# Management Discussion and Analysis — Financial Review

## Economic and Financial Environment

In 2018, the global economy continued its overall recovery, albeit with weakened growth momentum and less consistent growth patterns. The US economic recovery recorded solid gains, but showed signs of slowing down. The Eurozone's economic recovery weakened, and the Japanese economy experienced more fluctuations. The UK economy continued to grow at a slow pace, while remaining exposed to the uncertainties brought about by Brexit. The performance of emerging economies continued to diverge. In addition, the growth of international trade in goods slowed down and international direct investment aggregates decreased.

International financial markets experienced large fluctuations. The US Federal Reserve raised interest rates four times and kept reducing its balance sheet, the European Central Bank ceased its asset purchase programme, and the central banks of many emerging economies hiked interest rates. As a result, global liquidity tightened. In addition, the US Dollar Index rose, the Euro and the British pound fell against the US dollar, and the currencies of some emerging economies rebounded after a sharp drop. The stock markets of major economies reached a high point and then declined, while commodity prices fell due to concerns over trade tensions, Fed rate increases and the possible peaking of the economic cycle.

The Chinese economy remained stable, and its structure continued to be optimised. The services industry maintained a steady and rapid growth and consumption played a greater role in driving economic growth. The balance of payments was generally balanced and the price situations kept steady. In 2018, China's gross domestic product (GDP) increased by 6.6%, with the consumer price index (CPI) rising by 2.1%. Total retail sales of consumer goods (TRSCG) increased by 9.0%, and total fixed asset investments (TFAI) grew by 5.9%.

The Chinese government implemented a prudent monetary policy. Adhering to the fundamental requirement that the financial sector should serve the real economy, it strengthened financial support in this regard, especially for micro and small-sized enterprises and private enterprises. In general, financial markets operated smoothly. Market liquidity was kept at a reasonable and adequate level, financial institution loans grew fairly rapidly and RMB exchange rates remained basically stable and more flexible. The outstanding broad money supply (M2) grew by 8.1% year on year. The outstanding RMB loans increased by RMB16.2 trillion, RMB2.6 trillion more than that of the prior year. The outstanding all-system financing aggregates was RMB200.8 trillion, an increase of 9.8% compared with the prior year. Bond issuance expanded to a total of RMB43.1 trillion, an increase of 7.5% compared with the prior year. The central parity rate of the RMB against the USD fell by 4.8% compared with the prior year-end.

China's banking sector continued to operate in a sound manner. Banking institutions dedicated themselves to serving the real economy, strived to prevent and mitigate financial risks and constantly promoted China's two-way opening up policy. Thanks to these comprehensive efforts, each project yielded fruitful outcomes. It promoted the development of inclusive finance by addressing the difficulties and high costs of financing for micro and small-sized enterprises and the private enterprises. The banking sector continuously increased its efforts to tackle financial markets disorders, to promote structural deleveraging and to reinforce risk prevention and resolution in priority areas. It also vigorously advanced FinTech innovation and improved service quality and efficiency. As at the end of 2018, the total assets of China's banking industry grew by 6.3% from the prior year-end to RMB268.2 trillion, while total liabilities increased by 5.9% to RMB246.6 trillion. Commercial banking institutions recorded an aggregate profit of RMB1.83 trillion. Outstanding non-performing loans (NPLs) stood at RMB2.03 trillion, with an NPL ratio of 1.83%.

## Income Statement Analysis

In 2018, the Group achieved a profit for the year of RMB192.435 billion, an increase of RMB7.449 billion or 4.03% compared with the prior year. It realised a profit attributable to equity holders of the Bank of RMB180.086 billion, an increase of RMB7.679 billion or 4.45% compared with the prior year. Return on average total assets (ROA) was 0.94%, and return on average equity (ROE) was 12.06%.

The principal components and changes of the Group's consolidated income statement are set out below:

Unit: RMB million, except percentages

| Items | 2018 | 2017 | Change | Change (%) |
|---|---|---|---|---|
| Net interest income | **359,706** | 338,389 | 21,317 | 6.30% |
| Non-interest income | **144,100** | 145,372 | (1,272) | (0.87%) |
| Including: net fee and commission income | **87,208** | 88,691 | (1,483) | (1.67%) |
| Operating income | **503,806** | 483,761 | 20,045 | 4.14% |
| Operating expenses | **(176,979)** | (173,859) | (3,120) | 1.79% |
| Impairment losses on assets | **(99,294)** | (88,161) | (11,133) | 12.63% |
| Operating profit | **227,533** | 221,741 | 5,792 | 2.61% |
| Profit before income tax | **229,643** | 222,903 | 6,740 | 3.02% |
| Income tax expense | **(37,208)** | (37,917) | 709 | (1.87%) |
| Profit for the year | **192,435** | 184,986 | 7,449 | 4.03% |
| Profit attributable to equity holders of the Bank | **180,086** | 172,407 | 7,679 | 4.45% |

A detailed review of the Group's principal items in each quarter of 2018 is summarised in the following table:

Unit: RMB million

| | For the three-month period ended | | | |
|---|---|---|---|---|
| Items | 31 December 2018 | 30 September 2018 | 30 June 2018 | 31 March 2018 |
| Operating income | 127,947 | 124,377 | 125,396 | 126,086 |
| Profit attributable to equity holders of the Bank | 26,812 | 44,186 | 60,087 | 49,001 |
| Net cash flow from operating activities | 91,303 | 211,986 | (23,613) | 382,682 |

## *Net Interest Income and Net Interest Margin*

In 2018, the Group achieved a net interest income of RMB359.706 billion, an increase of RMB21.317 billion or 6.30% compared with the prior year. The average balances[1] and average interest rates of the major interest-earning assets and interest-bearing liabilities of the Group, as well as the impact on interest income/expense of variances in the volume factor and the interest factor[2], are summarised in the following table:

Unit: RMB million, except percentages

| | 2018 | | | 2017 | | | Analysis of changes in interest income/expense | | |
|---|---|---|---|---|---|---|---|---|---|
| Items | Average balance | Interest income/ expense | Average interest rate | Average balance | Interest income/ expense | Average interest rate | Volume factor | Interest rate factor | Total |
| **Interest-earning assets** | | | | | | | | | |
| Loans | **11,107,013** | **469,098** | **4.22%** | 10,601,544 | 414,695 | 3.91% | 19,764 | 34,639 | 54,403 |
| Investments | **4,497,016** | **144,326** | **3.21%** | 4,290,094 | 132,167 | 3.08% | 6,373 | 5,786 | 12,159 |
| Balances with central banks and due from and placements with banks and other financial institutions | **3,282,457** | **74,476** | **2.27%** | 3,468,502 | 75,754 | 2.18% | (4,056) | 2,778 | (1,278) |
| **Total** | **18,886,486** | **687,900** | **3.64%** | 18,360,140 | 622,616 | 3.39% | 22,081 | 43,203 | 65,284 |
| **Interest-bearing liabilities** | | | | | | | | | |
| Due to customers | **14,072,677** | **229,998** | **1.63%** | 13,488,149 | 204,794 | 1.52% | 8,885 | 16,319 | 25,204 |
| Due to and placements from banks and other financial institutions | **3,042,646** | **76,478** | **2.51%** | 2,934,718 | 63,634 | 2.17% | 2,342 | 10,502 | 12,844 |
| Bonds issued | **580,755** | **21,718** | **3.74%** | 432,587 | 15,799 | 3.65% | 5,408 | 511 | 5,919 |
| **Total** | **17,696,078** | **328,194** | **1.85%** | 16,855,454 | 284,227 | 1.69% | 16,635 | 27,332 | 43,967 |
| **Net interest income** | | **359,706** | | | 338,389 | | 5,446 | 15,871 | 21,317 |
| **Net interest margin** | | | **1.90%** | | | 1.84% | | | 6 Bps |

Notes:

1 In 2018, investments include debt securities at fair value through other comprehensive income, debt securities at amortised cost, investment trusts and asset management plans, etc. In the data of the previous reporting period, investments included available-for-sale debt securities, held-to-maturity debt securities, debt securities classified as loans and receivables, trading debt securities, debt securities designated at fair value through profit and loss, investment trusts and asset management plans.

2 Balances with central banks and due from and placements with banks and other financial institutions include mandatory reserves, surplus reserves, other placements with central banks and due from and placements with banks and other financial institutions.

3 Due to and placements from banks and other financial institutions include due to and placements from banks and other financial institutions, due to central banks and other funds.

4 For the calculation of net interest margin, the interest of financial assets and financial liabilities at fair value through profit or loss under IFRS 9 is not recognised. Pursuant to the principle of matching returns with assets, personal credit card instalment is now categorised under non-interest-earning assets.

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1 Average balances are average daily balances derived from the Group's management accounts (unaudited).

2 The impact on interest income/expense of variances in the volume factor is calculated based on the changes in average balances of interest-earning assets and interest-bearing liabilities during the reporting period. The impact on interest income/expense of variances in interest rate factor is calculated based on the changes in the average interest rates of interest-earning assets and interest-bearing liabilities during the reporting period. The impact relating to the combined changes in both the volume factor and the interest rate factor has been classified as changes in interest rate factor.

The average balances and average interest rates of domestic loans and due to customers, classified by business type, are summarised in the following table:

Unit: RMB million, except percentages

| Items | 2018 | | 2017 | | Change | |
|---|---|---|---|---|---|---|
| | **Average balance** | **Average interest rate** | Average balance | Average interest rate | Average balance | Average interest rate |
| **Domestic RMB businesses** | | | | | | |
| **Loans** | | | | | | |
| Corporate loans | **4,754,363** | **4.47%** | 4,500,691 | 4.40% | 253,672 | 7 Bps |
| Personal loans | **3,448,247** | **4.67%** | 3,250,322 | 4.25% | 197,925 | 42 Bps |
| Trade bills | **165,797** | **4.47%** | 181,448 | 4.09% | (15,651) | 38 Bps |
| **Total** | **8,368,407** | **4.55%** | 7,932,461 | 4.33% | 435,946 | 22 Bps |
| Including: | | | | | | |
| Medium- and long-term loans | **5,828,652** | **4.77%** | 5,446,487 | 4.53% | 382,165 | 24 Bps |
| Short-term loans within 1 year and others | **2,539,755** | **4.06%** | 2,485,974 | 3.90% | 53,781 | 16 Bps |
| **Due to customers** | | | | | | |
| Corporate demand deposits | **3,097,595** | **0.65%** | 2,914,497 | 0.62% | 183,098 | 3 Bps |
| Corporate time deposits | **2,254,006** | **2.77%** | 2,206,175 | 2.73% | 47,831 | 4 Bps |
| Personal demand deposits | **1,948,774** | **0.66%** | 1,798,631 | 0.62% | 150,143 | 4 Bps |
| Personal time deposits | **2,575,439** | **2.68%** | 2,629,645 | 2.71% | (54,206) | (3) Bps |
| Other | **528,899** | **4.19%** | 374,257 | 3.77% | 154,642 | 42 Bps |
| **Total** | **10,404,713** | **1.79%** | 9,923,205 | 1.76% | 481,508 | 3 Bps |
| **Domestic foreign currency businesses** | | | | | Unit: USD million, except percentages | |
| **Loans** | **49,355** | **3.08%** | 51,280 | 2.47% | (1,925) | 61 Bps |
| **Due to customers** | | | | | | |
| Corporate demand deposits | **45,065** | **0.62%** | 43,947 | 0.22% | 1,118 | 40 Bps |
| Corporate time deposits | **29,668** | **1.89%** | 22,550 | 1.33% | 7,118 | 56 Bps |
| Personal demand deposits | **27,047** | **0.05%** | 27,714 | 0.05% | (667) | – |
| Personal time deposits | **19,125** | **0.63%** | 20,445 | 0.59% | (1,320) | 4 Bps |
| Other | **2,002** | **2.30%** | 2,308 | 2.17% | (306) | 13 Bps |
| **Total** | **122,907** | **0.83%** | 116,964 | 0.49% | 5,943 | 34 Bps |

Notes:

1 "Due to customers — Other" includes structured deposits.

2 According to the principle of matching income and related assets, personal credit card instalment is classified as non-interest-earning asset.

In 2018, the Group's net interest margin was 1.90%, an increase of 6 basis points compared with the prior year. Specifically, the net interest margin of its domestic RMB businesses was 2.11%, an increase of 7 basis points compared with the prior year. Major factors that affected the Group's net interest margin include:

First, the Bank continuously improved its asset and liability structure. In response to changes in the external environment, the Bank adjusted its existing assets and liabilities and efficiently allocated their increments, resulting in continuous improvement to its asset and liability structure. In 2018, the proportion of the average balance of domestic RMB medium- and long-term loans to domestic RMB loans business increased by 0.99 percentage point compared with the prior year. The proportion of the average balance of the domestic RMB demand deposits to domestic RMB deposit business increased by 1.00 percentage point compared with the prior year.

Second, the PBOC reduced reserve requirement ratios. In 2018, the PBOC cut the reserve requirement ratios four times, and the applicable RMB deposit reserve requirement ratio of the Bank decreased compared with the prior year-end.

### *Non-interest Income*

In 2018, the Group reported a non-interest income of RMB144.100 billion[3], a decrease of RMB1.272 billion or 0.87% compared with the prior year. Non-interest income represented 28.60% of operating income.

#### Net Fee and Commission Income

The Group earned a net fee and commission income of RMB87.208 billion, a decrease of RMB1.483 billion or 1.67% compared with the prior year. Net fee and commission income represented 17.31% of operating income. This was primarily attributable to a decrease in income from the wealth management business and agency insurance business of domestic commercial banks compared to the prior year. At the same time, the Bank followed the trend of fast-paced development of consumer finance, and realised a rapid increase in income from credit card business and others.

Unit: RMB million, except percentages

| Items | 2018 | 2017 | Change | Change (%) |
|---|---|---|---|---|
| **Group** | | | | |
| Agency commissions | **20,212** | 23,310 | (3,098) | (13.29%) |
| Bank card fees | **29,943** | 25,798 | 4,145 | 16.07% |
| Settlement and clearing fees | **13,670** | 12,323 | 1,347 | 10.93% |
| Credit commitment fees | **13,181** | 15,090 | (1,909) | (12.65%) |
| Consultancy and advisory fees | **3,534** | 5,615 | (2,081) | (37.06%) |
| Spread income from foreign exchange business | **7,740** | 8,083 | (343) | (4.24%) |
| Custodian and other fiduciary service fees | **3,597** | 3,527 | 70 | 1.98% |
| Other | **8,120** | 7,054 | 1,066 | 15.11% |
| **Fee and commission income** | **99,997** | 100,800 | (803) | (0.80%) |
| **Fee and commission expense** | **(12,789)** | (12,109) | (680) | 5.62% |
| **Net fee and commission income** | **87,208** | 88,691 | (1,483) | (1.67%) |
| **Domestic** | | | | |
| Agency commissions | **14,353** | 17,074 | (2,721) | (15.94%) |
| Bank card fees | **26,364** | 22,442 | 3,922 | 17.48% |
| Settlement and clearing fees | **12,082** | 10,773 | 1,309 | 12.15% |
| Credit commitment fees | **6,760** | 7,513 | (753) | (10.02%) |
| Consultancy and advisory fees | **3,331** | 5,415 | (2,084) | (38.49%) |
| Spread income from foreign exchange business | **7,088** | 7,096 | (8) | (0.11%) |
| Custodian and other fiduciary service fees | **3,474** | 3,421 | 53 | 1.55% |
| Other | **4,384** | 4,194 | 190 | 4.53% |
| **Fee and commission income** | **77,836** | 77,928 | (92) | (0.12%) |
| **Fee and commission expense** | **(7,642)** | (7,200) | (442) | 6.14% |
| **Net fee and commission income** | **70,194** | 70,728 | (534) | (0.76%) |

[3] In 2018 non-interest income includes the interest of financial assets and financial liabilities at fair value through profit or loss under IFRS 9.

### Other Non-interest Income

The Group realised other non-interest income of RMB56.892 billion, an increase of RMB0.211 billion or 0.37% compared with the prior year. This was primarily attributable to the following factors: (1) An increase in net gains from interest rate products compared with the prior year following re-classification adjustments under IFRS 9. (2) The recognised gains on the investment disposal for selling Chiyu Banking Corporation Limited in 2017. (3) A decrease in net gains from foreign exchange derivatives trading compared with the prior year, affected by market price fluctuations. Please refer to Notes V.3, 4, 5 to the Consolidated Financial Statements for detailed information.

## *Operating Expenses*

The Bank continued to operate its business in a prudent manner. It optimised and adjusted its cost structure, enhanced investment in technological innovation, seized the market opportunities arising from the Olympic Winter Games Beijing 2022, allocated greater resources to key areas, business frontlines and overseas institutions, and made greater efforts to support mobile finance, RMB internationalisation and the construction of smart service outlets. In 2018, the Group recorded operating expenses of RMB176.979 billion, an increase of RMB3.120 billion or 1.79% compared with the prior year. The Group's cost to income ratio (calculated in accordance with domestic regulations) was 28.09%, a decrease of 0.25 percentage point compared with the prior year. Please refer to Notes V.6, 7 to the Consolidated Financial Statements for detailed information.

Unit: RMB million, except percentages

| Items | 2018 | 2017 | Change | Change (%) |
|---|---|---|---|---|
| Staff costs | **85,391** | 82,061 | 3,330 | 4.06% |
| General operating and administrative expenses | **42,768** | 41,235 | 1,533 | 3.72% |
| Depreciation and amortisation | **13,451** | 13,667 | (216) | (1.58%) |
| Taxes and surcharges | **4,744** | 4,676 | 68 | 1.45% |
| Insurance benefits and claims | **17,008** | 22,607 | (5,599) | (24.77%) |
| Other | **13,617** | 9,613 | 4,004 | 41.65% |
| **Total** | **176,979** | 173,859 | 3,120 | 1.79% |

## *Impairment Losses on Assets*

The Bank continued to improve its comprehensive risk management system and adopted a proactive and forward-looking risk management approach, thus ensuring a basically stable credit asset quality. It stringently implemented a prudent risk provisioning policy and maintained an adequate capacity for risk mitigation. In 2018, the Group's impairment losses on loans and advances totalled RMB107.905 billion, an increase of RMB23.880 billion or 28.42% compared with the prior year. Please refer to the section "Risk Management — Credit Risk Management" and Notes V.9, 17, VI.3 to the Consolidated Financial Statements for more information on loan quality and allowance for loan impairment losses.

## *Income Tax Expense*

In 2018, the Group incurred income tax of RMB37.208 billion, a decrease of RMB0.709 billion or 1.87% compared with the prior year. The Group's effective tax rate was 16.20%, representing a decrease of 0.81 percentage point compared with the prior year. This was primarily attributable to an increase in bond investment, for which the Bank enjoyed a preferential rate of corporate income tax. Please refer to Note V.10 to the Consolidated Financial Statements for the reconciliation of statutory income tax expense to effective income tax expense.

## Financial Position Analysis

As at the end of 2018, the Group's total assets amounted to RMB21,267.275 billion, an increase of RMB1,799.851 billion or 9.25% compared with the prior year-end. The Group's total liabilities amounted to RMB19,541.878 billion, an increase of RMB1,651.133 billion or 9.23% compared with the prior year-end.

The principal components of the Group's consolidated statement of financial position are set out below:

Unit: RMB million, except percentages

| | As at 31 December 2018 | | As at 31 December 2017 | |
|---|---|---|---|---|
| Items | Amount | % of total | Amount | % of total |
| **Assets** | | | | |
| Loans and advances to customers, net | **11,515,764** | **54.15%** | 10,644,304 | 54.68% |
| Investments | **5,054,551** | **23.77%** | 4,554,722 | 23.40% |
| Balances with central banks | **2,331,053** | **10.96%** | 2,227,614 | 11.44% |
| Due from and placements with banks and other financial institutions | **1,405,534** | **6.61%** | 1,060,456 | 5.45% |
| Other assets | **960,373** | **4.51%** | 980,328 | 5.03% |
| **Total assets** | **21,267,275** | **100.00%** | 19,467,424 | 100.00% |
| **Liabilities** | | | | |
| Due to customers | **14,883,596** | **76.16%** | 13,657,924 | 76.34% |
| Due to and placements from banks and other financial institutions and due to central banks | **3,250,997** | **16.64%** | 2,961,151 | 16.55% |
| Other borrowed funds | **814,888** | **4.17%** | 529,756 | 2.96% |
| Other liabilities | **592,397** | **3.03%** | 741,914 | 4.15% |
| **Total liabilities** | **19,541,878** | **100.00%** | 17,890,745 | 100.00% |

Note: "Other borrowed funds" includes bonds issued and other borrowings.

### *Loans and Advances to Customers*

In line with China's macroeconomic policies and the financial demands of the real economy, the Bank rationally allocated credit extension and expanded its lending scale at a stable and moderate pace. It continuously improved its credit structure, and proactively supported the credit needs of key regions and industries. The Bank strictly controlled credit facilities granted to industries characterised by high pollution, high energy consumption and overcapacity. It also continued to implement a differentiated residential mortgage loan policy and steadily expanded its personal loan business. As at the end of 2018, the Group's loans and advances to customers amounted to RMB11,819.272 billion, an increase of RMB922.714 billion or 8.47% compared with the prior year-end. Specifically, the Group's RMB loans and advances to customers totalled RMB9,095.562 billion, an increase of RMB770.549 billion or 9.26% compared with the prior year-end, while its foreign currency loans amounted to USD396.857 billion, an increase of USD3.305 billion or 0.84% compared with the prior year-end. Please refer to Note V.17 to the Consolidated Financial Statements for detailed information.

The Bank further improved its risk management, paid close attention to changes in the macroeconomic situation, strengthened risk identification and management in key areas and made greater efforts to dispose of non-performing assets (NPAs), thus maintaining a basically stable asset quality. As at the end of 2018, the balance of the Group's allowance for loan impairment losses amounted to RMB303.781 billion, an increase of RMB51.527 billion compared with the prior year-end. The balance of the Group's restructured loans amounted to RMB10.002 billion, an increase of RMB1.865 billion compared with the prior year-end.

Unit: RMB million, except percentages

| | As at 31 December 2018 | | As at 31 December 2017 | |
|---|---|---|---|---|
| Items | Amount | % of total | Amount | % of total |
| Corporate Loans | **7,347,598** | **62.17%** | 6,972,701 | 63.99% |
| Personal Loans | **4,440,085** | **37.57%** | 3,923,857 | 36.01% |
| Accrued Interest | **31,589** | **0.26%** | N.A. | N.A. |
| **Total Loans** | **11,819,272** | **100.00%** | 10,896,558 | 100.00% |

### *Investments*

The Bank tracked financial market dynamics, increased its bond investments and continuously improved its investment structure.

As at the end of 2018, the Group held investments of RMB5,054.551 billion, an increase of RMB499.829 billion or 10.97% compared with the prior year-end. Specifically, the Group's RMB investments totalled RMB3,978.636 billion, an increase of RMB447.963 billion or 12.69% compared with the prior year-end, while foreign currency investments totalled USD156.766 billion, an increase of USD45 million or 0.03% compared with the prior year-end.

The classification of the Group's financial investment portfolio is shown below:

Unit: RMB million, except percentages

| | As at 31 December 2018 | | As at 31 December 2017 | |
|---|---|---|---|---|
| Items | Amount | % of total | Amount | % of total |
| Financial assets at fair value through profit or loss | **370,491** | **7.33%** | 193,611 | 4.25% |
| Financial assets at fair value through other comprehensive income | **1,879,759** | **37.19%** | N.A. | N.A. |
| Financial assets at amortised cost | **2,804,301** | **55.48%** | N.A. | N.A. |
| Investment securities available for sale | **N.A.** | **N.A.** | 1,857,222 | 40.78% |
| Debt securities held to maturity | **N.A.** | **N.A.** | 2,089,864 | 45.88% |
| Financial investments classified as loans and receivables | **N.A.** | **N.A.** | 414,025 | 9.09% |
| **Total** | **5,054,551** | **100.00%** | 4,554,722 | 100.00% |

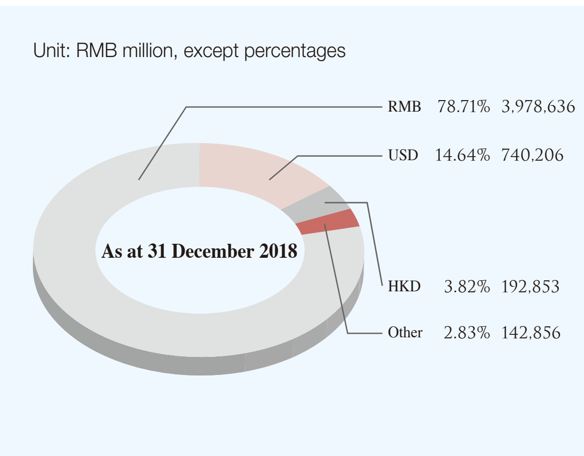
### Investments by Issuer Type

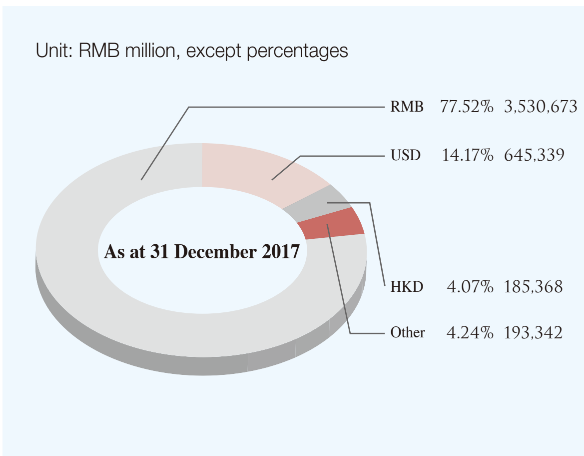
Unit: RMB million, except percentages

| Items | As at 31 December 2018 | | As at 31 December 2017 | |
|---|---|---|---|---|
| | Amount | % of total | Amount | % of total |
| **Debt securities** | | | | |
| **Issuers in the Chinese mainland** | | | | |
| Government | **2,654,129** | **52.51%** | 2,403,536 | 52.77% |
| Public sectors and quasi-governments | **84,364** | **1.67%** | 64,016 | 1.40% |
| Policy banks | **484,992** | **9.59%** | 519,245 | 11.40% |
| Financial institutions | **496,675** | **9.83%** | 322,827 | 7.09% |
| Corporates | **191,690** | **3.79%** | 188,811 | 4.15% |
| China Orient Asset Management Corporation | **153,627** | **3.04%** | 158,806 | 3.49% |
| **Subtotal** | **4,065,477** | **80.43%** | 3,657,241 | 80.30% |
| **Issuers in Hong Kong, Macao, Taiwan and other countries and regions** | | | | |
| Governments | **366,602** | **7.25%** | 377,196 | 8.28% |
| Public sectors and quasi-governments | **108,739** | **2.15%** | 92,211 | 2.02% |
| Financial institutions | **174,719** | **3.46%** | 191,321 | 4.20% |
| Corporates | **153,056** | **3.03%** | 115,164 | 2.53% |
| **Subtotal** | **803,116** | **15.89%** | 775,892 | 17.03% |
| **Equity instruments and others** | **185,958** | **3.68%** | 121,589 | 2.67% |
| **Total** | **5,054,551** | **100.00%** | 4,554,722 | 100.00% |

Note: "Equity instruments and others" includes accrued interest.

### Investments by Currency



**Top Ten Financial Bonds by Value Held by the Group**

Unit: RMB million, except percentages

| Bond Name | Par Value | Annual Rate | Maturity Date | Impairment Allowance |
|---|---|---|---|---|
| Bond issued by policy banks in 2016 | 15,363 | 2.65% | 2019-10-20 | – |
| Bond issued by policy banks in 2018 | 14,012 | 4.98% | 2025-01-12 | – |
| Bond issued by policy banks in 2017 | 12,662 | 3.88% | 2020-04-19 | – |
| Bond issued by policy banks in 2017 | 11,100 | 4.39% | 2027-09-08 | – |
| Bond issued by policy banks in 2017 | 9,729 | 3.54% | 2020-01-06 | – |
| Bond issued by policy banks in 2018 | 9,320 | 4.73% | 2025-04-02 | – |
| Bond issued by policy banks in 2017 | 9,309 | 3.98% | 2020-04-19 | – |
| Bond issued by policy banks in 2018 | 8,962 | 4.99% | 2023-01-24 | – |
| Bond issued by policy banks in 2014 | 8,566 | 5.44% | 2019-04-08 | – |
| Bond issued by policy banks in 2017 | 7,845 | 4.02% | 2022-04-17 | – |

Note: Financial bonds refer to debt securities issued by financial institutions in the bond market, including the bonds issued by policy banks, other banks and non-bank financial institutions, but excluding restructured bonds and PBOC bills.

## *Due to Customers*

The Bank aligned itself with the trend towards interest rate liberalisation, accelerated product and service innovation and thus enhanced its financial services offering. As a result, its liability business grew steadily. It further improved salary payment agency, payment collection and other basic services, optimised the functions of personal certificates of deposit (CDs), steadily expanded its administrative institution customer base and solidified its relationships with basic settlement and cash management customers. As a result, it achieved steady growth in customer deposits.

As at the end of 2018, the Group's due to customers amounted to RMB14,883.596 billion, an increase of RMB1,225.672 billion or 8.97% compared with the prior year-end. Specifically, the Group's RMB due to customers totalled RMB11,256.454 billion, an increase of RMB1,020.125 billion or 9.97% compared with the prior year-end, while its foreign currency due to customers stood at USD528.491 billion, an increase of USD4.847 billion or 0.93%.

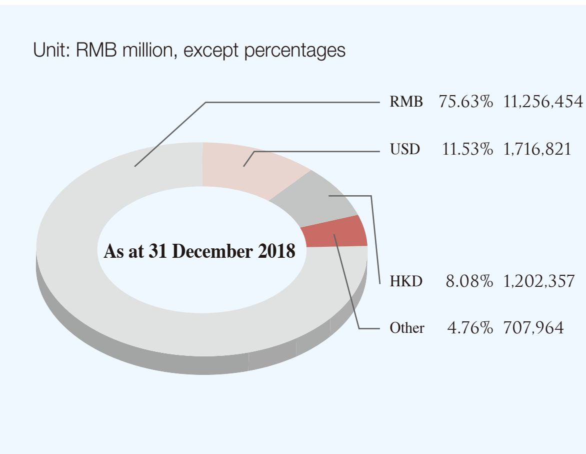
The principal components of due to customers of the Group and its domestic institutions are set out below:

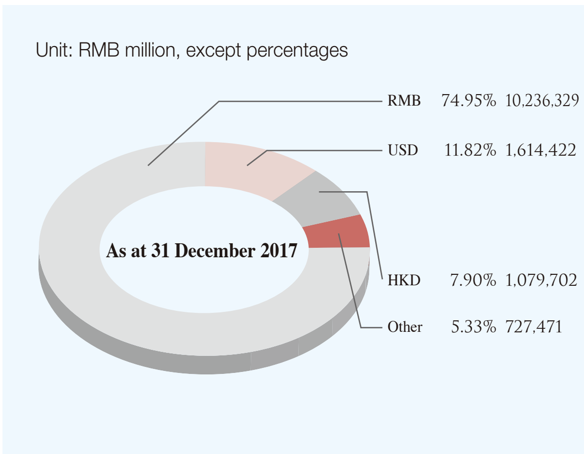
Unit: RMB million, except percentages

| Items | As at 31 December 2018 | | As at 31 December 2017 | |
|---|---|---|---|---|
| | Amount | % of total | Amount | % of total |
| **Group** | | | | |
| **Corporate deposits** | | | | |
| Demand deposits | **4,178,962** | **28.08%** | 3,955,206 | 28.96% |
| Time deposits | **3,507,071** | **23.56%** | 3,213,375 | 23.53% |
| Structured deposits | **246,380** | **1.66%** | 215,193 | 1.58% |
| **Subtotal** | **7,932,413** | **53.30%** | 7,383,774 | 54.07% |
| **Personal deposits** | | | | |
| Demand deposits | **2,935,661** | **19.72%** | 2,613,409 | 19.13% |
| Time deposits | **3,148,265** | **21.15%** | 3,060,245 | 22.41% |
| Structured deposits | **338,544** | **2.28%** | 157,574 | 1.15% |
| **Subtotal** | **6,422,470** | **43.15%** | 5,831,228 | 42.69% |
| **Certificates of deposit** | **287,808** | **1.93%** | 377,460 | 2.76% |
| **Others** | **240,905** | **1.62%** | 65,462 | 0.48% |
| **Total** | **14,883,596** | **100.00%** | 13,657,924 | 100.00% |
| **Domestic** | | | | |
| **Corporate deposits** | | | | |
| Demand deposits | **3,588,353** | **30.19%** | 3,368,630 | 31.05% |
| Time deposits | **2,520,127** | **21.20%** | 2,361,406 | 21.76% |
| Structured deposits | **229,768** | **1.93%** | 201,916 | 1.86% |
| **Subtotal** | **6,338,248** | **53.32%** | 5,931,952 | 54.67% |
| **Personal deposits** | | | | |
| Demand deposits | **2,312,488** | **19.45%** | 1,992,092 | 18.36% |
| Time deposits | **2,685,026** | **22.59%** | 2,714,253 | 25.01% |
| Structured deposits | **331,064** | **2.79%** | 155,076 | 1.43% |
| **Subtotal** | **5,328,578** | **44.83%** | 4,861,421 | 44.80% |
| **Others** | **219,969** | **1.85%** | 58,045 | 0.53% |
| **Total** | **11,886,795** | **100.00%** | 10,851,418 | 100.00% |

Note: "Others" are inclusive of accrued interest in 2018.

## Due to Customers by Currency



### *Equity*

As at the end of 2018, the Group's total equity stood at RMB1,725.397 billion, an increase of RMB148.718 billion or 9.43% compared with the prior year-end. This was primarily attributable to the following factors: (1) Starting on 1 January 2018, the Group applied IFRS 9, which caused total equity to decrease RMB35.417 billion. (2) In 2018, it realised a profit for the year of RMB192.435 billion, among which the profit attributable to equity holders of the Bank was RMB180.086 billion. (3) As per the 2017 profit distribution plan approved at the 2017 Annual General Meeting, the Bank paid a cash dividend of RMB51.812 billion. (4) The Bank paid a dividend on its preference shares of RMB6.791 billion. Please refer to the "Consolidated Statement of Changes in Equity" in the Consolidated Financial Statements for detailed information.

## Off-balance Sheet Items

Off-balance sheet items include derivative financial instruments, contingent liabilities and commitments, etc.

The Group entered into various derivative financial instruments relating to foreign currency exchange rates, interest rates, equity, credit, precious metals and other commodities for trading, hedging, asset and liability management and on behalf of customers. Please refer to Note V.16 to the Consolidated Financial Statements for the contractual/notional amounts and fair values of derivative instruments.

Contingent liabilities and commitments include legal proceedings and arbitrations, assets pledged, collateral accepted, capital commitments, operating leases, Treasury bonds redemption commitments, credit commitments and underwriting obligations, etc. Please refer to Note V.41 to the Consolidated Financial Statements for more detailed information on contingent liabilities and commitments.

## Cash Flow Analysis

As at the end of 2018, the balance of the Group's cash and cash equivalents was RMB1,688.600 billion, an increase of RMB729.848 billion compared with the prior year-end.

In 2018, net cash flow from operating activities was an inflow of RMB662.358 billion, an increase of RMB256.222 billion compared with the prior year. This was mainly attributable to the increase in the net increase of balances with customer deposits and due to banks and other financial institutions and a net decrease of balances with due to central banks, whereas it was a net increase in the prior year.

Net cash flow from investing activities was an outflow of RMB182.493 billion, a decrease of RMB322.597 billion compared with the prior year. This was mainly attributable to the increase of proceeds from financial investment compared with the prior year.

Net cash flow from financing activities was an inflow of RMB229.337 billion, an increase of RMB163.753 billion compared with the prior year. This was mainly attributable to the increase of proceeds from issuance of bonds compared with the prior year.

## Segment Reporting by Geography

The Group conducts its business activities in the Chinese mainland, Hong Kong, Macao, Taiwan and other countries and regions. A geographical analysis of profit contribution and the related assets and liabilities is set forth in the following table:

Unit: RMB million

| | Chinese mainland | | Hong Kong, Macao and Taiwan | | Other countries and regions | | Elimination | | Group | |
|---|---|---|---|---|---|---|---|---|---|---|
| Items | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 | 2018 | 2017 |
| Net interest income | **303,945** | 284,930 | **38,831** | 37,745 | **16,930** | 15,714 | **–** | – | **359,706** | 338,389 |
| Non-interest income | **89,099** | 85,774 | **51,143** | 57,401 | **6,647** | 6,856 | **(2,789)** | (4,659) | **144,100** | 145,372 |
| Including: net fee and commission income | **70,194** | 70,728 | **14,083** | 15,073 | **4,367** | 4,336 | **(1,436)** | (1,446) | **87,208** | 88,691 |
| Operating expenses | **(131,958)** | (126,351) | **(39,956)** | (43,172) | **(6,967)** | (6,265) | **1,902** | 1,929 | **(176,979)** | (173,859) |
| Impairment losses on assets | **(98,872)** | (85,286) | **(1,114)** | (1,722) | **692** | (1,153) | **–** | – | **(99,294)** | (88,161) |
| Profit before income tax | **162,224** | 159,067 | **51,004** | 51,414 | **17,302** | 15,152 | **(887)** | (2,730) | **229,643** | 222,903 |
| **As at the year-end** | | | | | | | | | | |
| Assets | **16,932,306** | 15,503,536 | **4,197,031** | 3,534,044 | **2,009,680** | 1,911,087 | **(1,871,742)** | (1,481,243) | **21,267,275** | 19,467,424 |
| Liabilities | **15,625,811** | 14,285,717 | **3,844,519** | 3,235,718 | **1,943,129** | 1,850,392 | **(1,871,581)** | (1,481,082) | **19,541,878** | 17,890,745 |

As at the end of 2018, total assets[4] of the Bank's Chinese mainland segment amounted to RMB16,932.306 billion, an increase of RMB1,428.770 billion or 9.22% compared with the prior year-end, representing 73.18% of the Group's total assets. In 2018, this segment recorded a profit before income tax of RMB162.224 billion, an increase of RMB3.157 billion or 1.98% compared with the prior year, representing 70.37% of the Group's profit before income tax for the year.

Total assets of the Hong Kong, Macao and Taiwan segment amounted to RMB4,197.031 billion, an increase of RMB662.987 billion or 18.76% compared with the prior year-end, representing 18.14% of the Group's total assets. In 2018, this segment recorded a profit before income tax of RMB51.004 billion, a decrease of RMB0.410 billion or 0.80% compared with the prior year, representing 22.12% of the Group's profit before income tax for the year.

Total assets of the other countries and regions segment amounted to RMB2,009.680 billion, an increase of RMB98.593 billion or 5.16% compared with the prior year-end, representing 8.68% of the Group's total assets. In 2018, this segment recorded a profit before income tax of RMB17.302 billion, an increase of RMB2.150 billion or 14.19% compared with the prior year, representing 7.51% of the Group's profit before income tax for the year.

Please refer to the section "Business Review" for more detailed information on the Group's business segments.

## Critical Accounting Estimates and Judgements

The Bank makes accounting estimates and judgements that affect the reported amounts of assets and liabilities of the next financial year. These estimates and judgements are continually evaluated and are based on historical experience, expectations of future events that are believed to be reasonable under the circumstances and other factors. The management believes that the accounting estimates and judgements have properly reflected the Bank's operating environment. Please refer to Notes II and III to the Consolidated Financial Statements for more detailed information related to the Bank's accounting policies and accounting estimates.

4 The figures for segment assets, segment profit before income tax and their respective proportions are prior to intragroup elimination.

## Fair Value Measurement

**Movement of Financial Instruments Measured at Fair Value**

Unit: RMB million

| Items | As at 31 December 2018 | As at 31 December 2017 | Change in the year | Impact on profit for the year |
|---|---|---|---|---|
| Financial assets at fair value through profit or loss | | | | |
| Debt securities | **273,447** | 168,399 | 105,048 | (164) |
| Loans | **N.A.** | 5,493 | N.A. | |
| Equity instruments | **47,061** | 8,029 | 39,032 | |
| Fund investments and other | **49,983** | 11,690 | 38,293 | |
| Loans and advances to customers | **227,643** | N.A. | N.A. | 739 |
| Financial assets at fair value through other comprehensive income | | | | |
| Debt securities | **1,862,232** | N.A. | N.A. | 46 |
| Equity instruments and other | **17,527** | N.A. | N.A. | |
| Investment securities available for sale | | | | |
| Debt securities | **N.A.** | 1,769,758 | N.A. | N.A. |
| Equity instruments | **N.A.** | 38,694 | N.A. | |
| Fund investments and other | **N.A.** | 48,770 | N.A. | |
| Derivative financial assets | **124,126** | 94,912 | 29,214 | 6 |
| Derivative financial liabilities | **(99,254)** | (111,095) | 11,841 | |
| Due to and placements from banks and other financial institutions at fair value | **(876)** | (1,246) | 370 | (6) |
| Due to customers at fair value | **(24,141)** | (372,767) | 348,626 | – |
| Bonds issued at fair value | **(20,517)** | (1,907) | (18,610) | (41) |
| Short position in debt securities | **(14,327)** | (17,219) | 2,892 | (35) |

The Bank has put in place a sound internal control mechanism for fair value measurement. In accordance with the *Guidelines on Market Risk Management in Commercial Banks*, the *Regulatory Guidelines on Valuation of Financial Instruments in Commercial Banks*, CAS and IFRS, with reference to the New Basel Capital Accord, and drawing on the best practices of leading international banks regarding valuations, the Bank formulated the *Valuation Policy of Financial Instrument Fair Values of Bank of China Limited* to standardise the fair value measurement of financial instruments and enable timely and accurate financial information disclosure. Please refer to Note VI.6 to the Consolidated Financial Statements for more detailed information related to the fair value measurement.

## Other Financial Information

There are no differences in the equity and profit for the year of the Group prepared in accordance with IFRS to those prepared in accordance with CAS. Please refer to Supplementary Information I to the Consolidated Financial Statements for detailed information.