowances HK$'m	Classified or impaired loans written off HK$'m
Loans for use in Hong Kong				
Industrial, commercial and financial				
– Property development	80	–	25	–
– Property investment	4	–	–	–
– Financial concerns	20	–	–	–
– Stockbrokers	–	–	2	–
– Wholesale and retail trade	9	13	50	18
– Manufacturing	55	3	19	2
– Transport and transport equipment	25	1	50	1
– Recreational activities	–	–	5	–
– Information technology	18	–	11	–
– Others	8	8	125	8
Individuals				
– Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	1	–	–	–
– Loans for purchase of other residential properties	26	–	6	–
– Credit card advances	223	220	248	228
– Others	544	171	190	182
Total loans for use in Hong Kong	1,013	416	731	439
Trade finance	31	10	21	62
Loans for use outside Hong Kong	463	141	204	–
Gross advances to customers	1,507	567	956	501

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

(ii) Geographical analysis of gross advances to customers

The following geographical analysis of advances to customers is based on the locations of the counterparties, after taking into account the transfer of risk. For an advance to customer guaranteed by a party situated in a location different from the customer, the risk will be transferred to the location of the guarantor.

Gross advances to customers

	2017 HK$'m	2016 HK$'m
Hong Kong	**911,691**	781,395
Mainland of China	**135,825**	123,517
Others	**96,943**	83,281
	1,144,459	988,193
Collectively assessed impairment allowances in respect of the gross advances to customers		
Hong Kong	**2,741**	2,022
Mainland of China	**450**	399
Others	**402**	358
	3,593	2,779

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

Overdue advances

	2017 HK$'m	2016 HK$'m
Hong Kong	**3,061**	3,418
Mainland of China	**181**	162
Others	**928**	971
	4,170	4,551
Individually assessed impairment allowances in respect of the overdue advances		
Hong Kong	**65**	112
Mainland of China	**53**	8
Others	**220**	189
	338	309
Collectively assessed impairment allowances in respect of the overdue advances		
Hong Kong	**95**	96
Mainland of China	**2**	2
Others	**5**	15
	102	113

4. Financial risk management (continued)

4.1 Credit risk (continued)

(B) Gross advances and other accounts (continued)

(f) Concentration of advances to customers (continued)

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

Classified or impaired advances

	2017 HK$'m	2016 HK$'m
Hong Kong	**1,379**	1,716
Mainland of China	**111**	75
Others	**589**	491
	2,079	2,282
Individually assessed impairment allowances in respect of the classified or impaired advances		
Hong Kong	**113**	411
Mainland of China	**70**	11
Others	**308**	228
	491	650
Collectively assessed impairment allowances in respect of the classified or impaired advances		
Hong Kong	**46**	52
Mainland of China	**1**	1
Others	**2**	7
	49	60

(C) Repossessed assets

During the year, the Group obtained assets by taking possession of collateral held as security. The nature and carrying value of these assets held as at 31 December are summarised as follows:

	2017 HK$'m	2016 HK$'m
Commercial properties	**8**	–
Industrial properties	**1**	–
Residential properties	**21**	38
	30	38

4. Financial risk management (continued)

4.1 Credit risk (continued)

(C) Repossessed assets (continued)

The estimated market value of repossessed assets held by the Group as at 31 December 2017 amounted to HK$77 million (2016: HK$72 million). The repossessed assets comprise properties in respect of which the Group has acquired access or control (e.g. through court proceedings or voluntary actions by the proprietors concerned) for release in full or in part of the obligations of the borrowers.

When the repossessed assets are not readily convertible into cash, the Group may consider the following alternatives:

– adjusting the selling prices

– selling the loans together with the assets

– arranging loan restructuring

(D) Balances and placements with banks and other financial institutions

The following tables present an analysis of balances and placements with banks and other financial institutions that are neither overdue nor impaired as at 31 December by rating agency designation.

	2017			
	Aaa to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Central banks	**84,559**	**6,217**	**8,547**	**99,323**
Other banks and other financial institutions	**265,886**	**40,599**	**3,219**	**309,704**
	350,445	**46,816**	**11,766**	**409,027**

	2016			
	Aaa to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Central banks	68,724	6,918	6,715	82,357
Other banks and other financial institutions	186,584	26,327	759	213,670
	255,308	33,245	7,474	296,027

As at 31 December 2017, there were no overdue or impaired balances and placements with banks and other financial institutions (2016: Nil).

4. Financial risk management (continued)

4.1 Credit risk (continued)

(E) Debt securities and certificates of deposit

The following tables present an analysis of the carrying value of debt securities and certificates of deposit by issue rating. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	2017					
	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	**169,826**	**135,479**	**205,403**	**35,848**	**15,145**	**561,701**
Held-to-maturity securities	**16,909**	**1,581**	**20,933**	**6,174**	**4,962**	**50,559**
Loans and receivables	**–**	**–**	**499**	**–**	**–**	**499**
Financial assets at fair value through profit or loss	**18,003**	**13,639**	**29,692**	**9,662**	**2,593**	**73,589**
	204,738	**150,699**	**256,527**	**51,684**	**22,700**	**686,348**

	2016					
	Aaa HK$'m	Aa1 to Aa3 HK$'m	A1 to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Available-for-sale securities	106,276	171,851	186,790	41,867	20,654	527,438
Held-to-maturity securities	19,805	21,671	12,365	5,108	1,919	60,868
Loans and receivables	–	149	786	–	–	935
Financial assets at fair value through profit or loss	14,927	16,615	14,817	6,501	3,456	56,316
	141,008	210,286	214,758	53,476	26,029	645,557

4. Financial risk management (continued)

4.1 Credit risk (continued)

(E) Debt securities and certificates of deposit (continued)

The following tables present an analysis of debt securities and certificates of deposit neither overdue nor impaired as at 31 December by issue rating. In the absence of such issue ratings, the ratings designated for the issuers are reported.

	2017					
	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	**169,826**	**135,479**	**205,403**	**35,848**	**15,145**	**561,701**
Held-to-maturity securities	**16,909**	**1,581**	**20,933**	**6,174**	**4,962**	**50,559**
Loans and receivables	**–**	**–**	**499**	**–**	**–**	**499**
Financial assets at fair value through profit or loss	**18,003**	**13,639**	**29,692**	**9,662**	**2,593**	**73,589**
	204,738	**150,699**	**256,527**	**51,684**	**22,700**	**686,348**

	2016					
	Aaa HK$'m	Aa1 to Aa3 HK$'m	A1 to A3 HK$'m	Lower than A3 HK$'m	Unrated HK$'m	Total HK$'m
Available-for-sale securities	106,276	171,851	186,790	41,867	20,654	527,438
Held-to-maturity securities	19,804	21,671	12,365	5,108	1,919	60,867
Loans and receivables	–	149	786	–	–	935
Financial assets at fair value through profit or loss	14,927	16,615	14,817	6,501	3,456	56,316
	141,007	210,286	214,758	53,476	26,029	645,556

The impaired debt securities are analysed as follows:

	2017 HK$'m	2016 HK$'m
Held-to-maturity securities	**–**	1

As at 31 December 2017, there were no impaired certificates of deposit and no overdue debt securities and certificates of deposit (2016: Nil).

4. Financial risk management (continued)

4.2 Market risk

Market risk refers to the risk of loss arising from movements in the value of foreign exchange, interest rate, equity and commodity positions held by the Group due to the volatility of financial market price (foreign exchange rate, interest rate, equity price, commodity price). The Group adopts a moderate market risk appetite to achieve a balance between risk and return. The Group's objective in managing market risk is to secure healthy growth of the treasury business, by effective management of potential market risk in the Group's business, according to the Group's overall risk appetite and strategy of treasury business on the basis of a well-established risk management regime and related management measures.

In accordance with the Group's corporate governance principles in respect of risk management, the Board and RMC, 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 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 business requirements and risk tolerance levels. In line with the requirements set in the Group policy, the subsidiaries 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 RMC, MC, CRO and the DCE in charge of the treasury business or the head of the respective business unit respectively. Treasury business units of BOCHK and subsidiaries (as for Group Limit) are required to conduct their business within approved market risk indicators and limits.

(A) VAR

The Group uses the VAR to measure and report general market risks to the RMC 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.

4. Financial risk management (continued)

4.2 Market risk (continued)

(A) VAR (continued)

The following table sets out the VAR for all general market risk exposure[1] of the Group.

	Year	At 31 December HK$'m	Minimum for the year HK$'m	Maximum for the year HK$'m	Average for the year HK$'m
VAR for all market risk	**2017**	**28.3**	**27.1**	**80.9**	**49.7**
	2016	61.2	29.4	70.5	45.9
VAR for foreign exchange risk	**2017**	**13.1**	**12.5**	**54.1**	**31.2**
	2016	57.1	24.3	62.4	35.8
VAR for interest rate risk	**2017**	**25.1**	**19.3**	**82.4**	**44.4**
	2016	44.9	15.3	57.4	28.8
VAR for equity risk	**2017**	**2.1**	**0.7**	**5.9**	**2.6**
	2016	3.2	0.0	5.7	2.1
VAR for commodity risk	**2017**	**1.1**	**0.5**	**2.0**	**1.3**
	2016	1.2	0.0	1.4	0.3

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.

4. Financial risk management (continued)

4.2 Market risk (continued)

(B) Currency risk

The Group's assets and liabilities are denominated in major currencies, particularly HK Dollar, 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.

	2017							
	Equivalent in million of HK$							
	US Dollars	Pound Sterling	Japanese Yen	Euro	Renminbi	Australian Dollars	Other foreign currencies	Total foreign currencies
Spot assets	850,639	23,799	90,147	52,557	365,422	42,746	47,941	1,473,251
Spot liabilities	(742,593)	(15,363)	(11,352)	(25,620)	(288,947)	(19,414)	(50,633)	(1,153,922)
Forward purchases	909,676	16,490	30,145	61,278	356,964	21,391	86,722	1,482,666
Forward sales	(1,014,314)	(25,073)	(108,992)	(88,054)	(433,565)	(44,640)	(83,140)	(1,797,778)
Net options position	(684)	6	(6)	(48)	44	(14)	10	(692)
Net long/(short) position	2,724	(141)	(58)	113	(82)	69	900	3,525

	2016							
	Equivalent in million of HK$							
	US Dollars	Pound Sterling	Japanese Yen	Euro	Renminbi	Australian Dollars	Other foreign currencies	Total foreign currencies
Spot assets	729,472	20,711	128,359	40,591	260,636	22,537	28,637	1,230,943
Spot liabilities	(617,520)	(14,351)	(9,056)	(28,397)	(250,559)	(19,823)	(32,101)	(971,807)
Forward purchases	1,095,599	26,200	58,711	56,669	579,902	28,125	55,743	1,900,949
Forward sales	(1,196,764)	(32,618)	(178,070)	(68,865)	(588,688)	(30,925)	(52,907)	(2,148,837)
Net options position	1,123	2	1	1	(733)	(3)	1	392
Net long/(short) position	11,910	(56)	(55)	(1)	558	(89)	(627)	11,640

4. Financial risk management (continued)

4.2 Market risk (continued)

(B) Currency risk (continued)

	2017					
	Equivalent in million of HK$					
	US Dollars	Renminbi	Malaysian Ringgit	Baht	Other foreign currencies	Total foreign currencies
Net structural position	**3,531**	**–**	**2,651**	**2,350**	**1,015**	**9,547**

	2016					
	Equivalent in million of HK$					
	US Dollars	Renminbi	Malaysian Ringgit	Baht	Other foreign currencies	Total foreign currencies
Net structural position	–	791	2,175	–	160	3,126

(C) Interest rate risk

Interest rate risk means the risks to a bank's earnings and economic value arising from movements in interest rate and term structures of the bank's asset and liability positions. The Group's interest rate risk exposures are mainly structural. The major types of interest rate risk from structural positions are:

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

– Basis risk: different pricing basis for different transactions resulting that the yield on assets and cost of liabilities may change by different amounts within the same repricing period;

– Yield curve risk: non-parallel shifts in the yield curve that may have an adverse impact on net interest income or economic value; and

– Option risk: exercise of the options embedded in assets, liabilities or off-balance sheet items that can cause a change in the cash flows of assets and liabilities.

4. Financial risk management (continued)

4.2 Market risk (continued)

(C) Interest rate risk (continued)

The Group's risk management framework applies also to interest rate risk management. The ALCO exercises its oversight of interest rate risk in accordance with the "BOCHK Group Banking Book Interest Rate Risk Management Policy" approved by the RMC. 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, Treasury, 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 RMC, 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, RMC 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 the RMC 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 RMC on these two indicators to monitor and control the Group's banking book interest rate risk.

The Group uses scenario analyses and stress tests to assess the banking book interest rate risk that the Group would face under adverse circumstances. Scenario analyses and stress tests are also used to assess the impact on net interest income and economic value arising from the optionality of savings deposits, the prepayment of mortgage loans and the prepayment of debt securities with embedded options.

4. Financial risk management (continued)

4.2 Market risk (continued)

(C) Interest rate risk (continued)

The Group is principally exposed to HK Dollar, US Dollar and Renminbi in terms of interest rate risk. As at 31 December 2017, if market interest rates had a 100 basis point parallel upward shift of the yield curve with other variables held constant, the sensitivities on net interest income over a twelve-month period and on reserves for the Group would have been as follows:

	Impact on net interest income over the next twelve months at 31 December		Impact on reserves at 31 December	
	2017 HK$'m	2016 HK$'m	**2017 HK$'m**	2016 HK$'m
Total	**961**	185	**(6,750)**	(5,365)
Of which:				
HK Dollar	**2,326**	1,572	**(388)**	(522)
US Dollar	**(947)**	(525)	**(4,787)**	(3,866)
Renminbi	**(241)**	(583)	**(836)**	(747)

Note: The comparative information of impact on reserve for the year 2016 has been restated due to the assumption change of hedge relationship for available-for-sale portfolio.

The overall impact on net interest income of the above currencies is positive in 2017, which is mainly because of the increase in HKD non-interest bearing funding. Reserves would have been reduced because of the expected reduction in valuation of available-for-sale portfolio (available-for-sale portfolio includes available-for-sale securities and relevant interest rate derivatives under hedge accounting) due to a parallel shift up of 100 basis points in the yield curve. The reduction of reserves is increased compared with 2016 because the size of available-for-sale portfolio in capital market is increased.

The sensitivities above are for illustration only and are based on several assumptions, including, but not limited to, the change in the correlation between interest rates of relevant currencies, parallel movement of interest rates, the absence of actions that would be taken to mitigate the impact of interest rate risk, the effectiveness of hedge accounting, all positions being assumed to run to maturity, behavioural assumptions of products in which actual repricing date differs from contractual repricing date or products without contractual maturity. The above exposures form only a part of the Group's overall interest rate risk exposures.

4. Financial risk management (continued)

4.2 Market risk (continued)

(C) Interest rate risk (continued)

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

	2017						
	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	341,939	–	–	–	–	22,266	364,205
Placements with banks and other financial institutions maturing between one and twelve months	–	37,210	21,846	–	–	–	59,056
Financial assets at fair value through profit or loss	10,940	9,239	17,242	13,824	29,203	12,746	93,194
Derivative financial instruments	–	–	–	–	–	33,541	33,541
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	146,200	146,200
Advances and other accounts	954,188	137,995	54,737	28,502	6,374	7,813	1,189,609
Investment in securities							
– Available-for-sale securities	73,072	102,698	116,481	164,179	105,271	5,413	567,114
– Held-to-maturity securities	1,231	2,467	7,989	24,074	14,798	–	50,559
– Loans and receivables	–	499	–	–	–	–	499
Interests in associates and joint ventures	–	–	–	–	–	417	417
Investment properties	–	–	–	–	–	19,669	19,669
Properties, plant and equipment	–	–	–	–	–	47,261	47,261
Other assets (including deferred tax assets)	4,338	–	–	–	–	70,091	74,429
Total assets	1,385,708	290,108	218,295	230,579	155,646	365,417	2,645,753
Liabilities							
Hong Kong SAR currency notes in circulation	–	–	–	–	–	146,200	146,200
Deposits and balances from banks and other financial institutions	184,518	7,163	362	825	–	30,206	223,074
Financial liabilities at fair value through profit or loss	7,102	4,116	7,068	955	479	–	19,720
Derivative financial instruments	–	–	–	–	–	31,044	31,044
Deposits from customers	1,333,365	160,565	140,233	1,254	–	136,096	1,771,513
Debt securities and certificates of deposit in issue	7,091	1,971	12,579	–	–	–	21,641
Other accounts and provisions (including current and deferred tax liabilities)	13,697	–	–	–	–	49,311	63,008
Insurance contract liabilities	–	–	–	–	–	103,229	103,229
Subordinated liabilities	–	–	63	18,917	–	–	18,980
Total liabilities	1,545,773	173,815	160,305	21,951	479	496,086	2,398,409
Interest sensitivity gap	(160,065)	116,293	57,990	208,628	155,167	(130,669)	247,344

4. Financial risk management (continued)

4.2 Market risk (continued)

(C) Interest rate risk (continued)

	2016						
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Non-interest bearing HK$'m	Total HK$'m
Assets							
Cash and balances with banks and other financial institutions	214,279	–	–	–	–	22,027	236,306
Placements with banks and other financial institutions maturing between one and twelve months	–	30,211	42,399	–	–	–	72,610
Financial assets at fair value through profit or loss	5,510	8,217	13,224	15,326	19,816	5,265	67,358
Derivative financial instruments	–	–	–	–	–	64,332	64,332
Hong Kong SAR Government certificates of indebtedness	–	–	–	–	–	123,390	123,390
Advances and other accounts	784,676	110,128	57,107	41,013	7,662	7,439	1,008,025
Investment in securities							
– Available-for-sale securities	54,940	119,259	106,325	142,154	104,760	4,409	531,847
– Held-to-maturity securities	779	3,979	17,073	24,584	14,453	–	60,868
– Loans and receivables	–	–	935	–	–	–	935
Interests in associates and joint ventures	–	–	–	–	–	319	319
Investment properties	–	–	–	–	–	18,227	18,227
Properties, plant and equipment	–	–	–	–	–	45,812	45,812
Other assets (including deferred tax assets)	3,383	–	–	–	–	68,035	71,418
Assets held for sale	32,358	6,837	6,394	5,197	4	2,503	53,293
Total assets	1,095,925	278,631	243,457	228,274	146,695	361,758	2,354,740
Liabilities							
Hong Kong SAR currency notes in circulation	–	–	–	–	–	123,390	123,390
Deposits and balances from banks and other financial institutions	152,209	15,236	9,574	632	184	21,098	198,933
Financial liabilities at fair value through profit or loss	3,705	5,578	2,161	1,335	592	–	13,371
Derivative financial instruments	–	–	–	–	–	49,304	49,304
Deposits from customers	1,142,641	185,224	80,793	398	–	110,811	1,519,867
Debt securities and certificates of deposit in issue	–	–	–	1,121	–	–	1,121
Other accounts and provisions (including current and deferred tax liabilities)	15,803	–	–	–	–	45,757	61,560
Insurance contract liabilities	–	–	–	–	–	86,534	86,534
Subordinated liabilities	–	–	79	19,014	–	–	19,093
Liabilities associated with assets held for sale	28,917	7,428	7,145	67	–	3,456	47,013
Total liabilities	1,343,275	213,466	99,752	22,567	776	440,350	2,120,186
Interest sensitivity gap	(247,350)	65,165	143,705	205,707	145,919	(78,592)	234,554

4. Financial risk management (continued)

4.3 Liquidity risk

Liquidity risk is the risk that banks may not be able to obtain sufficient and timely funding at reasonable cost to meet their obligations as they fall due. The Group maintains sound liquidity risk appetite to provide stable, reliable and adequate sources of cash to meet liquidity needs under normal circumstances or stressed scenarios; and to survive with net positive cumulative cash flow in extreme scenarios, without requesting the HKMA to act as the lender of last resort.

The Group's liquidity risk management objective is to effectively manage the liquidity of on- and off-balance sheet items with reasonable cost based on the liquidity risk appetite to achieve sound operation and sustainable profitability. Deposits from customers are the Group's primary source of funds. To ensure stable and sufficient source of funds are in place, the Group actively attracts new deposits, keeps the core deposit and obtains supplementary funding from the interbank market and by issuing bills in the capital market. According to different term maturities and the results of funding needs estimated from stressed scenarios, the Group adjusts its asset structure (including loans, bonds investment, interbank placement, etc.) to maintain sufficient liquid assets which provides adequate funds in support of normal business needs and ensure its ability to raise funds at a reasonable cost to serve external claims in case of emergency. The Group is committed to diversify the source of funds and the use of funds to avoid excessive concentration of assets and liabilities and prevent triggering liquidity risk due to the break of funding strand when problem occurred in one concentrated funding source. The Group has established intra-group liquidity risk management guideline to manage the liquidity funding among different entities within the Group, and to restrict their reliance of funding on each other. The Group also pays attention to manage liquidity risk created by off-balance sheet activities, such as loan commitments, derivatives, options and other complex structured products. The Group has an overall liquidity risk management strategy to cover the liquidity management of foreign currency assets and liabilities, collateral, intra-day liquidity, intra-group liquidity, the liquidity risk arising from other risks, etc., and has formulated corresponding contingency plan.

The RMC is the decision-making authority of liquidity risk management, and assumes the ultimate responsibility of liquidity risk management. As authorised by the RMC, 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 the RMC. 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, Treasury, and Investment Management, etc. to assist the ALCO to perform liquidity management functions according to their specific responsibilities.

The Group established liquidity risk management indicators and limits to identify, measure, monitor and control liquidity risk on daily basis. These indicators and limits include, but are not limited to liquidity coverage ratio ("LCR"), loan-to-deposit ratio, Maximum Cumulative Cash Outflow ("MCO") and liquidity cushion. The Group applies cash flow analysis to assess the Group's liquidity condition under normal conditions and also performs a liquidity stress test (including institution specific, general market crisis and combined crisis) and other methods at least on monthly basis to assess the Group's capability to withstand various severe liquidity crises. Also, relevant management information systems such as Assets and Liabilities Management System and Basel Liquidity Ratio Management System are developed to provide data and the preparation for regular management reports to facilitate liquidity risk management duties.

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

In accordance with the requirements of Supervisory Policy Manual LM-2 "Sound Systems and controls for Liquidity Risk Management" issued by the HKMA, the Group has implemented behaviour model and assumptions of cash flow analysis and stress test to enhance the Group's cash flow analysis under both normal and stressed conditions. In cash flow analysis under normal circumstances, assumptions have been made relating to on-balance sheet items (such as deposits from customers) and off-balance sheet items (such as loan commitments). According to various characteristics of the assets, liabilities and off-balance sheet items, the Group forecasts the future cash flow based on contractual maturity date and the assumptions of customer behaviour and balance sheet changes. The Group establishes MCO indicator which predicts the future 30 days maximum cumulative net cash outflow in normal situations based on the above assumptions, to assess if the Group has sufficient financing capacity to meet the cash flow gap in order to achieve the objective of continuing operation. As at 31 December 2017, before taking the cash inflow through the sale of outstanding marketable securities into consideration, BOCHK's 30 day cumulative cash flow was a net cash inflow, amounting to HK$85,602 million (2016: HK$64,212 million) and was in compliance with the internal limit requirements.

In the liquidity stress test, institution specific, general market crisis and combined crisis scenarios have been set up, combined crisis scenario is a combination of institution specific and general market crisis to assess the Group's capability to withstand a more severe liquidity crisis, with a more stringent set of assumptions being adopted. Stress test assumptions include the run-off rate of retail, wholesale and interbank deposits; drawdown rate of loan commitments and trade-related contingent liabilities; delinquency ratio and rollover rate of customer loans; and haircut of interbank placement and marketable securities. As at 31 December 2017, the Group was able to maintain a net cash inflow under the three stressed scenarios, indicating the Group has the ability to meet financing needs under stressed conditions. In addition, the Group has a policy in place to maintain a liquidity cushion which includes high quality or comparable quality marketable securities issued or guaranteed by sovereigns, central banks, public sector entities or multilateral development banks with 0% or 20% risk weight or marketable securities issued by non-financial corporate with a corresponding external credit rating of A- or above to ensure funding needs even under stressed scenarios. As at 31 December 2017, the liquidity cushion (before haircut) of BOCHK was HK$420,770 million (2016: HK$353,048 million). A contingency plan is being established which details the conditions to trigger the plan based on stress test results and early warning indicators, the action plans and relevant procedures and responsibility of relevant departments.

The LCR is calculated in accordance with the Banking (Liquidity) Rules effective from 1 January 2015, the Group, being classified as category 1 authorised institution by the HKMA, is required to calculate LCR on consolidated basis. During the year of 2017, the Group is required to maintain a LCR not less than 80%.

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 the RMC for approval.

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

The Group has established a set of uniform liquidity risk management policies which serve as standards and guidance to all the Group's members for liquidity risk management. On the basis of the Group's uniform policy, each of the subsidiaries develops its own liquidity management policies according to its own characteristics, and assumes its own liquidity risk management responsibility. Subsidiaries are required to report their respective liquidity positions on a regular basis to RMD (Interest Rate and Liquidity Risk Management) of BOCHK, which consolidates this information and evaluates group-wide liquidity risk.

(A) Liquidity coverage ratio

	2017	2016
Average value of liquidity coverage ratio		
– First quarter	**121.41%**	112.92%
– Second quarter	**123.88%**	109.70%
– Third quarter	**121.12%**	118.69%
– Fourth quarter	**135.64%**	107.02%

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 BOCHK's website at www.bochk.com.

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(B) Maturity analysis

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

	2017							
	On demand HK$'m	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Indefinite HK$'m	Total HK$'m
Assets								
Cash and balances with banks and other financial institutions	248,168	108,624	–	–	–	–	7,413	364,205
Placements with banks and other financial institutions maturing between one and twelve months	–	–	37,210	21,846	–	–	–	59,056
Financial assets at fair value through profit or loss								
– Held for trading								
– Debt securities	–	5,726	6,909	15,328	9,753	4,726	–	42,442
– Certificates of deposit	–	488	566	289	138	2	–	1,483
– Designated at fair value through profit or loss								
– Debt securities	–	547	91	205	4,317	24,184	161	29,505
– Certificates of deposit	–	–	–	3	156	–	–	159
– Equity securities and fund	–	–	–	–	–	–	12,746	12,746
– Other debt instruments	–	3,861	995	2,003	–	–	–	6,859
Derivative financial instruments	10,492	4,134	4,097	6,697	5,521	2,600	–	33,541
Hong Kong SAR Government certificates of indebtedness	146,200	–	–	–	–	–	–	146,200
Advances and other accounts								
– Advances to customers	131,093	27,852	50,152	163,762	521,048	244,342	2,126	1,140,375
– Trade bills	20	6,813	16,782	19,360	–	–	–	42,975
– Advances to banks and other financial institutions	–	8	862	809	4,580	–	–	6,259
Investment in securities								
– Available-for-sale								
– Debt securities	–	59,390	64,221	111,790	192,123	107,211	204	534,939
– Certificates of deposit	–	1,716	8,222	9,723	6,884	217	–	26,762
– Held-to-maturity								
– Debt securities	–	1,312	2,615	8,162	23,795	14,657	–	50,541
– Certificates of deposit	–	–	–	–	18	–	–	18
– Loans and receivables								
– Debt securities	–	–	499	–	–	–	–	499
– Equity securities and fund	–	–	–	–	–	–	5,413	5,413
Interests in associates and joint ventures	–	–	–	–	–	–	417	417
Investment properties	–	–	–	–	–	–	19,669	19,669
Properties, plant and equipment	–	–	–	–	–	–	47,261	47,261
Other assets (including deferred tax assets)	28,492	18,168	777	1,183	9,472	16,300	37	74,429
Total assets	564,465	238,639	193,998	361,160	777,805	414,239	95,447	2,645,753
Liabilities								
Hong Kong SAR currency notes in circulation	146,200	–	–	–	–	–	–	146,200
Deposits and balances from banks and other financial institutions	172,832	40,956	8,099	362	825	–	–	223,074
Financial liabilities at fair value through profit or loss	–	7,102	4,118	7,070	954	476	–	19,720
Derivative financial instruments	6,668	5,600	5,033	6,800	4,634	2,309	–	31,044
Deposits from customers	1,114,239	355,222	160,565	140,233	1,254	–	–	1,771,513
Debt securities and certificates of deposit in issue								
– Debt securities	–	7,091	1,971	12,579	–	–	–	21,641
Other accounts and provisions (including current and deferred tax liabilities)	35,835	15,223	2,103	3,008	6,831	8	–	63,008
Insurance contract liabilities	35,707	418	890	3,781	14,214	48,219	–	103,229
Subordinated liabilities	–	–	422	16	18,542	–	–	18,980
Total liabilities	1,511,481	431,612	183,201	173,849	47,254	51,012	–	2,398,409
Net liquidity gap	(947,016)	(192,973)	10,797	187,311	730,551	363,227	95,447	247,344

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

	2016							
	On demand HK$'m	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Indefinite HK$'m	Total HK$'m
Assets								
Cash and balances with banks and other financial institutions	115,448	108,175	–	–	–	–	12,683	236,306
Placements with banks and other financial institutions maturing between one and twelve months	–	–	30,211	42,399	–	–	–	72,610
Financial assets at fair value through profit or loss								
– Held for trading								
– Debt securities	–	1,415	3,723	9,430	13,083	3,417	–	31,068
– Certificates of deposit	–	–	1,140	412	591	–	–	2,143
– Designated at fair value through profit or loss								
– Debt securities	–	109	281	3,339	3,054	16,174	–	22,957
– Certificates of deposit	–	2	–	2	144	–	–	148
– Equity securities and fund	–	–	–	–	–	–	5,265	5,265
– Other debt instruments	–	4,097	1,680	–	–	–	–	5,777
Derivative financial instruments	14,662	8,965	10,119	21,369	6,533	2,684	–	64,332
Hong Kong SAR Government certificates of indebtedness	123,390	–	–	–	–	–	–	123,390
Advances and other accounts								
– Advances to customers	93,552	23,458	62,492	134,763	443,501	224,874	2,124	984,764
– Trade bills	6	5,094	4,229	7,916	–	–	–	17,245
– Advances to banks and other financial institutions	–	3	1	577	5,435	–	–	6,016
Investment in securities								
– Available-for-sale								
– Debt securities	–	37,531	80,722	79,913	167,355	105,014	–	470,535
– Certificates of deposit	–	2,985	16,078	30,274	7,357	209	–	56,903
– Held-to-maturity								
– Debt securities	–	870	3,965	17,402	24,301	14,311	1	60,850
– Certificates of deposit	–	–	–	–	–	18	–	18
– Loans and receivables								
– Debt securities	–	–	–	935	–	–	–	935
– Equity securities and fund	–	–	–	–	–	–	4,409	4,409
Interests in associates and joint ventures	–	–	–	–	–	–	319	319
Investment properties	–	–	–	–	–	–	18,227	18,227
Properties, plant and equipment	–	–	–	–	–	–	45,812	45,812
Other assets (including deferred tax assets)	30,971	15,449	585	942	7,620	15,806	45	71,418
Assets held for sale	6,097	6,304	4,791	9,851	18,486	5,684	2,080	53,293
Total assets	384,126	214,457	220,017	359,524	697,460	388,191	90,965	2,354,740
Liabilities								
Hong Kong SAR currency notes in circulation	123,390	–	–	–	–	–	–	123,390
Deposits and balances from banks and other financial institutions	152,559	19,576	15,136	9,574	1,904	184	–	198,933
Financial liabilities at fair value through profit or loss	–	3,705	5,582	2,238	1,257	589	–	13,371
Derivative financial instruments	10,511	3,394	7,375	20,140	5,218	2,666	–	49,304
Deposits from customers	980,039	273,413	185,224	80,793	398	–	–	1,519,867
Debt securities and certificates of deposit in issue								
– Debt securities	–	–	–	10	1,111	–	–	1,121
Other accounts and provisions (including current and deferred tax liabilities)	36,350	14,271	1,763	2,532	6,644	–	–	61,560
Insurance contract liabilities	26,730	284	476	1,146	13,969	43,929	–	86,534
Subordinated liabilities	–	–	418	16	18,659	–	–	19,093
Liabilities associated with assets held for sale	24,404	7,694	7,467	7,186	262	–	–	47,013
Total liabilities	1,353,983	322,337	223,441	123,635	49,422	47,368	–	2,120,186
Net liquidity gap	(969,857)	(107,880)	(3,424)	235,889	648,038	340,823	90,965	234,554

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(B) Maturity analysis (continued)

The above maturity classifications have been prepared in accordance with relevant provisions under the Banking (Disclosure) Rules. The Group has reported assets such as advances and debt securities which have been overdue for not more than one month as "On demand". In the case of an asset that is repayable by different payments or instalments, only that portion of the asset that is actually overdue is reported as overdue. Any part of the asset that is not due is reported according to the residual maturity unless the repayment of the asset is in doubt in which case the amount is reported as "Indefinite". The above assets are stated after deduction of provisions, if any.

The analysis of debt securities by remaining period to maturity is disclosed in order to comply with relevant provisions under the Banking (Disclosure) Rules. The disclosure does not imply that the securities will be held to maturity.

The above analysis in respect of insurance contract liabilities represents the estimated timing of net cash outflows resulting from recognised insurance contract liabilities on the balance sheet as at 31 December.

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities

(a) Non-derivative cash flows

The tables below summarise the cash flows of the Group as at 31 December for non-derivative financial liabilities by remaining contractual maturity.

	2017					
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Total HK$'m
Financial liabilities						
Hong Kong SAR currency notes in circulation	146,200	–	–	–	–	146,200
Deposits and balances from banks and other financial institutions	213,821	8,132	393	900	–	223,246
Financial liabilities at fair value through profit or loss	7,107	4,132	7,121	1,020	500	19,880
Deposits from customers	1,469,664	161,052	142,016	1,296	–	1,774,028
Debt securities and certificates of deposit in issue	7,096	1,976	12,962	–	–	22,034
Subordinated liabilities	–	542	558	21,209	–	22,309
Other financial liabilities	40,769	486	834	–	–	42,089
Total financial liabilities	1,884,657	176,320	163,884	24,425	500	2,249,786

	2016					
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Total HK$'m
Financial liabilities						
Hong Kong SAR currency notes in circulation	123,390	–	–	–	–	123,390
Deposits and balances from banks and other financial institutions	172,143	15,185	9,665	1,945	187	199,125
Financial liabilities at fair value through profit or loss	3,707	5,600	2,272	1,322	625	13,526
Deposits from customers	1,253,530	185,650	81,625	409	–	1,521,214
Debt securities and certificates of deposit in issue	–	–	39	1,151	–	1,190
Subordinated liabilities	–	538	555	22,140	–	23,233
Other financial liabilities	40,678	397	459	5	–	41,539
Financial liabilities associated with assets held for sale	32,086	7,446	7,241	69	–	46,842
Total financial liabilities	1,625,534	214,816	101,856	27,041	812	1,970,059

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(b) Derivative cash flows

The tables below summarise the cash flows (including assets held for sale and liabilities associated with assets held for sale) of the Group by remaining contractual maturity as at 31 December for derivative financial liabilities that will be settled on a net basis, together with all derivative financial instruments that will be settled on a gross basis regardless of whether the contract is in an asset or liability position. The amounts disclosed in the tables are the contractual undiscounted cash flows, except for certain derivatives which are disclosed at fair value.

The Group's derivative financial instruments that will be settled on a net basis mainly include interest rate swaps whereas derivative financial instruments that will be settled on a gross basis mainly include currency forwards and currency swaps.

	2017					
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Total HK$'m
Derivative financial liabilities settled on a net basis	**(7,463)**	**(720)**	**(1,126)**	**(3,577)**	**(856)**	**(13,742)**
Derivative financial instruments settled on a gross basis						
Total inflow	**635,704**	**462,071**	**492,297**	**125,606**	**5,181**	**1,720,859**
Total outflow	**(636,212)**	**(462,229)**	**(491,628)**	**(125,756)**	**(5,192)**	**(1,721,017)**

	2016					
	Up to 1 month HK$'m	1 to 3 months HK$'m	3 to 12 months HK$'m	1 to 5 years HK$'m	Over 5 years HK$'m	Total HK$'m
Derivative financial liabilities settled on a net basis	(10,810)	(423)	(574)	(2,631)	(1,213)	(15,651)
Derivative financial instruments settled on a gross basis						
Total inflow	659,303	483,596	845,015	100,984	2,005	2,090,903
Total outflow	(651,702)	(480,745)	(844,041)	(100,928)	(2,021)	(2,079,437)

4. Financial risk management (continued)

4.3 Liquidity risk (continued)

(C) Analysis of undiscounted cash flows by contractual maturities (continued)

(c) Off-balance sheet items

Loan commitments

The contractual amounts of the Group's off-balance sheet financial instruments as at 31 December 2017 that the Group commits to extend credit to customers and other facilities amounted to HK$569,658 million (2016: HK$533,322 million). Those loan commitments can be drawn within one year.

Financial guarantees and other financial facilities

Financial guarantees and other financial facilities of the Group as at 31 December 2017 amounting to HK$66,800 million (2016: HK$51,165 million) are maturing no later than one year.

4.4 Insurance risk

The Group is in the business of insuring against the risk of mortality, morbidity, disability, critical illness, accidents and related risks. The Group manages these risks through the application of its underwriting policies and reinsurance arrangements.

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

Within the insurance process, concentrations of risk may arise where a particular event or series of events could impact heavily on the Group's liabilities. Such concentrations may arise from a single insurance contract or through a small number of related contracts, and relate to circumstances where significant liabilities could arise.

For the in-force insurance contracts, most of the underlying insurance liabilities are related to endowment, universal life, annuity, whole life and unit-linked insurance products. For most of the insurance policies issued, the Group has a retention limit on any single life insured. The Group cedes the excess of the insured benefit over the limit to reinsurer under an excess of loss reinsurance arrangement. For some of the insurance liabilities, the Group has entered into reinsurance arrangements that reinsure most of insurance risk.

Uncertainty in the estimation of future benefit payments and premium receipts for long-term insurance contracts arises from the unpredictability of long-term changes in overall levels of mortality, morbidity and persistency. In this regard, the Group has conducted relevant experience studies. The results of such studies are considered in determining the assumptions of insurance liability which include appropriate level of prudential margins.

4. Financial risk management (continued)

4.4 Insurance risk (continued)

(A) Process used to decide on assumptions

In determining the long term business fund liabilities, the Group follows the Insurance (Determination of Long Term Liabilities) Rules and makes prudent assumptions which include appropriate margins for adverse deviation of the relevant factors. It takes account of all prospective liabilities as determined by the policy terms and conditions for each existing contract, taking credit for premiums payable after the valuation date. The determination of liability is based on current assumptions made as at the valuation date as to mortality rates, and takes into account of various appropriate discount rates, and with due regard to the reasonable expectation of policyholders. A prudent margin for adverse deviations is included in the assumptions.

The assumptions adopted for the insurance liabilities disclosed in this note are summarised as follows:

Mortality and Morbidity

The amount of liability in respect of any category of contract shall, where relevant, be determined on the basis of prudent rates of mortality and morbidity, plus a margin for adverse deviation. The assumptions used for determination of future liabilities are based on population statistics or reinsurance information, adjusted where appropriate to reflect the Group's own experience and relevant reinsurance arrangements.

Interest rates adopted for valuation purpose

Homogeneous life insurance policies are grouped into segments and are matched by specific assets. The duration of liabilities under each segment is calculated for valuation purpose.

Investment guarantee of investment contract with discretionary participating feature

The amount of the liability in respect of the investment guarantee provided by the investment contract with discretionary participation feature is determined by stochastic analysis based on historical economic data to reflect the value-at-risk at 99% confidence level.

Acquisition expense

The acquisition expense assumptions used for determination of future liabilities are based on the Group's own experience. The Group has changed the acquisition expense assumptions for new business written based on updated expense experience of the Group.

(B) Change in assumptions

The Group has changed the interest rates adopted for valuation purposes to reflect the changes in the market interest rates and the yields of investment portfolio backing the policy liabilities. The valuation interest rate assumptions used for the year end valuation purpose were in the range of 0% to 3.57% in 2017 (2016: 0% to 3.51%).

4. Financial risk management (continued)

4.4 Insurance risk (continued)

(C) Sensitivity analysis

The following table presents the sensitivity of the long-term business fund liabilities to movements in the key assumptions used in the estimation of insurance liabilities:

Sensitivity analysis – life and annuity insurance contracts:

Scenario	Change in variable	Decrease in profit after tax due to changes in insurance liabilities 2017 HK$'m	2016 HK$'m
Worsening of mortality & morbidity	10%	**(129)**	(84)
Lowering of interest rate	50 basis points	**(1,158)**	(800)

The above analyses are based on a change in an assumption while holding all other assumptions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may be correlated – for example, changes in interest rate and in market values; and changes in lapses and in future mortality and morbidity.

Sensitivity analysis – Linked long term insurance contracts, Retirement scheme management category III insurance contracts, and Retirement scheme management category I investment contracts with "DPF":

The reserves on Retirement scheme management category III insurance contracts, Retirement scheme management category I investment contracts with "DPF" and non-unitised reserve on Linked long term insurance contracts are insignificant to the whole portfolio, and no sensitivity analysis has been performed. The insurance liabilities for these three components contributed to less than 0.08% of the total insurance liabilities at the balance sheet date.

For unit-linked fund liabilities (unitised reserve), the liabilities are backed by the unit-linked fund asset values.

Among linked long term insurance contracts, there are contracts with minimum guaranteed death benefits that expose the Group to the risk arising from declines in the value of underlying investments. This may increase the Group's net exposure to mortality risk.

4.5 Capital management

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

4. Financial risk management (continued)

4.5 Capital management (continued)

The Group has developed and maintained a sound framework of policies and controls on capital management to support the development of the Group's business and to meet the statutory capital adequacy ratio. The ALCO monitors the Group's capital adequacy. The Group has complied with all the statutory capital requirements of the HKMA for the reported periods in respect of banking operation as further elaborated below.

The Group has adopted the foundation internal ratings-based ("FIRB") approach to calculate the credit risk capital charge for the majority of its non-securitisation exposures and the internal ratings-based (securitisation) approach to calculate the credit risk capital charge for its securitisation exposures. A small residual credit exposures which includes the credit exposures of oversea subsidiaries or branches are remained under the standardised (credit risk) ("STC") approach. The Group has adopted the standardised credit valuation adjustment ("CVA") method to calculate the capital charge for the CVA risk of the counterparty.

The Group continues to adopt the internal models ("IMM") approach to calculate the general market risk capital charge for foreign exchange and interest rate exposures and, with the approval from the HKMA, exclude its structural FX positions in the calculation of the market risk capital charge. The Group continues to adopt the standardised (market risk) ("STM") approach to calculate the market risk capital charge for the remaining exposures.

The Group continues to adopt standardised (operational risk) ("STO") approach to calculate the operational risk capital charge.

The Group has continued to adopt an internal capital adequacy assessment process ("ICAAP") to comply with the HKMA's requirements in the Supervisory Policy Manual "Supervisory Review Process" in 2017. Based on the HKMA's guidelines on Pillar II, ICAAP has been initiated to assess the extra capital needed to cover the material risks not captured or not adequately captured under Pillar I, and therefore minimum Common Equity Tier 1 capital ratio, minimum Tier 1 capital ratio and minimum Total capital ratio are determined. Meanwhile, operating ranges for the aforementioned capital ratios have also been established which enable the flexibility for future business growth and efficiency of capital utilisation. The Group considers this ICAAP as an on-going process for capital management and periodically reviews and adjusts its capital structure where appropriate in relation to the overall risk profile.

In addition, the capital plan of the Group is drawn up annually and then submitted to the Board for approval after endorsement of the ALCO. The plan is built up by assessing the implications of various factors upon capital adequacy such as the business strategies, return on equity, risk appetite, credit rating, as well as regulatory requirements. Hence, the future capital requirement is determined and capital sources are identified also. The plan is to ensure the Group maintains adequate capital and appropriate capital structure which align with its business development needs, thereby achieving an optimal balance among risk, return and capital adequacy.

(A) Basis of regulatory consolidation

The consolidation basis for regulatory purposes comprises the positions of BOCHK and certain subsidiaries specified by the HKMA in accordance with the Banking (Capital) Rules. For accounting purposes, subsidiaries are consolidated in accordance with HKFRSs and the list of subsidiaries is set out in "Appendix – Subsidiaries of the Company".

The Company, its subsidiaries of BOC Group Life Assurance Company Limited, BOCHK Asset Management (Cayman) Limited and BOC Insurance (International) Holdings Company 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.

4. Financial risk management (continued)

4.5 Capital management (continued)

(A) Basis of regulatory consolidation (continued)

The particulars of the above-mentioned subsidiaries of BOCHK are as follows:

Name	2017		2016	
	Total assets HK$'m	Total equity HK$'m	Total assets HK$'m	Total equity HK$'m
BOC Group Trustee Company Limited	**200**	**200**	200	200
BOCI-Prudential Trustee Limited	**506**	**464**	457	429
China Bridge (Malaysia) Sdn. Bhd.	**37**	**31**	27	23
Bank of China (Hong Kong) Nominees Limited	**–**	**–**	–	–
Bank of China (Hong Kong) Trustees Limited	**15**	**15**	10	10
BOCHK Information Technology (Shenzhen) Co., Ltd.	**355**	**238**	309	204
BOCHK Information Technology Services (Shenzhen) Co., Ltd.	**366**	**312**	313	269
Che Hsing (Nominees) Limited	**1**	**1**	1	1
Po Sang Financial Investment Services Company Limited	**363**	**346**	365	346
Po Sang Securities and Futures Limited	**990**	**511**	603	466
Sin Chiao Enterprises Corporation, Limited	**7**	**7**	6	6
Sin Hua Trustee Limited	**4**	**4**	4	4
Billion Express Development Inc.[1]	**–**	**–**	–	–
Billion Orient Holdings Ltd.[1]	**–**	**–**	–	–
Elite Bond Investments Ltd.[1]	**–**	**–**	–	–
Express Capital Enterprise Inc.[1]	**–**	**–**	–	–
Express Charm Holdings Corp.[1]	**–**	**–**	–	–
Express Shine Assets Holdings Corp.[1]	**–**	**–**	–	–
Express Talent Investment Ltd.[1]	**–**	**–**	–	–
Gold Medal Capital Inc.[1]	**–**	**–**	–	–
Gold Tap Enterprises Inc.[1]	**–**	**–**	–	–
Maxi Success Holdings Ltd.[1]	**–**	**–**	–	–
Smart Linkage Holdings Inc.[1]	**–**	**–**	–	–
Smart Union Capital Investments Ltd.[1]	**–**	**–**	–	–
Success Trend Development Ltd.[1]	**–**	**–**	–	–
Wise Key Enterprises Corp.[1]	**–**	**–**	–	–
Sino Information Services Company Limited[2]	**–**	**–**	–	–
Chiyu Banking Corporation (Nominees) Limited[3]	**–**	**–**	139	139
Grace Charter Limited[3]	**–**	**–**	–	(11)
Seng Sun Development Company, Limited[3]	**–**	**–**	41	41

4. Financial risk management (continued)

4.5 Capital management (continued)

(A) Basis of regulatory consolidation (continued)

Notes:
1. The acquisition of the 14 special purpose vehicle companies was completed on 9 January 2017.
2. Sino Information Services Company Limited was dissolved on 14 February 2017.
3. The disposal of Chiyu Banking Corporation (Nominees) Limited, Grace Charter Limited and Seng Sun Development Company, Limited was completed on 27 March 2017.

The principal activities of the above subsidiaries are set out in "Appendix – Subsidiaries of the Company".

There were no subsidiaries which are included within the regulatory scope of consolidation but not included within the accounting scope of consolidation as at 31 December 2017 (2016: Nil).

There were also no subsidiaries which are included within both the accounting scope of consolidation and the regulatory scope of consolidation where the methods of consolidation differ as at 31 December 2017 (2016: Nil).

(B) Capital ratio

The capital ratios are analysed as follows:

	2017	2016
CET1 capital ratio	**16.52%**	17.64%
Tier 1 capital ratio	**16.52%**	17.69%
Total capital ratio	**20.39%**	22.35%

4. Financial risk management (continued)

4.5 Capital management (continued)

(B) Capital ratio (continued)

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

	2017 HK$'m	2016 HK$'m
CET1 capital: instruments and reserves		
Directly issued qualifying CET1 capital instruments	**43,043**	43,043
Retained earnings	**142,208**	129,644
Disclosed reserves	**43,673**	41,446
Minority interests arising from CET1 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in CET1 capital of the consolidation group)	**–**	722
CET1 capital before regulatory deductions	**228,924**	214,855
CET1 capital: regulatory deductions		
Valuation adjustments	**(12)**	(78)
Deferred tax assets net of deferred tax liabilities	**(51)**	(77)
Gains and losses due to changes in own credit risk on fair valued liabilities	**(69)**	(202)
Cumulative fair value gains arising from the revaluation of land and buildings (own-use and investment properties)	**(48,556)**	(46,443)
Regulatory reserve for general banking risks	**(10,224)**	(9,227)
Total regulatory deductions to CET1 capital	**(58,912)**	(56,027)
CET1 capital	**170,012**	158,828
AT1 capital: instruments		
AT1 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in AT1 capital of the consolidation group)	**–**	458
AT1 capital	**–**	458
Tier 1 capital	**170,012**	159,286

4. Financial risk management (continued)

4.5 Capital management (continued)

(B) Capital ratio (continued)

	2017 HK$'m	2016 HK$'m
Tier 2 capital: instruments and provisions		
Capital instruments subject to phase out arrangements from Tier 2 capital	**11,576**	15,435
Tier 2 capital instruments issued by consolidated bank subsidiaries and held by third parties (amount allowed in Tier 2 capital of the consolidation group)	**–**	221
Collective impairment allowances and regulatory reserve for general banking risks eligible for inclusion in Tier 2 capital	**6,390**	5,371
Tier 2 capital before regulatory deductions	**17,966**	21,027
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	**21,850**	20,899
Total regulatory deductions to Tier 2 capital	**21,850**	20,899
Tier 2 capital	**39,816**	41,926
Total capital	**209,828**	201,212

The capital buffer ratios are analysed as follows:

	2017	2016
Capital conservation buffer ratio	**1.250%**	0.625%
Higher loss absorbency ratio	**0.750%**	0.375%
Countercyclical capital buffer ratio	**0.934%**	0.484%

The additional information of capital disclosures and countercyclical capital buffer ratio disclosures is available under section "Regulatory Disclosures" on BOCHK's website at www.bochk.com.

(C) Leverage ratio

The leverage ratio is analysed as follows:

	2017 HK$'m	2016 HK$'m
Tier 1 capital	**170,012**	159,286
Leverage ratio exposure	**2,461,068**	2,155,889
Leverage ratio	**6.91%**	7.39%

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

5. Fair values of assets and liabilities

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy as defined in HKFRS 13, "Fair value measurement". The categorisation are determined with reference to the observability and significance of the inputs used in the valuation methods and based on the lowest level input that is significant to the fair value measurement as a whole:

– Level 1: based on quoted prices (unadjusted) in active markets for identical assets or liabilities. This category includes equity securities listed on exchange, debt instruments issued by certain governments, certain exchange-traded derivative contracts and precious metals.

– Level 2: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is observable, either directly or indirectly. This category includes majority of the OTC derivative contracts, debt securities and certificates of deposit with quote from pricing services vendors, issued structured deposits and other debt instruments. It also includes precious metals and properties with insignificant adjustments made to observable market inputs.

– Level 3: based on valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable. This category includes equity investment, debt instruments and certain OTC derivative contracts with significant unobservable components. It also includes properties with significant adjustments made to observable market inputs.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by reassessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

5.1 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.

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

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 and correlations, 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 and other debt instruments

The fair value of these instruments is determined by obtaining quoted market prices from exchange, dealer or independent pricing service vendors or using discounted cash flow technique. Discounted cash flow model is a valuation technique that measures present value using estimated expected future cash flows from the instruments and then discounts these flows using a discount rate or discount margin that reflects the credit spreads required by the market for instruments with similar risk. These inputs are observable or can be corroborated by observable or unobservable market data.

Asset backed securities

For this class of instruments, external prices are obtained from independent third parties. The valuation of these securities, depending on the nature of transaction, is estimated from market standard cash flow models with input parameter which include spreads to discount rates, default and recovery rates and prepayment rates that may be observable or compiled through matrix pricing for similar issues.

Derivatives

OTC derivative contracts include forward, swap and option contracts on foreign exchange, interest rate, equity, commodity or credit. The fair values of these contracts are mainly measured using valuation techniques such as discounted cash flow models and option pricing models. The inputs can be observable or unobservable market data. Observable inputs include interest rate, foreign exchange rates, equity and stock prices, commodity prices, credit default swap spreads, volatilities and correlations. Unobservable inputs 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 ("CVAs") and debit valuation adjustments ("DVAs") are applied to the Group's OTC derivatives. These adjustments reflect market factors movement, expectations of counterparty creditworthiness and the Group's own credit spread respectively. They are mainly determined for each counterparty and are dependent on expected future values of exposures, default probabilities and recovery rates.

Financial liabilities designated at fair value through profit or loss

This class of instruments includes certain deposits received from customers that are embedded with derivatives. The plain vanilla contracts are valued in the similar way described in previous debt securities section. The fair value of structured deposits is derived from the fair value of the underlying deposit by using discounted cash flow analysis taking the Group's own credit risk into account, and the fair value of the embedded derivatives determined as described in the paragraph above on derivatives.

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy

	2017			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Financial assets				
Financial assets at fair value through profit or loss (Note 23)				
– Trading assets				
– Debt securities and certificates of deposit	1,947	41,978	–	43,925
– Equity securities	203	–	–	203
– Other debt instruments	–	6,859	–	6,859
– Financial assets designated at fair value through profit or loss				
– Debt securities and certificates of deposit	–	26,552	3,112	29,664
– Equity securities	3,481	–	–	3,481
– Fund	6,969	1,580	513	9,062
Derivative financial instruments (Note 24)	10,510	23,031	–	33,541
Available-for-sale securities (Note 27)				
– Debt securities and certificates of deposit	111,552	449,139	1,010	561,701
– Equity securities	4,468	134	811	5,413
– Fund	–	–	–	–
Financial liabilities				
Financial liabilities at fair value through profit or loss (Note 33)				
– Trading liabilities	–	16,936	–	16,936
– Financial liabilities designated at fair value through profit or loss	–	2,784	–	2,784
Derivative financial instruments (Note 24)	6,703	24,341	–	31,044

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(A) Fair value hierarchy (continued)

	2016			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Financial assets				
Financial assets at fair value through profit or loss (Note 23)				
– Trading assets				
– Debt securities and certificates of deposit	587	32,462	162	33,211
– Equity securities	76	–	–	76
– Other debt instruments	–	5,777	–	5,777
– Financial assets designated at fair value through profit or loss				
– Debt securities and certificates of deposit	–	20,227	2,878	23,105
– Equity securities	2,008	–	–	2,008
– Fund	3,181	–	–	3,181
Derivative financial instruments (Note 24)	14,658	49,674	–	64,332
Available-for-sale securities (Note 27)				
– Debt securities and certificates of deposit	122,789	402,914	1,735	527,438
– Equity securities	3,304	237	718	4,259
– Fund	150	–	–	150
Financial liabilities				
Financial liabilities at fair value through profit or loss (Note 33)				
– Trading liabilities	–	9,946	–	9,946
– Financial liabilities designated at fair value through profit or loss	–	3,425	–	3,425
Derivative financial instruments (Note 24)	10,775	38,529	–	49,304

There were no financial asset and liability transfers between level 1 and level 2 for the Group during the year (2016: Nil).

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items

	2017				
	Financial assets				
	Trading assets	Financial assets designated at fair value through profit or loss		Available-for-sale securities	
	Debt securities and certificates of deposit HK$'m	Debt securities and certificates of deposit HK$'m	Fund HK$'m	Debt securities and certificates of deposit HK$'m	Equity securities HK$'m
At 1 January 2017	162	2,878	–	1,735	718
Gains					
– Income statement					
– Net trading gain	–	–	–	–	–
– Net gain on financial instruments designated at fair value through profit or loss	–	234	43	–	–
– Other comprehensive income					
– Change in fair value of available-for-sale securities	–	–	–	157	88
Additions	–	–	470	–	5
Disposals, redemptions and maturity	(157)	–	–	(287)	–
Transfer out of level 3	(5)	–	–	(238)	–
Reclassification	–	–	–	(357)	–
At 31 December 2017	–	3,112	513	1,010	811
Total unrealised gains for the year included in income statement for financial assets held as at 31 December 2017					
– Net trading gain	–	–	–	–	–
– Net gain on financial instruments designated at fair value through profit or loss	–	234	43	–	–
	–	234	43	–	–

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

	2016				
	Financial assets				
	Trading assets	Financial assets designated at fair value through profit or loss		Available-for-sale securities	
	Debt securities and certificates of deposit HK$'m	Debt securities and certificates of deposit HK$'m	Fund HK$'m	Debt securities and certificates of deposit HK$'m	Equity securities HK$'m
At 1 January 2016	–	1,829	–	1,095	287
(Losses)/gains					
– Income statement					
– Net trading loss	(8)	–	–	–	–
– Net gain on financial instruments designated at fair value through profit or loss	–	20	–	–	–
– Other comprehensive income					
– Change in fair value of available-for-sale securities	–	–	–	(40)	17
Additions	170	1,029	–	1,265	419
Disposals, redemptions and maturity	–	–	–	–	–
Transfer out of level 3	–	–	–	–	–
Reclassification	–	–	–	–	–
Classified as assets held for sale	–	–	–	(585)	(5)
At 31 December 2016	162	2,878	–	1,735	718
Total unrealised (losses)/gains for the year included in income statement for financial assets held as at 31 December 2016					
– Net trading loss	(8)	–	–	–	–
– Net gain on financial instruments designated at fair value through profit or loss	–	20	–	–	–
	(8)	20	–	–	–

5. Fair values of assets and liabilities (continued)

5.1 Financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

As at 31 December 2017 and 2016, financial instruments categorised as level 3 are mainly comprised of debt securities and certificates of deposit, fund and unlisted equity shares.

Certain debt securities and certificates of deposit were transferred out of level 3 during 2017 due to change of valuation observability. For certain illiquid debt securities and certificates of deposit and fund, the Group obtains valuation quotations from counterparties which may be based on unobservable inputs with significant impact on the valuation. Therefore, these instruments have been classified by the Group as level 3. The Group has established internal control procedures to control the Group's exposure to such financial instruments.

The fair values of unlisted available-for-sale equity shares are determined with reference to multiples of comparable listed companies, such as average of the price/earning ratios of comparables, or net asset value, if appropriate comparables are not available. The fair value is positively correlated to the price/earning ratios of appropriate comparables or net asset values. Had the net asset value of the underlying equity investments increased/decreased by 5%, the Group's other comprehensive income would have increased/decreased by HK$41 million (2016: HK$36 million).

5.2 Financial instruments not measured at fair value

Fair value estimates are made at a specific point in time based on relevant market information and information about various financial instruments. The following methods and assumptions have been used to estimate the fair value of each class of financial instrument as far as practicable.

Balances with/from banks and other financial institutions and trade bills

Substantially all the financial assets and liabilities mature within one year from the balance sheet date and their carrying value approximates fair value.

Advances to customers and banks and other financial institutions

Substantially all the advances to customers and banks and other financial institutions are on floating rate terms, bear interest at prevailing market interest rates and their carrying value approximates fair value.

Held-to-maturity securities

The fair value of held-to-maturity securities is determined by using the same approach as those debt securities and certificates of deposit and asset backed securities measured at fair value as described in Note 5.1.

5. Fair values of assets and liabilities (continued)

5.2 Financial instruments not measured at fair value (continued)

Loans and receivables

A discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity.

Deposits from customers

Substantially all the deposits from customers mature within one year from the balance sheet date and their carrying value approximates fair value.

Debt securities and certificates of deposit in issue

The fair value of these instruments is determined by using the same approach as those debt securities and certificates of deposit measured at fair value as described in Note 5.1.

Subordinated liabilities

Fair value for subordinated notes is based on market prices or broker/dealer price quotations. The subordinated loan is on floating rate terms, bears interest at prevailing market interest rates and its carrying value approximates fair value.

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.

	2017		2016	
	Carrying value HK$'m	**Fair value HK$'m**	Carrying value HK$'m	Fair value HK$'m
Financial assets				
Held-to-maturity securities (Note 27)	**50,559**	**50,979**	60,868	61,358
Loans and receivables (Note 27)	**499**	**498**	935	935
Financial liabilities				
Debt securities and certificates of deposit in issue (Note 35)	**21,641**	**21,578**	1,121	1,126
Subordinated liabilities (Note 39) – Subordinated notes	**18,917**	**20,985**	19,014	21,143

5. Fair values of assets and liabilities (continued)

5.2 Financial instruments not measured at fair value (continued)

The following tables show the fair value hierarchy for financial instruments with fair values disclosed.

	2017			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Financial assets				
Held-to-maturity securities	**972**	**49,653**	**354**	**50,979**
Loans and receivables	**–**	**498**	**–**	**498**
Financial liabilities				
Debt securities and certificates of deposit in issue	**–**	**21,578**	**–**	**21,578**
Subordinated liabilities – Subordinated notes	**–**	**20,985**	**–**	**20,985**

	2016			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Financial assets				
Held-to-maturity securities	1,233	60,125	–	61,358
Loans and receivables	–	935	–	935
Financial liabilities				
Debt securities and certificates of deposit in issue	–	1,126	–	1,126
Subordinated liabilities – Subordinated notes	–	21,143	–	21,143

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value

The Group uses valuation techniques or quoted market prices in active market to determine the fair value of non-financial instruments.

Investment properties and premises

The Group's properties can be divided into investment properties and premises. All of the Group's investment properties and premises were revalued as at year end. This year, the valuations were carried out by an independent firm of chartered surveyors, Knight Frank Petty Limited, who have among their staff Fellow and Members of The Hong Kong Institute of Surveyors with recent experience in the locations and categories of properties being valued. The Group's Management had discussions with the surveyors on the valuation methods, valuation assumptions and valuation results when the valuation is performed at each interim and annual reporting date. There has been no change in valuation methods during the year and the methods used are consistent with last year.

(i) Valuation methods and inputs used in Level 2 fair value measurements

The fair value of properties classified as Level 2 is determined using either the market comparison approach by reference to recent sales price of comparable properties or the income capitalisation approach by reference to market rent and capitalisation rate, with appropriate adjustments to reflect the differences between the comparable properties and the subject properties. These adjustments are considered as insignificant to the entire measurement.

The Group's properties are located in Hong Kong, certain major cities in the PRC, Thailand and Malaysia where the property markets are considered active and transparent. Sales price, market rent and capitalisation rate of comparable properties are generally observable either directly or indirectly in these markets.

(ii) Information about Level 3 fair value measurements

The fair value of all of the Group's properties classified as Level 3, except for the bank vault, is determined using either the market comparison approach or the income capitalisation approach, adjusted for a premium or a discount specific to the features of the Group's properties compared to the comparable properties.

The fair value of the bank vault is determined using the depreciated replacement cost approach as no direct comparable is available given the specialised nature of the property. The major inputs are the market value of the existing land, the current cost of replacing the property and the depreciation rate. Appropriate adjustments are made to reflect the specialised nature of the property.

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value (continued)

Investment properties and premises (continued)

(ii) Information about Level 3 fair value measurements (continued)

The valuation methods and significant unobservable inputs used in the fair value measurement of the Group's properties classified as Level 3 are as follows:

	Valuation method	Significant unobservable inputs	Weighted average	Relationship of unobservable inputs to fair value
Bank vault	Depreciated replacement cost approach	Depreciation rate	2% (2016: 2%) per year	The higher the depreciation rate, the lower the fair value.
		Premium on specialised nature of the property	+15% (2016: +15%) to building cost	The higher the premium, the higher the fair value.
Other properties	Market comparison approach or income capitalisation approach	Premium/(discount) on features of the property compared to comparable properties	-11% (2016: -6%)	The higher the premium, the higher the fair value. The higher the discount, the lower the fair value.

Premium/(discount) on features of a property is determined after taken into account various factors, such as time for market movement, location, accessibility, building age/condition, floor level, size, layout, etc., with reference to the differences in features with comparable properties.

Precious metals

The fair values of precious metals are determined by obtaining quoted market prices in active market or market quote with certain adjustments.

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value (continued)

(A) Fair value hierarchy

	2017			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Non-financial assets				
Investment properties (Note 29)	**–**	**359**	**19,310**	**19,669**
Properties, plant and equipment (Note 30)				
– Premises	**–**	**1,215**	**43,114**	**44,329**
Other assets (Note 31)				
– Precious metals	**5,501**	**790**	**–**	**6,291**

	2016			
	Level 1 HK$'m	Level 2 HK$'m	Level 3 HK$'m	Total HK$'m
Non-financial assets				
Investment properties (Note 29)	–	862	17,365	18,227
Properties, plant and equipment (Note 30)				
– Premises	–	1,659	41,698	43,357
Other assets (Note 31)				
– Precious metals	4,511	1,122	–	5,633

There were no non-financial asset transfers between level 1 and level 2 for the Group during the year (2016: Nil).

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items

	2017	
	Non-financial assets	
		Properties, plant and equipment
	Investment properties HK$'m	Premises HK$'m
At 1 January 2017	17,365	41,698
Gains		
– Income statement		
– Net gain from fair value adjustments on investment properties	1,133	–
– Net gain from revaluation of premises	–	4
– Other comprehensive income		
– Revaluation of premises	–	1,999
Depreciation	–	(999)
Additions	10	102
Disposals	–	(1)
Transfer into level 3	500	857
Transfer out of level 3	–	(251)
Reclassification	302	(302)
Exchange difference	–	7
At 31 December 2017	19,310	43,114
Total unrealised gains for the year included in income statement for non-financial assets held as at 31 December 2017		
– Net gain from fair value adjustments on investment properties	1,133	–
– Net gain from revaluation of premises	–	4
	1,133	4

5. Fair values of assets and liabilities (continued)

5.3 Non-financial instruments measured at fair value (continued)

(B) Reconciliation of level 3 items (continued)

	2016	
	Non-financial assets	
		Properties, plant and equipment
	Investment properties HK$'m	Premises HK$'m
At 1 January 2016	14,635	45,906
Gains/(losses)		
– Income statement		
– Net gain from fair value adjustments on investment properties	427	–
– Net loss from revaluation of premises	–	(9)
– Other comprehensive income		
– Revaluation of premises	–	(70)
Depreciation	–	(1,021)
Additions	6	483
Disposals	–	–
Transfer into level 3	–	778
Transfer out of level 3	(215)	(167)
Reclassification	2,709	(2,709)
Exchange difference	–	(3)
Classified as assets held for sale	(197)	(1,490)
At 31 December 2016	17,365	41,698
Total unrealised gains/(losses) for the year included in income statement for non-financial assets held as at 31 December 2016		
– Net gain from fair value adjustments on investment properties	441	–
– Net loss from revaluation of premises	–	(7)
	441	(7)

The transfer of properties into and out of level 3 is due to change in the premium/(discount) on features applied between the subject and comparable properties during the year. Premium/(discount) on features is determined with reference to differences in features between the subject properties and the comparable properties recently transacted in the market. As comparable properties that come from recent market transactions may be different in each year, the premium/(discount) on features applied between the subject and comparable properties would change from year to year accordingly. As a result, the significance of adjustments made to observable market inputs may vary and lead to the transfer of properties into and out of level 3.

6. Net interest income

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Interest income		
Due from banks and other financial institutions	**9,540**	4,551
Advances to customers	**25,927**	21,710
Investment in securities and financial assets at fair value through profit or loss	**13,269**	10,319
Others	**215**	196
	48,951	36,776
Interest expense		
Due to banks and other financial institutions	**(2,077)**	(1,841)
Deposits from customers	**(10,560)**	(7,773)
Debt securities and certificates of deposit in issue	**(289)**	(318)
Subordinated liabilities	**(932)**	(594)
Others	**(385)**	(226)
	(14,243)	(10,752)
Net interest income	**34,708**	26,024

Included within interest income is HK$3 million (2016: HK$5 million) of interest with respect to income accrued on advances classified as impaired for the year ended 31 December 2017. There was no interest income accrued on impaired investment in securities for the year ended 31 December 2017 (2016: HK$1 million).

Included within interest income and interest expense are HK$47,159 million (2016: HK$36,495 million) and HK$14,570 million (2016: HK$11,235 million), before hedging effect, for financial assets and financial liabilities that are not recognised at fair value through profit or loss respectively.

7. Net fee and commission income

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Fee and commission income		
Loan commissions	**3,559**	3,522
Credit card business	**3,202**	3,703
Securities brokerage	**2,624**	1,954
Insurance	**1,326**	1,630
Funds distribution	**985**	735
Bills commissions	**802**	724
Payment services	**629**	631
Trust and custody services	**555**	470
Currency exchange	**433**	336
Safe deposit box	**291**	277
Others	**999**	950
	15,405	14,932
Fee and commission expense		
Credit card business	**(2,327)**	(2,842)
Securities brokerage	**(312)**	(244)
Insurance	**(311)**	(292)
Others	**(939)**	(870)
	(3,889)	(4,248)
Net fee and commission income	**11,516**	10,684
Of which arise from:		
Financial assets or financial liabilities not at fair value through profit or loss		
– Fee and commission income	**3,850**	3,887
– Fee and commission expense	**(50)**	(34)
	3,800	3,853
Trust and other fiduciary activities		
– Fee and commission income	**739**	654
– Fee and commission expense	**(23)**	(22)
	716	632

8. Net trading gain

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Net gain from:		
Foreign exchange and foreign exchange products	**157**	3,719
Interest rate instruments and items under fair value hedge	**739**	867
Commodities	**205**	32
Equity and credit derivative instruments	**225**	88
	1,326	4,706

9. Net gain on other financial assets

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Net gain on available-for-sale securities	**1,107**	999
Net gain on held-to-maturity securities	**26**	12
Others	**30**	(5)
	1,163	1,006

10. Other operating income

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Dividend income from investment in securities		
– Listed investments	**129**	87
– Unlisted investments	**48**	45
Gross rental income from investment properties	**594**	494
Less: Outgoings in respect of investment properties	**(100)**	(72)
Others	**260**	261
	931	815

Included in the "Outgoings in respect of investment properties" is HK$1 million (2016: HK$6 million) of direct operating expenses related to investment properties that were not let during the year.

11. Net insurance benefits and claims and movement in liabilities

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Gross insurance benefits and claims and movement in liabilities		
Claims, benefits and surrenders paid	**(11,624)**	(15,561)
Movement in liabilities	**(14,257)**	(5,579)
	(25,881)	(21,140)
Reinsurers' share of benefits and claims and movement in liabilities		
Reinsurers' share of claims, benefits and surrenders paid	**5,392**	10,925
Reinsurers' share of movement in liabilities	**2,768**	(1,160)
	8,160	9,765
Net insurance benefits and claims and movement in liabilities	**(17,721)**	(11,375)

12. Net charge of impairment allowances

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Advances to customers		
Individually assessed		
– New allowances	**(303)**	(249)
– Releases	**301**	165
– Recoveries	**73**	91
Net reversal of individually assessed loan impairment allowances	**71**	7
Collectively assessed		
– New allowances	**(1,204)**	(707)
– Releases	**8**	40
– Recoveries	**58**	46
Net charge of collectively assessed loan impairment allowances	**(1,138)**	(621)
Net charge of loan impairment allowances	**(1,067)**	(614)
Others	**(9)**	13
Net charge of impairment allowances	**(1,076)**	(601)

13. Operating expenses

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Staff costs (including directors' emoluments)		
– Salaries and other costs	**7,371**	6,521
– Pension cost	**442**	418
	7,813	6,939
Premises and equipment expenses (excluding depreciation)		
– Rental of premises	**698**	664
– Information technology	**549**	519
– Others	**457**	408
	1,704	1,591
Depreciation	**1,949**	1,805
Auditor's remuneration		
– Audit services	**28**	26
– Non-audit services	**9**	13
Other operating expenses	**2,200**	2,138
	13,703	12,512

Contingent rent included in the "Rental of premises" amounted to HK$16 million during the year (2016: HK$16 million).

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

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Net gain from fair value adjustments on investment properties	**1,197**	429

15. Net loss from disposal/revaluation of properties, plant and equipment

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Net loss from disposal of equipment, fixtures and fittings	**(15)**	(7)
Net loss from revaluation of premises	**(10)**	(7)
	(25)	(14)

16. Taxation

Taxation in the income statement represents:

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Current tax		
Hong Kong profits tax		
– Current year taxation	**5,507**	4,586
– Over-provision in prior years	**(82)**	(60)
	5,425	4,526
Overseas taxation		
– Current year taxation	**869**	532
	6,294	5,058
Deferred tax		
Origination and reversal of temporary differences and unused tax credits	**(246)**	(290)
	6,048	4,768

Hong Kong profits tax has been provided at the rate of 16.5% (2016: 16.5%) on the estimated assessable profits arising in Hong Kong during the year. Taxation on overseas profits has been calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the countries/regions 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:

	2017 HK$'m	2016 HK$'m
CONTINUING OPERATIONS		
Profit before taxation	**35,262**	29,971
Calculated at a taxation rate of 16.5% (2016: 16.5%)	**5,818**	4,945
Effect of different taxation rates in other countries/regions	**84**	93
Income not subject to taxation	**(448)**	(261)
Expenses not deductible for taxation purposes	**258**	44
Tax losses not recognised	**2**	1
Over-provision in prior years	**(82)**	(60)
Foreign withholding tax	**416**	6
Taxation charge	**6,048**	4,768
Effective tax rate	**17.2%**	15.9%

17. Dividends

	2017		2016	
	Per share HK$	**Total HK$'m**	Per share HK$	Total HK$'m
Interim dividend paid	**0.545**	**5,762**	0.545	5,762
Special dividend paid	**0.095**	**1,005**	0.710	7,507
Proposed final dividend	**0.758**	**8,014**	0.625	6,608
	1.398	**14,781**	1.880	19,877

At a meeting held on 30 August 2017, the Board declared an interim dividend of HK$0.545 per ordinary share for the first half of 2017 amounting to approximately HK$5,762 million and a special dividend of HK$0.095 per ordinary share amounting to approximately HK$1,005 million.

At a meeting held on 29 March 2018, the Board proposed to recommend to the Annual General Meeting on 27 June 2018 a final dividend of HK$0.758 per ordinary share for the year ended 31 December 2017 amounting to approximately HK$8,014 million. This proposed final dividend is not reflected as a dividend payable in these financial statements, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2018.

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

The calculation of basic earnings per share for the year ended 31 December 2017 is based on the consolidated profit for the year and profit from continuing operations attributable to equity holders of the Company of approximately HK$31,070 million and HK$28,481 million (2016: HK$55,876 million and HK$24,574 million) respectively and on the ordinary shares in issue of 10,572,780,266 shares (2016: 10,572,780,266 ordinary shares).

There was no dilution of earnings per share as no potential ordinary shares were in issue for the year ended 31 December 2017 (2016: Nil).

19. Retirement benefit costs

Retirement benefits are provided to eligible employees of the Group. In Hong Kong, defined contribution schemes for the Group's employees are ORSO schemes exempted under the MPF Schemes Ordinance and the BOC-Prudential Easy Choice MPF Scheme.

Under the ORSO schemes, employees make monthly contributions to the ORSO schemes equal to 5% of their basic salaries, while the employer makes monthly contributions equal to 5% to 15% of the employees' monthly basic salaries, depending on years of service. The employees are entitled to receive 100% of the employer's contributions upon retirement, early retirement or termination of employment after completing 10 years of service. Employees with 3 to 9 years of service are entitled to receive the employer's contributions at a scale ranging from 30% to 90% upon termination of employment for other reasons other than summary dismissal. All employer's contributions received by employee are subject to MPF Schemes Ordinance.

With the implementation of the MPF Schemes Ordinance on 1 December 2000, the Group also participates in the BOC-Prudential Easy Choice MPF Scheme, of which the trustee is BOCI-Prudential Trustee and the investment manager is BOCI-Prudential Manager, which are related parties of the Company.

19. Retirement benefit costs (continued)

The Group's total contributions made to the ORSO schemes for the year ended 31 December 2017 amounted to approximately HK$337 million (2016: approximately HK$354 million), after a deduction of forfeited contributions of approximately HK$10 million (2016: approximately HK$9 million). For the MPF Scheme, the Group contributed approximately HK$83 million (2016: approximately HK$85 million) for the year ended 31 December 2017.

20. Directors', senior management's and key personnel's emoluments

(a) Directors' and senior management's emoluments

(i) Directors' emoluments

Details of the emoluments paid to or receivable by the directors of the Company in respect of their services rendered for the Company and managing the subsidiaries within the Group during the year are as follows:

	2017			
	Directors' fee HK$'000	Basic salaries, allowances and benefits in kind HK$'000	Bonus HK$'000	Total HK$'000
Executive Directors				
YUE Yi (Chief Executive)	–	7,140	4,166	11,306
LI Jiuzhong	–	4,664	2,394	7,058
	–	11,804	6,560	18,364
Non-executive Directors				
CHEN Siqing	–	–	–	–
TIAN Guoli [Note 1]	–	–	–	–
GAO Yingxin	–	–	–	–
REN Deqi	–	–	–	–
CHENG Eva*	500	–	–	500
CHOI Koon Shum*	588	–	–	588
KOH Beng Seng*	650	–	–	650
TUNG Savio Wai-Hok*	712	–	–	712
XU Luode [Note 1]	–	–	–	–
	2,450	–	–	2,450
	2,450	11,804	6,560	20,814

Note 1: Resigned during the year.

Mr GAO Yingxin has been re-designated from the Non-executive Director to the Executive Director and appointed as the Vice Chairman and Chief Executive effective from 1 January 2018. Mr YUE Yi resigned as Vice Chairman, Executive Director and Chief Executive effective from 1 January 2018.

20. Directors', senior management's and key personnel's emoluments (continued)

(a) Directors' and senior management's emoluments (continued)

(i) Directors' emoluments (continued)

	2016			
	Directors' fee HK$'000	Basic salaries, allowances and benefits in kind HK$'000	Bonus HK$'000	Total HK$'000
Executive Directors				
YUE Yi (Chief Executive)	–	6,750	3,953	10,703
LI Jiuzhong	–	4,480	2,311	6,791
	–	11,230	6,264	17,494
Non-executive Directors				
CHEN Siqing	–	–	–	–
TIAN Guoli	–	–	–	–
GAO Yingxin	–	–	–	–
REN Deqi	–	–	–	–
CHENG Eva*	300	–	–	300
CHOI Koon Shum*	199	–	–	199
KOH Beng Seng*	450	–	–	450
TUNG Savio Wai-Hok*	528	–	–	528
XU Luode	–	–	–	–
SHAN Weijian*	173	–	–	173
	1,650	–	–	1,650
	1,650	11,230	6,264	19,144

* Independent Non-executive Directors

There were no directors waived emoluments for the year ended 31 December 2017 (2016: Nil).

20. Directors', senior management's and key personnel's emoluments (continued)

(a) Directors' and senior management's emoluments (continued)

(ii) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include two (2016: two) directors whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining three (2016: three) individuals during the year are as follows:

	2017 HK$'m	2016 HK$'m
Basic salaries and allowances	**11**	11
Bonus	**9**	8
Contributions to pension schemes	**1**	1
	21	20

Emoluments paid to or receivable by individuals during the year with reference to their tenure are within the following bands:

	Number of individuals	
	2017	2016
HK$6,000,001 to HK$6,500,000	**–**	1
HK$6,500,001 to HK$7,000,000	**2**	2
HK$7,000,001 to HK$7,500,000	**1**	–

(iii) Senior management's emoluments

Emoluments paid to or receivable by individuals during the year with reference to their tenure as senior management are within the following bands:

	Number of individuals	
	2017	2016
HK$4,500,001 to HK$5,000,000	**1**	1
HK$5,000,001 to HK$5,500,000	**2**	2
HK$5,500,001 to HK$6,000,000	**1**	1
HK$6,500,001 to HK$7,000,000	**1**	2
HK$7,000,001 to HK$7,500,000	**1**	–
HK$10,500,001 to HK$11,000,000	**–**	1
HK$11,000,001 to HK$11,500,000	**1**	–

20. Directors', senior management's and key personnel's emoluments (continued)

(b) Remuneration for Senior Management and Key Personnel under CG-5

Pursuant to CG-5 Guideline on a Sound Remuneration System issued by the HKMA, details of the remuneration for Senior Management and Key Personnel of the Group during the year are as follows:

(i) Remuneration awarded during the year

	2017					
	Senior Management			Key Personnel		
	Non-deferred HK$'m	Deferred HK$'m	Total HK$'m	Non-deferred HK$'m	Deferred HK$'m	Total HK$'m
Fixed remuneration						
Cash	**38**	**–**	**38**	**64**	**–**	**64**
Variable remuneration						
Cash	**12**	**5**	**17**	**31**	**14**	**45**
	50	**5**	**55**	**95**	**14**	**109**

	2016					
	Senior Management			Key Personnel		
	Non-deferred HK$'m	Deferred HK$'m	Total HK$'m	Non-deferred HK$'m	Deferred HK$'m	Total HK$'m
Fixed remuneration						
Cash	36	–	36	60	–	60
Variable remuneration						
Cash	13	5	18	29	9	38
	49	5	54	89	9	98

The remuneration above includes 9 (2016: 10) members of Senior Management and 25 (2016: 26) members of Key Personnel.

20. Directors', senior management's and key personnel's emoluments (continued)

(b) Remuneration for Senior Management and Key Personnel under CG-5 (continued)

(ii) Deferred remuneration

	2017		2016	
	Senior Management HK$'m	**Key Personnel HK$'m**	Senior Management HK$'m	Key Personnel HK$'m
Deferred remuneration				
Vested	**4**	**8**	4	9
Unvested	**10**	**24**	9	18
	14	**32**	13	27
At 1 January	**9**	**18**	8	18
Awarded	**5**	**14**	5	9
Paid out	**(4)**	**(8)**	(4)	(9)
Reduced through performance adjustments	**–**	**–**	–	–
At 31 December	**10**	**24**	9	18

For the purpose of disclosure, Senior Management and Key Personnel are defined as follows:

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

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

21. Cash and balances with banks and other financial institutions

	2017 HK$'m	2016 HK$'m
Cash	**14,234**	12,889
Balances with central banks	**88,554**	72,022
Balances with other banks and other financial institutions	**152,793**	43,220
Placements with central banks maturing within one month	**9,283**	8,371
Placements with other banks and other financial institutions maturing within one month	**99,341**	99,804
	364,205	236,306

22. Placements with banks and other financial institutions maturing between one and twelve months

	2017 HK$'m	2016 HK$'m
Placements with central banks maturing between one and twelve months	**1,486**	1,964
Placements with other banks and other financial institutions maturing between one and twelve months	**57,570**	70,646
	59,056	72,610

23. Financial assets at fair value through profit or loss

	Trading assets		Financial assets designated at fair value through profit or loss		Total	
	2017 HK$'m	2016 HK$'m	2017 HK$'m	2016 HK$'m	2017 HK$'m	2016 HK$'m
At fair value						
Treasury bills	**17,780**	10,448	**–**	–	**17,780**	10,448
Other debt securities	**24,662**	20,620	**29,505**	22,957	**54,167**	43,577
	42,442	31,068	**29,505**	22,957	**71,947**	54,025
Certificates of deposit	**1,483**	2,143	**159**	148	**1,642**	2,291
Total debt securities and certificates of deposit	**43,925**	33,211	**29,664**	23,105	**73,589**	56,316
Equity securities	**203**	76	**3,481**	2,008	**3,684**	2,084
Fund	**–**	–	**9,062**	3,181	**9,062**	3,181
Total securities	**44,128**	33,287	**42,207**	28,294	**86,335**	61,581
Other debt instruments	**6,859**	5,777	**–**	–	**6,859**	5,777
	50,987	39,064	**42,207**	28,294	**93,194**	67,358

23. Financial assets at fair value through profit or loss (continued)

Total securities are analysed by place of listing as follows:

	Trading assets		Financial assets designated at fair value through profit or loss	
	2017 HK$'m	2016 HK$'m	**2017 HK$'m**	2016 HK$'m
Debt securities and certificates of deposit				
– Listed in Hong Kong	**9,339**	10,913	**8,864**	5,861
– Listed outside Hong Kong	**4,818**	4,096	**13,052**	9,953
	14,157	15,009	**21,916**	15,814
– Unlisted	**29,768**	18,202	**7,748**	7,291
	43,925	33,211	**29,664**	23,105
Equity securities				
– Listed in Hong Kong	**203**	76	**2,375**	1,624
– Listed outside Hong Kong	**–**	–	**1,106**	384
	203	76	**3,481**	2,008
Fund				
– Unlisted	**–**	–	**9,062**	3,181
Total securities	**44,128**	33,287	**42,207**	28,294

Total securities are analysed by type of issuer as follows:

	Trading assets		Financial assets designated at fair value through profit or loss	
	2017 HK$'m	2016 HK$'m	**2017 HK$'m**	2016 HK$'m
Sovereigns	**28,714**	21,473	**215**	1,247
Public sector entities	**703**	660	**–**	–
Banks and other financial institutions	**12,051**	7,720	**27,793**	18,421
Corporate entities	**2,660**	3,434	**14,199**	8,626
Total securities	**44,128**	33,287	**42,207**	28,294

24. Derivative financial instruments and hedge accounting

The Group enters into exchange rate, interest rate, commodity, equity and credit related derivative financial instrument contracts for trading and risk management purposes.

Currency forwards represent commitments to purchase and sell foreign currency on a future date. Interest rate futures are contractual obligations to receive or pay a net amount based on changes in interest rates or buy or sell interest rate financial instruments on a future date at an agreed price in the financial market under the administration of the stock exchange. Forward rate agreements are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contract rate of interest and the current market rate, based on a notional principal amount.

Currency, interest rate and commodity swaps are commitments to exchange one set of cash flows or commodity for another. Swaps result in an exchange of currencies, interest rates (for example, fixed rate for floating rate), or precious metals (for example, silver swaps) or a combination of all these (for example, cross-currency interest rate swaps). Except for certain currency swap contracts, no exchange of principal takes place.

Foreign currency, interest rate, precious metal and equity options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of the financial instrument at a predetermined price. In consideration for the assumption of foreign exchange and interest rate risk, the seller receives a premium from the purchaser. Options are negotiated over-the-counter between the Group and its counterparty or traded through the stock exchange (for example, exchange-traded stock option).

The contract/notional amounts and fair values of derivative financial instruments held by the Group are set out in the following tables. The contract/notional amounts of these instruments indicate the volume of transactions outstanding at the balance sheet dates and certain of them provide a basis for comparison with the fair values of instruments recognised on the balance sheet. However, they do not necessarily indicate the amounts of future cash flows involved or the current fair values of the instruments and, therefore, do not indicate the Group's exposure to credit or market risks. The derivative financial instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in foreign exchange rates, market interest rates, commodity prices or equity prices relative to their terms. The aggregate fair values of derivative financial instruments can fluctuate significantly from time to time.

(a) Derivative financial instruments

The Group trades derivative products (both exchange-traded or OTC) mainly for customer business. The Group strictly follows risk management policies and requirement in providing derivative products to our customers and in trading of derivative products in the interbank market.

Derivatives are also used to manage the interest rate risk of the banking book. A derivative instrument must be included in the approved product list before any transactions for that instrument can be made. There are limits to control the notional amount of exposure arising from derivative transactions, and the maximum tenor of the deal is set. Every derivative transaction must be input into the relevant system for settlement, mark-to-market revaluation, reporting and control.

24. Derivative financial instruments and hedge accounting (continued)

(a) Derivative financial instruments (continued)

The following tables summarise the contract/notional amounts and fair values of each class of derivative financial instrument as at 31 December:

	2017		
	Contract/ notional amounts HK$'m	**Fair values**	
		Assets HK$'m	**Liabilities HK$'m**
Exchange rate contracts			
Spot, forwards and futures	**354,350**	**12,043**	**(9,238)**
Swaps	**1,460,316**	**13,923**	**(15,641)**
Options	**59,734**	**138**	**(107)**
	1,874,400	**26,104**	**(24,986)**
Interest rate contracts			
Futures	**17,306**	**8**	**(1)**
Swaps	**931,923**	**6,786**	**(5,403)**
	949,229	**6,794**	**(5,404)**
Commodity contracts	**28,001**	**559**	**(570)**
Equity contracts	**6,655**	**78**	**(81)**
Credit derivative contracts	**586**	**6**	**(3)**
	2,858,871	**33,541**	**(31,044)**

	2016		
	Contract/ notional amounts HK$'m	Fair values	
		Assets HK$'m	Liabilities HK$'m
Exchange rate contracts			
Spot, forwards and futures	326,303	17,619	(11,509)
Swaps	1,840,736	38,487	(31,320)
Options	42,029	349	(391)
	2,209,068	56,455	(43,220)
Interest rate contracts			
Futures	2,543	1	(8)
Swaps	875,810	6,555	(5,320)
	878,353	6,556	(5,328)
Commodity contracts	26,091	1,240	(675)
Equity contracts	4,628	78	(81)
Credit derivative contracts	388	3	–
	3,118,528	64,332	(49,304)

24. Derivative financial instruments and hedge accounting (continued)

(b) Hedge accounting

The fair values of derivative financial instruments designated as hedging instruments as at 31 December are as follows:

	2017		2016	
	Assets HK$'m	Liabilities HK$'m	Assets HK$'m	Liabilities HK$'m
Fair value hedges	**2,339**	**(555)**	2,797	(1,065)

The Group uses interest rate swaps to hedge against change in fair value of financial assets and liabilities arising from movements in market interest rates.

Gains or losses on fair value hedges reflected in net trading gain for the year are as follows:

	2017		2016	
	Hedged assets HK$'m	Hedged liabilities HK$'m	Hedged assets HK$'m	Hedged liabilities HK$'m
Net gain/(loss)				
– Hedging instruments	**591**	**(464)**	1,962	(487)
– Hedged items	**(271)**	**563**	(1,372)	483
	320	**99**	590	(4)

25. Advances and other accounts

	2017 HK$'m	2016 HK$'m
Personal loans and advances	**327,783**	292,710
Corporate loans and advances	**816,676**	695,483
Advances to customers	**1,144,459**	988,193
Loan impairment allowances (Note 26)		
– Individually assessed	**(491)**	(650)
– Collectively assessed	**(3,593)**	(2,779)
	1,140,375	984,764
Trade bills	**42,975**	17,245
Advances to banks and other financial institutions	**6,259**	6,016
	1,189,609	1,008,025

As at 31 December 2017, advances to customers included accrued interest of HK$1,717 million (2016: HK$1,388 million).

As at 31 December 2017, no impairment allowance was made in respect of trade bills and advances to banks and other financial institutions (2016: Nil).

26. Loan impairment allowances

	2017		
	Individually assessed		
	Personal HK$'m	Corporate HK$'m	Total HK$'m
At 1 January 2017, as previously reported	9	440	449
Effect of merger of entities under common control	1	200	201
At 1 January 2017, as restated	10	640	650
Charged/(credited) to income statement (Note 12)	14	(85)	(71)
Loans written off during the year as uncollectible	(1)	(167)	(168)
Recoveries	5	68	73
Unwind of discount on impairment allowances	–	(3)	(3)
Exchange difference	–	10	10
At 31 December 2017	28	463	491

	2017		
	Collectively assessed		
	Personal HK$'m	Corporate HK$'m	Total HK$'m
At 1 January 2017, as previously reported	304	2,371	2,675
Effect of merger of entities under common control	14	90	104
At 1 January 2017, as restated	318	2,461	2,779
Charged to income statement (Note 12)	715	423	1,138
Loans written off during the year as uncollectible	(394)	(5)	(399)
Recoveries	58	–	58
Exchange difference	5	12	17
At 31 December 2017	702	2,891	3,593

26. Loan impairment allowances (continued)

	2016		
	Individually assessed		
	Personal HK$'m	Corporate HK$'m	Total HK$'m
At 1 January 2016, as previously reported	9	569	578
Effect of merger of entities under common control	–	144	144
At 1 January 2016, as restated	9	713	722
(Credited)/charged to income statement	(3)	33	30
Loans written off during the year as uncollectible	(3)	(107)	(110)
Recoveries	7	91	98
Unwind of discount on impairment allowances	–	(6)	(6)
Exchange difference	–	(1)	(1)
Classified as assets held for sale	–	(83)	(83)
At 31 December 2016	10	640	650

	2016		
	Collectively assessed		
	Personal HK$'m	Corporate HK$'m	Total HK$'m
At 1 January 2016, as previously reported	278	2,227	2,505
Effect of merger of entities under common control	6	128	134
At 1 January 2016, as restated	284	2,355	2,639
Charged to income statement	402	246	648
Loans written off during the year as uncollectible	(408)	(5)	(413)
Recoveries	46	–	46
Exchange difference	(1)	(1)	(2)
Classified as assets held for sale	(5)	(134)	(139)
At 31 December 2016	318	2,461	2,779

27. Investment in securities

	2017			
	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	**180,160**	**–**	**–**	**180,160**
Other debt securities	**354,779**	**50,541**	**499**	**405,819**
	534,939	**50,541**	**499**	**585,979**
Certificates of deposit	**26,762**	**18**	**–**	**26,780**
Total debt securities and certificates of deposit	**561,701**	**50,559**	**499**	**612,759**
Equity securities	**5,413**	**–**	**–**	**5,413**
Fund	**–**	**–**	**–**	**–**
	567,114	**50,559**	**499**	**618,172**

	2016			
	At fair value	At amortised cost		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m	Total HK$'m
Treasury bills	142,263	–	–	142,263
Other debt securities	328,272	60,850	935	390,057
	470,535	60,850	935	532,320
Certificates of deposit	56,903	18	–	56,921
Total debt securities and certificates of deposit	527,438	60,868	935	589,241
Equity securities	4,259	–	–	4,259
Fund	150	–	–	150
	531,847	60,868	935	593,650

27. Investment in securities (continued)

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

	2017		
	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	**70,453**	**10,355**	**–**
– Listed outside Hong Kong	**191,158**	**19,646**	**–**
	261,611	**30,001**	**–**
– Unlisted	**300,090**	**20,558**	**499**
	561,701	**50,559**	**499**
Equity securities			
– Listed in Hong Kong	**4,468**	**–**	**–**
– Listed outside Hong Kong	**134**	**–**	**–**
– Unlisted	**811**	**–**	**–**
	5,413	**–**	**–**
Fund			
– Unlisted	**–**	**–**	**–**
	567,114	**50,559**	**499**
Market value of listed held-to-maturity securities		**30,443**	

	2016		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
Debt securities and certificates of deposit			
– Listed in Hong Kong	55,218	8,214	–
– Listed outside Hong Kong	169,052	24,714	–
	224,270	32,928	–
– Unlisted	303,168	27,940	935
	527,438	60,868	935
Equity securities			
– Listed in Hong Kong	2,906	–	–
– Listed outside Hong Kong	635	–	–
– Unlisted	718	–	–
	4,259	–	–
Fund			
– Unlisted	150	–	–
	531,847	60,868	935
Market value of listed held-to-maturity securities		33,218	

27. Investment in securities (continued)

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

	2017		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
Sovereigns	**233,050**	**964**	**–**
Public sector entities	**35,849**	**9,525**	**–**
Banks and other financial institutions	**192,778**	**20,548**	**499**
Corporate entities	**105,437**	**19,522**	**–**
	567,114	**50,559**	**499**

	2016		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
Sovereigns	187,870	1,172	–
Public sector entities	29,819	11,608	–
Banks and other financial institutions	214,576	27,248	935
Corporate entities	99,582	20,840	–
	531,847	60,868	935

27. Investment in securities (continued)

The movements in investment in securities are summarised as follows:

	2017		
	Available-for-sale securities HK$'m	**Held-to-maturity securities HK$'m**	**Loans and receivables HK$'m**
At 1 January 2017, as previously reported	**531,036**	**60,194**	**935**
Effect of merger of entities under common control	**811**	**674**	**–**
At 1 January 2017, as restated	**531,847**	**60,868**	**935**
Additions	**541,193**	**4,915**	**3,864**
Disposals, redemptions and maturity	**(511,733)**	**(22,838)**	**(4,320)**
Amortisation	**65**	**(76)**	**20**
Change in fair value	**1,663**	**–**	**–**
Reclassification	**(6,097)**	**6,097**	**–**
Exchange difference	**10,176**	**1,593**	**–**
At 31 December 2017	**567,114**	**50,559**	**499**

	2016		
	Available-for-sale securities HK$'m	Held-to-maturity securities HK$'m	Loans and receivables HK$'m
At 1 January 2016, as previously reported	432,929	81,843	3,166
Effect of merger of entities under common control	671	844	–
At 1 January 2016, as restated	433,600	82,687	3,166
Additions	759,501	9,804	2,230
Disposals, redemptions and maturity	(641,517)	(29,292)	(4,080)
Amortisation	(264)	(191)	21
Change in fair value	(1,473)	–	–
Reclassification	1,437	(1,437)	–
Exchange difference	(6,581)	(703)	129
Classified as assets held for sale	(12,856)	–	(531)
At 31 December 2016	531,847	60,868	935

27. Investment in securities (continued)

The Group reclassified certain debt securities with fair value of HK$6,097 million (2016: HK$1,828 million) out of available-for-sale category into held-to-maturity category during the year. The Group had the intention and ability to hold these reclassified debt securities until maturity at the date of reclassification.

There were no debt securities reclassified out of held-to-maturity category into available-for-sale category during the year (2016: HK$3,265 million).

28. Interests in associates and joint ventures

	2017 HK$'m	2016 HK$'m
At 1 January	**319**	376
Share of results	**132**	96
Share of tax	**(32)**	(22)
Dividend received	**(2)**	(2)
Derecognition	**–**	(129)
At 31 December	**417**	319

The particulars of the Group's associates and joint ventures, all of which are unlisted, are as follows:

Name	**Place of incorporation and operation**	**Issued share capital/ registered capital**	**Interest held**	**Principal activities**
Associates:				
BOC Services Company Limited	PRC	Registered capital RMB50,000,000	45%	Credit card back-end service support
Joint ventures:				
Joint Electronic Teller Services Limited	Hong Kong	Ordinary shares HK$10,026,000	19.96%	Operation of a private inter-bank message switching network in respect of ATM services
Golden Harvest (Cayman) Limited	Cayman Islands	Ordinary shares US$100	49%	Investment holding

Golden Harvest (Cayman) Limited was incorporated on 23 May 2017.

28. Interests in associates and joint ventures (continued)

	Associates		Joint ventures	
	2017 HK$'m	2016 HK$'m	**2017 HK$'m**	2016 HK$'m
Interests in associates/joint ventures	**350**	256	**67**	63
Share of profit/total comprehensive income for the year of associates/joint ventures	**94**	69	**6**	5

29. Investment properties

	2017 HK$'m	2016 HK$'m
At 1 January	**18,227**	15,262
Additions	**13**	6
Disposals	**(2)**	–
Fair value gains	**1,197**	415
Reclassification from properties, plant and equipment (Note 30)	**234**	2,748
Classified as assets held for sale	**–**	(204)
At 31 December	**19,669**	18,227

The carrying value of investment properties is analysed based on the remaining terms of the leases as follows:

	2017 HK$'m	2016 HK$'m
Held in Hong Kong		
On long-term lease (over 50 years)	**4,526**	4,153
On medium-term lease (10 to 50 years)	**14,835**	13,799
Held outside Hong Kong		
On long-term lease (over 50 years)	**77**	59
On medium-term lease (10 to 50 years)	**203**	194
On short-term lease (less than 10 years)	**28**	22
	19,669	18,227

As at 31 December 2017, investment properties were included in the balance sheet at valuation carried out at 31 December 2017 on the basis of their fair value by an independent firm of chartered surveyors, Knight Frank Petty Limited. The fair value represents the price that would be received to sell each investment property in an orderly transaction with market participants at the measurement date.

30. Properties, plant and equipment

	Premises HK$'m	Equipment, fixtures and fittings HK$'m	Total HK$'m
Net book value at 1 January 2017, as previously reported	**43,357**	**2,375**	**45,732**
Effect of merger of entities under common control	**–**	**80**	**80**
Net book value at 1 January 2017, as restated	**43,357**	**2,455**	**45,812**
Additions	**112**	**1,408**	**1,520**
Disposals	**(8)**	**(20)**	**(28)**
Revaluation	**2,119**	**–**	**2,119**
Depreciation for the year (Note 13)	**(1,024)**	**(925)**	**(1,949)**
Reclassification to investment properties (Note 29)	**(234)**	**–**	**(234)**
Exchange difference	**7**	**14**	**21**
Net book value at 31 December 2017	**44,329**	**2,932**	**47,261**
At 31 December 2017			
Cost or valuation	**44,329**	**9,595**	**53,924**
Accumulated depreciation and impairment	**–**	**(6,663)**	**(6,663)**
Net book value at 31 December 2017	**44,329**	**2,932**	**47,261**
The analysis of cost or valuation of the above assets is as follows:			
At 31 December 2017			
At cost	**–**	**9,595**	**9,595**
At valuation	**44,329**	**–**	**44,329**
	44,329	**9,595**	**53,924**
Net book value at 1 January 2016, as previously reported	48,244	2,273	50,517
Effect of merger of entities under common control	–	53	53
Net book value at 1 January 2016, as restated	48,244	2,326	50,570
Additions	560	958	1,518
Disposals	(1)	(8)	(9)
Revaluation	(144)	–	(144)
Depreciation for the year	(1,060)	(771)	(1,831)
Reclassification to investment properties (Note 29)	(2,748)	–	(2,748)
Exchange difference	(4)	(6)	(10)
Classified as assets held for sale	(1,490)	(44)	(1,534)
Net book value at 31 December 2016	43,357	2,455	45,812
At 31 December 2016			
Cost or valuation	43,357	8,356	51,713
Accumulated depreciation and impairment	–	(5,901)	(5,901)
Net book value at 31 December 2016	43,357	2,455	45,812
The analysis of cost or valuation of the above assets is as follows:			
At 31 December 2016			
At cost	–	8,356	8,356
At valuation	43,357	–	43,357
	43,357	8,356	51,713

30. Properties, plant and equipment (continued)

The carrying value of premises is analysed based on the remaining terms of the leases as follows:

	2017 HK$'m	2016 HK$'m
Held in Hong Kong		
On long-term lease (over 50 years)	**13,734**	13,821
On medium-term lease (10 to 50 years)	**30,221**	29,212
Held outside Hong Kong		
On long-term lease (over 50 years)	**5**	4
On medium-term lease (10 to 50 years)	**290**	256
On short-term lease (less than 10 years)	**79**	64
	44,329	43,357

As at 31 December 2017, premises were included in the balance sheet at valuation carried out at 31 December 2017 on the basis of their fair value by an independent firm of chartered surveyors, Knight Frank Petty Limited. The fair value represents the price that would be received to sell each premises in an orderly transaction with market participants at the measurement date.

As a result of the above-mentioned revaluations, changes in value of the premises were recognised as follows:

	2017 HK$'m	2016 HK$'m
Decrease in valuation charged to income statement	**(10)**	(9)
Increase/(decrease) in valuation credited/(charged) to other comprehensive income	**2,129**	(135)
	2,119	(144)

As at 31 December 2017, the net book value of premises that would have been included in the Group's balance sheet had the premises been carried at cost less accumulated depreciation and impairment losses was HK$7,295 million (2016: HK$7,117 million).

31. Other assets

	2017 HK$'m	2016 HK$'m
Repossessed assets	**30**	38
Precious metals	**6,291**	5,633
Reinsurance assets	**43,717**	38,605
Accounts receivable and prepayments	**24,333**	27,057
	74,371	71,333

32. Hong Kong SAR currency notes in circulation

The Hong Kong SAR currency notes in circulation are secured by deposit of funds in respect of which the Hong Kong SAR Government certificates of indebtedness are held.

33. Financial liabilities at fair value through profit or loss

	2017 HK$'m	2016 HK$'m
Trading liabilities		
– Short positions in Exchange Fund Bills and Notes	**16,936**	9,946
Financial liabilities designated at fair value through profit or loss		
– Structured deposits (Note 34)	**2,784**	3,425
	19,720	13,371

The carrying amount of financial liabilities designated at fair value through profit or loss as at 31 December 2017 was less than the amount that the Group would be contractually required to pay at maturity to the holders by HK$3 million (2016: HK$9 million). The amount of change in the fair values of financial liabilities at fair value through profit or loss, during the year and cumulatively, attributable to changes in own credit risk was insignificant.

34. Deposits from customers

	2017 HK$'m	2016 HK$'m
Current, savings and other deposit accounts (per balance sheet)	**1,771,513**	1,519,867
Structured deposits reported as financial liabilities at fair value through profit or loss (Note 33)	**2,784**	3,425
	1,774,297	1,523,292
Analysed by:		
Demand deposits and current accounts		
– Corporate	**145,025**	128,178
– Personal	**58,806**	45,810
	203,831	173,988
Savings deposits		
– Corporate	**370,256**	326,866
– Personal	**539,928**	478,965
	910,184	805,831
Time, call and notice deposits		
– Corporate	**408,944**	363,424
– Personal	**251,338**	180,049
	660,282	543,473
	1,774,297	1,523,292

35. Debt securities and certificates of deposit in issue

	2017 HK$'m	2016 HK$'m
Debt securities, at amortised cost	**21,641**	1,121

36. Other accounts and provisions

	2017 HK$'m	2016 HK$'m
Other accounts payable	**52,950**	52,625
Provisions	**17**	242
	52,967	52,867

37. Deferred taxation

Deferred tax is recognised in respect of the temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements and unused tax credits in accordance with HKAS 12 "Income Taxes".

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

	2017					
	Accelerated tax depreciation HK$'m	Property revaluation HK$'m	Losses HK$'m	Impairment allowances HK$'m	Others HK$'m	Total HK$'m
At 1 January 2017, as previously reported	**612**	**6,467**	**–**	**(430)**	**(1,132)**	**5,517**
Effect of merger of entities under common control	**(1)**	**–**	**–**	**4**	**(7)**	**(4)**
At 1 January 2017, as restated	**611**	**6,467**	**–**	**(426)**	**(1,139)**	**5,513**
Charged/(credited) to income statement (Note 16)	**82**	**(116)**	**–**	**(123)**	**(89)**	**(246)**
Charged to other comprehensive income	**–**	**298**	**–**	**–**	**81**	**379**
Exchange difference	**–**	**–**	**–**	**–**	**–**	**–**
At 31 December 2017	**693**	**6,649**	**–**	**(549)**	**(1,147)**	**5,646**

	2016					
	Accelerated tax depreciation HK$'m	Property revaluation HK$'m	Losses HK$'m	Impairment allowances HK$'m	Others HK$'m	Total HK$'m
At 1 January 2016, as previously reported	597	7,192	–	(459)	(936)	6,394
Effect of merger of entities under common control	(1)	–	(2)	(2)	(3)	(8)
At 1 January 2016, as restated	596	7,192	(2)	(461)	(939)	6,386
Charged/(credited) to income statement	29	(206)	2	(57)	(69)	(301)
Credited to other comprehensive income	–	(311)	–	–	(164)	(475)
Exchange difference	–	–	–	2	–	2
Classified as assets held for sale and liabilities associated with assets held for sale	(14)	(208)	–	90	33	(99)
At 31 December 2016	611	6,467	–	(426)	(1,139)	5,513

37. Deferred taxation (continued)

Deferred tax assets and liabilities are offset on an individual entity basis when there is a legal right to set off current tax assets against current tax liabilities and when the deferred taxation relates to the same authority. The following amounts, determined after appropriate offsetting, are shown in the balance sheet:

	2017 HK$'m	2016 HK$'m
Deferred tax assets	**(58)**	(85)
Deferred tax liabilities	**5,704**	5,598
	5,646	5,513

	2017 HK$'m	2016 HK$'m
Deferred tax assets to be recovered after more than twelve months	**(38)**	(16)
Deferred tax liabilities to be settled after more than twelve months	**6,794**	6,605
	6,756	6,589

As at 31 December 2017, the Group has not recognised deferred tax assets in respect of tax losses amounting to HK$25 million (2016: HK$13 million). Of the amount, HK$9 million (2016: HK$9 million) for the Group has no expiry date and HK$16 million (2016: HK$4 million) for the Group is scheduled to expire within six years under the current tax legislation in different countries/regions.

38. Insurance contract liabilities

	2017 HK$'m	2016 HK$'m
At 1 January	**86,534**	82,645
Benefits paid	**(10,815)**	(14,935)
Claims incurred and movement in liabilities	**27,510**	18,824
At 31 December	**103,229**	86,534

The insurance contract liabilities that are covered by reinsurance arrangements amounted to HK$38,074 million (2016: HK$33,471 million) and the associated reinsurance assets of HK$43,717 million (2016: HK$38,605 million) are included in "Other assets" (Note 31).

39. Subordinated liabilities

	2017 HK$'m	2016 HK$'m
Subordinated notes, at amortised cost with fair value hedge adjustment	**18,917**	19,014
Subordinated loan, at amortised cost	**63**	79
	18,980	19,093

In 2010, BOCHK issued listed subordinated notes with an aggregate amount of USD2,500 million, interest rate at 5.55% per annum payable semi-annually, due February 2020. Amounts qualified as Tier 2 capital instruments for regulatory purposes are shown in Note 4.5(B).

The subordinated loan is from BOC, the intermediate holding company, with interest rate at 12-month LIBOR plus 1.50% per annum payable annually. The subordinated loan is repayable on five equal annual installments starting September 2017 and matures on September 2021.

40. Discontinued operations and assets held for sale

(a) Disposal of NCB

On 18 December 2015, BOCHK (as seller) entered into a sale and purchase agreement with Cinda Financial Holdings Co., Limited (as buyer) and China Cinda (HK) Holdings Company Limited (as buyer's guarantor) in relation to the disposal of all the issued shares of NCB. The completion of the disposal was conditional upon the satisfaction of the conditions precedent set out in the sale and purchase agreement.

All the conditions precedent set out in the sale and purchase agreement were satisfied, and completion of the disposal took place on 30 May 2016 in accordance with the terms and conditions of the sale and purchase agreement. Upon completion, NCB ceased to be a subsidiary of BOCHK.

(b) Disposal of Chiyu

On 22 December 2016, BOCHK (as seller) entered into a sale and purchase agreement with Xiamen International Investment Limited and the Committee of Jimei Schools (each as a buyer) in relation to the disposal of a total of 2,114,773 ordinary shares of Chiyu. The completion of the disposal was conditional upon the satisfaction of all the conditions precedent set out in the sale and purchase agreement.

All the conditions precedent set out in the sale and purchase agreement were satisfied, and completion of the disposal took place on 27 March 2017 in accordance with the terms and conditions of the sale and purchase agreement. Upon completion, Chiyu ceased to be a subsidiary of BOCHK.

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

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

DISCONTINUED OPERATIONS	2017 HK$'m	2016 HK$'m
Interest income	**268**	4,030
Interest expense	**(75)**	(1,398)
Net interest income	**193**	2,632
Fee and commission income	**39**	769
Fee and commission expense	**–**	(13)
Net fee and commission income	**39**	756
Net trading gain	**2**	40
Net gain/(loss) on financial instruments designated at fair value through profit or loss	**1**	(8)
Net gain on other financial assets	**–**	108
Other operating income	**–**	9
Net operating income before impairment allowances	**235**	3,537
Net charge of impairment allowances	**(7)**	(420)
Net operating income	**228**	3,117
Operating expenses	**(87)**	(1,275)
Operating profit	**141**	1,842
Net loss from disposal of/fair value adjustments on investment properties	**–**	(14)
Net loss from disposal/revaluation of properties, plant and equipment	**–**	(2)
Profit before taxation	**141**	1,826
Taxation	**(22)**	(289)
Profit after taxation	**119**	1,537
Gain on disposal of discontinued operations	**2,504**	29,956
Profit from discontinued operations	**2,623**	31,493
Profit attributable to:		
Equity holders of the Company	**2,589**	31,302
Non-controlling interests	**34**	191
	2,623	31,493
	HK$	HK$
Earnings per share for profit attributable to equity holders of the Company		
Basic and diluted		
– profit from discontinued operations	**0.2449**	2.9606

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

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

	2017 HK$'m	2016 HK$'m
Operating activities	**2,000**	(17,543)
Investing activities	**(3)**	(67)
Financing activities	**–**	–
Net cash inflow/(outflow) incurred by discontinued operations	**1,997**	(17,610)

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

	2017 HK$'m	2016 HK$'m
Total consideration	**7,685**	68,000
Net assets disposed	**(7,044)**	(38,048)
Non-controlling interests	**2,078**	–
Cumulative translation reserve and reserve for fair value changes of available-for-sale securities reclassified to income statement	**(48)**	370
Transaction costs incurred in connection with the disposal	**(167)**	(366)
Gain on disposal of discontinued operations	**2,504**	29,956

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

The net assets of discontinued operations at the dates of disposal are as follows:

	Chiyu HK$'m	NCB HK$'m
Cash and balances with banks and other financial institutions	7,029	45,126
Placements with banks and other financial institutions maturing between one and twelve months	1,215	6,394
Financial assets at fair value through profit or loss	351	5,560
Derivative financial instruments	95	517
Advances and other accounts	31,411	168,185
Investment in securities	14,541	56,934
Investment properties	204	354
Properties, plant and equipment	1,537	7,049
Current tax assets	–	64
Deferred tax assets	63	71
Other assets	582	2,745
Deposits and balances from banks and other financial institutions	(2,765)	(18,495)
Financial liabilities at fair value through profit or loss	–	(4,579)
Derivative financial instruments	(8)	(229)
Deposits from customers	(46,277)	(215,253)
Other accounts and provisions	(725)	(15,346)
Current tax liabilities	(45)	(236)
Deferred tax liabilities	(164)	(813)
Net assets disposed	7,044	38,048

The net cash inflow from disposal of discontinued operations is analysed as follows:

	2017 HK$'m	2016 HK$'m
Total consideration received, satisfied by cash	**7,685**	68,000
Transaction costs incurred in connection with the disposal	**(167)**	(366)
Cash and cash equivalents disposed	**(6,708)**	(40,642)
Net cash inflow from disposal of discontinued operations	**810**	26,992

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

The major classes of assets held for sale and liabilities associated with assets held for sale are as follows:

	2017 HK$'m	2016 HK$'m
ASSETS HELD FOR SALE		
Cash and balances with banks and other financial institutions	–	5,233
Placements with banks and other financial institutions maturing between one and twelve months	–	1,038
Financial assets at fair value through profit or loss	–	654
Derivative financial instruments	–	98
Advances and other accounts	–	30,844
Investment in securities	–	13,387
Investment properties	–	204
Properties, plant and equipment	–	1,534
Deferred tax assets	–	61
Other assets	–	240
Total assets held for sale	–	53,293
LIABILITIES ASSOCIATED WITH ASSETS HELD FOR SALE		
Deposits and balances from banks and other financial institutions	–	977
Derivative financial instruments	–	12
Deposits from customers	–	45,370
Other accounts and provisions	–	438
Current tax liabilities	–	56
Deferred tax liabilities	–	160
Total liabilities associated with assets held for sale	–	47,013
	–	6,280

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

	2017 HK$'m	2016 HK$'m
Cumulative income recognised in other comprehensive income	–	1,014

41. Share capital

	2017 HK$'m	2016 HK$'m
Issued and fully paid:		
10,572,780,266 ordinary shares	**52,864**	52,864

42. Notes to consolidated cash flow statement

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

	2017 HK$'m	2016 HK$'m
Operating profit		
– from continuing operations	**33,990**	29,482
– from discontinued operations	**141**	1,842
	34,131	31,324
Depreciation	**1,949**	1,831
Net charge of impairment allowances	**1,083**	1,021
Unwind of discount on impairment allowances	**(3)**	(9)
Advances written off net of recoveries	**(436)**	(456)
Change in subordinated liabilities	**498**	71
Change in balances with banks and other financial institutions with original maturity over three months	**(264)**	(16,567)
Change in placements with banks and other financial institutions with original maturity over three months	**22,026**	(20,609)
Change in financial assets at fair value through profit or loss	**(24,597)**	(9,294)
Change in derivative financial instruments	**12,530**	(11,891)
Change in advances and other accounts	**(182,812)**	(90,255)
Change in investment in securities	**(28,691)**	(80,954)
Change in other assets	**(3,389)**	(7,441)
Change in deposits and balances from banks and other financial institutions	**25,929**	(20,417)
Change in financial liabilities at fair value through profit or loss	**6,349**	2,432
Change in deposits from customers	**252,553**	134,458
Change in debt securities and certificates of deposit in issue	**20,520**	(5,855)
Change in other accounts and provisions	**387**	21,140
Change in insurance contract liabilities	**16,695**	3,889
Effect of changes in exchange rates	**(15,936)**	(1,335)
Operating cash inflow/(outflow) before taxation	**138,522**	(68,917)
Cash flows from operating activities included		
– interest received	**48,305**	41,563
– interest paid	**12,599**	11,578
– dividend received	**177**	135

42. Notes to consolidated cash flow statement (continued)

(b) Reconciliation of liabilities arising from financing activities

	2017 HK$'m	2016 HK$'m
Subordinated liabilities		
At 1 January, as previously reported	**19,014**	19,422
Effect of merger of entities under common control	**79**	78
At 1 January, as restated	**19,093**	19,500
Cash flows:		
Repayment of subordinated liabilities	**(16)**	–
Interest paid for subordinated liabilities	**(595)**	(478)
	(611)	(478)
Non-cash changes:		
Exchange difference	**145**	10
Other changes	**353**	61
At 31 December	**18,980**	19,093

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

	2017 HK$'m	2016 HK$'m
Cash and balances with banks and other financial institutions with original maturity within three months	**346,547**	223,747
Placements with banks and other financial institutions with original maturity within three months	**17,140**	8,568
Treasury bills and certificates of deposit with original maturity within three months		
– financial assets at fair value through profit or loss	**1,000**	64
– investment in securities	**13,257**	17,195
	377,944	249,574

43. Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liability and commitment and the aggregate credit risk-weighted amount and is prepared with reference to the completion instructions for the HKMA return of capital adequacy ratio.

	2017 HK$'m	2016 HK$'m
Direct credit substitutes	**8,414**	6,247
Transaction-related contingencies	**30,092**	12,649
Trade-related contingencies	**28,294**	32,269
Commitments that are unconditionally cancellable without prior notice	**397,100**	388,739
Other commitments with an original maturity of		
– up to one year	**17,976**	12,095
– over one year	**154,582**	132,488
	636,458	584,487
Credit risk-weighted amount	**74,844**	60,730

The credit risk-weighted amount is calculated in accordance with the Banking (Capital) Rules. The amount is dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

44. Capital commitments

The Group has the following outstanding capital commitments not provided for in the financial statements:

	2017 HK$'m	2016 HK$'m
Authorised and contracted for but not provided for	**146**	404
Authorised but not contracted for	**3**	11
	149	415

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

45. Operating lease commitments

(a) As lessee

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

	2017 HK$'m	2016 HK$'m
Land and buildings		
– Not later than one year	**607**	630
– Later than one year but not later than five years	**634**	750
– Later than five years	**14**	4
	1,255	1,384

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:

	2017 HK$'m	2016 HK$'m
Land and buildings		
– Not later than one year	**543**	396
– Later than one year but not later than five years	**502**	392
	1,045	788

The Group leases its investment properties under operating lease arrangements, with leases typically for a period from one to three years. The terms of the leases generally require the tenants to pay security deposits and provide for rent adjustments according to the prevailing market conditions at the expiration of the lease.

46. Litigation

The Group has been served a number of claims and counterclaims by various independent parties. These claims and counterclaims are in relation to the normal commercial activities of the Group.

No material provision was made against these claims and counterclaims because the directors believe that the Group has meritorious defences against the claimants or the amounts involved in these claims are not expected to be material.

47. Segmental reporting

The Group manages the business mainly from a business segment perspective and over 90% of the Group's revenues, profits before tax and assets are derived from Hong Kong. Currently, four operating segments are identified: Personal Banking, Corporate Banking, Treasury and Insurance. The classification of the Group's operating segments is based on customer segment and product type, which is aligned with the RPC (relationship, product and channel) management model of the Group.

Both Personal Banking and Corporate Banking provide general banking services including various deposit products, overdrafts, loans, credit cards, trade related products and other credit facilities, investment and insurance products, and foreign currency and derivative products. Personal Banking mainly serves retail customers and small enterprises, while Corporate Banking mainly deals with corporate customers. Treasury manages the funding and liquidity, and the interest rate and foreign exchange positions of the Group in addition to proprietary trades. The Insurance segment represents business mainly relating to life insurance products, including individual life insurance and group life insurance products. "Others" mainly represents the Group's holdings of premises, investment properties, equity investments and interests in associates and joint ventures.

Measurement of segment assets, liabilities, income, expenses, results and capital expenditure is based on the Group's accounting policies. The segment information includes items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Inter-segment funding is charged according to the internal funds transfer pricing mechanism of the Group, which is primarily based on market rates with the consideration of specific features of the product.

As the Group derives a majority of revenue from interest and the senior management relies primarily on net interest income in managing the business, interest income and expense for all reportable segments are presented on a net basis. Under the same consideration, insurance premium income and insurance benefits and claims are also presented on a net basis.

47. Segmental reporting (continued)

	Personal Banking HK$'m	Corporate Banking HK$'m	Treasury HK$'m	Insurance HK$'m	Others HK$'m	Subtotal HK$'m	Eliminations HK$'m	Consolidated HK$'m
Year ended 31 December 2017								
CONTINUING OPERATIONS								
Net interest income/(expense)								
– External	3,194	13,488	15,381	2,687	(42)	34,708	–	34,708
– Inter-segment	6,467	(635)	(4,906)	(31)	(895)	–	–	–
	9,661	12,853	10,475	2,656	(937)	34,708	–	34,708
Net fee and commission income/(expense)	6,265	5,176	324	(658)	766	11,873	(357)	11,516
Net insurance premium income	–	–	–	14,683	–	14,683	(18)	14,665
Net trading gain/(loss)	876	208	63	100	(2)	1,245	81	1,326
Net gain/(loss) on financial instruments designated at fair value through profit or loss	9	–	(3)	2,168	–	2,174	7	2,181
Net gain on other financial assets	–	30	698	435	–	1,163	–	1,163
Other operating income	81	10	37	165	2,016	2,309	(1,378)	931
Total operating income	16,892	18,277	11,594	19,549	1,843	68,155	(1,665)	66,490
Net insurance benefits and claims and movement in liabilities	–	–	–	(17,721)	–	(17,721)	–	(17,721)
Net operating income before impairment allowances	16,892	18,277	11,594	1,828	1,843	50,434	(1,665)	48,769
Net charge of impairment allowances	(753)	(323)	–	–	–	(1,076)	–	(1,076)
Net operating income	16,139	17,954	11,594	1,828	1,843	49,358	(1,665)	47,693
Operating expenses	(8,077)	(3,136)	(1,366)	(427)	(2,362)	(15,368)	1,665	(13,703)
Operating profit/(loss)	8,062	14,818	10,228	1,401	(519)	33,990	–	33,990
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	1,197	1,197	–	1,197
Net loss from disposal/revaluation of properties, plant and equipment	(7)	(5)	(1)	–	(12)	(25)	–	(25)
Share of profits less losses after tax of associates and joint ventures	–	–	–	–	100	100	–	100
Profit before taxation	8,055	14,813	10,227	1,401	766	35,262	–	35,262
At 31 December 2017								
ASSETS								
Segment assets	357,707	868,696	1,234,936	130,597	65,675	2,657,611	(12,275)	2,645,336
Interests in associates and joint ventures	–	–	–	–	417	417	–	417
	357,707	868,696	1,234,936	130,597	66,092	2,658,028	(12,275)	2,645,753
LIABILITIES								
Segment liabilities	964,859	838,426	471,564	121,752	14,083	2,410,684	(12,275)	2,398,409
Year ended 31 December 2017								
CONTINUING OPERATIONS								
Other information								
Capital expenditure	27	4	–	32	1,470	1,533	–	1,533
Depreciation	529	158	104	18	1,140	1,949	–	1,949
Amortisation of securities	–	–	29	(20)	–	9	–	9

47. Segmental reporting (continued)

	Personal Banking HK$'m	Corporate Banking HK$'m	Treasury HK$'m	Insurance HK$'m	Others HK$'m	Subtotal HK$'m	Eliminations HK$'m	Consolidated HK$'m
Year ended 31 December 2016								
CONTINUING OPERATIONS								
Net interest income/(expense)								
– External	3,472	11,156	9,013	2,379	4	26,024	–	26,024
– Inter-segment	4,984	(49)	(4,241)	(12)	(682)	–	–	–
	8,456	11,107	4,772	2,367	(678)	26,024	–	26,024
Net fee and commission income/(expense)	5,598	4,985	107	(415)	690	10,965	(281)	10,684
Net insurance premium income	–	–	–	10,651	–	10,651	(17)	10,634
Net trading gain/(loss)	668	153	4,186	(332)	3	4,678	28	4,706
Net (loss)/gain on financial instruments designated at fair value through profit or loss	–	–	(1)	97	–	96	5	101
Net (loss)/gain on other financial assets	–	(5)	623	388	–	1,006	–	1,006
Other operating income	29	3	8	216	1,818	2,074	(1,259)	815
Total operating income	14,751	16,243	9,695	12,972	1,833	55,494	(1,524)	53,970
Net insurance benefits and claims and movement in liabilities	–	–	–	(11,375)	–	(11,375)	–	(11,375)
Net operating income before impairment allowances	14,751	16,243	9,695	1,597	1,833	44,119	(1,524)	42,595
Net (charge)/reversal of impairment allowances	(424)	(201)	24	–	–	(601)	–	(601)
Net operating income	14,327	16,042	9,719	1,597	1,833	43,518	(1,524)	41,994
Operating expenses	(6,836)	(2,798)	(1,094)	(367)	(2,941)	(14,036)	1,524	(12,512)
Operating profit/(loss)	7,491	13,244	8,625	1,230	(1,108)	29,482	–	29,482
Net gain from disposal of/fair value adjustments on investment properties	–	–	–	–	429	429	–	429
Net loss from disposal/revaluation of properties, plant and equipment	(5)	(6)	–	–	(3)	(14)	–	(14)
Share of profits less losses after tax of associates and joint ventures	–	–	–	–	74	74	–	74
Profit/(loss) before taxation	7,486	13,238	8,625	1,230	(608)	29,971	–	29,971
At 31 December 2016								
ASSETS								
Segment assets	318,935	713,562	1,101,385	111,186	67,990	2,313,058	(11,930)	2,301,128
Interests in associates and joint ventures	–	–	–	–	319	319	–	319
Assets held for sale	9,299	23,999	19,142	–	1,660	54,100	(807)	53,293
	328,234	737,561	1,120,527	111,186	69,969	2,367,477	(12,737)	2,354,740
LIABILITIES								
Segment liabilities	796,943	749,843	421,728	103,783	13,406	2,085,703	(12,530)	2,073,173
Liabilities associated with assets held for sale	35,820	10,823	288	–	289	47,220	(207)	47,013
	832,763	760,666	422,016	103,783	13,695	2,132,923	(12,737)	2,120,186
Year ended 31 December 2016								
CONTINUING OPERATIONS								
Other information								
Capital expenditure	26	3	–	18	1,437	1,484	–	1,484
Depreciation	384	152	75	13	1,181	1,805	–	1,805
Amortisation of securities	–	–	(430)	(8)	–	(438)	–	(438)

48. Assets pledged as security

As at 31 December 2017, the liabilities of the Group amounting to HK$11,111 million (2016: HK$10,686 million) were secured by assets deposited with central depositories to facilitate settlement operations. In addition, the liabilities of the Group amounting to HK$14,477 million (2016: HK$19,260 million) were secured by debt securities related to sale and repurchase arrangements. The amount of assets pledged by the Group to secure these liabilities was HK$26,002 million (2016: HK$30,903 million) mainly included in "Trading assets" and "Investment in securities".

49. Offsetting financial instruments

The following tables present details of the Group's financial instruments subject to offsetting, enforceable master netting arrangements and similar agreements.

	2017					
				Related amounts not set off in the balance sheet		
	Gross amounts of recognised financial assets HK$'m	Gross amounts of recognised financial liabilities set off in the balance sheet HK$'m	Net amounts of financial assets presented in the balance sheet HK$'m	Financial instruments HK$'m	Cash collateral received HK$'m	Net amount HK$'m
Assets						
Derivative financial instruments	33,458	–	33,458	(23,094)	(4,427)	5,937
Reverse repurchase agreements	9,012	–	9,012	(9,012)	–	–
Securities borrowing agreements	2,503	–	2,503	(2,503)	–	–
Other assets	17,432	(10,545)	6,887	–	–	6,887
	62,405	(10,545)	51,860	(34,609)	(4,427)	12,824

	2017					
				Related amounts not set off in the balance sheet		
	Gross amounts of recognised financial liabilities HK$'m	Gross amounts of recognised financial assets set off in the balance sheet HK$'m	Net amounts of financial liabilities presented in the balance sheet HK$'m	Financial instruments HK$'m	Cash collateral pledged HK$'m	Net amount HK$'m
Liabilities						
Derivative financial instruments	30,963	–	30,963	(23,094)	(676)	7,193
Repurchase agreements	14,477	–	14,477	(14,477)	–	–
Other liabilities	11,265	(10,545)	720	–	–	720
	56,705	(10,545)	46,160	(37,571)	(676)	7,913

49. Offsetting financial instruments (continued)

	2016					
				Related amounts not set off in the balance sheet		
	Gross amounts of recognised financial assets HK$'m	Gross amounts of recognised financial liabilities set off in the balance sheet HK$'m	Net amounts of financial assets presented in the balance sheet HK$'m	Financial instruments HK$'m	Cash collateral received HK$'m	Net amount HK$'m
Assets						
Derivative financial instruments	63,869	–	63,869	(36,951)	(6,795)	20,123
Reverse repurchase agreements	5,949	–	5,949	(5,949)	–	–
Securities borrowing agreements	1,000	–	1,000	(1,000)	–	–
Other assets	15,931	(9,044)	6,887	–	–	6,887
	86,749	(9,044)	77,705	(43,900)	(6,795)	27,010

	2016					
				Related amounts not set off in the balance sheet		
	Gross amounts of recognised financial liabilities HK$'m	Gross amounts of recognised financial assets set off in the balance sheet HK$'m	Net amounts of financial liabilities presented in the balance sheet HK$'m	Financial instruments HK$'m	Cash collateral pledged HK$'m	Net amount HK$'m
Liabilities						
Derivative financial instruments	48,972	–	48,972	(36,951)	(4,446)	7,575
Repurchase agreements	19,260	–	19,260	(19,260)	–	–
Other liabilities	9,693	(9,044)	649	–	–	649
	77,925	(9,044)	68,881	(56,211)	(4,446)	8,224

For master netting agreements of OTC derivative, sale and repurchase and securities lending and borrowing transactions entered into by the Group, related amounts with the same counterparty can be offset if an event of default or other predetermined events occur.

50. Transfers of financial assets

The transferred financial assets of the Group below that do not qualify for derecognition are debt securities held by counterparties as collateral under sale and repurchase agreements.

	2017		2016	
	Carrying amount of transferred assets HK$'m	**Carrying amount of associated liabilities HK$'m**	Carrying amount of transferred assets HK$'m	Carrying amount of associated liabilities HK$'m
Repurchase agreements	**14,767**	**14,477**	20,080	19,260

51. Loans to directors

Particulars of loans made to directors of the Company pursuant to section 383 of the Hong Kong Companies Ordinance and Part 3 of the Companies (Disclosure of Information about Benefits of Directors) Regulation are as follows:

	2017 HK$'m	2016 HK$'m
Aggregate amount of relevant transactions outstanding at year end	**5**	874
Maximum aggregate amount of relevant transactions outstanding during the year	**877**	2,243

52. Significant related party transactions

The Group is subject to the control of the State Council of the PRC Government through China Investment Corporation ("CIC"), its wholly-owned subsidiary Central Huijin Investment Ltd. ("Central Huijin"), and BOC in which Central Huijin has controlling equity interests.

52. Significant related party transactions (continued)

(a) Transactions with the parent companies and the other companies controlled by the parent companies

General information of the parent companies:

The Group is controlled by BOC. Central Huijin is the controlling entity of BOC, and it is a wholly-owned subsidiary of CIC which is a wholly state-owned company engaging in foreign currency investment management.

Central Huijin has controlling equity interests in certain other entities in the PRC.

The Group enters into banking and other transactions with these entities in the normal course of business which include loans, investment securities, money market and reinsurance transactions.

The majority of transactions with BOC arise from money market activities. As at 31 December 2017, the related aggregate amounts due from and to BOC of the Group were HK$186,565 million (2016: HK$106,281 million) and HK$60,385 million (2016: HK$58,654 million) respectively. The aggregate amounts of income and expenses of the Group arising from these transactions with BOC for the year ended 31 December 2017 were HK$2,320 million (2016: HK$1,436 million) and HK$459 million (2016: HK$306 million) respectively. The related party transactions above constitute connected transactions as defined in Chapter 14A of the Listing Rules but under exemption from its disclosure requirement.

The transactions with BOC disclosed in Note 57 also constitute connected transactions as defined in Chapter 14A of the Listing Rules and announcements had been made by the Group on 30 June 2016, 6 January 2017, 28 February 2017, 6 July 2017 and 3 November 2017.

Transactions with other companies controlled by BOC are not considered material.

(b) Transactions with government authorities, agencies, affiliates and other state controlled entities

The Group is subject to the control of the State Council of the PRC Government through CIC and Central Huijin, which also directly or indirectly controls a significant number of entities through its government authorities, agencies, affiliates and other state controlled entities. The Group enters into banking transactions with government authorities, agencies, affiliates and other state controlled entities in the normal course of business at commercial terms.

These transactions include, but are not limited to, the following:

- lending, provision of credits and guarantees, and deposit taking;
- inter-bank balance taking and placing;
- sales, purchases, underwriting and redemption of bonds issued by other state controlled entities;
- rendering of foreign exchange, remittance and investment related services;
- provision of fiduciary activities; and
- purchase of utilities, transport, telecommunication and postage services.

52. Significant related party transactions (continued)

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

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

	2017 HK$'m	2016 HK$'m
Income statement items		
Associates		
– Fee and commission expenses	**36**	–
– Other operating expenses	**72**	70
Other related parties		
– Fee and commission income	**10**	9
Balance sheet item		
Associates		
– Other accounts and provisions	**4**	3

The related party transactions in respect of the fee and commission expenses and other operating expenses arising from associates above constitute connected transactions as defined in Chapter 14A of the Listing Rules and the required disclosures are provided in "Connected transactions" on pages 282 to 283.

(d) Key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including directors and senior management. The Group accepts deposits from and grants loans and credit facilities to key management personnel in the ordinary course of business. During both the current and prior years, no material transaction was conducted with key management personnel of the Company and its holding companies, as well as parties related to them.

The compensation of key management personnel for the year ended 31 December is detailed as follows:

	2017 HK$'m	2016 HK$'m
Salaries and other short-term employee benefits	**48**	46

53. International claims

The below analysis is prepared with reference to the completion instructions for the HKMA return of international banking statistics. International claims are exposures to counterparties on which the ultimate risk lies based on the locations of the counterparties after taking into account the transfer of risk, and represent the sum of cross-border claims in all currencies and local claims in foreign currencies. For a claim guaranteed by a party situated in a location different from the counterparty, the risk will be transferred to the location of the guarantor. For a claim on an overseas branch of a bank whose head office is located in another location, the risk will be transferred to the location where its head office is located.

Claims on individual countries/regions, after risk transfer, amounting to 10% or more of the aggregate international claims of the Group are shown as follows:

	2017				
			Non-bank private sector		
	Banks HK$'m	**Official sector HK$'m**	**Non-bank financial institutions HK$'m**	**Non-financial private sector HK$'m**	**Total HK$'m**
Mainland of China	**401,249**	**95,744**	**25,940**	**142,557**	**665,490**
Hong Kong	**11,186**	**–**	**19,529**	**311,584**	**342,299**

	2016				
			Non-bank private sector		
	Banks HK$'m	Official sector HK$'m	Non-bank financial institutions HK$'m	Non-financial private sector HK$'m	Total HK$'m
Mainland of China	317,073	83,649	19,218	130,223	550,163
Hong Kong	4,557	3,516	16,287	271,107	295,467

54. Non-bank Mainland exposures

The analysis of non-bank Mainland exposures is based on the categories of non-bank counterparties and the types of direct exposures with reference to the completion instructions for the HKMA return of Mainland activities, which includes the Mainland exposures extended by BOCHK and its local banking subsidiaries.

		2017		
	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	277,878	46,003	323,881
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	67,154	11,268	78,422
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	53,490	11,078	64,568
Other entities of central government not reported in item 1 above	4	29,972	1,029	31,001
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	75,825	21,261	97,086
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	2,624	828	3,452
Total	8	506,943	91,467	598,410
Total assets after provision	9	2,445,769		
On-balance sheet exposures as percentage of total assets	10	20.73%		

54. Non-bank Mainland exposures (continued)

		2016		
	Items in the HKMA return	On-balance sheet exposure HK$'m	Off-balance sheet exposure HK$'m	Total exposure HK$'m
Central government, central government-owned entities and their subsidiaries and joint ventures	1	247,107	47,259	294,366
Local governments, local government-owned entities and their subsidiaries and joint ventures	2	65,980	10,126	76,106
PRC nationals residing in Mainland or other entities incorporated in Mainland and their subsidiaries and joint ventures	3	51,955	11,584	63,539
Other entities of central government not reported in item 1 above	4	26,874	1,812	28,686
Other entities of local governments not reported in item 2 above	5	–	–	–
PRC nationals residing outside Mainland or entities incorporated outside Mainland where the credit is granted for use in Mainland	6	60,043	11,796	71,839
Other counterparties where the exposures are considered to be non-bank Mainland exposures	7	4,144	199	4,343
Total	8	456,103	82,776	538,879
Total assets after provision	9	2,176,247		
On-balance sheet exposures as percentage of total assets	10	20.96%		

55. Balance sheet and statement of changes in equity

(a) Balance sheet

As at 31 December	2017 HK$'m	2016 HK$'m
ASSETS		
Bank balances with a subsidiary	**1,798**	62
Investment in securities	**2,886**	2,532
Investment in subsidiaries	**55,322**	55,089
Amounts due from a subsidiary	**3,831**	3,659
Other assets	**1**	–
Total assets	**63,838**	61,342
LIABILITIES		
Amounts due to a subsidiary	**3**	1
Total liabilities	**3**	1
EQUITY		
Share capital	**52,864**	52,864
Reserves	**10,971**	8,477
Total equity	**63,835**	61,341
Total liabilities and equity	**63,838**	61,342

Approved by the Board of Directors on 29 March 2018 and signed on behalf of the Board by:

CHEN Siqing
Director

GAO Yingxin
Director

55. Balance sheet and statement of changes in equity (continued)

(b) Statement of changes in equity

		Reserves		
	Share capital HK$'m	Reserve for fair value changes of available-for-sale securities HK$'m	Retained earnings HK$'m	Total equity HK$'m
At 1 January 2016	52,864	1,203	7,245	61,312
Profit for the year	–	–	20,404	20,404
Other comprehensive income:				
Available-for-sale securities	–	73	–	73
Total comprehensive income	–	73	20,404	20,477
Dividends	–	–	(20,448)	(20,448)
At 31 December 2016	52,864	1,276	7,201	61,341
At 1 January 2017	**52,864**	**1,276**	**7,201**	**61,341**
Profit for the year	**–**	**–**	**15,515**	**15,515**
Other comprehensive income:				
Available-for-sale securities	**–**	**354**	**–**	**354**
Total comprehensive income	**–**	**354**	**15,515**	**15,869**
Dividends	**–**	**–**	**(13,375)**	**(13,375)**
At 31 December 2017	**52,864**	**1,630**	**9,341**	**63,835**

56. Principal subsidiaries

The particulars of all direct and indirect subsidiaries of the Company are set out in "Appendix – Subsidiaries of the Company". The following is a list of principal subsidiaries as at 31 December 2017:

Name	Place of incorporation and operation	Issued share capital	Interest held	Principal activities
Bank of China (Hong Kong) Limited	Hong Kong	Ordinary shares HK$43,042,840,858	*100%	Banking business
BOC Group Life Assurance Company Limited	Hong Kong	Ordinary shares HK$3,538,000,000	*51%	Life insurance business
BOC Credit Card (International) Limited	Hong Kong	Ordinary shares HK$480,000,000	100%	Credit card services
Bank of China (Malaysia) Berhad	Malaysia	Ordinary shares RM760,518,480	100%	Banking business
Bank of China (Thai) Public Company Limited	Thailand	Ordinary shares Baht10,000,000,000	100%	Banking business
Po Sang Securities and Futures Limited	Hong Kong	Ordinary shares HK$335,000,000	100%	Securities and futures brokerage

* Shares held directly by the Company

The particulars of a subsidiary with significant non-controlling interests are as follows:

BOC Group Life Assurance Company Limited

	2017	2016
Proportion of ownership interests and voting rights held by non-controlling interests	**49%**	49%

	2017 HK$'m	2016 HK$'m
Profit attributable to non-controlling interests	**586**	510
Accumulated non-controlling interests	**4,334**	3,627
Summarised financial information:		
– total assets	**130,597**	111,186
– total liabilities	**121,752**	103,783
– profit for the year	**1,196**	1,041
– total comprehensive income for the year	**1,492**	754

57. Application of merger accounting

On 9 January 2017, BOCHK acquired the entire issued share capital of BOC Thailand from BOC (0.01% of which was owned through the acquisition of the 14 special purpose vehicle companies incorporated in the British Virgin Islands) for a total consideration of HK$2,996 million in cash. On 10 July 2017 and 6 November 2017, BOCHK acquired the Indonesia Business and Cambodia Business from BOC for a total consideration of HK$2,053 million and HK$1,569 million in cash respectively. BOC Thailand, Indonesia Business, Cambodia Business and BOCHK are all under the common control of BOC before and after the combination. The Group has applied the merger accounting method in accordance with the Accounting Guideline 5 "Merger Accounting for Common Control Combinations" issued by the HKICPA in the preparation of financial statements. The comparative amounts have been restated accordingly as if the business of BOC Thailand, Indonesia Business and Cambodia Business had always been carried out by the Group.

The statements of the adjustments to the consolidated equity as at 31 December are as follows:

	2017			
	Before combination HK$'m	**Entities under common control HK$'m**	**Adjustment HK$'m**	**After combination HK$'m**
Share capital	**52,864**	**3,455**	**(3,455)**	**52,864**
Merger reserve	**–**	**–**	**(3,163)**	**(3,163)**
Retained earnings and other reserves	**191,921**	**1,117**	**–**	**193,038**
	244,785	**4,572**	**(6,618)**	**242,739**
Non-controlling interests	**4,605**	**–**	**–**	**4,605**
	249,390	**4,572**	**(6,618)**	**247,344**

	2016			
	Before combination HK$'m	Entities under common control HK$'m	Adjustment HK$'m	After combination HK$'m
Share capital	52,864	3,455	(3,455)	52,864
Merger reserve	–	–	3,455	3,455
Retained earnings and other reserves	171,789	539	–	172,328
	224,653	3,994	–	228,647
Non-controlling interests	5,907	–	–	5,907
	230,560	3,994	–	234,554

58. Ultimate holding company

The Group is subject to the control of the State Council of the PRC Government through China Investment Corporation, its wholly-owned subsidiary Central Huijin Investment Ltd. ("Central Huijin"), and BOC in which Central Huijin has controlling equity interests.

59. Comparative amounts

In respect of the acquisition of BOC Thailand, Indonesia Business and Cambodia Business from BOC on 9 January 2017, 10 July 2017 and 6 November 2017 respectively as explained in Note 57, the Group has applied merger accounting method for the business combination under common control. Comparative amounts in the financial statements have been restated as if the business of BOC Thailand, Indonesia Business and Cambodia Business had always been carried out by the Group.

60. Events after the balance sheet date

As stated in the Company's announcement dated 29 December 2017, all of the conditions precedent respectively set out in the Philippines Agreement and the Vietnam Agreement entered into between BOCHK and BOC were satisfied or, as appropriate, waived and completion of the transfers of the Philippines Business and the Vietnam Business took place on 29 January 2018 pursuant to the respective terms and conditions of the Philippines Agreement and the Vietnam Agreement. Upon completion, each of Bank of China Limited – Manila Branch and Bank of China – Hochiminh City Branch became a branch owned by BOCHK, and all the assets and liabilities arising in connection with the Philippines Business and the Vietnam Business were transferred to and assumed by BOCHK pursuant to the respective terms and conditions of the Philippines Agreement and the Vietnam Agreement.

61. Approval of financial statements

The financial statements were approved and authorised for issue by the Board of Directors on 29 March 2018.

Unaudited Supplementary Financial Information

1. Regulatory Disclosures

The Regulatory Disclosures, together with the disclosures in this Annual Report, contained all the disclosures required by the Banking (Disclosure) Rules issued by the HKMA. The Regulatory Disclosures is available under section "Regulatory Disclosures" on BOCHK's website at www.bochk.com.

This Annual Report and the Regulatory Disclosures are prepared according to the Group's disclosure policy. The disclosure policy sets out a robust mechanism for the Group's disclosures of financial information on a legitimate and compliant basis. It depicts the principles and internal control measures to ensure the timeliness, fairness, accuracy, integrity, completeness and legitimacy of financial disclosures.

2. Connected transactions

In 2017, BOCHK, a wholly-owned subsidiary of the Company, and its subsidiaries engaged on a regular basis in the usual course of their business in numerous transactions with BOC and its Associates. As BOC is the Company's controlling shareholder and therefore a connected person of the Company, all such transactions constituted connected transactions for the purposes of the Listing Rules. The Group is subject to the control of the State Council of the PRC Government through China Investment Corporation ("CIC"), its wholly-owned subsidiary Central Huijin Investment Ltd. ("Central Huijin"), and BOC in which Central Huijin has controlling equity interests. Central Huijin is the ultimate controlling shareholder of the Company. Central Huijin has accepted PRC Government's authorisation in carrying out equity investment in core financial enterprises. For the purposes of this report, therefore, Central Huijin and its Associates have not been treated as connected persons to the Company.

The transactions fell into the following two categories:

1. exempted transactions entered into in the ordinary and usual course of business and under normal commercial terms or better. Such transactions were (1) fully exempted from shareholders' approval, annual review and all disclosure requirements and/or (2) exempted from shareholders' approval requirement by virtue of Rules 14A.76 and 14A.87 to 14A.101 of the Listing Rules;

2. certain continuing connected transactions conducted pursuant to the Services and Relationship Agreement entered into among, inter alia, the Company and BOC dated 6 July 2002 (as amended and supplemented from time to time, which has been amended for a period of three years commencing 1 January 2017), whereas BOC has agreed to, and agreed to procure its Associates to, enter into all future arrangements with the Group on an arm's length basis, on normal commercial terms and at rates no less favourable than those offered to independent third parties, in relation to certain areas including, among others, information technology services, training services, physical bullion agency services, correspondent banking arrangements, treasury transactions, provision of insurance and syndicated loans, and the Company has agreed to, and agreed to procure its subsidiaries to, enter into all future arrangements on the same basis, provided that the rates offered by the Group to BOC and its Associates will be no more favourable than those offered to independent third parties. The Services and Relationship Agreement has also been last amended to allow (i) for the provision of business development, investment products and asset management and referral services between BOC and its Associates and the Group; (ii) the provision of computer systems and information technology services between BOC and its Associates and the Group; and (iii) the provision of support and services by BOC and its Associates to BOCHK's branches and subsidiaries in the Southeast Asian region when they become branches and subsidiaries of BOCHK. On 14 December 2016 the Company made an announcement (the "Announcement") in accordance with Rule 14A.35 of the Listing Rules, and has got the approval from the independent shareholders on 28 June 2017. The Announcement listed those continuing connected transactions that exceeded the de minimus threshold and set out caps in respect of such transactions for 2017-2019. These transactions were conducted in the ordinary and usual course of its business and on normal commercial terms or better. Details of these continuing connected transactions are set out below and are described in the announcements which may be viewed at the Company's website. The Company has complied with the disclosure requirements in accordance with Chapter 14A of the Listing Rules.

2. Connected transactions (continued)

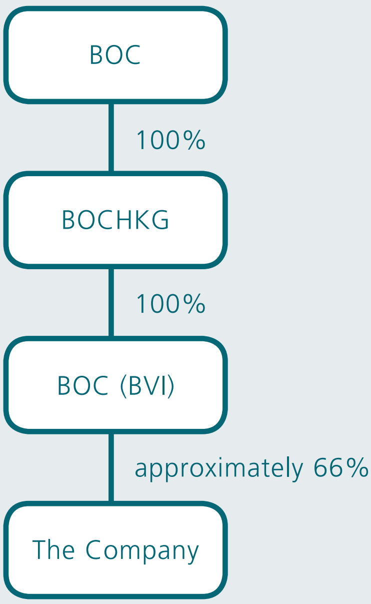
Type of Transaction	2017 Cap (HK$'m)	2017 Actual Amount (HK$'m)
Information Technology Services	1,000	74
Property Transactions	1,000	190
Bank-note Delivery	1,000	267
Provision of Insurance Cover	1,000	203
Card Services	1,000	260
Custody Business	1,000	55
Contact Centre Services	1,000	72
Business Development Services	1,000	26
Securities Transactions	4,500	238
Fund Distribution Transactions	4,500	32
Insurance Agency	4,500	878
Investment Products Transactions	150,000	1,422
Asset Management and Referral Services	4,500	80
Foreign Exchange Transactions	4,500	(105)
Derivatives Transactions	4,500	57
Trading of Financial Assets	150,000	25,025
Inter-bank Capital Markets	150,000	13,409

3. Reconciliation between HKFRSs vs IFRSs/CASs

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 IFRSs and CASs for which the Company and its subsidiaries will form part of the consolidated financial statements. The requirements of CASs have substantially converged with HKFRSs and IFRSs.

The consolidated financial information of "BOC Hong Kong Group" for the periods disclosed by BOC in its consolidated financial statements is not the same as the consolidated financial information of the Group for the periods published by the Company pursuant to applicable laws and regulations in Hong Kong. There are two reasons for this.

First, the definitions of "BOC Hong Kong Group" (as adopted by BOC for the purpose of its own financial disclosure) and "Group" (as adopted by the Company in preparing and presenting its consolidated financial information) are different: "BOC Hong Kong Group" refers to BOCHKG and its subsidiaries, whereas "Group" refers to the Company and its subsidiaries (see the below organisation chart). Though there is difference in definitions between "BOC Hong Kong Group" and "Group", their financial results for the periods presented are substantially the same. This is because BOCHKG and BOC (BVI) are holding companies only and have no substantive operations of their own.



Second, the Group has prepared its consolidated financial statements in accordance with HKFRSs; whereas the consolidated financial information reported to BOC is prepared in accordance with IFRSs and CASs respectively. There is a difference in the election of subsequent measurement basis of bank premises by the Group and by BOC respectively.

3. Reconciliation between HKFRSs vs IFRSs/CASs (continued)

The Board considers that the best way to ensure that shareholders and the investing public understand the material differences between the consolidated financial information of the Group published by the Company on the one hand, and the consolidated financial information of BOC Hong Kong Group disclosed by BOC in its consolidated financial statements on the other hand, is to present reconciliations of the profit after tax/net assets of the Group prepared under HKFRSs to the profit after tax/net assets of the Group prepared under IFRSs and CASs respectively for the periods presented.

The major differences which arise from the difference in measurement basis relate to the following:

(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 IFRSs and CASs. 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 IFRSs and CASs, including the gain on disposal of discontinued operations.

(b) Deferred tax adjustments

These represent the deferred tax effect of the aforesaid adjustments.

Profit after tax/net assets reconciliation

HKFRSs vs IFRSs/CASs

	Profit after tax		Net assets	
	2017 HK$'m	2016 HK$'m	**2017 HK$'m**	2016 HK$'m
Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under HKFRSs	**31,837**	56,696	**247,344**	234,554
Add: IFRSs/CASs adjustments				
Restatement of carrying value of bank premises	**1,507**	6,223	**(34,213)**	(34,426)
Deferred tax adjustments	**(120)**	(938)	**5,827**	5,843
Profit after tax/net assets of BOC Hong Kong (Holdings) Limited prepared under IFRSs/CASs	**33,224**	61,981	**218,958**	205,971

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$283,000,000	100.00%	Investment holding
BOC Insurance (International) Holdings Company Limited	Hong Kong 6 June 2017	Ordinary shares HK$100	100.00%	Investment holding
Indirectly held:				
BOC Credit Card (International) Limited	Hong Kong 9 September 1980	Ordinary shares HK$480,000,000	100.00%	Credit card services
BOC Group Trustee Company Limited	Hong Kong 1 December 1997	Ordinary shares HK$200,000,000	66.00%	Trustee services
BOCI-Prudential Trustee Limited	Hong Kong 11 October 1999	Ordinary shares HK$300,000,000	42.24%*	Trustee services
Bank of China (Malaysia) Berhad	Malaysia 14 April 2000	Ordinary shares RM760,518,480	100.00%	Banking business
China Bridge (Malaysia) Sdn. Bhd.	Malaysia 24 April 2009	Ordinary shares RM1,000,000	100.00%	China visa application
Bank of China (Thai) Public Company Limited[1]	Thailand 1 April 2014	Ordinary shares Baht10,000,000,000	100.00%	Banking business
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
BOCHK Financial Products (Cayman) Ltd.	Cayman Islands 10 November 2006	Ordinary shares US$50,000	100.00%	Issuing structured notes
BOCHK Information Technology (Shenzhen) Co., Ltd.	PRC 16 April 1990	Registered capital HK$70,000,000	100.00%	Property holding and investment
BOCHK Information Technology Services (Shenzhen) Co., Ltd.	PRC 26 May 1993	Registered capital HK$40,000,000	100.00%	Information technology services
Che Hsing (Nominees) Limited	Hong Kong 23 April 1980	Ordinary shares HK$10,000	100.00%	Nominee services
Po Sang Financial Investment Services Company Limited	Hong Kong 23 September 1980	Ordinary shares HK$335,000,000	100.00%	Gold trading and investment holding
Po Sang Securities and Futures Limited	Hong Kong 19 October 1993	Ordinary shares HK$335,000,000	100.00%	Securities and futures brokerage
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

Subsidiaries of the Company (continued)

Name	Place and date of incorporation/ operation	Issued share capital/ registered capital	Interest held	Principal activities
Billion Express Development Inc.[1]	British Virgin Islands 7 February 2014	Ordinary shares US$1	100.00%	Investment holding
Billion Orient Holdings Ltd.[1]	British Virgin Islands 3 February 2014	Ordinary shares US$1	100.00%	Investment holding
Elite Bond Investments Ltd.[1]	British Virgin Islands 7 February 2014	Ordinary shares US$1	100.00%	Investment holding
Express Capital Enterprise Inc.[1]	British Virgin Islands 3 February 2014	Ordinary shares US$1	100.00%	Investment holding
Express Charm Holdings Corp.[1]	British Virgin Islands 7 February 2014	Ordinary shares US$1	100.00%	Investment holding
Express Shine Assets Holdings Corp.[1]	British Virgin Islands 3 January 2014	Ordinary shares US$1	100.00%	Investment holding
Express Talent Investment Ltd.[1]	British Virgin Islands 13 February 2014	Ordinary shares US$1	100.00%	Investment holding
Gold Medal Capital Inc.[1]	British Virgin Islands 3 January 2014	Ordinary shares US$1	100.00%	Investment holding
Gold Tap Enterprises Inc.[1]	British Virgin Islands 13 February 2014	Ordinary shares US$1	100.00%	Investment holding
Maxi Success Holdings Ltd.[1]	British Virgin Islands 7 February 2014	Ordinary shares US$1	100.00%	Investment holding
Smart Linkage Holdings Inc.[1]	British Virgin Islands 13 February 2014	Ordinary shares US$1	100.00%	Investment holding
Smart Union Capital Investments Ltd.[1]	British Virgin Islands 3 January 2014	Ordinary shares US$1	100.00%	Investment holding
Success Trend Development Ltd.[1]	British Virgin Islands 18 February 2014	Ordinary shares US$1	100.00%	Investment holding
Wise Key Enterprises Corp.[1]	British Virgin Islands 18 February 2014	Ordinary shares US$1	100.00%	Investment holding
BOCHK Asset Management Limited	Hong Kong 28 October 2010	Ordinary shares HK$272,500,000	100.00%	Asset management

* 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.

Note 1: The acquisition of Bank of China (Thai) Public Company Limited and the 14 special purpose vehicle companies was completed on 9 January 2017.

Sino Information Services Company Limited was dissolved on 14 February 2017.

The disposal of Chiyu Banking Corporation Limited, Chiyu Banking Corporation (Nominees) Limited, Grace Charter Limited and Seng Sun Development Company, Limited was completed on 27 March 2017.

BOC Insurance (International) Holdings Company Limited was incorporated on 6 June 2017.

Definitions

In this Annual Report, unless the context otherwise requires, the following terms shall have the meanings set out below:

Terms	Meanings
"ABS"	Asset-backed Securities
"ADR"	American Depositary Receipt
"ADS(s)"	American Depositary Share(s)
"ALCO"	the Asset and Liability Management Committee
"AT1"	Additional Tier 1
"ATM"	Automated Teller Machine
"Associates"	has the meaning ascribed to "associates" in the Listing Rules
"BOC"	Bank of China Limited, a joint stock commercial bank with limited liability established under the laws of the PRC, the H shares and A shares of which are listed on the Hong Kong Stock Exchange and the Shanghai Stock Exchange respectively
"BOC (BVI)"	BOC Hong Kong (BVI) Limited, a company incorporated under the laws of the British Virgin Islands and a wholly-owned subsidiary of BOCHKG
"BOCCC"	BOC Credit Card (International) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOCHK
"BOCG Insurance"	Bank of China Group Insurance Company Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOC
"BOCHKG"	BOC Hong Kong (Group) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOC
"BOCHK" or "the Bank"	Bank of China (Hong Kong) Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of the Company
"BOCI"	BOC International Holdings Limited, a company incorporated under the laws of Hong Kong and a wholly-owned subsidiary of BOC
"BOCI-Prudential Manager"	BOCI-Prudential Asset Management Limited, a company incorporated under the laws of Hong Kong, in which BOCI Asset Management Limited, a wholly-owned subsidiary of BOC International Holdings Limited, and Prudential Corporation Holdings Limited hold equity interests of 64% and 36% respectively
"BOCI-Prudential Trustee"	BOCI-Prudential Trustee Limited, a company incorporated under the laws of Hong Kong, in which BOC Group Trustee Company Limited and Prudential Corporation Holdings Limited hold equity interests of 64% and 36% respectively
"BOC Life"	BOC Group Life Assurance Company Limited, a company incorporated under the laws of Hong Kong, in which the Group and BOCG Insurance hold equity interests of 51% and 49% respectively
"BOC Malaysia"	Bank of China (Malaysia) Berhad, a wholly-owned subsidiary of BOCHK
"BOC Thailand"	Bank of China (Thai) Public Company Limited, a wholly-owned subsidiary of BOCHK
"Board" or "Board of Directors"	the Board of Directors of the Company
"CAS"	Chinese Accounting Standard for Business Enterprises
"CE"	Chief Executive
"CET1"	Common Equity Tier 1
"CFO"	Chief Financial Officer
"CIC"	China Investment Corporation
"CRO"	Chief Risk Officer
"CVA"	Credit Valuation Adjustment

Terms	Meanings
"Central Huijin"	Central Huijin Investment Ltd.
"Chiyu"	Chiyu Banking Corporation Limited, a company incorporated under the laws of Hong Kong
"DCE"	Deputy Chief Executive
"DVA"	Debit Valuation Adjustment
"EV"	Economic Value Sensitivity Ratio
"FCC"	the Financial Crime Compliance Department
"FIRB"	Foundation Internal Ratings-based
"Fitch"	Fitch Ratings
"GDP"	Gross Domestic Product
"HIBOR"	Hong Kong Interbank Offered Rate
"HKAS"	Hong Kong Accounting Standard
"HKFRS"	Hong Kong Financial Reporting Standard
"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 of the PRC
"ICAAP"	Internal Capital Adequacy Assessment Process
"IFRS"	International Financial Reporting Standard
"IMM"	Internal Models
"IT"	Information Technology
"LCO"	the Legal & Compliance and Operational Risk Management Department
"LCR"	Liquidity Coverage Ratio
"LIBOR"	London Interbank Offered Rate
"Listing Rules"	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited
"MBS"	Mortgage-backed Securities
"MC"	the Management Committee
"MPF"	Mandatory Provident Fund
"MPF Schemes Ordinance"	the Mandatory Provident Fund Schemes Ordinance, Chapter 485 of the Laws of Hong Kong, as amended
"mainland" or "Mainland of China"	the mainland of the PRC
"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
"PVBP"	Price Value of a Basis Point

Definitions

Terms	Meanings
"QDII"	Qualified Domestic Institutional Investors
"RMC"	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"	Small and Medium-sized Enterprise
"STC"	Standardised (Credit Risk)
"STM"	Standardised (Market Risk)
"STO"	Standardised (Operational Risk)
"Standard & Poor's"	Standard & Poor's Ratings Services
"Stock Exchange" or "Hong Kong Stock Exchange" or "Stock Exchange of Hong Kong"	The Stock Exchange of Hong Kong Limited
"the Company"	BOC Hong Kong (Holdings) Limited, a company incorporated under the laws of Hong Kong
"the Group"	the Company and its subsidiaries collectively referred as the Group
"US"	the United States of America
"VAR"	Value at Risk

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This annual report is printed on elemental chlorine free paper with varnishing, an environmentally friendly technique, on the cover. We strive to protect the environment and undertake corporate citizenship for the betterment of our future generations.

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

24/F Bank of China Tower, 1 Garden Road, Hong Kong
www.bochk.com

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