Financial Review

PROFIT

ICBC recorded an operating profit of RMB 43,917 million, with total profits of RMB 6,217 million, an increase of RMB 324 million or 5.5% as compared to 2001. Provisions amounted to RMB 25,590 million, and the write-off of interest receivable and non-credit asset loss totaled RMB 12,110 million.

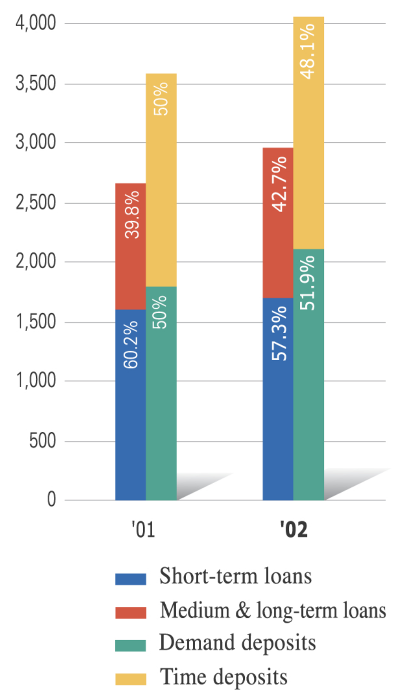
Item (RMB million)	2002	2001
Total profits	6,217	5,893
Provisions	25,590	17,478
Write-off of interest receivable	8,207	7,354
Write-off of non-credit asset loss	3,903	3,659
OPERATING PROFIT	43,917	34,384

NET INTEREST INCOME

At the beginning of the year, the PBOC lowered the benchmark interest rates for both deposits and loans, which resulted in a decline of both interest income and expenses for ICBC. Despite the fact that the decrease of the nominal loan interest rate was double that of the nominal deposit rate, and also that the Ministry of Finance shortened the overdue interest tenor from 180 days to 90 days after which the accrued interest income should be recorded off balance sheet, the Bank still managed to grow its interest income by 2.4%, whilst interest expenses witnessed a slide-down of 15%, increasing the actual net interest spread by 0.17 percentage points. Thereby the Bank achieved a 32.5% growth in net interest income. In addition, both the well optimized tenor structure of the assets and liabilities, with a higher proportion of demand deposits and medium-to-long-term loans, and improved asset quality over the past three years have also contributed to the growth of the interest income.

TENOR STRUCTURE OF DEPOSITS AND LOANS

Unit: RMB billion

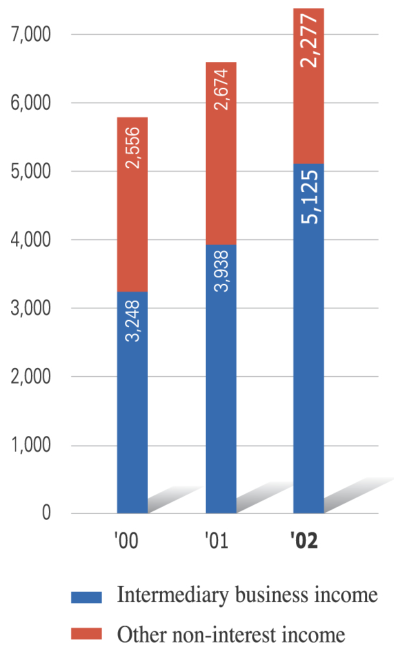


NON-INTEREST INCOME

In 2002, ICBC made a total of RMB 7,402 million in non-interest income, up RMB 790 million or 12% as compared with 2001. Of this, 75% was other operating income, including RMB 5,125 million of intermediary business income, up nearly RMB 1.2 billion, or 30%, and RMB 437 million of other income.

NON-INTEREST INCOME

Unit: RMB million



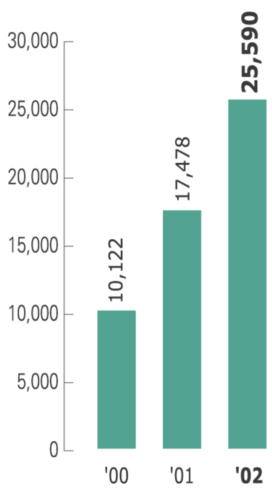
OPERATING EXPENSES

Operating expenses for 2002 totaled RMB 40,672 million, an increase of RMB 991 million or 2.5% as compared with 2001, of which fixed-assets depreciation was RMB 6,557 million, up RMB 1,213 million. Due to the reduction of the tax rate, business tax and surcharges reduced by RMB 915 million, or 10.3% as compared with the previous year.

PROVISIONS

PROVISIONS

Unit: RMB million



The Bank stepped up its efforts to deal with its non-performing loans. In 2002, the Bank had set aside RMB 25,590 million in provisions, up RMB 8,112 million or 46.4% over 2001. The provision accounted for 28.5% of the operating income and 58.3% of the operating profit respectively.

MAIN CHANGES IN THE BALANCE SHEET

The Bank's total assets amounted to RMB 4,734,236 million, 9.6% higher than 2001, mainly due to 11% growth in loans and 25% growth in investments . The total liabilities were RMB 4,556,381 million, up 10.4%. The increase was mainly due to a 13.3%, or RMB 476,400 million growth in various types of deposits. The paid-in capital decreased by RMB 6,687 million, mainly caused by the following equity transfers: the transfer of RMB 5,934 million worth of debt for equity swap to China Huarong Assets Management Corporation as required by the Ministry of Finance, the delivery of RMB 738 million worth of equity in China Securities Co., Ltd., and four other financial companies at zero value, and also the transfer of RMB 15 million worth of equity in China Financial Data Network Co., Ltd. to China Telecom Group at zero value. The undistributed profit declined by RMB 6,594 million mainly due to the RMB 10.85 billion of specific provision made during the year. Therefore, the change in the paid-in capital and the undistributed profit resulted in a decline of the owners' equity by RMB 13,139 million from the previous year.

IT Projects

To improve the service and management of the Bank by utilizing modern information technology has been one of ICBC's core strategies over recent years. The Bank has built a world-class centralized production system and, based on an advanced IT infrastructure, developed a series of modern management systems and banking products which helped to enhance the competitiveness of the Bank. The re-engineering of the IT infrastructure, which further pushed management restructuring and business innovation, has consolidated the Bank's efforts in becoming a real modern and operationally centralized commercial bank.

DATA CENTER CONSOLIDATION

Data center consolidation has been a pioneering IT project not only for ICBC , but also for the financial industry as a whole in China. After three years of preliminary work, the project was successfully completed ahead of schedule in October 2002. The original 36 data centers across the country were consolidated into two big centers, at which all the business data of the whole bank can be processed in a standardized way. Eight different types of state-of-the-art techniques such as the "parallel sysplex" were applied for the first time in China, which enhanced the system’s efficiency and security. The two newly consolidated centers now conduct the daily data processing for all of the main businesses of the Bank, and handle an average of 90 million transactions with a peak volume of 110 million transactions on a daily basis.

COMPREHENSIVE BUSINESS PROCESSING SYSTEM

The new generation of comprehensive business processing system has been developed to improve the Bank's competitiveness and to cater for increasing market demands. After four years of design and development and three years of pilot application, the integrated version went into full operation at all tier-one branches in May 2002. ICBC was the first bank in China to implement such an integrated and standardized application platform for its core business. The new system is able to provide customer-oriented and one-stop comprehensive services to replace the traditional product-oriented service model and enables the Head Office to better monitor the business across the whole bank through a set of standardized performance indicators. The implementation of the credit information and management sub-system imposes programmed controls to strictly standardize the credit approval working procedures and makes real-time credit risk monitoring possible. These have all contributed to enhancing the credit risk management capabilities of the Bank.

DATA WAREHOUSE CONSTRUCTION

Following the principles of "unified planning and management" as well as through implementation with continuous improvement on an incremental basis, the Bank completed the development, pilot testing and implementation of a Customer Relationship Management System (CRMS) for private customers combined with an integrated statement analysis system. The data warehouse constitutes a technological platform which makes it possible for the Bank to provide customers with personalized services, and also, through improved accurate and efficient management on information, to increase the level of automation in management processes and support decision-making in a more scientific manner.

Risk Management

CREDIT RISK MANAGEMENT

The credit risk management was further enhanced, which was mainly reflected through improved early-warning, monitoring and control of risks, more scientific and systematic internal rating, more diversified credit portfolio, substantial reduction of non-performing loans and prompt recovery of distressed assets.

Credit Risk Management System

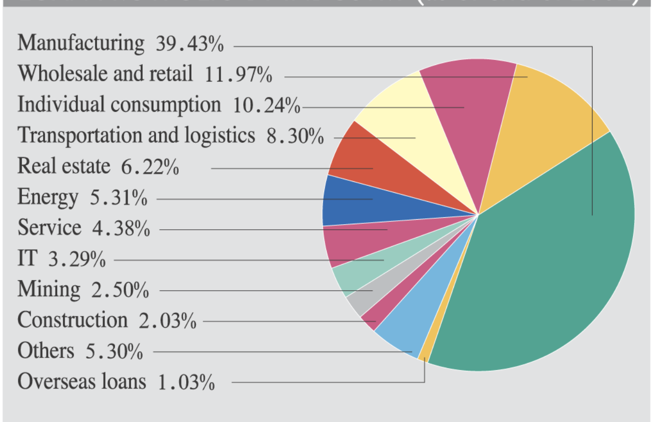
Credit Underwriting Controls	Credit policies and rules	The Bank makes credit decisions by reference to comprehensive review of the client's financial conditions, industry, state policies and the regional economic condition of the area in which the exposure is focused. Accordingly, the Bank classifies its clients into "supportive", "maintained", "to-be-closed-down" and "to-be-exited" accounts and the project loans into four categories from "supportive" to "exit". Credit policies and credit work flow have been formalized with a view to standardizing the credit management process.
	Credit rating	An objective and fair-minded evaluation of clients' creditworthiness which leverages the Bank's Internal Rating Mechanisms and constitutes an important criteria for granting loans.
	Bankwide credit facilities	The Credit-Facility Evaluation Center has been set up internally to grant a ceiling credit facility to single corporate borrowers and a credit facility cap for a corporate group and its related companies.
Loan Approval	Authorization system	Basic authorization, on-authorization and special authorization are granted to domestic branches and business departments and are reviewed on an annual basis.
	Credit assessment and approval	Rigorous credit assessment and approval procedures, properly centralized credit approval systems and clear accountability for credit assessment and approval are all crucial to the improvement of the credit decision-making process. The key credit examiner responsibility system and the Credit Policy Committees are established at all levels. Very large deals and deals for special purposes are subject to the approval of the Credit Policy Committee at the Head Office. Tier-one and tier-two branches can approve credit decisions within their level of authorization.
Post-loan Monitoring	Loan monitoring management	Loan monitoring is accomplished through the credit management information system and specialized credit management reports. New loans are monitored on a daily basis, analysed in terms of industries and regions, and the overall credit allocation is adjusted based on asset quality and the risks perceived.
	Off-site monitoring of asset quality	Loans are monthly monitored following the four-catogary and five-catogary classification systems. Changes in non-performing loans, in both relative and absolute terms, are factors that are taken into consideration in the performance evaluation of the branches.
	On-site inspection	On-site and off-site reviews are carried out to identify existing and potential credit risks. Early warning mechanisms have been established and problem loans are disposed of in accordance with the relevant authority limits and working procedures, as stipulated in the Bank's internal rules, to prevent, control and mitigate risks.

Internal Rating System

Drawing on international best practices, ICBC drafted out *Evaluation of Corporate Clients* and other internal rating rules and measures. An internal rating system has been created which rates clients, according to their solvency, from the highest AAA to AA+, AA, AA-, A+, A, A-, BBB, BB and with B being the lowest with reference to market benchmarks based on industry and size of company. This is a three-dimensional system, which takes into account 9 quantitative basic indicators, 11 quantitative amendment indicators and a number of qualitative indicators as well. In addition, the Bank worked out a set of internal rules and measures in 2002, for example, *Rules for Reviewing Financial Statements of Corporate Clients*, *Detailed Measures on Reviewing Financial Statements of Corporate Clients*, and *Rules for Rating Real Estate Developers, Schools, Hospitals and Legal Entities in the Construction Industry*. Software for the computerized reviewing of financial statements has been developed and circulated for widespread use within the Bank, which ensures the accuracy and reliability of the information used for ratings. Ratings were assigned to 260,000 corporate clients in 2002, a significant step forward for the Bank's internal rating systems.

Credit Risk Exposures

LOAN PROTFOLIO BY INDUSTRY (as of end of 2002)



The Bank maintained its cautious approach towards lending during the past year. Firstly, the Bank increased its loans to infrastructure projects, key fundamental industries, urban construction in large- and medium-sized cities, the IT industry, non-productive circulatory sector, consumer credit and other emerging industries, and meanwhile reduced its exposure to uncompetitive traditional industries with surplus productive capacity and adamantly exited highly risky markets which generated low economic returns. Secondly, the majority of new loans were extended to clients rated at AA or higher; and a moderate proportion of loans were extended to AA-, A+ and A clients, or to A- rated clients after careful scrutiny; outstanding loan exposures were reduced for clients rated at BBB or lower and, in particular, quick collection actions were implemented for those rated at BB, lower or not rated at all. Thirdly, branches in financially developed regions with better risk control capabilities were given differentially more authority in the credit underwriting process.

Credit Asset Quality

The year 2002 witnessed a drastic decline in the non-performing loans due to a more optimal credit underwriting structure, improved internal controls and greater efforts in the recovery of existing NPLs. The non-performing ratio fell from 29.78% to 25.69%, down 4.09 percentage points, or RMB32.1 billion according to the five-category classification method; it fell from 25.71% to 22.21%, down 3.5 percentage points, or RMB26.7 billion in accordance with the four-category classification method.

LOAN CLASSIFICATION

Unit : RMB million

ITEM	31-12-2002		31-12-2001	
	Outstanding	%	Outstanding	%
TOTAL LOANS	2,957,837	100.00	2,659,466	100.00
FIVE-CATEGORY CLASSIFICATION				
Performing	1,833,541	61.99	1,447,547	54.43
Special mention	364,418	12.32	419,930	15.79
Non-performing in total	759,878	25.69	791,989	29.78
Substandard	117,781	3.98	169,142	6.36
Doubtful	458,618	15.51	449,716	16.91
Loss	183,479	6.20	173,131	6.51
FOUR-CATEGORY CLASSIFICATION				
Performing	2,300,817	77.79	1,975,717	74.29
Non-performing in total	657,020	22.21	683,749	25.71
Overdue	21,392	0.72	44,679	1.68
Doubtful	593,057	20.05	593,593	22.32
Bad loan	42,571	1.44	45,477	1.71

The retail lending business maintained high credit quality with an NPL ratio (according to five-category classification) of 0.97% for consumer loans and 1.05% for mortgage loans. Against the background of the fast booming mortgage market, the Bank, alert to real estate bubbles, took effective steps to manage underlying risks, and has kept property developing loans to residential mortgage loans at 1:3.5.

In 2002, the Bank, for the first time, disclosed its NPL figures in accordance with the internationally accepted five-category classification method with improved credit quality reporting and information disclosure processes. The five-category classification was introduced and modified in compliance with the People's Bank of China's requirements to accurately reflect asset quality. In addition, the Bank appointed an internationally well-known accounting firm to conduct an across-the-board audit of the financial statements of the Shanghai Municipal and Zhejiang Provincial branches prepared in accordance with International Accounting Standards. The result of the audits indicates that the reported financial condition and the asset quality of the two branches are true and fair. The coverage of the audit will be further enlarged to other branches in 2003.

Disposal of NPLs

Specialized centers have been created in 15 tier-one branches and 156 tier-two branches for the purpose of the specialized resolution of non-performing loans through cash recovery, merger and acquisition, obtaining guarantees, seizing assets for repayment of loans, and the charge-off of bad loans. Last year RMB 69.84 billion of non-performing loans were recovered or disposed of, of which RMB 35.76 billion were recovered in cash.

LIQUIDITY MANAGEMENT

RMB Liquidity Management

ICBC established a multi-level liquidity reserve mechanism, which is in compliance with the PBOC's regulations on liquidity management, to ensure that the Bank could meet the demands for deposit payments and business development. ICBC also worked on adjusting the asset structure and increased the proportion of easily liquefiable and high-yield fixed-income investments which bring both liquidity and profitability to the Bank. Given the booming capital and money markets, ICBC has actively involved itself in capital market investment and money market financing, commercial bills and stock financing. In 2002, the Bank invested RMB 89.8 billion in purchasing treasury bonds and bonds issued by financial institutions in the primary market. The transaction volume of open-market treasury bill repo and commercial paper finance totaled RMB 53.5 billion and RMB 875.9 billion respectively.

RMB liquidity is managed in a centralized way. The Head Office keeps a close eye on the liquidity of the branches, following a principle of strict deposit reserve requirements with real-time clearing and centralized monitoring of positions, and with particular attention to the stability of savings deposits, corporate deposits and deposits from other banks. The daily position of each branch is monitored on a real-time basis and managed at the Head Office level.

Foreign Exchange Liquidity Management

The Head Office is responsible for foreign exchange liquidity management across the Bank as a whole. Foreign exchange deposits constitute the majority of the Bank's foreign exchange funds. By developing various deposit sources, the Bank has maintained a stable source of long-term foreign exchange funds, which is complemented by financing from the international market. In terms of the management of foreign exchange, apart from the foreign exchange lending business, the Head Office centralizes all foreign exchange operations in the international market and also foreign exchange position management within the branch network. Some of the liquidity management measures include the participation in international inter-bank market activities and investment in highly rated and marketable bonds.

MARKET RISK MANAGEMENT

Interest Risk Management

Management of RMB Interest Rate

The interest rates for RMB lending and deposits are regulated by the People's Bank of China, and commercial banks can vary interest rates by a maximum of 30% above and 10% below the basis rate. Inter-bank lending rates and bond rates are market-determined. With the market trend towards the deregulation of interest rates and in line with building a diversifying portfolio of bank assets, the Bank closely follows, analyses and forecasts changes in RMB interest rates and minimizes the risks involved by matching the basis rates and the maturity of various types of assets and liabilities. Differentiated interest rates are applied to companies in different regions, industries and with different credit ratings. The rational pricing of loans on the basis of total cost management helps bring down interest rate risk caused by changes in interest rate structures.

Management of Foreign Exchange Interest Rate

The Bank carefully monitors the interest rate market and quickly adjusts the rates for large foreign currency deposits and lending in order to prevent mismatches between foreign exchange assets and liabilities and an unstable interest margin. In 2002, an internal transfer pricing mechanism based on market rates helped to enhance the analysis and rebalancing of the maturity structure of foreign exchange assets and liabilities. Interest rate risk was further mitigated by using a variety of derivative instruments.

Management of Exchange Rate Risk

Exchange rate risk has always been the focus of foreign exchange risk management, and the target is to ensure the matching of currencies between foreign exchange assets and liabilities. In 2002, the Bank managed the risk effectively by rebalancing the foreign exchange assets and liabilities structure in line with the changes in exchange rates in the international market and its business development needs. The branches effectively mitigated their exchange rate risks by entering into currency swap deals as hedges through the Head Office.

OPERATIONAL RISK AND OTHER RISK MANAGEMENT

Operational and other risks are managed by enhanced internal controls with a particular focus on prevention style controls. Comprehensive reviews were conducted on internal controls at one third of the grass root branches in 2002 and theme based internal audits were carried out on areas such as finance, bonds, settled assets, fee revenues, and the financial statement closing process. In 2002, 35,000 rectification proposals were put forward and RMB 22.42 million of problem assets were recovered thanks to over 10,000 auditing initiatives implemented within the Bank. Consequently, the Bank saw a 36.4% decline in financial crimes from the previous year and was strengthened in its ability to resist against such risks.

Anti-money Laundering Mechanism

An anti-money laundering program was launched last year. A steering team was organized at the Head Office headed by two Executive Vice Presidents. The team is responsible for investigating money laundering, formulating relevant policies and procedures, and overseeing the implementation of those policies. It also takes care of big and serious cases, and shares experience with domestic and international anti-money laundering organizations and financial regulators across the world.

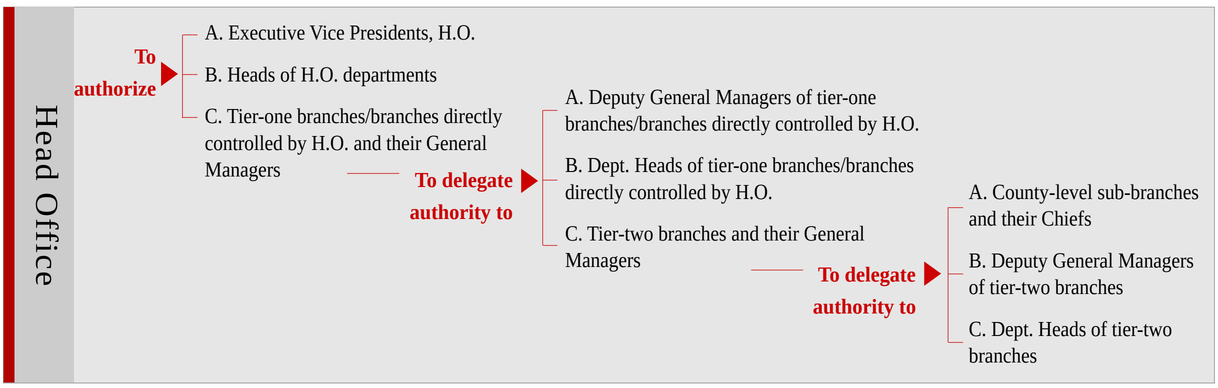
Corporate Governance

ICBC is committed to establishing and perfecting an open and transparent corporate governance framework, which embodies a vertical system of multi-level authorization and decision-making processes, an independent internal auditing and compliance system, and an organizational structure designed to meet the needs of the ever-growing business.

THE AUTHORIZATION MANAGEMENT SYSTEM

ICBC adopts a management system that consists of the Head Office and its branches. The subordinate branches are required to conduct their business and make decisions in accordance with the law and in compliance with the delegation of relevant authority from the upper levels of the organization. Authorization is further defined to include: basic authorization, delegated authorization, and special authorization. The legal department at each branch level is responsible for the management of the authorization system.

AUTHORIZATION FLOW CHART



Special Authorization is the authority granted to the subordinate branch from its upper-levels of the organization that exceeds the original scope, category and limit of the basic authority or delegated authority. The subordinate branch can also apply for such authorization from its superior branches if needed.

INDEPENDENT EXTERNAL AND INTERNAL AUDITING SYSTEMS

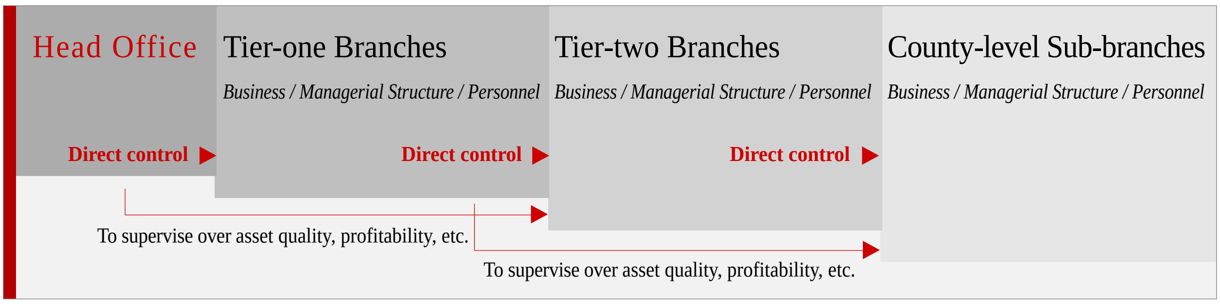
All tier-two branches and above have set up internal control and auditing departments, which are responsible for the internal audit and internal control functions, carrying out all types of auditing at all levels of ICBC, both at home and abroad. To ensure the objectivity, impartiality and independence of auditing, the auditing department of each branch is also required to supervise and review the branches directly under its control. An international accounting firm is appointed to conduct auditing on some of ICBC's branches. On top of all these, the Supervisory Board of ICBC, on behalf of the State, takes up the role of being an external independent monitoring body over the Bank.

REFORM OF THE MANAGEMENT STRUCTURE

Reform and Development of Branch Management

The branch management system with the Head Office having a direct control over the tier-one branches, while monitoring tier-two branch activities and all subordinate branches was further refined. A Branch Management Committee has been established at the Head Office to coordinate the management and supervision of the branches. A process was established for the review of applications to establish new or to close unnecessary subordinate branches. Supervisory rules and regulations for major business product types have also been established.

BRANCH MANAGEMENT FLOW CHART



The Head Office utilizes information technology to enhance its capability to supervise and control the branches. The Head Office not only supervises over the business, the managerial structure and the personnel of the tier-two branches, but also assesses the profitability and asset quality of the tier-two branches using a series of performance indicators, and accordingly gives advice to the tier-two branches on the modification of their managerial structure, business authorizations, resource allocation decisions, appointments of management teams, as well as their rewards and any disciplinary measures. All these measures lay the foundation for a flat management structure supporting the branches in the future.

An internal grading system for subordinate branches is established to grade the branches, based on both performance measures and business scale, the results of which are used as a key reference in resource allocation decisions. In this way, the Bank further strengthens the incentive and control mechanisms, and also reduces bureaucracy amongst the management structure.

ICBC adopted strategies that balance between rationalization and expansion. There were 2,415 inefficient business outlets closed in 2002 and 1,550 new ones opened or upgraded. With all these efforts, the total number of business outlets, schools and other affiliated units was reduced to 25,960 while the efficiency of the organizational structure has been improved.

Restructuring At The Head Office Level

At the Head Office level, two new departments, the Institutional Banking Department and the Investment Banking Department, were established. Further set up within the Credit Management Department were a Credit-Limit Center, a Credit Assessment and Approval Center, a Credit Monitoring and Inspection Center and an Industry Analysis Center. All of these helped to strengthen the marketing and risk management functions of the Head Office.

Reform Of The Legal Structure Of Internal Organizations

ICBC Card Center

ICBC Card Center was newly founded in May 2002 with the aims of invigorating the Bank's card business and strengthening its competitiveness. Born out of the Credit Card Department of ICBC, the Center is the first professional business entity dedicated to the bank card business in China. ICBC Card Center has developed an internal organizational structure and operational processes that meet both the international and the professional standards for a bank card business and the requirements for a separate, legally identifiable corporate management system. Successfully transformed from an extensive operational function to an integrated business role, the Bank's card business has continued to gain energy and competitiveness through such reforms.

ICBC Bills Discounting Department

It was the first nation-wide and professional bills discounting body approved by the People's Bank of China. The founding of the Department signified that the bills discounting business in China has entered into a new phase of professional, standardized and large-scale operations. Ever since its establishment in November 2000, the Bills Discounting Department has generated total profits of over RMB 100 million for three consecutive years, with an average revenue in excess of RMB 1.5 million per staff and with RMB 270.55 billion of accumulated traded volume, without incurring any non-performing assets.

ICBC was the first among its domestic banking peers to have introduced a centralized bankwide approach to run the bank card and bills discounting businesses. In addition, reforms continued around the logistical functions throughout ICBC in a further effort to streamline the core functions of the whole bank.

Overseas Expansion Strategies

ICBC is actively engaged in implementing its international business strategy by means of restructuring, merging or acquiring of banks, and opening new overseas branches and offices, in order to establish a global business network that covers all the major international financial centers. ICBC shall further improve the managerial and risk control capabilities of the overseas branches and offices, with enhanced service functions, more innovative products and by further optimizing the allocation of resources, with a view to enhancing the overall competitiveness of the Bank's cross-border business network as the overseas branches continue to play a more important role.

FUTURE GOALS FOR GROWTH

After successfully achieving the three-year profit target by the end of 2002, ICBC will enter into a new stage of development starting from 2003 through to 2010, continuing its reform towards a modern commercial bank. The future growth can be divided into three phases. The first phase, from 2003 to 2006, is to strive to lower ICBC's NPL ratio to below 10% and thus to improve the asset quality and financial conditions of the whole bank; the second phase, from 2007 to 2009, is to focus on building sufficient provisions and making up for the deficiencies in capital adequacy; and in the third phase, the Bank shall strive to further reduce the NPL ratio to 3% to 5% and increase operating profit to around RMB 100 billion and net profits to RMB 80 billion by the end of 2010. This allows the Bank to reach the medium to high level of the international banking standard in terms of operating and financial indicators.

With this accomplished, ICBC should fully meet up with international banking supervision standards and the requirements for an IPO, and thus become a large-scale modern commercial bank with considerable international appeal.