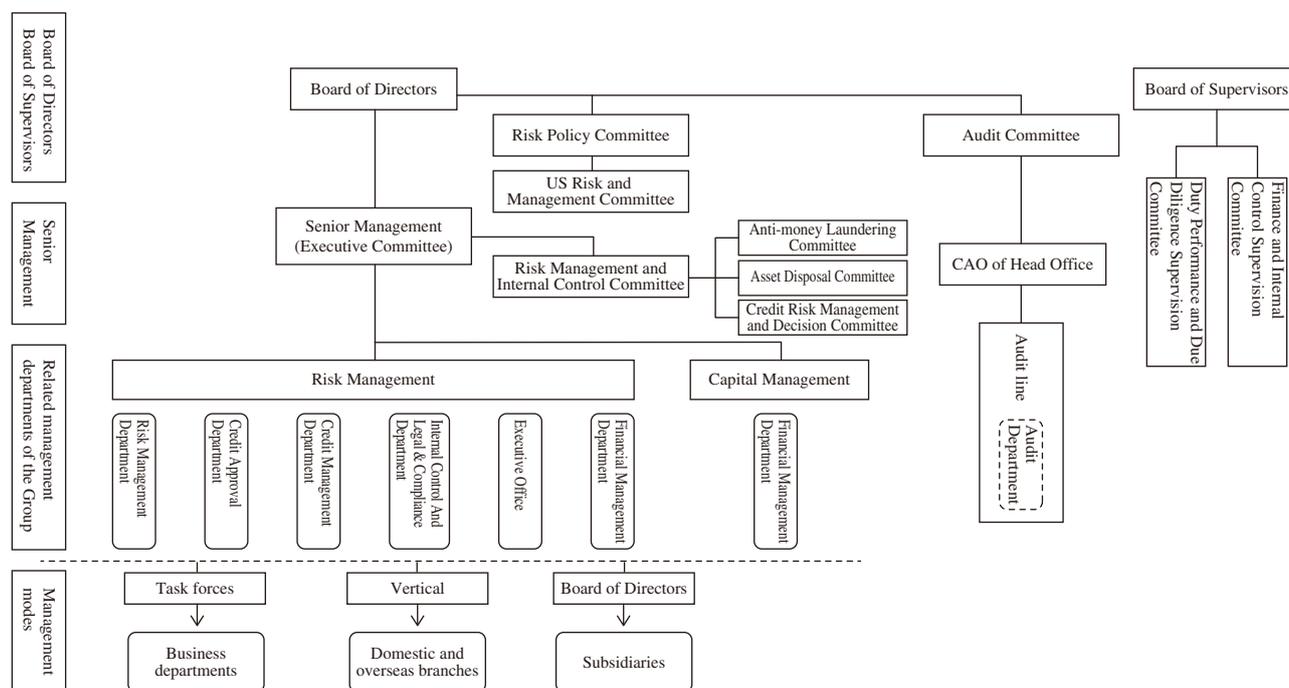


Management Discussion and Analysis — Risk Management

The Bank continued to improve its risk management system in line with the Group’s strategies. To ensure compliant operations, it implemented local and overseas regulatory requirements and carried out in-depth rectification and accountability for regulatory initiatives such as the governance of market disruptions, on-site efficiency examination of risk management and internal control, and quarterly regulatory notifications. The Bank also improved its risk management system, promoted the building of the “Three Lines of Defence” for risk management, updated the Group’s risk appetite, and continuously made its comprehensive risk management reporting more forward-looking and predictable. It comprehensively improved the effectiveness of the

Group’s consolidated risk management and control. The Bank continued to develop and refine its risk measurement model, and completed the development and launch of online models for inclusive finance. It pushed forward the development of advanced capital management approaches, deepened the application of advanced approaches, and actively implemented an asset-light strategy. The Bank conducted intelligent risk control in an all-round manner, built up the Group’s comprehensive risk management portal system, and promoted the digital transformation of risk management. It strengthened its risk data governance, as well as improving its risk data standards and single risk reporting system.

The risk management framework of the Bank is set forth below:



Credit Risk Management

Closely tracking changes in macroeconomic and financial conditions, the Bank advanced development, made structural adjustments, controlled and mitigated credit risks, and consolidated fundamentals of risk management during the reporting period. It pushed forward the optimisation of its credit structure, further improved its

credit risk management policies, strengthened credit asset quality management and took a proactive and forward-looking stance on risk management.

The Bank continuously adjusted and optimised its credit structure. With the aim of advancing strategic implementation and balancing risk, capital and return, it improved the management plans for its

Management Discussion and Analysis — Risk Management

credit portfolios. In line with national industrial policies and regional policy orientation, the Bank intensified its support to the real economy, boosted the high-quality development of the manufacturing industry, bolstered the improvement of weak links in infrastructure, and supported the development of private enterprises and inclusive finance, so as to push forward the continuous improvement of its business model. It also enacted guidelines for industrial lending and continued to push forward the building of an industrial policy system so as to optimise its credit structure.

Taking a customer-centric approach, the Bank further strengthened its unified credit granting management and enhanced full-scope centralised credit risk management. It continuously improved its long-acting credit management mechanism and asset quality monitoring system, strengthened the control of customer concentration, and further raised the effectiveness of potential risk identification, control and mitigation. The Bank enhanced the supervision of risk analysis and asset quality control in key regions, as well as strengthening window guidance on all business lines. In addition, it constantly identified, measured and monitored large exposures in line with related management requirements.

In terms of corporate banking, the Bank further strengthened risk identification and control in key fields and proactively reduced and exited credit relationships in such fields. It strictly controlled the outstanding amount and use of loans through limit management, and prevented and mitigated risk from overcapacity industries. It assisted local governments in mitigating implicit debt risk. In addition, the Bank implemented the government's macro-control policies and regulatory measures in the real estate sector so as to strengthen the risk management of real estate loans. In terms of personal banking, the Bank reinforced the management of credit granting approval, improved approval quality, and prevented the risks of excessive credit and cross-infection while supporting the development of its personal credit business. It also strengthened the risk control of key products and regions.

The Bank strengthened country risk management. It performed an annual review of country risk ratings and implemented limit management and control of country risk exposures. It collected statistics on, assessed, monitored, analysed and reported its exposures on a regular basis. The Bank regularly published country risk analysis reports within the Group and made timely assessments of the impact of material country risk events. In addition, the Bank adopted differentiated management of potentially high-risk and sensitive countries and regions. The Bank's net exposure to country risk mainly concentrated on countries and regions that have relatively low or low ratings, and its overall country risk remained at a reasonable level.

The Bank spared no efforts in the collection and mitigation of NPAs, coordinated internal and external collection resources, and continued to adopt the centralised and tiered management of NPA projects. It made breakthroughs in key regions and key projects and improved the quality and efficiency of disposals. The Bank proactively explored the application of "Internet Plus" in NPA collection, and diversified its disposal channels. In addition, it adopted policies based on the actual conditions of individual enterprises and took multiple measures where necessary. It gave full play to the role of creditor committees and enhanced the application of debt-for-equity swaps and restructuring efforts to help enterprises get out of difficulties, with the aim of realising mutual benefit for the Bank and the enterprises, and to support the real economy.

The Bank scientifically measured and managed the quality of credit assets based on the *Guidelines for Loan Credit Risk Classification*, which requires Chinese commercial banks to classify loans into the following five categories: pass, special-mention, substandard, doubtful and loss, among which loans classified as substandard, doubtful and loss are recognised as NPLs. In order to further refine its credit asset risk management, the Bank used a 13-tier risk classification criteria scheme for corporate loans to companies in the Chinese mainland, covering on-

Management Discussion and Analysis — Risk Management

balance sheet and off-balance sheet credit assets. In addition, the Bank strengthened risk classification management of key industries, regions and material risk events, and dynamically adjusted classification results. It strengthened the management of loan terms, managed overdue loans by the name list system and made timely adjustments to risk classification results, so as to truly reflect asset quality. The overseas institutions of the Bank operated in line with the *Guidelines for Loan Credit Risk Classification* or the local applicable rules and requirements on credit risk classification, whichever was stricter.

As at the end of 2019, the Group's NPLs⁵ totalled RMB178.235 billion, an increase of RMB11.294 billion compared with the prior year-end. The NPL ratio was 1.37%, down by 0.05 percentage point

compared with the prior year-end. The Group's allowance for impairment losses on loans and advances was RMB325.923 billion, an increase of RMB22.142 billion compared with the prior year-end. The coverage ratio of allowance for loan impairment losses to NPLs was 182.86%, up by 0.89 percentage point from the prior year-end. The NPLs of the Bank's institutions in the Chinese mainland totalled RMB169.951 billion, an increase of RMB7.173 billion compared with the prior year-end. The NPL ratio of the Bank's institutions in the Chinese mainland was 1.65%, down by 0.11 percentage point compared with the prior year-end. The Group's outstanding special-mention loans stood at RMB289.314 billion, a decrease of RMB53.049 billion compared with the prior year-end, accounting for 2.22% of total loans and advances, down by 0.68 percentage point from the prior year-end.

Five-category Loan Classification

Unit: RMB million, except percentages

| Items | As at 31 December 2019 | | As at 31 December 2018 | |
|-------------------------|------------------------|----------------|------------------------|----------------|
| | Amount | % of total | Amount | % of total |
| Group | | | | |
| Pass | 12,566,640 | 96.41% | 11,278,379 | 95.68% |
| Special-mention | 289,314 | 2.22% | 342,363 | 2.90% |
| Substandard | 77,459 | 0.59% | 49,788 | 0.42% |
| Doubtful | 51,804 | 0.40% | 49,341 | 0.42% |
| Loss | 48,972 | 0.38% | 67,812 | 0.58% |
| Total | 13,034,189 | 100.00% | 11,787,683 | 100.00% |
| NPLs | 178,235 | 1.37% | 166,941 | 1.42% |
| Chinese mainland | | | | |
| Pass | 9,885,045 | 95.95% | 8,818,838 | 95.10% |
| Special-mention | 247,412 | 2.40% | 291,933 | 3.15% |
| Substandard | 72,611 | 0.70% | 48,281 | 0.52% |
| Doubtful | 50,334 | 0.49% | 47,536 | 0.51% |
| Loss | 47,006 | 0.46% | 66,961 | 0.72% |
| Total | 10,302,408 | 100.00% | 9,273,549 | 100.00% |
| NPLs | 169,951 | 1.65% | 162,778 | 1.76% |

⁵ Total loans and advances to customers in "Risk Management — Credit risk management" section are exclusive of accrued interest.

Management Discussion and Analysis — Risk Management

Migration Ratio

| Items | Unit: % | | |
|-----------------|---------|-------|-------|
| | 2019 | 2018 | 2017 |
| Pass | 1.40 | 2.20 | 1.97 |
| Special-mention | 21.45 | 23.70 | 20.37 |
| Substandard | 40.86 | 51.89 | 57.97 |
| Doubtful | 18.76 | 33.57 | 31.98 |

In accordance with IFRS 9, the Bank assesses expected credit losses with forward-looking information and makes relevant allowances. In particular, it makes allowances for assets classified as stage 1 and assets classified as stage 2 and stage 3 according to the expected credit losses over 12 months and the expected credit losses over the entire lifetime of the asset, respectively. As at the end of 2019, the Group's stage 1, stage 2 and stage 3 loans totalled RMB12,514.948 billion, RMB336.902 billion and RMB178.235 billion respectively, accounting for 96.04%, 2.59% and 1.37% of total loans respectively.

As at the end of 2019, the Group's credit-impaired loans totalled RMB178.235 billion, an increase of RMB11.283 billion compared with the prior year-end. The credit-impaired loans to total loans ratio was 1.37%, a decrease of 0.05 percentage point compared with the prior year-end. Credit-impaired loans of the Bank's institutions in the Chinese mainland totalled RMB169.951 billion, an increase of RMB7.173 billion compared with the prior year-end. The credit-impaired loans to total loans ratio of the Bank's institutions in the Chinese mainland was 1.65%, down by 0.11 percentage point compared with the prior year-end. The Bank's operations in Hong Kong, Macao, Taiwan and other countries and regions reported credit-impaired loans of RMB8.284 billion and a credit-impaired loans to total loans ratio of 0.30%, an increase of RMB4.110 billion and an increase of 0.13 percentage point compared with the prior year-end respectively.

Movement of Credit-Impaired Loans

| Items | Unit: RMB million | | |
|--------------------------------------|-------------------|----------|----------|
| | 2019 | 2018 | 2017 |
| Group | | | |
| Balance at the beginning of the year | 166,952 | 157,882 | 145,311 |
| Increase during the year | 94,870 | 83,009 | 71,573 |
| Decrease during the year | (83,587) | (73,939) | (59,002) |
| Balance at the end of the year | 178,235 | 166,952 | 157,882 |
| Chinese mainland | | | |
| Balance at the beginning of the year | 162,778 | 154,208 | 141,458 |
| Increase during the year | 88,658 | 80,680 | 69,854 |
| Decrease during the year | (81,485) | (72,110) | (57,104) |
| Balance at the end of the year | 169,951 | 162,778 | 154,208 |

Management Discussion and Analysis — Risk Management

Loans and Credit-Impaired Loans by Currency

Unit: RMB million

| Items | As at 31 December 2019 | | As at 31 December 2018 | | As at 31 December 2017 | |
|-------------------------|------------------------|----------------|------------------------|----------------|------------------------|----------------|
| | Total loans | Impaired loans | Total loans | Impaired loans | Total loans | Impaired loans |
| Group | | | | | | |
| RMB | 10,125,083 | 150,532 | 9,074,501 | 151,313 | 8,325,013 | 145,605 |
| Foreign currency | 2,909,106 | 27,703 | 2,713,182 | 15,639 | 2,571,545 | 12,277 |
| Total | 13,034,189 | 178,235 | 11,787,683 | 166,952 | 10,896,558 | 157,882 |
| Chinese mainland | | | | | | |
| RMB | 10,041,692 | 149,808 | 8,991,494 | 151,292 | 8,243,556 | 145,540 |
| Foreign currency | 260,716 | 20,143 | 282,055 | 11,486 | 339,629 | 8,668 |
| Total | 10,302,408 | 169,951 | 9,273,549 | 162,778 | 8,583,185 | 154,208 |

The Bank makes adequate and timely allowances for loan impairment losses based on the expected credit loss (ECL) module in accordance with the principles of authenticity and forward-lookingness. Please refer to Notes II.4 and VI.3 to the Consolidated Financial Statements for the accounting policy in relation to allowances for impairment losses.

In 2019, the Group's impairment losses on loans and advances stood at RMB98.771 billion, a decrease of RMB9.134 billion compared with the prior year. The credit cost was 0.80%, down 0.15 percentage point compared with the prior year. Specifically, the Bank's institutions in the Chinese mainland registered impairment losses on loans and advances of RMB97.456 billion, a decrease of RMB9.394 billion compared with the prior year. The credit cost of the Bank's institutions in the Chinese mainland was 1.00%, down 0.20 percentage point compared with the prior year.

The Bank continued to focus on controlling borrower concentration risk and was in full compliance with regulatory requirements on borrower concentration.

Unit: %

| Indicators | Regulatory Standard | As at 31 December 2019 | As at 31 December 2018 | As at 31 December 2017 |
|---|---------------------|------------------------|------------------------|------------------------|
| Loan concentration ratio of the largest single borrower | ≤10 | 3.2 | 3.6 | 3.8 |
| Loan concentration ratio of the ten largest borrowers | ≤50 | 14.5 | 15.3 | 17.4 |

Notes:

- 1 Loan concentration ratio of the largest single borrower = total outstanding loans to the largest single borrower ÷ net regulatory capital.
- 2 Loan concentration ratio of the ten largest borrowers = total outstanding loans to the top ten borrowers ÷ net regulatory capital.

Please refer to Notes V.17 and VI.3 to the Consolidated Financial Statements for detailed information regarding loan classification, stage determination, credit-impaired loans and allowance for loan impairment losses.

Management Discussion and Analysis — Risk Management

The following table shows the top ten individual borrowers as at the end of 2019.

Unit: RMB million, except percentages

| | Industry | Related Parties or not | Outstanding loans | % of total loans |
|------------|--|------------------------|-------------------|------------------|
| Customer A | Manufacturing | No | 69,762 | 0.54% |
| Customer B | Transportation, storage and postal services | No | 49,085 | 0.38% |
| Customer C | Transportation, storage and postal services | No | 36,645 | 0.28% |
| Customer D | Commerce and services | No | 31,923 | 0.24% |
| Customer E | Transportation, storage and postal services | No | 31,691 | 0.24% |
| Customer F | Real estate | No | 22,000 | 0.17% |
| Customer G | Transportation, storage and postal services | No | 20,711 | 0.16% |
| Customer H | Commerce and services | No | 20,185 | 0.15% |
| Customer I | Production and supply of electricity, heating, gas and water | No | 20,031 | 0.15% |
| Customer J | Transportation, storage and postal services | No | 17,398 | 0.13% |

Market Risk Management

In response to changes in the market environment, the Bank continued to refine its market risk management system in order to effectively control its market risk.

The Bank enhanced the effectiveness of its market risk management by improving its market risk appetite transmission mechanism, enriching the Group's market risk management framework and optimising the Group's market risk limit management model. It strengthened risk judgment and analysis, intensified and coordinated derivative risk management and control, and conducted more proactive and forward-looking risk management. The Bank also optimised the flexibility of its counterparty credit risk control mechanism, and enhanced risk warning and mitigation capacity. It continuously promoted the building of the market risk system and improved the accuracy of risk measurement. Please refer to Note VI.4 to the Consolidated Financial Statements for detailed information regarding market risk.

The Bank closely tracked market and policy changes, reviewed and revised relevant policies and regulations for the Group's securities and asset management businesses, strongly supported new businesses in the development of the direct financing market and pushed forward the establishment of new mechanisms. It continued to conduct default risk inspection of credit bonds, strengthened the early warning of risk events, and improved work quality and effectiveness. The Bank also further strengthened the Group's coordinated management of the risks arising in the securities and asset management businesses.

In terms of exchange rate risk management, the Bank sought to achieve currency matching between fund source and application and managed exchange rate risk through timely settlement and hedging, thus effectively controlling its foreign exchange exposure.

Management Discussion and Analysis — Risk Management

Management of Interest Rate Risk in the Banking Book

Based on the principles of “matching, comprehensiveness and prudence”, the Bank strengthened the management of interest rate risk in the banking book (IRRBB). The Bank’s IRRBB management strategy is to control risks within an acceptable level by considering factors such as the Bank’s risk appetite and risk profile, as well as macro-economic and market conditions, so as to achieve a reasonable balance between risk and return and thus maximise shareholder value.

The Bank assessed the interest rate risk in the banking book mainly through the analysis of interest rate repricing gaps, and made timely adjustments to the structure of its assets and liabilities or implemented risk hedging based on changes in the market situation. Assuming that the yield curves of all currencies were to shift up or down by 25 basis points in parallel, the Group’s sensitivity analysis of net interest income on all currencies is as follows⁶:

Unit: RMB million

| Items | As at 31 December 2019 | | | | As at 31 December 2018 | | | |
|-------------|------------------------|----------------|--------------|-------------|------------------------|-------|-------|-------|
| | RMB | USD | HKD | Other | RMB | USD | HKD | Other |
| Up 25 bps | (3,962) | (1,077) | 534 | (29) | (3,520) | (670) | 328 | (274) |
| Down 25 bps | 3,962 | 1,077 | (534) | 29 | 3,520 | 670 | (328) | 274 |

Liquidity Risk Management

The Bank endeavoured to develop a sound liquidity risk management system with the aim of effectively identifying, measuring, monitoring and controlling liquidity risk at the institution and Group level, including that of branches, subsidiaries and business lines, thus ensuring that liquidity demand is met in a timely manner and at a reasonable cost.

Adhering to an appropriate balance of safety, liquidity and profitability, and following regulatory requirements, the Bank improved its liquidity risk management in a forward-looking and scientific manner. It enhanced liquidity risk management at the institution and Group level, including that of branches, subsidiaries and business lines. It formulated sound liquidity risk management policies and contingency plans, periodically re-examined liquidity risk limits, upgraded the early warning system for liquidity risk, and strengthened the management of high-quality liquid assets, in order to strike an appropriate balance between risk and return. In addition, the Bank regularly improved its liquidity stress-testing scheme and performed stress tests on a quarterly basis. The test results indicated that the Bank had adequate payment ability to cope with distressed scenarios.

⁶ This analysis is based on the approach prescribed by the CBIRC, which includes interest-sensitive off-balance sheet positions.

Management Discussion and Analysis — Risk Management

As at the end of 2019, the Group's liquidity risk indicator met regulatory requirements. The Group's liquidity ratio is shown in the table below (in accordance with the relevant provisions of regulatory authorities in the Chinese mainland):

Unit: %

| Ratio | | Regulatory standard | As at 31 December 2019 | As at 31 December 2018 | As at 31 December 2017 |
|-----------------|------------------|---------------------|------------------------|------------------------|------------------------|
| Liquidity ratio | RMB | ≥25 | 54.6 | 58.7 | 47.1 |
| | Foreign currency | ≥25 | 60.4 | 54.8 | 56.9 |

Liquidity gap analysis is one of the methods used by the Bank to assess liquidity risk. Liquidity gap results are periodically calculated, monitored and used for sensitivity analysis and stress testing. As at the end of 2019, the Bank's liquidity gap was as follows (please refer to Note VI.5 to the Consolidated Financial Statements):

Unit: RMB million

| Items | As at 31 December 2019 | As at 31 December 2018 |
|-------------------------|------------------------|------------------------|
| Overdue/undated | 2,077,009 | 2,071,988 |
| On demand | (8,035,944) | (7,669,897) |
| Up to 1 month | (1,010,716) | (651,459) |
| 1–3 months (inclusive) | (348,821) | (591,520) |
| 3–12 months (inclusive) | 269,460 | (54,305) |
| 1–5 years (inclusive) | 2,721,272 | 3,238,374 |
| Over 5 years | 6,304,436 | 5,382,216 |
| Total | 1,976,696 | 1,725,397 |

Note: Liquidity gap = assets that mature in a certain period – liabilities that mature in the same period.

Reputational Risk Management

The Bank earnestly implemented regulatory requirements on reputational risk management, continued to enhance its reputational risk management system and mechanism and strengthened the consolidated management of reputational risk, so as to enhance its overall reputational risk management capabilities. It attached great importance to the investigation and pre-warning of potential reputational risk factors, strengthened public opinion monitoring, continued to conduct reputational risk identification, assessment and reporting, established a coordination mechanism between reputational risk management departments and liable departments, and dealt appropriately with reputational risk events, thus

effectively protecting its brand reputation. In addition, the Bank continued to roll out reputational risk training so as to enhance employees' awareness and foster a culture of reputational risk management.

Internal Control and Operational Risk Management

Internal Control

The Board of Directors, senior management and their special committees earnestly performed their duties regarding internal control and supervision, emphasised early risk warning and prevention, and thus improved the Group's level of compliance operation.

Management Discussion and Analysis — Risk Management

The Bank continued to adopt the “Three Lines of Defence” mechanism for internal control. The first line of defence consists of business departments and all banking outlets. They are the owners of, and are accountable for, local risks and controls. They undertake self-directed risk control and management functions in the course of their business operations, including formulating and implementing policies, conducting business examination, reporting control deficiencies and organising rectifications.

The second line of defence consists of the internal control and risk management departments of the Bank’s institutions at all levels. They are responsible for the overall planning, implementing, examining and assessing of risk management and internal control, as well as for identifying, measuring, monitoring and controlling risks. They led the first line of defence to enhance its use of the Group’s operational risk monitoring and analysis platform, and are responsible for staff non-compliance sanctions and management accountability. Through regular monitoring of material risks, the Bank identified and mitigated risks in a timely manner and promoted the optimisation of business processes and systems.

The third line of defence rests in the audit department of the Bank. The audit department is responsible for performing internal audit of the Bank’s internal control and risk management in respect of its adequacy and effectiveness. The Bank continued to push forward the reform of its human resource management system for the audit line, and further intensified the vertical management of its audit function. It enhanced audit team building, pushed forward the implementation of its three-year plan for IT applications in audit, reinforced the use of IT-based audit approaches, continuously conducted audit circulatory monitoring, and established an audit working mechanism for identifying and revealing material risks. Taking an issue-oriented approach, the Bank focused on comprehensive

audits of its institutions and special audits of its businesses. It strengthened audits and inspections of high-risk institutions and businesses, as well as those fields prioritised by the Group and of special concern to regulators. The audit department concentrated its attention on systemic, trending, emerging and important issues, so as to practically perform its internal audit function. It continued to apply a normalised supervision mechanism for the rectification of audit findings, and urged the timely and effective rectification of issues, so as to continually improve the Bank’s internal governance and control mechanism.

Rigorously implementing the requirements of the CBIRC, the Bank organised bank-wide risk inspections to actively identify and mitigate risks, raised employees’ compliance awareness and fostered an internal control compliance culture by carrying out such campaigns as “consolidating the results achieved in cracking down on irregularities and boosting compliant operations”, together with case-based warning education and illegal fund-raising risk investigation and rectification. In addition, the Bank introduced internal control and compliance management evaluation so as to enhance routine management and control at all levels.

The Bank continued to implement the *Basic Standard for Enterprise Internal Control* and its supporting guidelines, adhering to the primary goal of ensuring the effectiveness of its internal control over financial reporting and the accuracy of its financial information. It also constantly improved non-financial internal control. The Bank earnestly implemented the *Guidelines for Internal Control of Commercial Banks* by following the basic principles of “complete coverage, checks and balances, prudence and correspondence”, so as to promote internal control governance and an organisational structure characterised by a reasonable delegation of work, well-defined responsibilities and clear reporting lines.

Management Discussion and Analysis — Risk Management

The Bank established and implemented a systematic financial accounting policy framework in accordance with relevant accounting laws and regulations. As such, its accounting basis was solidified and the level of standardisation and refinement of its financial accounting management was further improved. The Bank has endeavoured to implement a sound accounting standards and establish a long-term accounting management mechanism since 2019. It continuously strengthened the quality management of its accounting information, so as to ensure internal control effectiveness over financial reporting. The financial statements of the Bank were prepared in accordance with the applicable accounting standards and related accounting regulations, and the financial position, operational performance and cash flows of the Bank were fairly presented in all material respects.

The Bank paid close attention to fraud risk prevention and control, proactively identifying, assessing, controlling and mitigating risks. In 2019, the Bank succeeded in preventing 218 external cases involving RMB140 million.

Operational Risk Management

The Bank continuously improved its operational risk management system. It promoted the application of operational risk management tools, including Risk and Control Assessment (RACA), Key Risk Indicators (KRI) and Loss Data Collection (LDC), etc., to identify, assess and monitor operational risks, thus continuously improving its risk management measures. The Bank enhanced its system support capability by optimising its operational risk management information system. It strengthened its business continuity management system, optimised its operating mechanism to

enhance operational sustainability, carried out disaster recovery drills and improved the Group's capacity for continuous business operation.

Compliance Management

The Bank continuously improved its compliance risk governance mechanism and management process to ensure the stable development and sustainable operation of the Group. It strengthened its anti-money-laundering (AML) and sanctions compliance policies, optimised AML resource allocation, deepened AML efforts and strengthened sanctions compliance monitoring and management. It intensified system and model building and improved system functionality. It endeavoured to build a proactive, forward-looking and robust management framework for overseas compliance through a compliance risk assessment programme. It improved the AML and sanctions compliance training management mechanism and conducted various forms of compliance training, so as to enhance all employees' compliance awareness and abilities.

The Bank enhanced the management of its connected transactions and internal transactions, revised management regulation and improved its management mechanism. It stepped up efforts in the management of connected parties and consolidated the foundation of its connected transaction management. It strengthened the routine monitoring and examination of connected transactions and strictly controlled their risks. In addition, it launched an internal transaction management system and continuously implemented internal transaction monitoring and reporting, thereby improving the quality and efficiency of its internal transaction management.

Management Discussion and Analysis — Risk Management

Capital Management

Adhering to the philosophy of high-quality development and centring on the objective of value creation, the Bank continued to improve its capital management system, moved more rapidly to replenish capital through external financing channels, and ramped up innovation in capital instruments. Through these efforts, the Bank established adequate capital levels and strong risk resilience, and further improved its capital use efficiency and value creation capabilities.

The Bank improved its internal refined management and raised awareness of value creation. By enhancing its capital budget and assessment mechanism, the Bank realised differentiated management and continuously upgraded its remuneration allocation system, which is linked to value creation. Giving full play to the guiding role of capital, the Bank pushed forward the adjustment of its on- and off-balance sheet asset structure, actively developed capital-light businesses and reasonably controlled the risk weighting of assets. In addition, the Bank stepped up efforts in system building, launched a capital management data platform, and thus cemented foundations for refined management. Meanwhile, the Bank accelerated external capital replenishment and enriched the variety of its capital instruments. During 2019, the Bank successfully issued RMB100.0 billion of preference shares, RMB40.0 billion of undated capital bonds and RMB70.0 billion of tier 2 capital bonds. The RMB40.0 billion of undated capital bonds were the first capital bonds in the Chinese banking industry to be classified as additional tier 1 capital instruments.

As at the end of 2019, the Group's capital adequacy ratio reached 15.59%, an increase of 0.62 percentage point from the end of 2018, reflecting the further consolidation of its capital base. The Bank will tap into its potential and continue to strengthen its capital management, promoting the high-quality development of its various businesses.

Capital Adequacy Ratios

As at the end of 2019, the capital adequacy ratios calculated in accordance with the *Capital Rules for Commercial Banks (Provisional)* are listed below:

Unit: RMB million, except percentages

| Items | Group | | Bank | |
|---|------------------|---------------|------------------|---------------|
| | As at 31 | As at 31 | As at 31 | As at 31 |
| | December 2019 | December 2018 | December 2019 | December 2018 |
| Net common equity tier 1 capital | 1,596,378 | 1,465,769 | 1,346,623 | 1,251,056 |
| Net tier 1 capital | 1,806,435 | 1,575,293 | 1,546,517 | 1,350,770 |
| Net capital | 2,201,278 | 1,922,350 | 1,927,188 | 1,683,893 |
| Common equity tier 1 capital adequacy ratio | 11.30% | 11.41% | 10.99% | 11.08% |
| Tier 1 capital adequacy ratio | 12.79% | 12.27% | 12.62% | 11.96% |
| Capital adequacy ratio | 15.59% | 14.97% | 15.72% | 14.92% |

Please refer to Note VI.7 to the Consolidated Financial Statements for detailed information.

Leverage Ratio

As at the end of 2019, the leverage ratio calculated in accordance with the *Administrative Measures for the Leverage Ratio of Commercial Banks (Revised)* and the *Capital Rules for Commercial Banks (Provisional)* is listed below:

Unit: RMB million, except percentages

| Items | As at 31 December 2019 | As at 31 December 2018 |
|---|------------------------|------------------------|
| Net tier 1 capital | 1,806,435 | 1,575,293 |
| Adjusted on- and off-balance sheet assets | 24,303,201 | 22,700,133 |
| Leverage ratio | 7.43% | 6.94% |

Please refer to Supplementary Information II.5 to the Consolidated Financial Statements for detailed information.