REPORT FROM THE BOARD OF DIRECTORS

CCB ANNUAL REPORT 2004

9 Report from the Board of Directors

9.1 Daily responsibilities of the Board of Directors

On 15 September 2004, the first meeting of the First Session of China Construction Bank Corporation's Board of Directors was held in Beijing. All of the 10 eligible directors attended the meeting and a quorum was met in accordance with *the PRC Company Law* and *the Articles of Association of China Construction Bank Corporation*. During the meeting, the following proposals were reviewed and passed:

the Proposal on the Election of the Chairman and Vice-Chairman for China Construction Bank Corporation;

the Proposal on the Appointment of the President for China Construction Bank Corporation;

the Proposal on the Appointments of Vice Presidents, the Chief Compliance Officer and Assistant Presidents for China Construction Bank Corporation;

the Detailed Implementation Procedures for the Strategy and Nomination Committee under the Board of Directors of China Construction Bank Corporation;

the Detailed Implementation Procedures for the Audit Committee under the Board of Directors of China Construction Bank Corporation;

the Detailed Implementation Procedures for the Risk Management Committee under the Board of Directors of China Construction Bank Corporation;

the Detailed Implementation Procedures for the Compensation and Evaluation Committee under the Board of Directors of China Construction Bank Corporation;

the Detailed Implementation Procedures for the Related Party Transactions Committee under the Board of Directors of China Construction Bank Corporation;

the Proposal on the Authorisation for the Chairman to Sign "the Separation Agreement of China Construction Bank"; and

the Proposal on Matters Relating to the Business Licences of the Overseas Branches.

On 29 November 2004, the second meeting of the First Session of China Construction Bank Corporation's Board of Directors was held in Beijing. All of the 10 eligible directors attended the meeting and a quorum was met in accordance with *the PRC Company Law* and *the Articles of Association of China Construction Bank Corporation*. During the meeting, the following proposals were reviewed and passed:

the Proposal on the Examination of Amendments to "the Articles of Association of China Construction Bank Corporation";

the Proposal on the Examination of Amendments to "the Rules and Procedures for the Board of Directors of China Construction Bank Corporation";

the Proposal on the Examination of Amendments to "the Detailed Implementation Procedures for the Strategy and Nomination Committee under the Board of Directors of China Construction Bank Corporation";

the Proposal on the Examination of Amendments to "the Detailed Implementation Procedures for Audit Committee under the Board of Directors of China Construction Bank Corporation";

the Proposal on the Examination of Amendments to "the Detailed Implementation Procedures for the Risk Management Committee under the Board of Directors of China Construction Bank Corporation";

the Proposal on the Examination of Amendments to "the Detailed Implementation Procedures for the Compensation and Evaluation Committee under the Board of Directors of China Construction Bank Corporation";

the Proposal on the Examination of Amendments to "the Detailed Implementation Procedures for the Related Party Transactions Committee under the Board of Directors of China Construction Bank Corporation";

the Detailed Guidelines on the President of China Construction Bank Corporation's roles and responsibilities;

the Proposal on the Examination of "the Implementation Procedures for the Management of Related Party Transactions of China Construction Bank Corporation (Draft)";

the Information Disclosure Guidelines for China Construction Bank Corporation;

the Proposal on the Examination of "the Implementation Procedures for the System of Independent Directors of China Construction Bank Corporation (Draft)";

the Detailed Guidelines on the Secretary to the Board of Directors of China Construction Bank Corporation's roles and responsibilities;

the Proposal on the Examination of Allowances for Independent Directors and "the Service Contracts of Independent Directors of China Construction Bank Corporation";

the Proposal on the Nomination of Directors and Independent Directors of China Construction Bank Corporation;

the Proposal on the Appointment of Secretary to the Board of Directors of China Construction Bank Corporation;

the Proposal on the Election of Members for the Strategy and Nomination Committee under the Board of Directors of China Construction Bank Corporation;

the Proposal on the Election of Members for the Audit Committee under the Board of Directors of China Construction Bank Corporation;

the Proposal on the Election of Members for the Risk Management Committee under the Board of Directors of China Construction Bank Corporation;

the Proposal on the Election of Members for the Compensation and Evaluation Committee under the Board of Directors of China Construction Bank Corporation;

the Proposal on the Election of Members for the Related Party Transactions Committee under the Board of Directors of China Construction Bank Corporation;

the Proposal for the Termination of Mr. Zheng Zhijie as Vice President of China Construction Bank Corporation; and

the Proposal to Convene for an Extraordinary Shareholders' General Meeting for China Construction Bank Corporation, etc.

On 27 December 2004, the third meeting of the First Session of China Construction Bank Corporation's Board of Directors was held in Beijing. All of the 13 eligible directors attended the meeting and a quorum was met in accordance with *the PRC Company Law* and *the Articles of Association of China Construction Bank Corporation*. During the meeting, the following proposals were reviewed and passed:

the Proposal on "the Profit Distribution Policy 2004 of China Construction Bank Corporation";

the Strategic Development Plan of China Construction Bank Corporation;

the Plans for Organisational Reform and Establishment of the Organisational Structure of China Construction Bank Corporation; and

the Proposal to Convene for an Extraordinary Shareholders' General Meeting for China Construction Bank Corporation, etc.

On 16 March 2005, the fourth meeting of the First Session of China Construction Bank Corporation's Board of Directors was held in Beijing. 11 of the 13 eligible directors attended the meeting and a quorum was met in accordance with *the PRC Company Law* and *the Articles of Association of China Construction Bank Corporation*. During the meeting, the resignation of Mr. Zhang Enzhao as the Chairman of China Construction Bank Corporation's Board of Directors due to personal reasons was approved.

On 25 March 2005, the fifth meeting of the First Session of China Construction Bank Corporation's Board of Directors was held in Beijing. All of the 12 eligible directors attended the meeting and a quorum was met in accordance with *the PRC Company Law* and *the Articles of Association of China Construction Bank Corporation*. During the meeting, it was agreed that an Extraordinary Shareholders' General Meeting was to be convened on 25 March 2005 and *the Proposal on the Appointment of Mr. Guo Shuqing as a director of China Construction Bank Corporation* and *the Proposal on the Election of external supervisors for China Corporation Bank Corporation* were submitted to the Extraordinary Shareholders' General Meeting for approval.

On 25 March 2005, the sixth meeting of the First Session of China Construction Bank Corporation's Board of Directors was held in Beijing. All of the 13 eligible directors attended the meeting and a quorum was met in accordance with *the PRC Company Law* and *the Articles of Association of China Construction Bank Corporation*. During the meeting, Mr.Guo Shuqing was elected as the Chairman of China Construction Bank Corporation's Board of Directors.

9.2 Financial review

Overview

In 2004, China's GDP growth of 9.5% was a key driver behind the global economy. Market competition intensified as interest rates became more competitive and the financial regulatory environment was strengthened. As a result, we were faced with new challenges in areas, such as operational management and business development. The Bank was cautious with its strategies, but remained eager to enter new markets and committed to strengthening its risk management environment. Overall, in 2004, our businesses experienced healthy and steady growth. Asset quality and operational efficiency were further enhanced resulting in record highs in key performance indicators.

In 2004, the Bank realised a profit before tax of RMB 50,216 million, an increase of RMB 12,743 million, or 34.0%, over the previous year. Of this, the net interest income was RMB 100,296 million, an increase of RMB 11,349 million over the previous year. Provisions for impairment were RMB 8,830 million, an increase of RMB 661 million over the previous year. Key performance indicators improved: return on asset was 1.30% and, excluding the impact of income tax exemption received as part of the shareholding restructuring programme, was 0.88%, an increase of 0.18 percentage points over the previous year; return on net assets was 25.40% and, excluding the impact of income tax exemption received as part of the shareholding restructuring programme, was 17.28%; and cost to income ratio was 39.17%, a decrease of 1.97 percentage points over the previous year.

In 2004, the Bank focused on enhancing asset quality and reducing the level of non-performing assets, thereby enhancing the efforts in rationalising non-performing assets. This resulted in marked improvements in our overall asset quality. At the end of 2004, non-performing loans were RMB 87,345 million and the non-performing loan ratio was 3.92%.

The Bank remained focused on maintaining stable and healthy operations. We successfully controlled the volume and rate of new loans, realising steady growth in total assets and improvements in the structure of our loan portfolio. By the end of 2004, the Bank's total assets amounted to RMB 3,904,785 million, an increase of RMB 351,715 million, or 9.9%, over the previous year. Of this, loans totalled RMB 2,225,585 million, an increase of RMB 229,595 million, or 11.5%, over the previous year. Total liabilities were RMB 3,710,041 million, an increase of RMB 343,201 million, or 10.2%, over the previous year. Of this, deposits from customers reached RMB 3,489,376 million, an increase of RMB 295,258 million, or 9.2%, over the previous year.

Profit and loss account

Key financials

Expressed in millions of RMB

	2004	2003
Net interest income	100,296	88,947
Interest income	145,724	130,305
Interest expense	45,428	41,358
Net non-interest income	10,623	6,754
General and administrative expenses	43,960	39,711
Provisions for impairment	8,830	8,169
Profit before tax	50,216	37,473

Net interest income

In 2004, we realised net interest income of RMB 100,296 million, an increase of RMB 11,349 million, or 12.8%, over the previous year. The increase in net interest income was primarily a result of overall business expansion. In our lending business, personal mortgage loans, infrastructure lending and discounted bills were the main contributors to the increase in new loans. The volume of debt investments also rose significantly as a result of the USD 22.5 billion capital injection from Huijin.

Net non-interest income

In 2004, the Bank realised net non-interest income of RMB 10,623 million, an increase of RMB 3,869 million, or 57.3%, over the previous year. This increase was primarily driven by the rapid growth experienced in our intermediary services. Fee and commission income from intermediary services grew significantly, realising net fee and commission income of RMB 6,368 million, an increase of RMB 1,787 million over the previous year; of which net income from equity investments amounted to RMB 2,408 million, an increase of RMB 1,277 million over the previous year.

General and administrative expenses

In 2004, the Bank's general and administrative expenses amounted to RMB 43,960 million, an increase of RMB 4,249 million, or 10.7%, over the previous year. The cost to income ratio decreased from 41.14% in 2003 to 39.17%. In recent years, the Bank has implemented stringent cost control measures and strengthened cost management. As a result, total costs were effectively controlled and operational efficiency was significantly increased. The increase in general and administrative expenses experienced in 2004 was mainly due to staff related social security expenses, expansion into new markets and product development.

Provisions for impairment

In 2004, the Bank made provisions for impairment of RMB 8,830 million, an increase of RMB 661 million. Of this, provision for loan losses amounted to RMB 5,586 million, a decrease of RMB 2,071 million over the previous year; provision for impairment of investments was RMB 1,902 million, an increase of RMB 1,828 million over the previous year; and provisions for impairment of fixed assets and other assets amounted to RMB 1,342 million, an increase of RMB 904 million over the previous year. The decrease in provision for loan losses was mainly due to the Bank strengthening its efforts in managing the overall loan quality. The Bank's provision for impairment of investments was primarily in respect of debt equity swap investments.

Balance sheet

In 2004, our business maintained healthy growth and the structure of our assets and liabilities was rationalised. Overall, the growth in loans and deposits remained the key driver to the increases in total assets and total liabilities. Within assets, changes in the geographical structure and types of our loan portfolio have resulted in marked improvements in the loan quality. The proportion of investments significantly increased as holding in debt investments grew substantially. Within liabilities, deposits maintained steady growth, while deposits and placements from banks and other financial institutions and other non-interest bearing liabilities also experienced different rates of growth.

Loans

In 2004, loans increased by RMB 229,595 million, an increase of 0.82 percentage points for loans as a proportion of total assets. As part of the rationalisation of our loan portfolio, discounted bills increased by RMB 53,456 million compared with the previous year. Our growth in new business was selectively concentrated in industries, such as manufacturing, transportation, storage and postal services, electricity power, gas and education.

When compared to the previous year, the growth in loans had significantly slowed down. This was mainly driven by our response to the government's macroeconomic and industrial output policies. Therefore, loan underwriting to industries, such as steel, cement, electrolytic aluminium and real estate, correspondingly decreased.

Investments

In 2004, the Bank's investments increased considerably, representing an increase of RMB 303,808 million and an increase of 5.75 percentage points as a proportion of the total assets over the previous year. Our investments are mainly focused on government bonds, bills issued by the PBOC and debt securities issued by policy banks of the PRC.

Deposits with central banks

By the end of 2004, deposits with central banks reached RMB 372,286 million, an increase of RMB 65,948 million over the previous year. This was mainly due to Renminbi denominated deposits, which were used to calculate the statutory deposit reserve, increasing by RMB 418,770 million and the PBOC increasing the statutory deposit reserve requirements ratio from 7% to 7.5% on 25 April 2004, which resulted in an increase of RMB 45,499 million in the statutory deposit reserve funds. Meanwhile, the surplus deposit reserve ratio was raised, which also resulted in an increase in deposits with central banks.

Deposits

During 2004, our deposit business maintained rapid growth. Deposits increased by RMB 295,258 million, or 9.2%, compared to the previous year, of which the increase in corporate deposits amounted to RMB 138,831 million, an increase of 8.2%; the increase in personal deposits amounted to RMB 156,427 million, an increase of 10.5%. This was mainly driven by the strengthened marketing culture and increased efforts to explore new market opportunities. This also resulted in a continuous increase in our market share. In addition, the external environment became increasingly favourable as the overall market expanded.

Shareholders'/ owner's equity

At the end of 2004, shareholders' equity amounted to RMB 194,744 million, an increase of RMB 8,514 million, or 4.6%, over the previous year. The increase in shareholders'/ owner's equity was mainly due to a capital injection of RMB 8,000 million from the three shareholders, State Grid, Shanghai Baosteel and Yangtze Power, in September 2004.

Capital adequacy ratio

At the end of 2004, our capital adequacy and core capital adequacy ratios were 11.29% and 8.57% respectively, in accordance with *the Regulation Governing the Capital Adequacy of Commercial* Banks issued by the CBRC on 23 February 2004. By the end of 2004, the Bank's core capital was RMB 194,240 million, net capital were RMB 255,990 million and total risk-weighted assets amounted to RMB 2,267,467 million. The increases in the Bank's capital adequacy ratios and capital strength were primarily due to the above mentioned capital injection of RMB 8,000 million received from the three shareholders, the issue of long-term subordinated bonds of RMB 40 billion, and our efforts to strengthen our capital management and improve the structure of our assets.

9.3 Business performance and developments

Corporate and institutional banking

We provide a wide range of deposits, loans and intermediary products and services to our corporate and institutional customers, and our traditional competitive advantage in infrastructure lending is represented by our medium and long-term loan products and agency, consultancy and advisory services. In recent years, the rapid development of intermediary services, discounted bills, cash management and custodial services has also become our new service offerings. Corporate and institutional banking is strategically important to the Bank's assets and liabilities and intermediary business, as well as a significant contributor to the Bank financially.

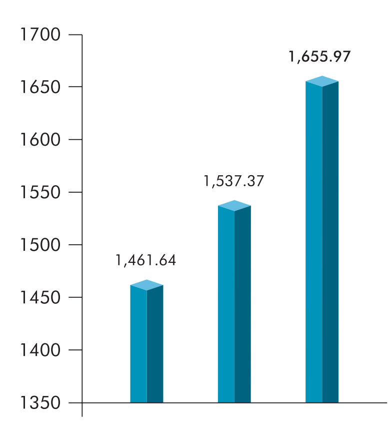
In 2004, we launched our marketing campaign under the theme: "combine intelligence and trust; strive for professionalism and integrity". We selected 24 competitive corporate and institutional banking products in response to market needs with the aim of reinforcing CCB's brand name in corporate banking products. We also strengthened our marketing efforts, targeting our corporate customers, multinational companies, government departments and financial institutions and signed strategic cooperation agreements with 7 target clients. Through the reorganisation of business capabilities and organisational structure, we have successfully realised the synergies between our intermediary services and our corporate loan products, thereby promoting the rapid development of our intermediary services.

Corporate and institutional lending

At the end of 2004, lending to corporate and institutional customers amounted to RMB 1,813,290 million, an increase of RMB 172,060 million over the previous year. Of this, discounted bills increased by RMB 53,456 million, contributing 31.1% of the total increase in lending to corporate and institutional customers.

Corporate and institutional loans (excluding discounted bills)

(In billions of RMB)



At the end of 2004, credit facilities granted to domestic financial institutions amounted to RMB 536,446 million. We continued to maintain a virtually zero non-performing loan ratio for all businesses within these credit facilities. We also became the first domestic bank in the country to be awarded permission to launch standard stock pledged lending business.

During the year, we effectively managed the growth of the Bank's corporate and institutional banking business and improved asset quality by strengthening portfolio management and rationalising the portfolio structure. We continued to focus our efforts on targeting strategic customer groups, and new loans granted to target customer groups in industries, such as the electric power and public road infrastructure, increased during the year as a proportion of total new loans .

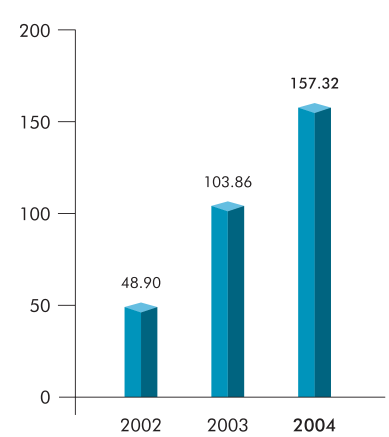
Also during 2004, we launched rediscounted commercial bills, with and without right of recourse, in response to the rapid development of the bill discounting market. The Bank's internally developed comprehensive discount processing system was launched in certain areas, which has further enhanced our service quality and the efficiency of our business delivery.

Corporate and institutional deposits

In 2004, we focused our efforts on enhancing the quality and stability of corporate and institutional deposits, and established new business relationships by

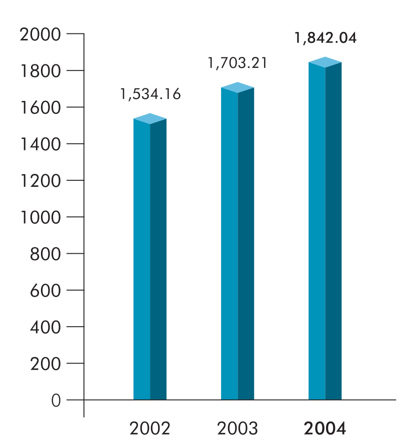
Discounted bills

(In billions of RMB)



Corporate and institutional deposits

(In billions of RMB)



attracting customers to open basic settlement accounts. By the end of 2004, corporate and institutional deposits amounted to RMB 1,842,044 million, an increase of RMB 138,831 million over the previous year, to which corporate and institutional deposits denominated in foreign currencies were a key contributor.

Corporate and institutional intermediary services

In 2004, the Bank focused on the three traditional intermediary services: agency, settlement and guarantee services. We also continued with our efforts to develop high value-added intermediary services, such as financial advisory, construction pricing advisory and cash management services, hence our influence over the intermediary services industry consistently increased. Net fee income from intermediary services for corporate and institutional customers for the year amounted to RMB 2,952 million, an increase of 11.6% over the previous year.

Agency business

Services to government departments: In 2004, we maintained our leading position in providing payment processing services to 61 State's departments and corporate customers, which represented 66.3% of the market share. We continued to be the largest settlement service provider to the lottery funds. The country's total sales in lottery tickets amounted to RMB 38,057 million in 2004, of which we provided settlement agency services for lottery funds amounted to RMB 25,940 million. The Bank gained the funds agency rights for the investment in railway projects totalling RMB 105.6 billion during the year and our market share of the fund settlement services for the Three Gorges Dam Resettlement Programme reached 98%.

Services to banking institutions: In 2004, we continued to provide fund settlement services to China Development Bank and Export-Import Bank of China, with a total transaction volume of RMB 32.6 billion, an increase of 24.4% over the previous year. We continued to be the leading provider of agency business to China Development Bank. We have also established agency service relationships with domestic and foreign operations of 70 domestic banks and developed a number of payment and settlement agency services.

Services to securities institutions: In 2004, we successfully launched an independent custodial system for securities settlement funds based on our VIP Service System and became the first domestic commercial bank to provide this type of service. By the end of 2004, we had started to officially provide independent custodial services for securities settlement funds with three securities companies. We provided such services to 554,000 corporate and personal customers, while pledged customer deposits increased by RMB 3,427 million.

Agency business for insurance companies: We have established extensive business relationships with a variety of large and medium domestic insurance companies, such as PICC Property and Casualty Company Limited, China Life Insurance Company Limited and Ping An Insurance (Group) Company of China, Limited. The total value of premiums collected was RMB 29,168 million and commission income reached RMB 330 million.

Services to other financial institutions: In 2004, the Bank entered into cooperation agreements with a number of automobile finance corporations and business relationships were established with 111 futures brokerage companies. We provided capital trust planning agency services for 43 trust funds on behalf of 20 trust companies, with a total transaction volume of RMB 2,867 million.

Consulting and advisory services

We provide financial advisory services to corporations and government agencies in investment, financing, mergers and acquisitions, asset management and other financial consulting services. In 2004, fee income from financial advisory and consulting services for our corporate customers amounted to RMB 302 million.

Cash management services

In 2004, our market presence in cash management services increased significantly. We participated as the only domestic bank in the EuroFinance Annual Conference on Cash and Treasury Management in Greater China, and were named the best domestic cash management bank in the country in a market survey conducted by EuroFinance Conference Limited. The Bank's main customers are large corporations and, in particular, we provide cash management services to group companies operating in multiple locations. We also help customers in designing cash management plans and provide efficient and low cost working capital management through our service platforms, namely the VIP Service System and electronic banking systems. We have also begun cooperating with foreign banks and have provided cash management services for a number of multinational companies. We have therefore started to build a market reputation for providing high quality cash management services. By the end of 2004, we had built 376 funds settlement networks and generated a total transaction volume of RMB 2,669.5 billion.

Guarantee services

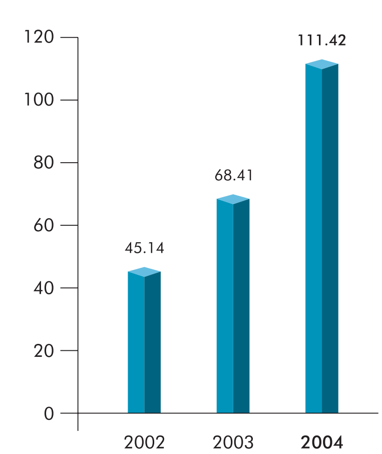
We offer our corporate customers products and services including bank acceptance bills, letters of credit, bid bonds, performance bonds and other forms of bank guarantees. At the end of 2004, the Bank had outstanding guarantees of RMB 233 million, an increase of RMB 53 million, or 29.1%, over the previous year.

Custodial services

We remain focused on expanding our custodial business and marketing our custodial products to leading investment funds and leading qualified foreign institutional investors ("QFII"). In 2004, we provided custodial services to the first domestic principal-guaranteed fund and increased the number of new products, such as money market funds and listed open-ended funds ("LOF"). While we were focused on increasing the number of custodial funds products, we were also driven to expand our QFII customer base. In 2004, we successfully won the QFII custody mandates for Hang Seng Bank and Power Corporation of Canada's QFIIs.

Income from custodial services for mutual funds

(In millions of RMB)



By the end of 2004, we had provided custodial services for 26 securities investment funds with a total net asset value reaching RMB 50,197 million, an increase of 41.8% over the previous year. Assets under custody amounted to RMB 13.3 billion, quadrupling the amount in the previous year. QFII funds under custody totalled USD 250 million, and we maintained our position as the leading Chinese bank in terms of the number of custodial customers and the value of assets under custody. During the year, we realised income of RMB 127 million from custodial services, of which, income from custodial services for mutual funds amounted to RMB 111 million, an increase of 62.9% compared with the previous year.

International business

Structured finance

In 2004, foreign currency on-lending transactions to domestic entities, our key structured finance product, reached transactions USD 205 million. During the year, the Bank signed 11 foreign currency denominated on-lending domestic agreements, with the Ministry of Railways for the import of road maintenance equipment from the United States of America and with China Railway Construction Corporation for the import of equipment from Germany, representing an increase of 99% over the previous year. As a result, 2004 demonstrated rapid growth for the second consecutive year.

In 2004, we furthered our product development in large aircraft structured financing transactions and completed aircraft financing business totalling USD 195 million as well as assisting a number of airline companies, including Air China Limited, in completing their debt restructuring exercises.

Trade finance

By the end of 2004, the Bank's trade finance lending amounted to RMB 5,762 million, an increase of RMB 612 million, or 11.9%, over the previous year. In response to customer needs, the Bank recently launched letter of credit at usance services at our overseas branches and trust receipt loans as part of our non-letter of credit products, for the relating transaction volume was nearly USD 334 million during the year. The transaction volume of our non-recourse letter of credit at usance business during 2004 reached USD 84.36 million, an increase of 261% over the previous year.

In 2004, our new generation trade finance system was successfully launched at the Shanghai, Jiangsu and Beijing branches. This will help to foster changes in our operating model for trade finance settlement by shifting to a more centralised approach.

International settlement

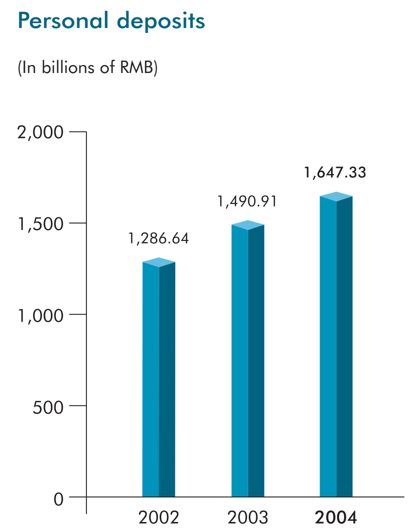
In 2004, our international settlements amounted to USD 107,592 million, an increase of USD 25,695 million, or 31.4%, over the previous year. The transaction volume for letters of credit, collections and remittances amounted to USD 21,434 million, USD 4,392 million and USD 81,766 million respectively.

Overseas banking business

Our global correspondent banking network covers countries, which are China's major trading partners, and includes major international banks. By the end of 2004, the Bank had established correspondent banking relationships at the head office level with 949 banks in 107 countries and regions and signed cooperation agreements with a number of overseas banks on a full scale or individual business type basis. We will continue to be active in expanding cooperation with overseas banks in areas such as money market placements, foreign bank lending, clearance, cross-border trade, cash management, trade finance and international finance. In 2004, the transaction volume of our correspondent clearance banking service for foreign banks amounted to RMB 18,708 million, an increase of 28.1% compared to the previous year.

Personal banking

We provide deposits, loans and a wide range of intermediary products and services including bank cards to our personal banking customers. In 2004, the Bank maintained steady growth in traditional products such as personal deposits and loans, while new businesses, such as personal intermediary services and wealth management, experienced rapid growth. The Bank has significantly enhanced its market competitiveness by rationalising its business structure and improving operational efficiency.



Personal deposits

Personal deposits provide a major source of funding for the Bank. In 2004, our personal deposit business grew steadily. By the end of 2004, the personal deposit balance increased to RMB 1,647,332 million, an increase of RMB 156,427 million, or 10.5%, over the previous year.

In 2004, we continued to improve our personal deposit-taking products by adding new features such as automated and scheduled rollover, to our personal time deposits, as well as improving the flexibility and convenience of our education savings deposits. Therefore, we have been able to further enhance the quality and efficiency of our customer services.

Personal lending

Residential mortgage lending

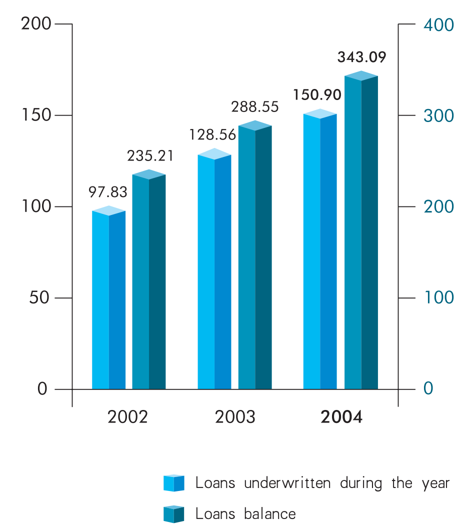
Residential mortgage loans account for the largest share of the Bank's personal lending business. It also has the highest growth potential and therefore brings relatively higher returns to the Bank. In 2004, we underwrote mortgage loans (including individual commercial property mortgage loans) totalling RMB 150,896 million. By the end of 2004, the year-end balance reached RMB 343,089 million, representing an increase of RMB 54,541 million, or 18.9%, over the previous year. In 2004, mortgage lending for the second-hand residential property market developed rapidly and became a new target growth area for the Bank. By the end of 2004, the new increase in mortgage loans for second-hand residential properties compared to the previous year amounted to RMB 10,660 million.

Consumer lending

In 2004, the government began to set up a nationwide personal credit information database. As personal income was on the rise, the growth opportunities for consumer lending business unfolded. We continued to develop new innovative products and, in 2004, we launched personal business assistance loans which supported the development of personal business enterprises. At the same time, the Bank developed a new cooperation model for group car purchases, which provide customers with a one-stop car buying services and enable the Bank, car suppliers and insurance companies to all benefit from the customer base. By the end of 2004, consumer lending amounted to RMB 63,509 million, an increase of RMB 3,614 million over the previous year, realising interest income totalling RMB 3,420 million.

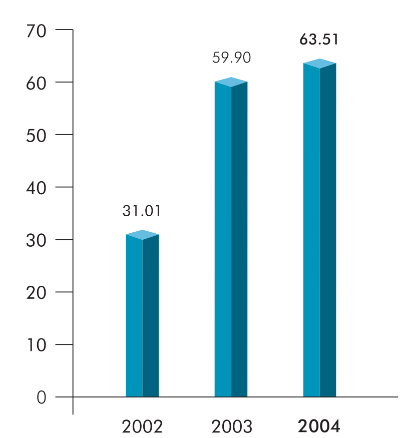
Personal mortgage loans

(In billions of RMB)



Consumer lending

(In billions of RMB)



Personal intermediary services

In 2004, our personal intermediary services achieved breakthrough growth. By the end of the year, income from personal intermediary services increased by 87.1% over the previous year. Income from personal intermediary services as a proportion of the Bank's total income from intermediary services rose by 11.86 percentage points when compared with the previous year. Among these services, bank card, Swift Remit and securities agency services accounted for 88.0% of the total income from personal intermediary services.

Bank card business

In 2004, our bank card business continued to experience rapid growth. The number of credit cards issued amounted to 6.25 million and transacted amounts reached RMB 25,357 million, an increase of 50.7% compared to the previous year. Of these, the number of dual currency credit cards issued reached 1.65 million and transacted amounts were RMB 6,604 million. Debit cards issued amounted to 149 million, an increase of 5.20 million over the previous year, and transacted amounts recorded a historical high of RMB 79,224 million, which nearly doubled the growth recorded in the previous year. In 2004, income from bank card business totalled RMB 2,316 million, an increase of RMB 1,309 million, or 130.0%, compared to the previous year.

In 2004, we strengthened our marketing initiatives for our bank card business and improved the card distribution network, thereby expanding our market capabilities. From September 2004, our Renminbi debit cards and quasi-credit cards could be used in Hong Kong and Macao. Based on statistics from China UnionPay Bank Card Information Exchange Centre, the cross-bank and cross-province entrusted settlement and agency settlement volumes of our bank card business ranked first and second respectively amongst the domestic banking industry.

Entrusted housing fund business

At the end of 2004, our entrusted housing fund deposits totalled RMB 154,131 million, representing a market share of 57.3%. Entrusted provident housing fund deposits amounted to RMB 104,037 million, which represented a market share of 57.9%, therefore maintaining our leading position in the market. By the end of 2004, the balance of the entrusted provident housing fund lending was RMB 119,081 million, an increase of RMB 24,616 million, or 26.1%, over the previous year, representing a market share of 56.9%.

Personal wealth management services

In 2004, our personal wealth management services developed and expanded in all aspects, while the number of VIP customers multiplied and our service offerings further improved. By the end of 2004, our personal VIP customers numbered near 484,000, a growth of 405,000, or 5 times, over the previous year. In 2004, there were 233 personal wealth management service centres, representing an increase of 53 outlets during the year. In addition, we have set up personal wealth management service outlets, including VIP designated service windows, open-plan service counters and private VIP rooms, at our branch outlets. The number of personal wealth management account managers reached over 6,000.

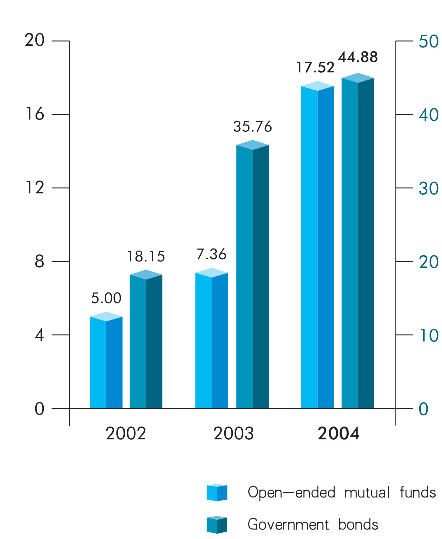
In 2004, we launched 10 VIP services specifically for our personal VIP customers. We developed VIP services through co-operating with 1,500 partners and launched personal wealth management consulting services. In addition, we designed an array of personal wealth management package products and provided professional personal wealth management planning services. Furthermore, we launched a new comprehensive and multi-features product – "Happy Investor" personal wealth management card.

Securities agency services

By the end of 2004, sales from acting as an agent for the trading of government bonds and open-ended mutual funds totalled RMB 62,402 million, which represented an increase of 44.7% over the previous year and marked a historical high. Of this, certificate government bonds sold amounted to RMB 42,554 million, which represented a market share of 17.0%, ranking second in the marketplace. Non-certificate government bonds sold amounted to RMB 2,329 million. Meanwhile, we acted as the agent

Total government bonds and open-ended mutual funds sold

(In billions of RMB)



for 14 open-ended mutual funds where sales volume amounted to RMB 17,519 million. The total agency sales volume and the number of investment funds sold both exceeded the sum of the previous three years.

Personal foreign currency services

We were authorised by the CBRC to conduct transactions in financial derivative products and became the first domestic bank to launch foreign currency structured products and services and "Profit from Exchange" products to our personal foreign currency depositors. In 2004, we issued, in total, 11 "Profit from Exchange" products in different maturities, structures and currencies, including USD, HKD and EUR. In total, foreign currency funds amounted to USD 2,196 million, customers numbered over 200,000 and the total transaction volume in foreign currency exchange amounted to USD 9,437 million.

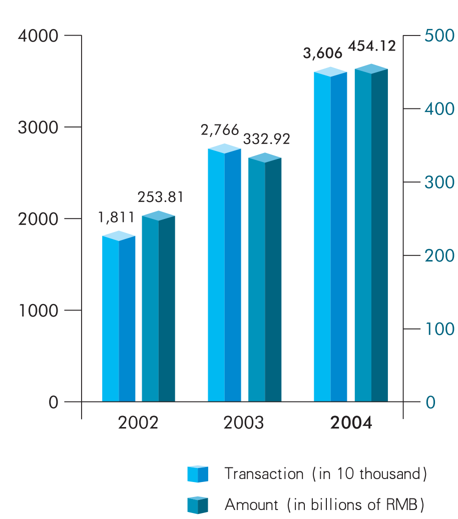
Swift Remit

In 2004, Swift Remit business sustained steady growth both in terms of business volume and commission income. By the end of 2004, the number of transactions reached 36.06 million, an increase of 30.4% over the previous year, which was equivalent to RMB 454,124 million, an increase of 36.4%. This resulted in fee and commission income of RMB 619 million, an increase of 25.8% over the previous year.

Treasury business

In 2004, while the global GDP grew at its fastest rate in nearly two decades, the increase in inflation remained steady. In the interest rate market, yields from US Treasury bills rose due to consecutive increases in the US Federal Fund rates which totalled 125 basis points by the year end. The US dollar remained weak throughout the year due to concerns over the US trade deficit.

Swift Remit transactions volume



In the domestic market, money market rates increased in the middle of the year, when the statutory deposit rate increased, and declined in the second half of year with the rising inflow of foreign currencies, leading to increased money supply. Prices of government bonds remained relatively low compared with previous years, which was mainly driven by the strengthened Consumer Price Index and increased interest rates.

We closely followed the above mentioned changes in the domestic and foreign financial markets, were flexible in our operational strategy and strengthened our risk management which all led to sound results recorded by our treasury business.

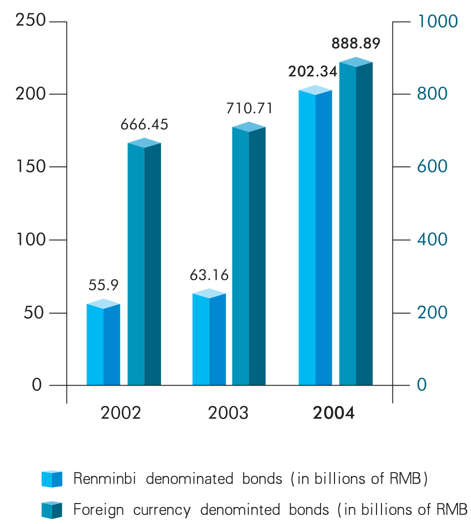
Results

In 2004, our treasury business in Renminbi experienced a steady increase in transaction volume, of which, volume in money market transactions amounted to RMB 118.4 billion, ranking first in the marketplace, while securities repurchase and reverse purchase reached RMB 1,287,800 million, ranking second in the marketplace. We underwrote RMB 328,150 million of issues in government and quasi-government bonds, subordinated bonds and central bank bills. The total transaction volume in the secondary bond market amounted to RMB 117.6 billion.

In 2004, the volume of foreign currency transactions experienced significant increase. At the end of 2004, foreign currency denominated money market placements amounted to USD 7,423 million, and investment in government bonds denominated in foreign currency was USD 24,448 million. Our investment portfolio also experienced steady growth as a result of a prudent investment strategy and close monitoring approach. Overall, this achieved diversification as well as profit growth in our portfolio during the year.

In 2004, Renminbi and foreign currency denominated transactions on behalf of our customers developed at a fast pace. By the end of 2004, Renminbi denominated bonds under custody were RMB 14,350 million, ranking third in the marketplace, and the transaction volume amounted to RMB 41,070 million. During the year, we conducted precious metal trading activities on behalf of 30 corporate customers with transaction volume totalling 4,624 kg. The volume of foreign currency exchange on behalf of our customers and trade-related foreign currency exchange and settlement reached USD 84.0 billion, an increase of 16% over the previous year, while derivative transactions conducted on behalf of our customers increased significantly and recorded a total transaction volume of USD 4,913 million, an increase of 85% over the previous year.

Renminbi and foreign currency denominated bonds



Investment strategy

Our short-term financing activities consist of short-term money market placements and the repurchase of debt securities. Our short-term financing objective is to achieve targeted returns on the amount of assets which we have determined to keep highly liquid. During the first half of 2004, we reduced our holding in debt securities with longer maturity profiles under increasingly volatile interest rate market conditions. As the market improved during the second half of 2004, we altered the make-up of our portfolio to achieve higher profitability.

Our investment strategy for long-term investments is primarily to achieve a targeted return with targeted maturity and duration profile. Such target profile is principally determined by our continuous assessment of interest rate and exchange rate risks, sovereign credit risks and other risks related to the securities.

Business expansion

In 2004, we were authorised by the CBRC to conduct transactions in all financial derivative products, including gold, but excluding equity and commodity-related derivatives. In the same year, we began further developing our Renminbi denominated bond repurchase and reverse purchase business and increased our proprietary investment and trading activities in subordinated bonds issued by policy banks and commercial banks and other money market products. We also completed the development work for our gold consignments and personal gold investment businesses, which was launched in February 2005.

In customer driven business, our foreign currency exchange agency business developed rapidly with the foreign currency option and structured foreign exchange forward businesses as our target growth areas. We remained innovative with our product development and launched several foreign currency structured deposit products focusing on the demands of our personal banking customers. Such efforts have contributed to the growth in foreign currency deposits and our market share in this area.

Overseas branches

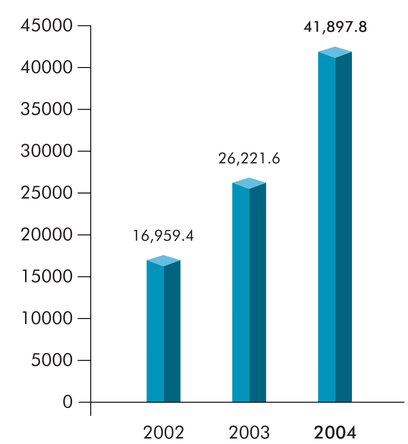
The Bank has overseas branches in Hong Kong, Singapore, Frankfurt, Johannesburg and Seoul and representative offices in London and New York. Our Tokyo branch has currently suspended operations according to the relevant Japanese legislations and we are currently applying for a renewal of the banking licence. In 2004, we selectively developed the overseas market with the aim of integrating our domestic and overseas businesses.

The principal activities of the overseas branches are to provide trade financing and lending to our customers. They have been active in participating in their local financial and debt securities markets as well as in the inter-bank lending markets. They also provide settlement and trade finance services to local Chinese companies and other local small to medium-sized enterprises. The Hong Kong Branch has entered into the inter-bank lending markets in Australia and the Middle East, and is currently working with Jian Sing Bank Limited of Hong Kong with plans to launch a series of personal banking services. The Singapore branch has started providing investment banking services to small and medium-sized Chinese enterprises to enable them to access the Singaporean capital markets, while our Frankfurt office, being our only operating outlet in Europe, assists our Head Office in conducting treasury activities and has therefore became our Euro clearing centre.

At the end of 2004, our overseas branches had total assets of USD 4,280 million, an increase of 5.7% over the previous year, while profit before tax was USD 41,897,800, an increase of 59.8% over the previous year.

Profit generated by overseas branches

(In USD'000)



Distribution channels

We deliver our products and services through a variety of distribution channels, including the traditional operating outlets, self-service banks and electronic banking. We believe that we have one of the most extensive distribution networks among the commercial banks in China. In 2004, we started to improve and integrate our various distribution channels with the aim of delivering more extensive, convenient and efficient service to our customers.

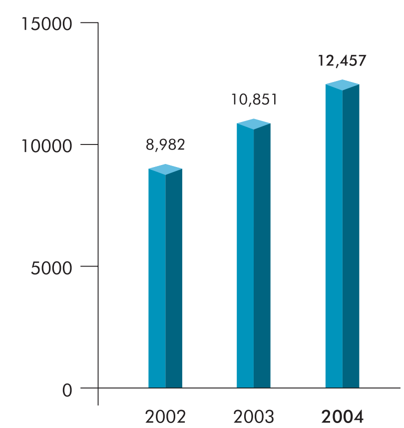
Outlet network

We conduct our business activities principally through our network of operating outlets, which includes branches, sub-branches, sub-operating offices and deposit-taking offices. By the end of 2004, we had 14,467 domestic and overseas outlets and subsidiaries. In 2004, we rationalised and improved the distribution structure of our domestic operating outlets by decreasing the number of operating outlets with lower efficiency and increasing our investment in areas with higher returns and growth potential, thereby centralising our operations. In 2004, we reduced the number of outlets by 2,005. While our sub-branches have maintained an effective coverage of our customers across the country, geographical distribution of our outlets has improved. The number of deposit-taking offices with only one single function has been proportionally reduced and we have gradually converted some into multi-functional outlets. As a result, sales volume and operational efficiency have effectively enhanced.

Self-service banks

In 2004, the Bank strengthened the development in its self-service banking business. At the end of 2004, we had 466 self-service banking outlets, an increase of 130 over the previous year. The number of automatic teller machines ("ATMs") in the year reached 12,457, an increase of 1,606, or 14.8%, over the previous year. We ranked second among the four major Chinese commercial banks in terms of the number of ATMs.

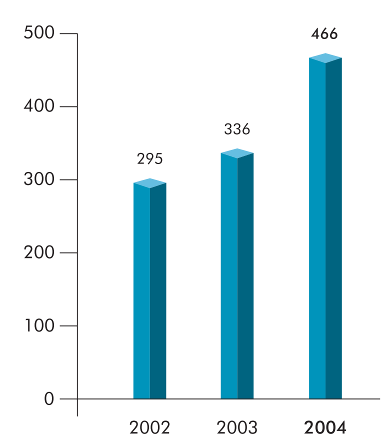
Number of ATMs



Electronic banking

In 2004, our electronic banking service expanded rapidly and the number of electronic banking customers across the Bank reached 15.20 million, an increase of 336% over the previous year. The number of transactions was 187.84 million, an increase of 179% over the previous year, and the transacted amount reached RMB 4,760.6 billion, an increase of 243% over the previous year. Our share in this market further increased in the year and the reputation of our electronic banking brand "e-Route" ("e 路通 ") was enhanced.

Number of self-service banking outlets



Internet banking

By the end of 2004, we had nearly 4.73 million Internet banking customers, 4.66 million of which were personal banking customers, an increase of 3.77 million over the previous year, 70,000 of which were corporate customers, an increase of 50,000 over the previous year. During the year, the total number of transactions was 61.28 million, an increase of 430% over the previous year. The transaction amount was RMB 2,800.8 billion, an increase of 166.4% over the previous year. In 2004, we entered into agreements to provide Internet banking service for a number of large corporate customers.

VIP Service System

The VIP Service System is directly connected to our computer systems, allowing these customers to monitor their accounts and effect various customised transactions on a real-time basis. It is also the first superior financial product of its kind among the domestic banks and has consistently maintained a leading position in the marketplace. At the end of 2004, we had over 350 preferred corporate customers using VIP Service System, including the State's ministries and commissions, large corporations and financial institutions. We are ranked top in the marketplace for supporting the MOF through the delegated payment processing system. Our cash management service is already used by many major group companies. A number of strategic clients have already linked up their internal information systems with our systems; our systems are also "directly linked" to other foreign banks. In 2004, transactions processed reached RMB 1,500.2 billion, an increase of 329% over the previous year, which represents 1.63 million transactions, an increase of 250% over the previous year.

The 95533 call centre service

Our customers enjoy convenient, efficient and secure banking service from the 95533 call centre by directly connecting through with their telephones or fax machines, 24 hours a day. The 95533 call centre service allows customers to enjoy over 20 types of services, such as enquiries on balances of accounts and transactions, balance transfers, Swift Remit, bill payments, bank securities account transfers and foreign currency exchange. It has become an important and indispensable transaction channel of the Bank. At the end of 2004, the number of registered customers reached 10.03 million, an increase of 348% over the previous year. Total transactions amounted to RMB 151.2 billion, an increase of 12.0% over the previous year and were equivalent to 115.43 million transactions, an increase of 32.9% compared with the previous year.

Mobile phone banking

On 19 July 2004, we officially launched the mobile phone BREW banking service with China Unicom, which was the first standardised mobile phone banking service launched nationwide by a major domestic commercial bank. Meanwhile, 12 tier-1 branches[6] also cooperated with China Mobile Communications Corporation and launched short messaging services providing financial information. With the launch of the various mobile phone banking services, our electronic banking service has demonstrated that the Bank leads the industry with the most comprehensive network of distribution channels. By the end of 2004, the number of customers, including short messaging service customers, amounted to over 420,000, and the transaction volume amounted to 7.35 million, equivalent to RMB 67.16 million.

[6] Tier-1 branch includes branches at province and autonomous region level, municipality directly under the central government level and special-listed city level.

Information Technology

In 2004, we launched a number of strategic projects, including the customer information integration and customer relationship management project, the corporate and institutional lending management information project, channel integration project and the internal rating-based system in accordance with our information technology plan. We completed preliminary planning for independent projects, such as the set-up of a data warehouse and management of information systems, after a thorough and comprehensive review process. We believe that through the implementation of such projects, we will build an integrated platform which is driven by and focuses on customer needs and fully supports a commercial bank's management decision making process.

We are in the process of implementing a data centre consolidation project to unify our core banking systems, which will allow real-time access to the majority of our customer transaction data. In 2004, we completed the link-up of our head office and 15 tier-1 branches and the progress of the northern and southern data centres has been sound to date. The centres are expected to be in full operation by the end of 2005.

In 2004, we sped up the progress in building and implementing the relevant information systems required to satisfy the needs of operational management and external information disclosure requirements. The credit management information system underwent large-scale upgrades and improvements. The second version of the credit management information system was launched across the Bank.

In 2004, we established a set of standard data protection and safety procedures, which is expected to be implemented by the first half of 2005. These standard procedures were based on international safety standards and data safety policies issued by relevant departments of the PRC government.

We aim to support and improve new product development and customer services, as well as enhance our capabilities in risk management and financial management. Therefore, our key targets for 2005 are: to complete the data centre consolidation project for the core business processing systems across the Bank; to implement an Enterprise Resource Planning ("ERP") system which aims to standardise financial operational procedures and enhance the quality of financial information disclosures; and to develop and implement a number of key projects, such as customer relationship management, and the channel integration to support the development of our corporate and personal businesses, the internal rating-based system ("IRB") and the assets and liabilities management system. The Bank plans to develop a disaster recovery centre in Shanghai for our northern and southern data centres and completing the first phase of this project will be one of our key tasks for 2005.

Major subsidiaries

Jian Sing Bank Limited

Jian Sing Bank Limited ("Jian Sing Bank") is a licensed commercial bank registered in Hong Kong and our wholly owned subsidiary. It mainly provides deposits and loans as well as intermediary services, such as remittance, letters of credit, guarantees and agency services, and commercial lending, trade finance and other services to small and medium-sized local enterprises. At the end of 2004, total assets of Jian Sing Bank reached USD 502 million and profit before tax was USD 5,439,700.

Sino-German Bausparkasse Co. Ltd.

Sino-German Bausparkasse Co. Ltd. ("Sino-German Bausparkasse"), a joint venture between the Bank and Bausparkasse Schwäebisch Hall, commenced operations in Tianjin on 15 February 2004. Sino-German Bausparkasse's registered capital is RMB 150 million, to which the Bank contributed RMB 112.65 million, representing 75.10% shareholding of the company. Its major business is mortgage savings credit business and providing customers with various forms of mortgage financing service.

9.4 Risk management

Building a modern risk management system

The Bank is committed to enhancing the capabilities and quality of its risk management by introducing new approaches and practices. As a result, we have achieved considerable improvements in asset quality and financial results.

In 2004, while we began to speed up the restructuring of our risk management system and mechanism in line with the basic requirements of the New Basel Capital Accord, we also focused our efforts on strengthening our risk management culture, the restructuring of our organisational structure, developing advanced technological tools and streamlining business processes and our team structure. This has put in place an initial framework for our risk management system covering credit, market and operational risks and enhanced the Bank's overall risk management capabilities.

◆ A risk management culture was gradually introduced throughout the Bank through concepts, such as maximising value while balancing risks and rewards, control of capital, comprehensive risk management and prioritisation of internal controls.

◆ We explored ways of restructuring our risk management organisational structure. We quickened the pace of building an independent and systematic risk management strategy and a corresponding framework. A vertical reporting line for our risk management function was promoted and we have built a team of risk managers. We are also looking into building a co-ordination system between business managers and risk managers which would achieve a risk-led process system.

◆ Risk management technology was improved. Based on the Credit Risk Rating and Early Warning System ("CRREW"), we launched a research project on the internal rating-based system and began building the foundation of the risk management platform. We gradually incorporated operational risk management when designing the structure of this platform. We also sped up the introduction of quality market risk management techniques, such as the use of sensitivity gap analysis to measure our exposure to fluctuations in interest rates, as well as other risk measurement techniques such as stress testing and scenario analysis on both individual portfolios and on a consolidated basis.

◆ The relating risk management systems were modified and improved, including strictly enforcing the single legal responsibility framework, refining the credit customer assessment and evaluation procedures, standardising and unifying the control of credit management and group risk exposure, strengthening the post-event sample credit review and risk monitoring analysis, implementing the five-category loan classification system and standardising the accountability system.

Since completing the incorporation of the joint stock limited liability company and further improvements in the corporate governance structure, the Bank has begun implementing changes to its risk management thereby further improving the overall risk management structure. The Risk Management Committee of the Board of Directors (the "Risk Management Committee") is responsible for formulating our risk strategy, reviewing risk management policies and monitoring their implementation, providing guidance on building our risk management and internal control systems, assessing the effectiveness of the organisational structure, reporting lines and working procedures for risk management, and conducting periodic assessments of our overall risk exposure.

In 2005, the Bank plans to implement a risk management structure in line with international practices, which reports directly to a Chief Risk Officer. We have further enhanced the independence and the effectiveness of our risk management bank-wide through reorganising the risk management organisational structure with clearly defined roles and responsibilities, implementing vertical management in risk management and credit approval and building and improving supplementary procedures for managing risk vertically.

Risk management's information system structure

The Bank has been striving to build a risk management information system to further enhance the standard of its risk management techniques. Currently, we have two major information systems for risk management: the Credit Management Information System ("CMIS") and the CRREW system.

In order to comply with the requirements of the New Basel Capital Accord and narrow the gap with leading international banks in respect of risk management, we began an independent research into the use of the internal rating-based system based on the successful launch of the CRREW system. A feasibility research report and a project plan for the blueprint design were prepared.

Credit risk management

Credit risk is the probability of loss resulting from the failure of a customer or counter party to meet its obligations or commitments to the Bank. We are exposed to credit risk primarily through the loan portfolios, discounting of bills and receivables, letters of credit, various forms of guarantees, investment portfolios and other on-and -off balance sheet credit risk exposures. Credit risk is one of the most important risks when managing a bank. The Bank is focused on and committed to improving its credit management technologies and strengthening its overall credit management practice.

Credit risk is monitored and centrally controlled by the Risk Management Department. Credit operations, credit approval and credit administration work together but are independent of each other to ensure that risk control and segregation of duties are fully effective. By building a team of credit management professionals throughout the Bank, we have significantly enhanced our credit risk management capability.

In 2003, the Bank conducted an assessment to review modifications to the five-category loan classification system and its provisioning policies in response to the revised regulatory requirements. Correspondingly, the credit ratings have been reassessed and provisions against doubtful debts have been revised according to the revised guidelines, which have been significantly realigned with relevant regulations and international best practice. By 2004, the revised five-category loan classification system and provisioning policies have been fully adopted.

Credit risk management and control policies

The Bank's credit risk strategy primarily follows the objective of maximising shareholder value by ensuring that the net income generated by the Bank's exposure is commensurate with the risk taken, avoiding undue risk concentration by rationalising the asset portfolio and realising continuous improvement in asset quality. To implement this strategy, the Bank has in place a credit management system, which comprises a series of standards, policies, procedures and systems allowing the Bank to effectively measure and control different types of credit exposure.

◆ *The China Construction Bank Corporation's Credit Manual* provides the Bank with a standardised set of comprehensive standards, policies and procedures with the aim of ensuring the alignment of credit risk management practices across all branches. *The China Construction Bank Corporation's Credit Manual* is regularly reviewed and updated during the year to ensure that the policies in place meet the demands of the Bank's continuously developing lending business closely.

◆ We operate under a system of delegated authorities, where clearly defined approval limits are assigned according to the approved credit strategy, authority level and differences in risk exposure across the lines of business. By the end of 2004, we revised our credit approval strategy and centralised most of the final decisions of the credit approval process at the Head Office and tier-1 branch levels. This has helped to unify the Bank's credit approval process and has enhanced the overall internal control environment.

◆ When evaluating the credit risk of customers or counterparties, our primary considerations are their financial strength and repayment ability. To effectively lower credit risk, we usually request security, such as collateral, from customers or counterparties.

◆ We continue to monitor loan asset quality through the use of the CMIS. The CRREW system has been successfully implemented for our corporate banking business and assists in monitoring loans by generating warning signals which indicate risk build-up in particular regions, industries, products, customers or types of loans. Therefore, the Bank's risk monitoring and management has been transformed from a post-event to a forward-looking approach.

◆ To ensure the effectiveness of the policies and procedures in place, credit risk management is subject to regular internal audit assessment. The Off-site Auditing System enables data to be collected from the branches. The system provides consistent and thorough analysis, detects problems, issues and irregularities and performs analysis for risk assessments. It also provides information for on-site auditing and facilitates the formulation of audit plans.

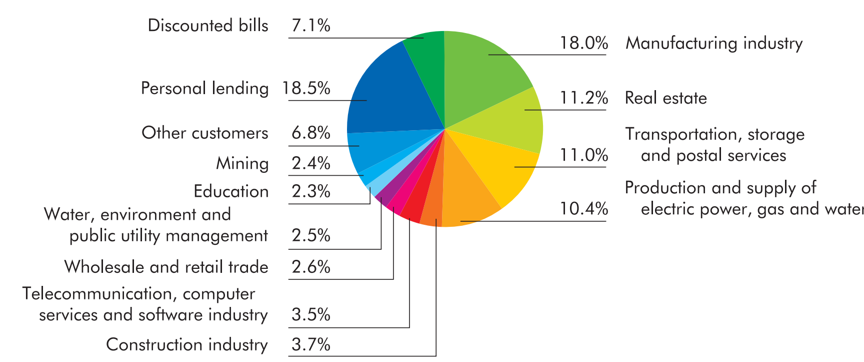
Risk-based loan classification system

The five-category loan classification system is based on the relevant regulatory requirements. We have therefore in place a set of clearly defined standards, methodology, procedures, organisational structure and tools to monitor and analyse loan data. During 2004, the five-category loan classification system was aligned with relevant regulations and adherence to the set classification criteria has been more rigorous.

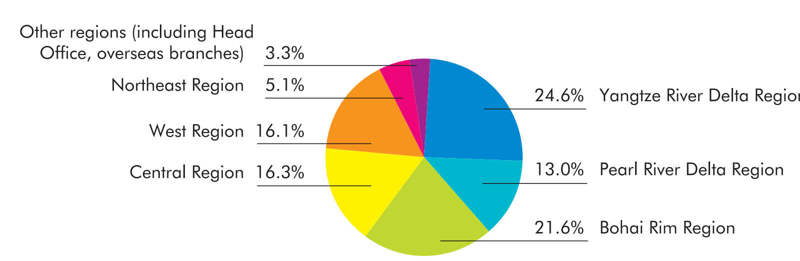
◆ *Assets subject to risk-based classification*. Assets subject to five-category classifications include loan assets denominated in all currencies and off balance sheet items, such as letters of credit, bank acceptances, guarantees, payments under guarantee and loan commitments.

◆ *Criteria of the risk-based loan classification*. The Bank adopts a risk-based loan classification methodology and classifies loans into five categories: pass, special-mention, substandard, doubtful and loss. The last three categories are defined as non-performing loans. For each type of loan, the Bank has defined clearly the primary classifications and relating general characteristics, which include the repayment ability of the borrower, repayment history, the borrower's willingness to pay and the loan collateral, etc.

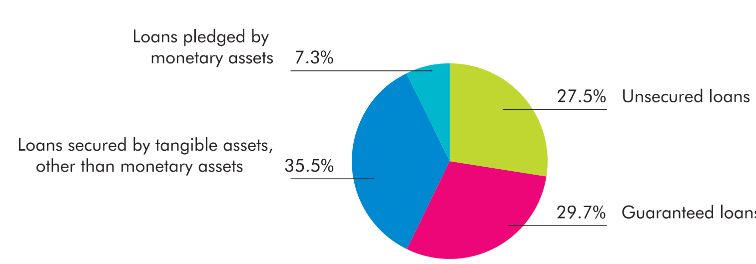
Loans balance by industry in 2004



Loans by region in 2004



Loans by type of security held in 2004



◆ *Classification methodology.* The classification is based on the assessment of repayment ability of borrowers which considers the borrowers' normal business revenues as the primary source of repayment, while treating loan guarantees as a secondary source of repayment. When defining the five-category classification for personal lending, a matrix methodology based on factors such as the overdue loans or overdrafts and loan guarantees is used.

◆ *Basic procedures in defining risk-based loan classification.* When performing the initial assessment and grading of the risk-based loan classification, the Bank follows a set of strictly defined standards, methodology, procedures and requirements. All grading approvals are made within a strict set of authority limits. The main procedures include: (1) initial assessment; (2) credit management discussions; (3) grading; (4) approval of grading; and (5) recommendations on risk management.

Loan portfolio

Loan portfolio management has always been one of the key areas of management focus. In recent years, we have ensured diversification and rationalisation of credit portfolios by spreading loans to various customers, industries, regions and maturity structures. This has, in turn, enhanced the overall profitability. The rate of loan growth in the second half of 2004 had decreased by 32.9% when compared to the first half of the year. This reflects our efforts to carefully manage our lending business with the aim of achieving healthy and steady growth, while maintaining the overall quality of the portfolio. At the end of the reporting period, loans to top 10 customers totalled RMB 106,308 million and accounted for 4.78% of the total loan balance. Please refer to the diagrams for the analysis of loans by industry, region and type of security.

Loan quality

At the end of 2004, the non-performing loan ratio was 3.92%, a decrease of 0.35 percentage points over the previous year. Total restructured loans amounted to RMB 2,563 million.

In 2004, the Bank modified the five-category loan classification system to align with relevant regulations. Provision for loan losses is therefore made where necessary and on a prudent and consistent basis with the newly established guidelines and international practices. Please see note 17 to the financial statements.

Loans grading profile (bank-wide level)

Expressed In millions of RMB

	31 December 2004		31 December 2003	
	Balance	Percentage	Balance	Percentage
Total loan balance	2,225,585	100%	1,995,990	100%
Pass	1,766,806	79.4%	1,545,165	77.4%
Special mention	371,434	16.7%	365,573	18.3%
Non-performing	87,345	3.9%	85,252	4.3%
Including: Substandard	51,418	2.3%	51,211	2.6%
Doubtful	31,058	1.4%	27,692	1.4%
Loss	4,869	0.2%	6,349	0.3%

Special assets resolution

In accordance with the Bank's credit risk management policies, some of the loans classified as substandard and all of the loans classified as doubtful or loss are transferred to a separate department, the Special Assets Resolution Department. Using a dedicated department to manage the recovery, activation and disposal of these non-performing assets has allowed us to build up considerable experience and expertise, and recovery rates have consistently improved.

In 2004, we continued to focus on recovering and disposing of non-performing assets and increasing the rate of cash recovery. We remained active in pursuing different types of disposal methods as well as exploring different ways of resolving repossessed assets. Therefore, we made some breakthroughs with the disposals of our repossessed assets. In 2004, we disposed of RMB 9,478 million and wrote off RMB 6,337 million non-performing loans assets.

Market risk management

Market risk is the risk that the Bank's earnings or capital, or its ability to meet business objectives, will be adversely or favourably affected by changes in the level or volatility of market rates or prices such as interest rates, foreign exchange rates, and equity and commodity prices. We have in place a market risk management system which uses and continues to introduce different quantitative techniques to measure, monitor and manage the Bank's market risks in an objective, effective and timely manner. Our aim is to have satisfactory financial returns while maintaining market risks within acceptable parameters.

Historically, the Bank operates in an environment where interest rates and exchange rates for both deposits and loans are set by the PRC government. As the PRC government gradually removes these restrictions and the domestic financial services sector becomes more competitive, the Bank's market risk exposure increases accordingly.

Risk Management Department is responsible for formulating market risk policies, assessing and evaluating risk conditions; and Asset and Liability Management Department is responsible for the whole bank's market risk management. Limits by location and portfolio are proposed by the businesses within the terms of agreed policy, taking into account factors such as product characteristics, staff experience, economic environment and market competition. We aim to continuously improve the overall structure and framework by using a combination of risk management techniques to enable us to effectively manage market risk on an individual level and portfolio basis.

Management monitors the Bank's market risk exposure by using a periodic reporting system, together with ad-hoc and on-line reporting. A summary market risk report for treasury transactions is produced on a daily basis, which details the Bank's market risk exposure against the agreed limits and highlights key issues for management.

Interest rate risk management

Most of our market risk is due to interest rate risk arising from mismatches in the maturities or repricing of our assets and liabilities. The resultant gap may cause net interest income to be affected by fluctuations in the prevailing levels of interest rates.

We manage our interest rate risk primarily by adjusting the maturity profile of our assets and liabilities based on our assessment of potential changes in interest rate. Since 2004, we have also begun to measure our exposure to fluctuations in interest rates using gap analysis, which provides a static view of the repricing characteristics of our assets and liabilities.

As at 31 December 2004, the Renminbi and foreign currency businesses' interest rate sensitivity gap for not more than 3 months totalled RMB -1,261,238 million and the Renminbi and foreign currency businesses' interest rate sensitivity gap for not more than 1 year amounted to RMB -340,585 million.

Value at Risk analysis ("VaR ") is a technique that estimates the potential losses that could occur on risk positions taken due to movements in market rates and prices over a specified time horizon and to a given level of confidence. VaR is currently used to measure the market exposure of the Bank's foreign currency denominated investment and trading portfolios. But due to the limitation on pricing data for the Reminbi business, the calculation cannot be used as a principal source of measurement.

The following table shows the VaR of our foreign currency denominated trading positions for 2004 and 2003:

Expressed in USD

	31 December 2004	31 December 2003
Interest rate risk	3,947,227	5,054
Foreign exchange risk	1,285	761
Diversification effect	1,873	932
Total VaR	3,946,639	4,883

Note: The above VaR should be viewed in the context of the following methodology limitations:

- The use of historical data as a proxy for estimating future events may not capture all potential events, particularly those which are extreme in nature. The model assumes that changes in risk factors follow a normal or logarithmic distribution. This may not be the case in reality and may lead to an underestimation of the probability of extreme market movement;

- The use of a 1-day holding period assumes that all positions can be liquidated or hedged in that period of time. This assumption may not fully reflect the market risk arising from times of severe illiquidity, when liquidation or hedging in that period of time may not be possible;

- The use of a 99% confidence level does not take into account of any losses that might occur beyond this level of confidence;

- VaR is calculated at the close of business with intra-day exposures excluded; and

- VaR does not necessarily capture all the market risks and may underestimate real market risk exposure.

The Bank recognises the above limitations, and uses a number of complementary techniques such as stress testing and scenario analysis both on individual portfolios and on a consolidated basis. When performing stress testing, we analyse the sensitivity of earnings from yield curve shifts and twists.

We also enter into derivative contracts such as swaps and options to hedge our interest rate risk exposure on foreign-currency-denominated trading and investment portfolios. We generally do not use these instruments to hedge our interest rate risk on Renminbi denominated securities as hedging instruments are not well-developed in the domestic market.

Exchange rate risk management

Whilst the Bank's predominant market risk is interest rate risk, we are exposed to exchange rate risk as a result of holding loans, deposits, securities and financial derivatives denominated in currencies other than Renminbi. Exchange rate risk arises from mismatches in the currency denomination of assets and liabilities and mismatches in our positions in foreign currency transactions both for proprietary accounts and on behalf of customers. We manage our exchange rate risks by seeking to match the amount and maturity period of our lending and borrowing on a currency-by-currency basis. We hedge the open positions from our proprietary currency transactions for foreign currency investments and inter -bank transactions by entering into currency spot and forward contracts. For most foreign currency purchases and transactions we execute on behalf of our customers, we generally seek to close our open positions within the same business day to the extent permissible by the State Administration of Foreign Exchange of the PRC.

Liquidity risk management

Liquidity is the risk that the Bank is unable to meet its payment obligations when they fall due or to replace funds when they are withdrawn. The Asset and Liabilities Management Department is responsible for managing the liquidity structure of the Bank's assets, liabilities and off-balance sheet commitments in order to ensure that the Bank can meet its current and future re-financing needs at acceptable costs, as well as managing the Bank's day-to-day liquidity.

To achieve centralised liquidity management, we have a uniform liquidity policy in place for all domestic tier-1 branches, with an authorised set of liquidity limits and ratios for all branches to follow, and any surplus funds are remitted to the Head Office.

Liquidity is managed by analysing sources and uses of funding, economic and business conditions and by projecting future cash flows. Regulatory and statutory liquidity requirements are also taken into account.

Key liquidity ratios for Renminbi domestic business

	Loan to deposit ratio	Liquidity ratio	Surplus reserve ratio	Inter-bank lending ratio
31 December 2004	60.98%	51.37%	4.69%	0.39%
31 December 2003	66.54%	44.64%	4.13%	0.49%

Liquidity positions are monitored daily, and reviewed quarterly, by senior management. The sources and maturities of assets and liabilities are closely monitored and diversified to avoid any undue concentration. In 2004, the loan to deposit ratio decreased from 66.54% at the end of 2003 to 60.98%, a reduction of 5.56 percentage points which reflects the Bank's tightened credit underwriting policy in response to the government's macroeconomic policies. The liquidity ratio increased from 44.64% in 2003 to 51.37%, an increase of 6.73 percentage points which is mainly a result of the Bank utilising its abundant capital and therefore increasing in its holding in placements and investments.

Operational risk management

Operational risk is the potential for direct or indirect financial loss arising from failed or inadequate internal processes, people and systems or from external events such as fraud, unauthorised transactions, error omission, negligence, inefficiency, systems failure and other events.

The Bank has formulated and implemented internal policies, procedures and criteria to manage operational risk. We have slowly built an operational risk management framework which covers all business functions ranging from finance, credit, accounting, settlement, savings, treasury, intermediary business, computer applications and management, special assets resolution and legal affairs. This has facilitated the Bank to comprehensively identify and address the operational risk inherent in all key products, activities, processes and systems. Key controls include:

◆ Segregation of duties whereby responsibilities within our operating departments, including the business departments, the Credit Approval Department, the Risk Management Department and the Audit Department, are clearly defined and separated;

◆ A centralised appointment and rotation system for key positions, in particular for key accounting and financial control positions at our branches;

◆ Delegation of authority for various business activities to branches within set limits according to their respective business scope, risk management capabilities and credit approval procedures. Authorisations are revised on a periodic basis to reflect changes in market conditions and business development and risk management needs;

◆ A dedicated anti-money laundering division under the Legal Department which is responsible for overseeing that cash management and account management are in compliance with the relevant regulations and for improving training on anti-money laundering to ensure our staff are well-equipped with the necessary knowledge and basic skills to combat money laundering;

◆ Accountability managed under a code of conduct. Enforcement and strict disciplinary measures in place for those violating our rules and regulations; and

◆ Contingency facilities maintained (including backup systems and disaster recovery schemes) to support all operations, especially back office operations, in the event of an unforeseen interruption. Insurance cover arranged to mitigate potential losses associated with certain operational events.

The Bank continues to be committed to seeking effective ways to control operational risks. Since 2003, the Risk Management Platform project was initiated with the aim of unifying our various risk management procedures and criteria across all business activities and branches. The project is based on five key elements of an internal control framework: internal control environment; internal control planning; internal control implementation, operation and monitoring; assessment and continuous enhancements; and information and communication.

Internal audit

The Audit Department's objective is to promote an effective internal control and corporate governance environment. It is responsible for auditing and evaluating the internal controls of the Bank's business operations, risk profiles and economic accountability of key managers, and proposing improvements to the Bank's risk management, internal controls and corporate governance processes.

In 2004, the Audit Department implemented a risk-focused audit strategy by conducting a number of audit projects such as audits of the carve-out of doubtful debts, the new loans origination process, residential mortgages and consumer lending, the bills discounting business, the foreign exchange business, and the information systems. Meanwhile, we enhanced the quality and effectiveness of our internal audit review by integrating both on and off-site audits, ensuring audit findings were resolved on a timely basis and management and information analysis of our audits were strengthened. We remain committed to investing in new audit techniques and computer aided tools and have completed the initial phases in developing a new risk assessment audit planning system, an internal controls audit assessment methodology and an audit information management system.

In 2005, as part of our efforts to increase the independence and authority of our internal controls, we are establishing a vertical internal audit structure that reports directly to the Board of Directors and its Audit Committee, the President and the Board of Supervisors.

9.5 Community involvement

To fulfil our corporate social responsibility, we support a variety of community activities to promote improvements in the community and social benefits. With an objective of helping the community to benefit from the development of the Bank, we have seen progress in areas such as education, aiding the poor, medical and sports, which have all benefited from our years of support.

◆ In 2004, the CCB Caring Foundation, established through employee donations, donated a total of RMB 2 million to help over 1,460 students with financial difficulties in 86 universities; RMB 500,000 to the China Youth Development Foundation to build a "CCB Hope Primary School" in Rongshui County of Guangxi Zhuang Municipality Autonomous Region; RMB 500,000 to the China Foundation for Justice and Courage, which honours and rewards individuals for exemplary and courageous actions and commitments. By the end of 2004, in total, the CCB Caring Foundation had donated RMB 28.25 million to the community; RMB 18 million to help over 13,160 students with financial difficulties in 86 universities; RMB 4.5 million to the China Youth Development Foundation to build over 20 Hope Primary Schools in 13 provinces, autonomous regions and municipalities directly under the central government throughout the country; and RMB 4.5 million to the China Foundation for Justice and Courage.

◆ In 2004, we continued to support the China Children and Teenagers' Fund and were entrusted to raise charity donations in aid of children in underprivileged areas wanting to return to school. Together with the China Children and Teenagers' Fund, we developed the "Change for Charity" donation boxes campaign. By the end of 2004, we helped to raise funds totalling RMB 2,187,100 on behalf of the China Children and Teenagers' Fund for underprivileged children to return to school. In 2004, as a result of our continued support and active aid assistance for the cause of children education, the Bank was awarded the "Children Care Outstanding Award" at the third "Chinese Children Charity Activity Day" jointly held by the Chinese People's Association for Friendship with Foreign Countries, the World Chinese Entrepreneurs General Association, the China International Institute of Multinational Corporations and China Children and Teenagers' Fund.