



創興銀行有限公司
Chong Hing Bank Limited

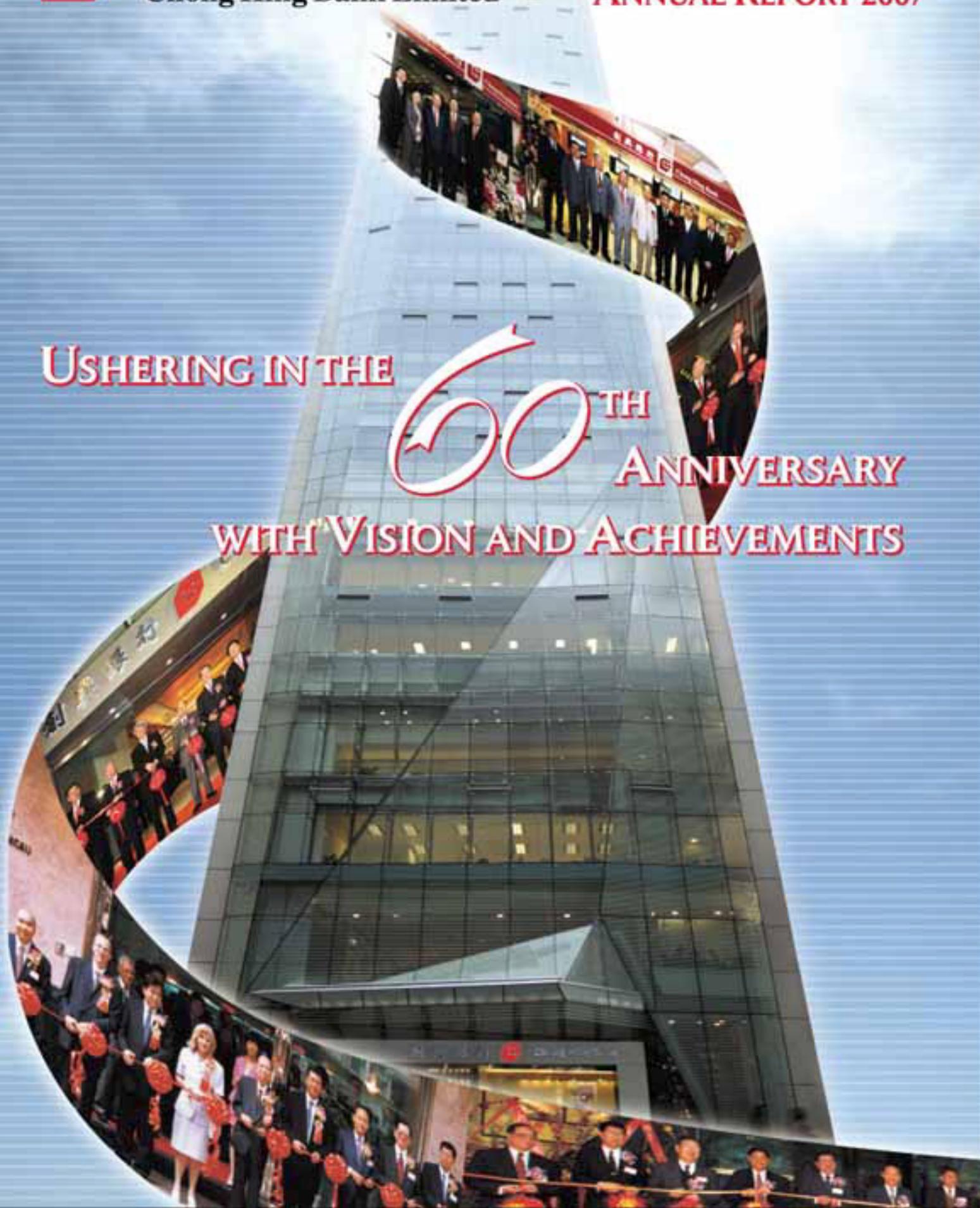
ANNUAL REPORT 2007

USHERING IN THE

60TH

ANNIVERSARY

WITH VISION AND ACHIEVEMENTS



CONTENTS

Five-year Financial Summary	2
Corporate Information	3
Abridged Corporate Structure	10
Share Trading Summary	11
Shareholders' Calendar	12
Notice of Annual General Meeting	13
Executive Chairman's Statement	16
Directors' Report	22
Corporate Governance Report.....	30
Independent Auditor's Report	36
Financial Statements	37
Consolidated Income Statement	39
Consolidated Balance Sheet	40
Balance Sheet	41
Consolidated Statement of Changes in Equity	42
Consolidated Cash Flow Statement	44
Notes to the Financial Statements	46
Unaudited Supplementary	
Financial Information	127
Head Office, Branches, Principal Subsidiaries	
and Affiliates	144

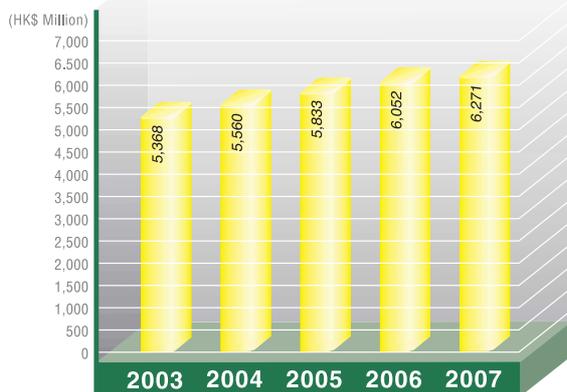
FIVE-YEAR FINANCIAL SUMMARY

TOTAL ADVANCES TO CUSTOMERS / TOTAL CUSTOMERS' DEPOSITS / TOTAL ASSETS



■ Total Advances To Customers
 ■ Total Customers' Deposits
 ■ Total Assets

CAPITAL RESOURCES



PROFIT ATTRIBUTABLE TO SHAREHOLDERS



Board of Directors

Executive Directors

Mr LIU Lit Man, GBS, JP, FIBA
(Executive Chairman)

Dr LIU Lit Mo, LLD, MBE, JP
(Vice Chairman)

Mr LIU Lit Chi
(Managing Director & Chief Executive Officer)

Mr Don Tit Shing LIU
(Deputy Chief Executive Officer)

Mr LAU Wai Man
(Deputy Chief Executive Officer)

Mr Wilfred Chun Ning LIU

Mr Frank Shui Sang JIN

Mr Andrew Chiu Wing TSANG

Mr George Har Kar WONG

Non-executive Directors

Mr Timothy George FRESHWATER

Mr WANG Xiaoming

Mr Andrew LIU

Mr Eiichi YOSHIKAWA

Mr Christopher Kwun Shing LIU

Mr Alfred Cheuk Yu CHOW, JP

Mr MENG Qinghui

Independent Non-executive Directors

Dr Robin Yau Hing CHAN, GBS, LLD, JP

Mr Wanchai CHIRANAKHORN

Mr CHENG Yuk Wo

Mr Andrew Chiu Cheung MA

General Managers

Mr Frederick Hoi Kit CHAN

Mr Patrick Siu Cheung WAT

Company Secretary & Legal Counsel

Mr Michael Kin Wah YEUNG

Registered Office

Ground Floor, Chong Hing Bank Centre
24 Des Voeux Road Central, Hong Kong
Telephone : (852) 3768 1111
Facsimile : (852) 3768 1888
Telex : 75700 LCHB HX
SWIFT BIC : LCHB HK HH
Website : <http://www.chbank.com>
E-mail : info@chbank.com

Principal Legal Advisers

Anthony Chiang & Partners

Deacons

K C Ho & Fong

Kwan & Chow

Slaughter and May

Auditors

Deloitte Touche Tohmatsu

Share Registrar and Transfer Office

Computershare Hong Kong Investor Services Limited

Stock Codes and Short Names

The Stock Exchange of Hong Kong Limited's Stock Codes and Short Names in respect of the Bank's (i) shares and (ii) subordinated notes due 2016 are (i) 1111 (CHONG HING BANK) and (ii) 1510 (CH BANK N1612), respectively.

BIOGRAPHICAL DATA ABOUT DIRECTORS AND SENIOR MANAGEMENT

Board of Directors

Executive Directors

Mr LIU Lit Man, GBS, JP, FIBA

aged 78, is the Executive Chairman of the Bank. He joined the Bank in 1950 and has been its Director since 1955. He is also the Chairman of both Liu Chong Hing Investment Limited and Chong Hing Insurance Company Limited. His other directorships include those in The Hong Kong and China Gas Company Limited and COSCO Pacific Limited. He was a Director of Tung Wah Group of Hospitals, the President of the Hong Kong Chiu Chow Chamber of Commerce (presently Permanent Honorary President), a founder and a Permanent Honorary Chairman of the Chiu Chow Association Building (Property Holding) Limited, as well as the founder and the first Chairman of Teochew International Convention (now Permanent Honorary Chairman). Presently he is a Permanent Honorary Chairman of The Chinese General Chamber of Commerce, Hong Kong. Mr Liu is also a founder and a Manager of Liu Po Shan Memorial College, a Director of New Asia College of The Chinese University of Hong Kong, and the founder of Chiu Chow Association Secondary School. In 1975, he was appointed a Justice of the Peace and was elected Fellow of the International Banker Association. He had been a Member of the Consultative Committee for the Basic Law from 1985 to 1990 and was a Member of the Selection Committee of the First Government of the Hong Kong Special Administrative Region. He was a Member of the First Election Committee constituted under the Chief Executive Election Ordinance. Mr Liu was awarded the Gold Bauhinia Star by the Government of the Hong Kong Special Administrative Region in July 2001.

Dr LIU Lit Mo, LLD, MBE, JP

aged 70, is the Vice Chairman and an Executive Director of the Bank. He was appointed a Director in 1958 and was a Deputy Managing Director of the Bank from 1961 to 1973. Dr Liu is also the Managing Director of Liu Chong Hing Investment Limited and a Director of China Motor Bus Company Limited. As for community service, Dr Liu was the Chairman of Tung Wah Group of Hospitals in 1967 and is now serving as an Adviser of the Group. He had also been President of the Hong Kong Chiu Chow Chamber of Commerce, Chairman of Hong Kong Football Association and District Governor of District 3450, Rotary International. Presently, he is a member of the Board of Trustees of United College, The Chinese University of Hong Kong and a Manager of Liu Po Shan Memorial College. He was awarded Silver Jubilee medal by Her Majesty the Queen in 1977. Dr Liu was conferred an Honorary Doctor's Degree in Laws by the Lingnan University in 2005.

Mr LIU Lit Chi

aged 68, is the Managing Director and Chief Executive Officer of the Bank. Mr Liu, who was educated in Hong Kong and the United Kingdom, was appointed as a Director since 1958 and an Executive Director since 1961. Mr Liu is also an Executive Director of Liu Chong Hing Investment Limited since 1972 and holds directorship in a number of companies in Hong Kong and elsewhere.

Mr Don Tit Shing LIU

aged 46, is an Executive Director and Deputy Chief Executive Officer of the Bank. He graduated from Oxford University and is an associate member of the Institute of Chartered Accountants in England & Wales and a fellow of the Hong Kong Institute of Certified Public Accountants. Mr Liu joined the Bank in 1992.

Mr LAU Wai Man

aged 49, is an Executive Director and Deputy Chief Executive Officer in charge of the China and Overseas Banking Division and Personal Wealth Management Division of the Bank. He holds a Bachelor of Law degree and a Master of Business Administration degree. Mr Lau is a member of the Hong Kong Institute of Certified Public Accountants, a fellow of the Association of Chartered Certified Accountants and a Certified Financial Planner^{CM}. He was a senior associate of the Australian Institute of Bankers. Mr Lau joined the Bank as the Chief Auditor in 1988 and became a Director of the Bank in August 2001. He was appointed a Deputy Chief Executive Officer of the Bank in July 2007. Before joining the Bank, he had worked for an international bank and an international accounting firm.

Mr Wilfred Chun Ning LIU

aged 46, is an Executive Director in charge of the Securities Business Division of the Bank. He holds a Bachelor's degree in Economics from University of Newcastle-upon-Tyne (UK). He joined the Bank in 1993 and became a Director in 1998.

Mr Frank Shui Sang JIN

aged 50, is an Executive Director in charge of the Finance and Treasury Management Division of the Bank. He holds a Master of Business Administration degree from the City University in London, and is a certified public accountant (practising) registered in Hong Kong. Mr Jin joined the Bank in 1997 and became a Director of the Bank in August 2001. Before joining the Bank, he held senior positions in an international accounting firm and a listed company.

Mr Andrew Chiu Wing TSANG

aged 50, is an Executive Director in charge of the Information Technology Division of the Bank. He holds a Master of Science degree in Electronic Commerce and Internet Computing from the University of Hong Kong, and is a member of the Institute of Chartered Accountants in England and Wales and a fellow member of the Hong Kong Institute of Certified Public Accountants. Mr Tsang joined the Bank in 2000 and became a Director of the Bank in August 2005. Before joining the Bank, he held senior positions in an international accounting firm and a major international bank in Hong Kong.

Mr George Har Kar WONG

aged 55, is an Executive Director in charge of the Credit Risk Management Division of the Bank. He is a member of the Institute of Chartered Accountants in England & Wales and the Hong Kong Institute of Certified Public Accountants. Mr Wong joined the Bank in 2002 and became a Director of the Bank in August 2005. Before joining the Bank, he held senior positions in an international accounting firm and a major international bank in Hong Kong.

Non-executive Directors

Mr Timothy George FRESHWATER

aged 63, was redesignated from independent non-executive director, an office that he had held since April 1997, to non-executive director of the Bank in September 2004. He is a solicitor in the UK and Hong Kong and is a past President of the Law Society of Hong Kong. After graduating from Cambridge University, he joined the international law firm Slaughter and May in 1967 and remained with them for 29 years, leaving in July 1996 to join Jardine Fleming. He became Chairman of Jardine Fleming in 1999. In 2001, Mr Freshwater joined Goldman Sachs (Asia) L.L.C. and is now Vice Chairman.

Mr WANG Xiaoming

aged 52, has been the Executive Director of the Board of COSCO International Holdings Ltd. since January 2006. Mr Wang is also the Director and Financial Controller of COSCO (Hong Kong) Group Limited. Mr Wang graduated from Shanghai Maritime University, the PRC, majoring in accounting and has the senior accountant qualification awarded by Ministry of Communications of the PRC. Mr Wang had been the Deputy Manager of the Audit Department of China Ocean Shipping (Group) Company, Finance Manager of COSCO Bulk Carrier Co. Limited, Deputy General Manager of Finance Division of China Ocean Shipping (Group) Company and General Manager of COSCO Finance Co. Limited. He has extensive experience in corporate financial management.

Mr Andrew LIU

aged 52, a member of the Board since 1977, was redesignated from executive director to non-executive director of the Bank in May 1999. Mr Liu is also a director of Liu Chong Hing Investment Limited. He is the Chief Executive Officer of CCMP Capital Asia Pte Ltd (formerly known as “JP Morgan Partners Asia Pte Ltd”). Mr Liu, holder of a Master of Arts degree from the Oxford University in England, was a solicitor with Slaughter and May in London before joining Morgan Stanley & Co Inc in New York in 1981. Mr Liu was promoted to Managing Director in 1990 before relocating to Morgan Stanley Asia Limited in Hong Kong, where he assumed the position of President and Managing Director until his resignation in September 1997. Mr Liu remains associated with Morgan Stanley as an Advisory Director. He is a son of Mr Liu Lit Man.

Mr Eiichi YOSHIKAWA

aged 51, has been a member of the Board since July 2007. Mr Yoshikawa is Director, Regional Head for Hong Kong and General Manager of The Bank of Tokyo-Mitsubishi UFJ, Ltd, Hong Kong Branch. He joined The Bank of Tokyo, Ltd (currently The Bank of Tokyo-Mitsubishi UFJ, Ltd) in 1981 and has about 26 years of experience in banking. Mr Yoshikawa's expertise lies in the area of Corporate Banking, Treasury and Corporate Planning activities. During this period, Mr Yoshikawa has been appointed to work in Ministry of Finance of Japan (currently Financial Service Agency of Japan), New York Office of Treasury Division, Tokyo-Mitsubishi Securities Co., Ltd (currently Mitsubishi UFJ Securities Co., Ltd). He has been a Director of Mitsubishi UFJ Securities (HK) Holdings Limited since 13 March 2007. He served as General Manager of Osaka Corporate Banking Division No. 3 before he was appointed to the current position at The Bank of Tokyo-Mitsubishi UFJ, Ltd on 25 January 2007. Mr Yoshikawa graduated from The University of Tokyo in 1981 with a Bachelor's degree in Law.

Mr Christopher Kwun Shing LIU

aged 32, is a qualified solicitor in both England & Wales and Hong Kong. A holder of a Master of Arts degree in Jurisprudence from the University of Oxford, Mr Liu is currently a practising solicitor and partner of Deacons in Hong Kong. Mr Liu served as alternate director to Dr Liu Lit Chung, a former director of the Bank, from July 2000 to July 2002. He became a director of the Bank in July 2002.

Mr Alfred Cheuk Yu CHOW, JP

aged 57, a member of the Board since February 2003, was redesignated from independent non-executive director to non-executive director of the Bank in September 2004. He graduated from the University of Hong Kong with a Bachelor of Laws Degree and a Master of Social Sciences (Public Administration) Degree. With 17 years working experience in the civil service and over 25 years as a solicitor, Mr Chow is presently the senior partner of Kwan & Chow, Solicitors, a law firm in Hong Kong. He is also a China-Appointed Attesting Officer.

Mr MENG Qinghui

aged 52, has been the Executive Director of the Board of COSCO International Holdings Ltd. since March 2002. He is also the Managing Director of Finance Division of COSCO (Hong Kong) Group Limited and the Non-executive Director of Soundwill Holdings Limited. Mr Meng graduated from Central South University and has the PRC accountant qualification. He has extensive experience in corporate financial management and accounting and is also familiar with corporate financial planning.

Independent Non-executive Directors

Dr Robin Yau Hing CHAN, GBS, LLD, JP

aged 75, a member of the Board since October 1981, was redesignated from non-executive director to independent non-executive director of the Bank in April 2005. Dr Chan is the Ex-officio Life Honorary Chairman of The Chinese General Chamber of Commerce, Hong Kong and the Vice Chairman of All-China Federation of Returned Overseas Chinese. Dr Chan had been a Deputy to the Chinese National People's Congress from March 1988 to February 2008. Dr Chan, the Chairman of Asia Financial Holdings Limited, also serves as an independent non-executive director for certain other listed companies.

Mr Wanchai CHIRANAKHORN

aged 68, an Independent Non-executive Director since September 1998, is the Chairman of Executive Board of Directors of C Wans Assets Co, Ltd. He has more than 25 years of experience as an international banker. Upon graduation from Baptist College, Hong Kong in 1964, he served in banks in Hong Kong, London, Bangkok and Malaysia. He joined the Bank in 1985 and became a Director in 1987. Before his departure in May 1995, Mr Chiranakhorn served as an Executive Director in charge of the Overseas Business Development Department. He was a Non-executive Director from May 1995 to September 1998.

Mr CHENG Yuk Wo

aged 47, has been an Independent Non-executive Director of the Bank since September 2004. Mr Cheng is also a member of the Bank's Audit Committee and Remuneration Committee. Mr Cheng, a co-founder of a Hong Kong merchant banking firm, is currently the proprietor of a certified public accountant practice in Hong Kong. Mr Cheng obtained a Master of Science (Economics) degree in Accounting and Finance from the London School of Economics, England and a Bachelor of Arts (Honours) degree in Accounting from the University of Kent, England. He is a fellow of the Institute of Chartered Accountants in England and Wales and the Hong Kong Institute of Certified Public Accountants, and a member of the Institute of Chartered Accountants of Ontario, Canada. Mr Cheng has more than 20 years of expertise in financial and corporate advisory services in mergers, acquisitions and investments. He had worked at Coopers and Lybrand (now known as PricewaterhouseCoopers) in London and Swiss Bank Corporation (now known as UBS AG) in Toronto, and held senior management positions in a number of Hong Kong listed companies. Mr Cheng also serves as an independent non-executive director and non-executive director for certain other listed companies.

Mr Andrew Chiu Cheung MA

aged 66, has been an Independent Non-executive Director of the Bank since August 2007. Mr Ma is a founder and former director of Andrew Ma DFK (CPA) Limited. He is presently a director of Mayee Management Limited. Mr Ma has more than 30 years' experience in the field of accounting and finance. He received his bachelor's degree in economics from The London School of Economics and Political Science (University of London) in England. Mr Ma is a fellow member of the Institute of Chartered Accountants in England & Wales and a fellow member of the Hong Kong Institute of Certified Public Accountants. He is also a fellow member of The Hong Kong Institute of Directors and The Taxation Institute of Hong Kong.

General Managers

Mr Frederick Hoi Kit CHAN

aged 47, General Manager, is the head of Operations Division. He graduated from Imperial College, University of London in Computing Science and obtained a Master of Business Administration degree from Henley Management College, U.K. He is a fellow of the Institute of Chartered Accountants in England & Wales, a member of the British Computer Society and a fellow of the Hong Kong Institute of Certified Public Accountants. Mr Chan has more than 20 years of experience in the financial services industry and worked for an international accounting firm and major international banks in London and Hong Kong in financial reporting and strategic management before joining the Bank in 2004.

Mr Patrick Siu Cheung WAT

aged 54, General Manager, is the head of Retail Banking Division. He holds a Bachelor of Arts degree from the University of Hong Kong in 1975. He has held senior positions in Finance, Business Development, Operations, Internal Control and Quality functions with major US banks in Hong Kong and UK. He has been trained in TQM (Total Quality Management) and as Black Belt in Six Sigma quality programs. Mr Wat is also responsible for change management and productivity improvements since joining the Bank in 2003.

Company Secretary & Legal Counsel

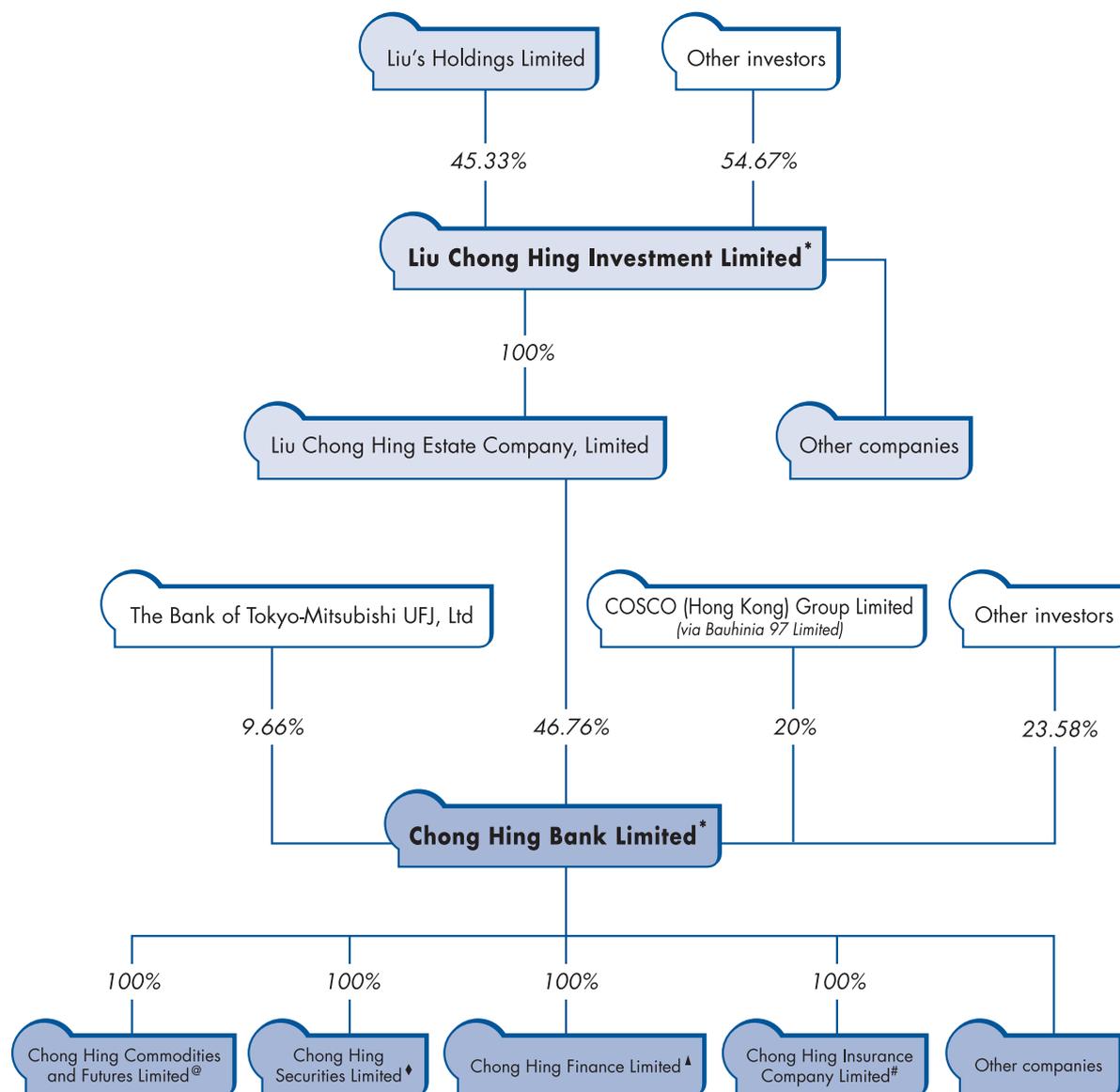
Mr Michael Kin Wah YEUNG

aged 51, obtained a Bachelor of Arts degree in legal studies, political science and philosophy from Rice University (Texas, USA) in 1980 and a Doctor of Jurisprudence degree from the School of Law of The University of Texas at Austin (Texas, USA) in 1983. Mr Yeung, who is registered in the Master Roll of Attorneys maintained by the Supreme Court of Illinois in the United States, had served as the company secretary of FPB Bank Holding Company Limited (the then Hong Kong-listed banking arm of the First Pacific Group) and South China Morning Post (Holdings) Limited (now known as SCMP Group Limited) before resuming his position as the company secretary of the Bank in 1997.

[#] Member of the Liu's family

ABRIDGED CORPORATE STRUCTURE

as at 5 March 2008



* Listed on The Stock Exchange of Hong Kong Limited

@ Registered with The Hong Kong Futures Exchange Limited as a participant

♦ Registered with The Stock Exchange of Hong Kong Limited as a participant

▲ Licensed under the Banking Ordinance as a deposit-taking company

Licensed under the Insurance Companies Ordinance as an insurance company

SHARE TRADING SUMMARY

for the year ended 31 December 2007

Trading of shares in Chong Hing Bank Limited*, a constituent stock of the Hang Seng Composite Index Series, on The Stock Exchange of Hong Kong Limited (“HKSE”) during 2007

Month	Unit Price (HK\$) (average for the month)				Monthly Turnover		Hang Seng Index# (average for the month)
	Open	High	Low	Close	Number of Shares	HK\$	Close
January	19.870	20.294	19.494	19.971	12,278,129	256,435,000	20,197.23
February	21.000	21.208	20.697	20.938	3,579,111	74,618,000	20,484.37
March	20.024	20.239	19.790	20.086	6,751,497	135,909,000	19,338.56
April	20.809	20.944	20.546	20.681	3,144,603	65,310,000	20,439.39
May	18.810	18.967	18.624	18.701	5,787,894	108,413,000	20,727.45
June	17.929	17.996	17.802	17.881	6,568,050	117,332,000	21,214.10
July	18.750	18.938	18.596	18.801	5,835,095	110,080,000	22,878.18
August	18.179	18.414	17.852	18.087	5,276,100	96,126,000	22,320.68
September	17.406	17.506	17.228	17.305	5,100,085	88,194,000	25,002.90
October	17.144	17.331	16.988	17.150	10,206,381	175,709,000	29,152.61
November	17.708	18.085	17.561	17.852	7,645,971	138,602,000	28,287.49
December	18.342	18.581	18.025	18.316	6,152,273	113,390,000	28,052.61
Average for the year	18.831	19.042	18.600	18.814	6,527,099	123,343,167	23,174.63

* Authorized	: 600,000,000 shares	Par value	: HK\$0.500 per share
Issued and fully-paid	: 435,000,000 shares	Board lot	: 1,000 shares
HKSE stock code	: 1111		
Year high	: HK\$24.200 (15 January)	Historic high	: HK\$27.600 (15 July 1997)
Year low	: HK\$16.420 (17 August)	Historic low	: HK\$3.650 (24 August 1998)

# Year high	: 31,958.41 (30 October)	Historic high	: 31,958.41 (30 October 2007)
Year low	: 18,659.23 (5 March)	Base value	: 100.00 (31 July 1964)

SHAREHOLDERS' CALENDAR

as at 5 March 2008

9 August 2007	Interim results for the first half of 2007 announced.
22 August 2007	Interim Report 2007 despatched.
12 through 14 September 2007 (both days inclusive)	Register of Members closed for the purpose of ascertaining dividend entitlements.
20 September 2007	Interim cash dividend for 2007 of HK\$0.21 per share paid.
5 March 2008	Final results for the year of 2007 announced.
31 March 2008	Annual Report 2007 will be despatched.
23 through 25 April 2008 (both days inclusive)	Register of Members will be closed for the purpose of ascertaining dividend entitlements.
30 April 2008	2008 Annual General Meeting will be held.
2 May 2008	If approved by shareholders at the 2008 Annual General Meeting, the final cash dividend for 2007 of HK\$0.44 per share will be paid.

NOTICE OF ANNUAL GENERAL MEETING

NOTICE IS HEREBY GIVEN THAT the annual general meeting of the shareholders of Chong Hing Bank Limited (the “Bank”) for the year of 2008 will be held on the 27th Floor, Chong Hing Bank Centre, 24 Des Voeux Road Central, Hong Kong on Wednesday, 30 April 2008 at 11:15 am for the purposes of conducting the following items of ordinary and special business:

Ordinary business

- (1) To receive and adopt the Financial Statements and the Reports of the Directors and Auditors for the year ended 31 December 2007.
- (2) To declare the final cash dividend for the year ended 31 December 2007.
- (3) To re-elect directors and fix their and the other directors’ remuneration.
- (4) To re-appoint auditors and authorise the directors to fix the auditors’ remuneration.

Special business

As special business, to consider and, if thought fit, pass, with or without modification, the following ordinary resolutions:

- (5) **THAT**
 - (a) the exercise by the directors during the Relevant Period of all the powers of the Bank to purchase Shares, subject to and in accordance with all applicable laws, be and is hereby generally and unconditionally approved;
 - (b) the aggregate nominal amount of Shares which may be purchased on The Stock Exchange of Hong Kong Limited or any other stock exchange recognised for this purpose by the Securities and Futures Commission of Hong Kong and The Stock Exchange of Hong Kong Limited under the Hong Kong Code on Share Repurchases pursuant to the approval in paragraph (a) above shall not exceed 10 per cent of the aggregate nominal amount of Shares in issue at the date of the passing of this resolution, and the said approval be and is hereby limited accordingly; and
 - (c) for the purpose of this resolution:

“Relevant Period” means the period from the passing of this resolution until whichever is the earliest of:

 - (i) the conclusion of the next annual general meeting of the Bank;
 - (ii) the expiration of the period within which the next annual general meeting of the Bank is required by law to be held; or
 - (iii) the revocation or variation of the authority given under this resolution by ordinary resolution of the shareholders in general meeting.

“Shares” means shares of all classes in the capital of the Bank including, without limitation, shares of HK\$0.50 each of the Bank.

NOTICE OF ANNUAL GENERAL MEETING

(6) THAT

- (a) subject to paragraph (c), the exercise by the directors of the Bank during the Relevant Period of all the powers of the Bank to allot, issue and deal with additional shares in the capital of the Bank and to make or grant offers, agreements and options which might require the exercise of such powers be and is hereby generally and unconditionally approved;
- (b) the approval in paragraph (a) shall authorise the directors of the Bank during the Relevant Period to make or grant offers, agreements and options which would or might require the exercise of such power after the end of the Relevant Period;
- (c) the aggregate nominal amount of share capital allotted or agreed conditionally or unconditionally to be allotted (whether pursuant to an option or otherwise) by the directors of the Bank pursuant to the approval in paragraph (a), otherwise than pursuant to (i) any Rights Issue, (ii) any scrip dividend or similar arrangement providing for the allotment and issue of shares in lieu of the whole or part of a dividend on shares of the Bank in accordance with the Articles of Association of the Bank, or (iii) any exercise of options granted under the share option scheme of the Bank adopted on 25 April 2002, shall not exceed the aggregate of:
 - (aa) 20 per cent of the aggregate nominal amount of the shares in the capital of the Bank in issue at the date of the passing of this resolution; and
 - (bb) (if the directors are so authorised by a separate ordinary resolution of the shareholders of the Bank) the nominal amount of any share capital of the Bank repurchased by the Bank subsequent to the passing of this resolution,

and the said approval be and is hereby limited accordingly; and

- (d) for the purpose of this resolution:

“Relevant Period” means the period from the passing of this resolution until whichever is the earliest of:

- (i) the conclusion of the next annual general meeting of the Bank;
- (ii) the expiration of the period within which the next annual general meeting of the Bank is required by law to be held; or
- (iii) the revocation or variation of the authority given under this resolution by ordinary resolution of the shareholders in general meeting.

“Rights Issue” means an offer of shares open for a period fixed by the directors of the Bank to holders of shares of the Bank or any class thereof on the register on a fixed record date in proportion to their then holdings of such shares or class thereof (subject to such exclusion or other arrangements as the directors of the Bank may deem necessary or expedient in relation to fractional entitlements or having regard to any restrictions or obligations under the laws of, or the requirements of any recognised regulatory body or any stock exchange in, any territory outside Hong Kong).

NOTICE OF ANNUAL GENERAL MEETING

- (7) **THAT** the directors of the Bank be and are hereby authorised to exercise the powers of the Bank referred to in paragraph (a) of the resolution set out as Resolution 6 in the notice convening this meeting in respect of the share capital of the Bank referred to in sub-paragraph (bb) of paragraph (c) of that resolution.

Any other ordinary business

- (8) To transact any other ordinary business.

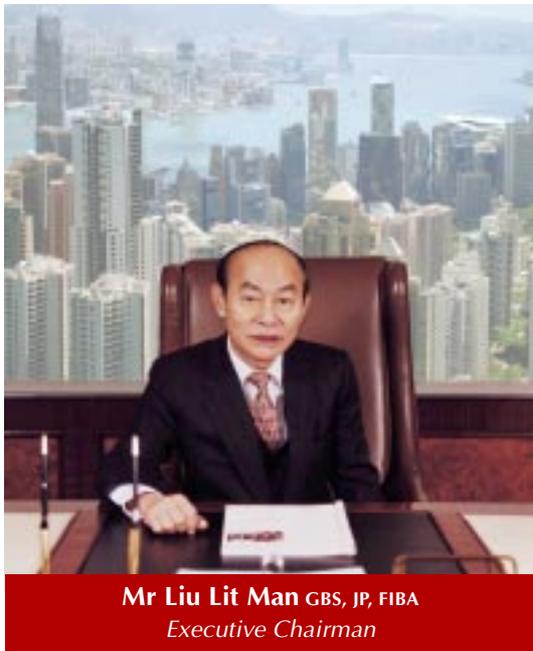
By Order of the Board
Michael K W Yeung
Company Secretary

31 March 2008

Notes:

- i. A shareholder entitled to attend and vote at the 2008 annual general meeting of the shareholders is entitled to appoint a proxy to attend and vote in his stead. A proxy does not have to be a shareholder of the Bank. Forms of proxy are to be lodged with the registered office of the Bank at Ground Floor, Chong Hing Bank Centre, 24 Des Voeux Road Central, Hong Kong not later than 48 hours before the time for the holding of the 2008 annual general meeting of the shareholders and any adjournment thereof.
- ii. The Register of Members of the Bank will be closed from Wednesday, 23 April 2008 to Friday, 25 April 2008 (both days inclusive), during which period no transfer of shares can be registered. In order to be entitled to attend and vote at the 2008 annual general meeting of the shareholders, and to qualify for the final dividend in question, all transfer documents, together with the relevant share certificates, must be lodged for registration with the Bank's share registrar and transfer office, Computershare Hong Kong Investor Services Limited of Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong, not later than 4:30 pm on Tuesday, 22 April 2008.
- iii. The Bank's Annual Report 2007 includes an Explanatory Statement on Resolutions 5 through 7 in question, information on the retiring directors to be re-elected at the 2008 annual general meeting of the shareholders, and the procedures for demanding and conducting a poll.

EXECUTIVE CHAIRMAN'S STATEMENT



Mr Liu Lit Man GBS, JP, FIBA
Executive Chairman

Economic Review

In 2007, the Hong Kong economy maintained its upward trend. Strong internal demand was a major booster for economic growth. Employment market saw great improvement with unemployment rate dropped to a low level of 4%. Consumption sentiment and the performance of all sectors were strong on the back of increasing individual income. Stimulated by the tide of initial public offerings and a series of favourable developments such as the expansion of the investment scope of the Qualified Domestic Institutional Investors and the listing of red chip enterprises in the Mainland's A-share market, the stock market saw the Hang Seng Index hit its all-time high of 31,958 points with total market value exceeding HK\$23,000 billion. The Index's annual growth of 39% in the year was the highest

ever since 1999. The growth of the property market has further picked up momentum. The transaction volume of property market skyrocketed by an annual rate of approximately 40% to over 140,000, an all-time high since 1997. Meanwhile, with the rising food prices, appreciation of Renminbi, the slumping US dollar and the surging oil price, Hong Kong's inflation has been intensified in the year. Exports recorded significant growth, due primarily to the prosperity of the mainland and emerging markets that substantially offset the negative impacts of the slackening US demand.

The global economy has been overshadowed by the worsening US subprime mortgage crisis. Resulting from such an uncertain market environment were volatile global financial markets and repeated stock market plunges. In September, the US Federal Reserve Board lowered the interest rate by 50 basis points, the first cut ever since June 2003, whereas a number of central banks sought to stabilise their financial markets by pumping funds into the market. On the threshold of 2008, the US Federal Reserve Board, out of the blue, cut the interest rate by 75 basis points in January, the most substantial slash in recent years, with a view to revitalising the economy. The market believes the US Federal Reserve Board will continue the cut following its five interest rate reductions of 225 basis points in total over the five months since September 2007.

EXECUTIVE CHAIRMAN'S STATEMENT

Results Announcement

The Bank's results for 2007 show a slight improvement. For the financial year of 2007, on an audited, consolidated basis, profit attributable to shareholders amounted to HK\$505,032,000, an increase of 0.38% over that for the year before. Total customers' deposits increased 10.34% to HK\$60,327,437,000. Total loans to customers (after accounting for impairment allowances) increased 18.03% to 31,873,474,000. On 31 December 2007, the Bank's loan portfolios were made up as follows: property developments and investments (27.24%), personal real estate purchases (16.98%), financial and securities concerns (9.05%), trade finance (2.90%), wholesale and retail trade (2.63%), manufacturing, transportation and other businesses (24.36%), loans outside Hong Kong (11.13%), and others (5.71%). Capital adequacy ratio decreased 8.79% to 14.22% at the end of 2007, while average liquidity ratio for 2007 increased 0.31% to 55.82%. Loan-to-deposit ratio increased 7.5% to 48.15%. Total assets, having increased 9.55% to HK\$69,052,401,000. Shareholders' funds (before final dividend), compared with the shareholders' funds for the previous year, increased 3.62% to HK\$6,270,788,000. Your board has recommended paying the final cash dividend of HK\$0.44 per share for the financial year of 2007 to shareholders whose names appear in the Register of Members at the close of business on Friday, 25 April 2008. Total dividends for the financial year of 2007 (including the interim cash dividend of HK\$0.21 per share paid earlier) amounted to HK\$0.65 per share.

Profit Analysis

On an audited, consolidated basis, net interest income rose 17.15% from that of 2006 to HK\$970,613,000 in 2007. Interest spread decreased 4.64% to 1.44%. After accounting for the net fee and commission income, which amounted to HK\$283,412,000, and the other operating income, which amounted to HK\$166,669,000, total operating income was HK\$1,420,694,000 and total operating expense was HK\$642,894,000. Cost-to-income ratio decreased 13.54% to 45.25%. Operating profit before impairment allowances, fair value adjustments and net (loss) gain on disposal increased 44.39% to HK\$777,800,000. The Bank made impairment allowances in the amount of HK\$82,922,000 for 2007, an increase of 38.66% against those made for 2006. As of 31 December 2007, the Bank's investment portfolio contained income notes issued by structured investment vehicles ("SIVs"), which were categorised as available-for-sale investments. The total amounts invested in these SIVs were HK\$568,212,000 (0.82% of total assets). The Bank evaluates such investments for impairment on a regular basis. Impairment losses of HK\$369,627,000 have been recognised for the year ended 31 December 2007 primarily due to downgrade of credit ratings and increase of funding costs for the SIVs. After accounting for the impairment allowances as well as the charge for taxation, profit attributable to shareholders amounted to HK\$505,032,000 (an increase of 0.38%), translating into earnings of HK\$1.16 per share. Net asset value per share (before final dividend), compared with the net asset value per share for the previous year, rose 3.62% to HK\$14.42.

EXECUTIVE CHAIRMAN'S STATEMENT

Business Review

Loan Business

Property mortgage remained a focus of the Bank during the year. After the launch of preferential residential mortgage loan schemes, the Bank initiated the “Lowest Interest Rate Guarantee for Residential Property Valued at HK\$2 Million” in March. It boosted the number and total amount of successfully-approved mortgage loans by over 100% in the second quarter, which outperformed the market average. The new mortgage loans drawn down grew by around 160% during the year. With effective promotion campaigns and attractive product designs, newly-approved personal loan amount of the Bank increased by an annual rate of approximately 47%. Tax loan amount also recorded a twofold increase. The new online application channel for personal loan was proven effective in attracting young customers.

Card Business

The Bank is committed to continually launching new offers and improving its service for the development of its card business. It has cooperated with various organisations for launching affinity cards to diversify its customer base. In June, to celebrate the 10th anniversary of Hong Kong's handover, China UnionPay Co., Ltd and the Bank jointly launched the first-ever limited edition of “China Unionpay Gift Card” in Hong Kong. In September, the Bank presented an affinity card named “Wah Yan One Family VISA Card” jointly with Wah Yan One Family Foundation. In October, “The Link Credit Card” was introduced with The Link Management Limited to bring shopping privileges to The Link's tenants and the public. A six-week large-scale road show promotion campaign was held for the launch of “The Link Credit Card” at 34 locations, including selected



Mr Don Liu Tit Shing, Executive Director and Deputy Chief Executive Officer of the Bank, and Mr Victor So Hing Woh, then Executive Director and Chief Executive Officer of The Link Management Limited, signed the agreement for “The Link Credit Card”.



Mr Liu Lit Chi, Managing Director and Chief Executive Officer of the Bank (left), and Mr Victor So Hing Woh, then Executive Director and Chief Executive Officer of The Link Management Limited (right), together with renowned gourmet, Mr Chua Lam, officiated at the launching ceremony of “The Link Credit Card”.

branches of the Bank and shopping malls managed by the Link. The number of participation of our front-line and department staff in this event was over 2,000 and more than 20,000 applications for the credit card were received.



Large-scale roadshows were held for promoting “The Link Credit Card” at shopping malls managed by the Link, with participation by the Bank's staff standing at 2,000-plus person-times.

Securities Business

In 2007, Hang Seng Index reached its historic high and the local stock market was fueled by exuberant investment sentiment. To capture such a favourable opportunity, Chong Hing Securities Limited, a wholly-owned subsidiary of the Bank, timely launched a series of privileges and services and established its first large-scale securities centre in Yuen Long. The centre, equipped with nearly 100 computers for customers to access real-time stock prices and other market information, commenced operation in September and the average daily utilisation rate of its quoting facilities exceeded 90%. In November, it opened another securities centre in Kwun Tong. The popularity of the centres was reflected in the significant growth of its overall business. Meanwhile, in order to attract young customers, it started to promote the online securities trading platform in the third quarter. Satisfactory results were achieved with prominent increase in the number of online securities accounts and transactions.



The first large-scale securities centre in Yuen Long of Chong Hing Securities Limited commenced operation in September 2007.



Mr Lau Wai Man, Executive Director and Deputy Chief Executive Officer of the Bank (right), and Mr Liu Yong Chun, Executive Vice President of China UnionPay Company Limited, officiated at the lighting ceremony at the "CUP Remittance" Press Conference.

China Business

As the Hong Kong economy continued to tie in closely with that of the Mainland with increasingly frequent capital flows, China UnionPay Co., Ltd and the Bank worked together and initiated "CUP Remittance", the first-ever instant remittance service between Hong Kong and the Mainland. The service reduced the time needed for fund transfer and satisfied the increasing demand of the customers. To further speed up the development of the China business, the Bank has set up a branch in each of Shantou and Macau and a representative office in each of Guangzhou and Shanghai. At the beginning of 2008, the Renminbi business of the Shantou Branch was approved by the relevant Chinese authorities, facilitating its further business expansion in mainland China.

EXECUTIVE CHAIRMAN'S STATEMENT

Corporate Responsibility

In 2007, the Bank strived to fulfill its mission as a “community bank” and provided comprehensive and quality banking services to the community. To further expand its service network, the Bank has opened 5 new branches, one in each of Jordan, Chai Wan, Kowloon Bay, Sau Mau Ping and Ho Man Tin, during the year. As at the end of the year, the Bank operated one headquarters and 47 branches in Hong Kong. More new branches are expected to be opened during the second quarter of 2008. Moreover, the Bank continued to support community



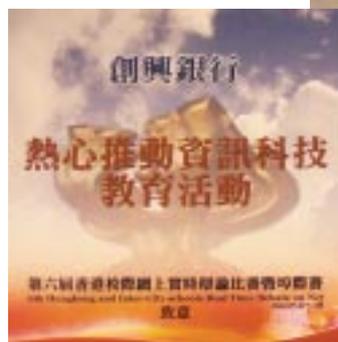
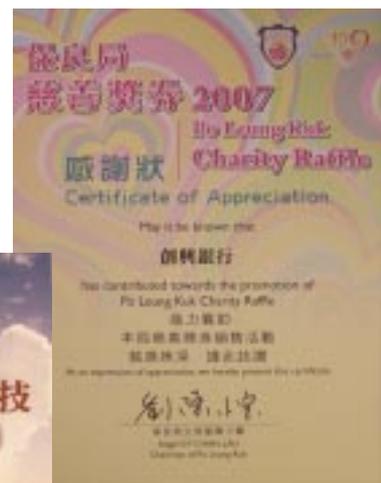
Kowloon Bay Branch commenced business on 23 August 2007.

activities through donation to non-profit making charities, sponsorship and volunteer work and was rewarded the Caring Company Logo 2007/08 by the Hong Kong Council of Social Service. The Bank encouraged its guests to make cash donation instead of sending flower bouquets to celebrate its renaming and the grand opening of its new headquarters. With the guests' overwhelming response, the Bank contributed an amount equivalent to the overall donations on a dollar-for-dollar basis to fund charitable educational projects in the impoverished areas in mainland China. During the year, part of the fund has been allocated to develop new teaching buildings for four rural primary schools in Kunming City and Baoshan City of Yunnan Province and Anlong County of Guizhou Province.

On the other hand, the Bank has been supporting the development of small and medium enterprises in Hong Kong and providing flexible banking services which suited their needs. The Bank was rewarded with the “SME's Best Partner Award 2007” by the Hong Kong Chamber of Small and Medium Business for its contribution.



Mr Frederick Chan Hoi Kit, General Manager, Operations Division of the Bank, received the “Caring Company 2007/08” logo awarded by the Hong Kong Council of Social Service to the Bank on 21 February 2008.



Directorate Changes

On 11 July 2007, Mr Lau Wai Man, Executive Director of the Bank, was appointed a Deputy Chief Executive Officer, and Mr Xu Minjie and Mr Eiichi Yoshikawa were appointed non-executive directors of the Bank by the board. Mr Toshiaki Arai resigned as a non-executive director of the Bank because of reallocation of duties within the Bank of Tokyo-Mitsubishi UFJ Group and Dr Sun Jiakang resigned as a non-executive director of the Bank because of reallocation of duties within the COSCO Group on that same day. Mr Andrew Chiu Cheung Ma was appointed an independent non-executive director of the Bank by the board on 9 August 2007. On 5 March 2008, Mr Xu Minjie and Mr Wang Zhi resigned as non-executive directors of the Bank because of the disposal of COSCO Pacific Limited's 20 percent shareholding interest in the Bank to COSCO (Hong Kong) Group Limited, and Mr Wang Xiaoming and Mr Meng Qinghui were appointed non-executive directors of the Bank by the board on that same day.

Prospects

It is anticipated that Hong Kong's economic growth will continue to be driven by internal demand this year. With wealth effects resulted from the fall of interest rate and the surge of asset prices, domestic consumption will remain its healthy upward trend. The strong momentum of the economies of the Mainland and the emerging markets will continue to be the main support of Hong Kong's export sector. Under the pressure arising from the Renminbi appreciation and the weakening US dollar, inflation in Hong Kong is prone to intensify dramatically.

It is expected the development of the global economy will be in steady pace. Despite the concern about the spread of the US subprime mortgage crisis, 2008 is the US presidential election year and stabilising measures for addressing the financial crisis of the nation are expected to be introduced. This development will also be a focus of the world.

Intense competition is inevitable in the Hong Kong banking sector where challenges ahead include the introduction of the new regulations, rising cost and loss of human resources. Yet, the sound foundation of the Hong Kong economy, desirable business environment and the close linkage with the mainland market all favour the optimistic economic prospects of Hong Kong. Ushering in its 60th anniversary this year, the Bank will strive to provide better quality and more innovative services and products by leveraging on its continuous business growth. It will also be committed to both becoming the most popular community bank and maximising the returns for shareholders.

Finally, on behalf of the board, I would like to wholeheartedly thank our customers, business partners and shareholders for their long-standing trust and support for the Bank, not to mention my fellow directors for the exercise of their wise judgment and all of our staff members for their unfailing dedication.

By Order of the Board

Liu Lit Man

Executive Chairman

5 March 2008

DIRECTORS' REPORT

The directors have pleasure in submitting their annual report and the audited consolidated financial statements for the year ended 31 December 2007.

PRINCIPAL ACTIVITIES

The Bank is engaged in the provision of banking and related financial services. The principal activities of its principal subsidiaries are set out in note 20 to the consolidated financial statements.

BUSINESS

The Group's total operating income (net of interest expense and fee and commission expense) is analysed and reported by significant business classes as follows:

	2007 HK\$'000	2006 HK\$'000
Corporate and retail banking	685,674	618,561
Treasury activities	424,754	372,117
Securities dealing activities	209,968	83,381
Other banking-related services	<u>100,298</u>	<u>56,169</u>
	<u><u>1,420,694</u></u>	<u><u>1,130,228</u></u>

The corporate and retail banking services provided by the Group are principally lending and trade finance facilities, consumer financing, overdraft facilities, mandatory provident fund services, provision of fixed deposits, current and savings accounts, credit cards and personal wealth management services. The Group also provides fully automated telephone and internet banking services to its customers. Other banking-related services offered include remittance and money exchange, safe deposit boxes, autopay and direct debit services.

Treasury activities mainly comprise inter-bank placement and deposit transactions, management of overall interest rate risk and liquidity of the Group and centralised cash management. Income from foreign exchange activities is principally generated from services provided to customers in the form of foreign exchange trading and forward contracts.

Securities dealing activities of the Group include securities trading, stockbroking and futures broking.

Other banking-related services of the Group include investment holding, insurance, other investment advisory services and property investments.

MAJOR CUSTOMERS

The directors believe that the five largest customers of the Group accounted for less than 30% of the total of interest income and operating income of the Group for the year.

RESULTS AND STATE OF AFFAIRS

The results of the Group for the year ended 31 December 2007 are set out in the consolidated income statement on page 39.

The state of affairs of the Group and the Bank as at 31 December 2007 are set out in the balance sheets on pages 40 and 41 respectively.

DIVIDENDS

An interim dividend of HK\$0.21 per share amounting to HK\$91,350,000 was paid to the shareholders during the year. The directors now recommend the payment of a final dividend for the year ended 31 December 2007 of HK\$0.44 per share amounting to HK\$191,400,000 to the shareholders on the Register of Members on 25 April 2008 and the retention of the remaining profit for the year.

SHARE CAPITAL

Details of the Bank's share capital are set out in note 27 to the consolidated financial statements. There was no movement in the Bank's share capital during the year.

RESERVES

Movements in the reserves of the Group and the Bank during the year are set out in the consolidated statement of changes in equity on pages 42 to 43 and note 28 to the consolidated financial statements, respectively.

INVESTMENT PROPERTIES

The Group's investment properties were revalued at 31 December 2007. The net increase in fair value arising on the revaluation, which has been credited directly to the consolidated income statement, amounted to HK\$14,391,000. During the year, the Group disposed of investment properties with a total carrying amount of HK\$36,400,000 for a net consideration of HK\$50,820,000, resulting in a net gain on disposal of HK\$14,420,000. Details of the investment properties of the Group and the Bank are set out in note 22 to the consolidated financial statements.

PROPERTY AND EQUIPMENT

Details of the movements in the property and equipment of the Group and the Bank are set out in note 23 to the consolidated financial statements.

SHARE OPTION SCHEME

The Bank's share option scheme (the "Scheme") was adopted pursuant to a resolution passed on 25 April 2002. Particulars of the Scheme are set out in note 30 to the consolidated financial statements. No options have been granted under the above-mentioned Scheme since the Scheme was adopted.

DIRECTORS' REPORT

DIRECTORS

The directors of the Bank during the year and up to date of this report are:

Executive Directors

Mr LIU Lit Man, GBS, JP, FIBA	<i>(Executive Chairman)</i>
Dr LIU Lit Mo, LLD, MBE, JP	<i>(Vice Chairman)</i>
Mr LIU Lit Chi	<i>(Managing Director and Chief Executive Officer)</i>
Mr Don Tit Shing LIU	<i>(Deputy Chief Executive Officer)</i>
Mr LAU Wai Man	<i>(Deputy Chief Executive Officer)</i>
Mr Wilfred Chun Ning LIU	
Mr Frank Shui Sang JIN	
Mr Andrew Chiu Wing TSANG	
Mr George Har Kar WONG	

Non-executive Directors

Mr Timothy George FRESHWATER
Mr WANG Xiaoming
Mr Andrew LIU
Mr Eiichi YOSHIKAWA
Mr Christopher Kwun Shing LIU
Mr Alfred Cheuk Yu CHOW, JP
Mr MENG Qinghui

Independent Non-executive Directors

Dr Robin Yau Hing CHAN, GBS, LLD, JP
Mr Wanchai CHIRANAKHORN
Mr CHENG Yuk Wo
Mr Andrew Chiu Cheung MA

Mr Lau Wai Man, executive director, was appointed as deputy chief executive officer on 11 July 2007. Mr Eiichi Yoshikawa (who was appointed as non-executive director on 11 July 2007), Mr Andrew Chiu Cheung Ma (who was appointed as independent non-executive director on 9 August 2007), Mr Wang Xiaoming and Mr Meng Qinghui (both were appointed as non-executive directors on 5 March 2008) shall retire and offer themselves for re-election at the forthcoming annual general meeting in accordance with Article 85 of the Bank's Articles of Association. Mr Toshiaki Arai and Dr Sun Jiakang resigned on 11 July 2007, and Mr Xu Minjie (who was appointed on 11 July 2007) and Mr Wang Zhi resigned on 5 March 2008, all as non-executive directors.

Article 101 of the Bank's Articles of Association stipulates that, among other things, one-third of the directors for the time being, who have been longest in office since their last election, shall be subject to retirement by rotation and re-election at each annual general meeting. Accordingly, Mr Lau Wai Man, Dr Robin Yau Hing Chan, Mr Wilfred Chun Ning Liu, Mr Frank Shui Sang Jin and Mr Cheng Yuk Wo shall retire and offer themselves for re-election at the forthcoming annual general meeting.

DIRECTORS' SERVICE CONTRACTS

No director proposed for re-election at the forthcoming annual general meeting has a service contract, which is not determinable by the Bank within one year without payment of compensation, other than statutory compensation.

DIRECTORS' (INCLUDING THE CHIEF EXECUTIVE OFFICER'S) INTERESTS AND SHORT POSITIONS IN SECURITIES

As at 31 December 2007, the interests and short positions of the directors (including the chief executive officer) in the securities and underlying securities of the Bank and its associated corporations (under Part XV of the Securities and Futures Ordinance (the "SFO")), as recorded in the register required to be kept under Section 352 of the SFO, were as follows:

Interests in securities

Director's name	Number of ordinary shares in the Bank				Percentage of issued share capital
	Personal interests	Spousal interests	Corporate interests	Total interests	
Liu Lit Man	3,447,928	—	243,407,628 <i>Note (1)</i>	246,855,556	56.74840
Liu Lit Mo	1,009,650	—	243,407,628 <i>Note (1)</i>	244,417,278	56.18788
Liu Lit Chi	313,248	—	245,670,839 <i>Notes (1) & (2)</i>	245,984,087	56.54807
Don T S Liu	15,000	—	—	15,000	0.00345
Robin Y H Chan	48,400	—	1,181,000 <i>Note (3)</i>	1,229,400	0.28262
Timothy G Freshwater	396	—	—	396	0.00009
Andrew Liu	60,000	—	—	60,000	0.01379

Notes:

- (1) 243,407,628 shares in the Bank are attributed as follows:
 - (i) 203,407,628 shares held by public listed Liu Chong Hing Investment Limited's wholly-owned subsidiary, Liu Chong Hing Estate Company, Limited ("Liu Chong Hing Estate"), in which each of Messrs Liu Lit Man, Liu Lit Mo and Liu Lit Chi is deemed under the SFO to be interested through Liu's Holdings Limited, a private company holding approximately 45% of Liu Chong Hing Investment Limited's issued and fully-paid share capital; and
 - (ii) 40,000,000 shares held by The Bank of Tokyo-Mitsubishi UFJ, Ltd ("Bank of Tokyo-Mitsubishi UFJ"). Pursuant to an agreement in 1994, Bank of Tokyo-Mitsubishi UFJ has granted an option to Liu Chong Hing Estate exercisable at any time during the term of that agreement to purchase all such shares and Bank of Tokyo-Mitsubishi UFJ is required to offer to sell all such shares to Liu Chong Hing Estate in certain circumstances. By virtue of the interests of Messrs Liu Lit Man, Liu Lit Mo and Liu Lit Chi in Liu Chong Hing Estate through Liu's Holdings Limited, each of them is deemed under the SFO to be interested in such shares.
- (2) 2,263,211 shares in the Bank are held by Alba Holdings Limited, shareholders of which include Mr Liu Lit Chi and his associates. Accordingly, Mr Liu Lit Chi is deemed under the SFO to be interested in such shares.
- (3) 1,181,000 shares in the Bank are held collectively by Asia Panich Investment Company (Hong Kong) Limited, Asia Insurance Company, Limited, Asia Investment Services Limited and United Asia Company Limited. These corporations or their directors are accustomed to acting in accordance with Dr Robin Y H Chan's directions or instructions.

DIRECTORS' REPORT

DIRECTORS' (INCLUDING THE CHIEF EXECUTIVE OFFICER'S) INTERESTS AND SHORT POSITIONS IN SECURITIES - continued

Other interests and short positions in securities

Under the SFO, other than those interests disclosed above, as at 31 December 2007, none of the directors (including the chief executive officer), nor their respective associates, had any other interests (nor any short positions) in any securities (nor in any underlying securities) in the Bank and its associated corporations. Moreover, as at 31 December 2007, none of the directors (including the chief executive officer), nor their respective spouses and children under 18 years of age, had been granted any rights to subscribe for the securities in the Bank and its associated corporations, much less had any such rights exercised.

SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN SECURITIES

As at 31 December 2007, the register maintained under Section 336 of the SFO showed that, other than the interests disclosed above in respect of certain directors (including the chief executive officer), the following parties had interests and short positions in the securities and underlying securities in the Bank:

Name	Capacity	Number of ordinary shares	Percentage of issued share capital
Liu Chong Hing Estate Company, Limited	Beneficial owner	203,407,628 <i>Notes (1) and (3)</i>	46.76
Liu Chong Hing Investment Limited	Interest of a controlled corporation	203,407,628 <i>Notes (1) and (3)</i>	46.76
Liu's Holdings Limited	Interest of a controlled corporation	203,407,628 <i>Notes (1) and (3)</i>	46.76
Bauhinia 97 Limited	Beneficial owner	87,000,000 <i>Note (2)</i>	20.00
COSCO (Hong Kong) Group Limited	Interest of a controlled corporation	87,000,000 <i>Note (2)</i>	20.00
China Ocean Shipping (Group) Company	Interest of a controlled corporation	87,000,000 <i>Note (2)</i>	20.00
The Bank of Tokyo-Mitsubishi UFJ, Ltd	Beneficial owner	42,000,000 <i>Note (3)</i>	9.66
Mitsubishi UFJ Financial Group, Inc	Interest of a controlled corporation	42,000,000 <i>Note (3)</i>	9.66
Third Avenue Management LLC	Investment manager	26,241,000 <i>Note (4)</i>	6.03

SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN SECURITIES **- continued**

Notes:

- (1) These interests are the same as those of certain directors (including the chief executive officer) disclosed above under the heading "DIRECTORS' (INCLUDING THE CHIEF EXECUTIVE OFFICER'S) INTERESTS AND SHORT POSITIONS IN SECURITIES" Note (1)(i). Liu Chong Hing Estate Company, Limited ("Liu Chong Hing Estate") is a wholly-owned subsidiary of Liu Chong Hing Investment Limited, a public company listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). Liu's Holdings Limited, a private company, had interest in about 45% of Liu Chong Hing Investment Limited's issued and fully-paid share capital. The references to the 203,407,628 shares in question all relate to the same block of 203,407,628 shares held by Liu Chong Hing Estate.
- (2) Bauhinia 97 Limited is a wholly-owned subsidiary of COSCO (Hong Kong) Group Limited, which in turn is a wholly-owned subsidiary of China Ocean Shipping (Group) Company. The references to the 87,000,000 shares in question all relate to the same block of 87,000,000 shares registered in the name of Bauhinia 97 Limited.
- (3) The Bank of Tokyo-Mitsubishi UFJ, Ltd is a wholly-owned subsidiary of Mitsubishi UFJ Financial Group, Inc. The references to the 42,000,000 shares in question both relate to the same block of 42,000,000 shares registered in the name of Bank of Tokyo-Mitsubishi UFJ.

Pursuant to an agreement in 1994, The Bank of Tokyo-Mitsubishi UFJ, Ltd has granted an option to Liu Chong Hing Estate exercisable at any time during the term of that agreement to purchase 40,000,000 of the 42,000,000 shares in question and The Bank of Tokyo-Mitsubishi UFJ, Ltd is required to offer to sell all such 40,000,000 shares to Liu Chong Hing Estate in certain circumstances.

- (4) Third Avenue Management LLC ("Third Avenue Management"), a United States based Registered Investment Adviser, acts as adviser to various portfolios held for the benefit of mutual funds, private partnerships, institutions, individuals, etc. Third Avenue Management has investment advisory authority over portfolios holding in the aggregate of 26,241,000 shares in the Bank.

Other than those interests and short positions in the securities and underlying securities in the Bank as disclosed above under Section 336 of the SFO, the Bank had not been notified of any other interests and short positions in its securities and underlying securities as at 31 December 2007.

DIRECTORS' INTERESTS IN CONTRACTS OF SIGNIFICANCE

Other than those interests disclosed below under the heading "CONNECTED TRANSACTIONS", no contracts of significance to which the Bank or any of its subsidiaries was a party and in which a director of the Bank had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

DIRECTORS' REPORT

CONNECTED TRANSACTIONS

The connected transactions between the Group, Liu Chong Hing Investment Limited and its subsidiaries (“Liu Chong Hing Investment Group”) and COSCO (Hong Kong) Group Limited, its subsidiaries, its holding companies and/or its fellow subsidiaries (“COSCO Group”) during the year are as follows:

- A. The Bank handled routine banking transactions for the members of the Liu Chong Hing Investment Group. Services provided by the Bank are cheque clearing, current, savings and deposit accounts, remittances, and other banking facilities.
- B. Members of the Group provided securities and futures brokerage, nominee and data processing services to members of the Liu Chong Hing Investment Group.
- C. Liu Chong Hing Investment Limited through its wholly-owned subsidiary, Liu Chong Hing Property Management and Agency Limited, provided property management, property consultancy and property maintenance services to the Bank.
- D. The Bank leased office premises of the Western Harbour Centre, a property owned by the Liu Chong Hing Investment Group. On the other hand, Liu Chong Hing Investment Limited subleased office premises of the Chong Hing Bank Centre from the Bank.
- E. The Bank and its subsidiaries provided banking and related financial services to the COSCO Group including cheque clearing, current and savings accounts and fixed deposits in a number of currencies, foreign exchange, remittances, stockbroking and nominee services. The Bank also provided loan facilities to the COSCO Group on a bilateral basis or through participation in syndicated loans.

Messrs Liu Lit Man, Liu Lit Mo, Liu Lit Chi, Don Tit Shing Liu, Robin Yau Hing Chan, Timothy George Freshwater and Andrew Liu are interested, directly or indirectly, in the respective share capital of Liu Chong Hing Investment Limited and/or the Bank.

The independent non-executive directors confirm that the transactions have been entered into by the Bank in the ordinary course of its business, on normal commercial terms, and in accordance with the terms which are fair and reasonable and in the interests of shareholders of the Bank as a whole.

Pursuant to Rule 14A.38 of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited, the board of directors engaged the auditors of the Bank to perform certain agreed upon procedures in respect of the continuing connected transactions of the Group. The auditors have reported their factual findings on these procedures to the board of directors. The independent non-executive directors have reviewed the continuing connected transactions and the report of the auditors and have confirmed that the transactions have been entered into by the Bank in the ordinary course of its business, on normal commercial terms, and in accordance with the terms of the agreement governing such transactions that are fair and reasonable and in the interests of shareholders of the Bank as a whole.

DECLARATION OF INTERESTS

No directors (other than the independent non-executive directors and Mr Eiichi Yoshikawa, a non-executive director) are interested in any business which may or may not compete, either directly or indirectly, with the business of the Bank.

Mr Eiichi Yoshikawa is the Director, Regional Head for Hong Kong and General Manager of The Bank of Tokyo-Mitsubishi UFJ, Ltd, Hong Kong Branch.

ARRANGEMENT TO PURCHASE SHARES OR DEBENTURES

Other than the share option scheme disclosed in note 30 to the consolidated financial statements, at no time during the year was the Bank or any of its subsidiaries a party to any arrangements to enable the directors of the Bank to acquire benefits by means of the acquisition of shares in, or debentures of, the Bank or any other body corporate.

PURCHASE, SALE OR REDEMPTION OF THE BANK'S LISTED SECURITIES

Neither the Bank nor any of its subsidiaries purchased, sold or redeemed any of the Bank's listed securities during the year.

DONATIONS

During the year, the Group made charitable and other donations amounting to approximately HK\$1,319,000 (2006: HK\$800,000).

STATEMENT OF COMPLIANCE

In preparing the accounts for 2007, the Bank has fully complied with the Banking (Disclosure) Rules, which have superseded the Supervisory Policy Manual "Financial Disclosure by Locally Incorporated Authorised Institutions" issued by the Hong Kong Monetary Authority.

EMOLUMENT POLICY

The Bank has set up a Remuneration Committee, responsibilities of which include reviewing and approving the performance-based remuneration packages payable to directors and senior management, by reference to the Bank's corporate goals and objectives.

SUFFICIENCY OF PUBLIC FLOAT

The Group has maintained a sufficient public float throughout the year ended 31 December 2007.

AUDITOR

Messrs Deloitte Touche Tohmatsu shall retire at the conclusion of the Bank's forthcoming annual general meeting. Being eligible, they shall offer themselves for re-appointment as the Bank's auditor at that meeting.

On behalf of the Board

Liu Lit Man

Executive Chairman

5 March 2008

CORPORATE GOVERNANCE REPORT

as at 5 March 2008

Corporate Governance Practices

The board of directors of the Bank (the “Board”) is well aware that maintaining good corporate governance standards is important to the effective and efficient operation of the Bank. The Board has therefore adopted and implemented various measures to ensure that a high standard of corporate governance practices is maintained. The directors confirm that, for the financial year ended 31 December 2007, the Bank has complied with the “Corporate Governance of Locally Incorporated Authorized Institutions” as set out in the Supervisory Policy Manual issued by the Hong Kong Monetary Authority and the Code on Corporate Governance Practices as set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Corporate Governance Code”) except, under the Bank’s Articles of Association, one-third (or, if the quotient resulting from the division of the number of directors by three is not a whole number, the number nearest one-third) of the directors for the time being, who have been longest in office since their last election, shall be subject to retirement by rotation and re-election at each annual general meeting. As between persons who became directors on the same day, those to retire shall (unless they otherwise agree between themselves) be determined by drawing lots. And as to those persons additionally appointed as directors or appointed as directors to fill casual vacancies by the Board, they shall hold office only until the next following annual general meeting and shall then be eligible for re-election (but not to be taken into account in determining the directors or the number of directors who are to retire by rotation) at that annual general meeting. The directors consider the Bank’s practice to be an appropriate alternative to that recommended under A.4.1 and A.4.2 of the Corporate Governance Code in respect of the appointment of non-executive directors for a specific term and the retirement by rotation of directors.

Board and Senior Management Oversight and Risk Management

The Bank, an authorized institution under the Banking Ordinance, is under the supervision of the Hong Kong Monetary Authority. Board and senior management oversight and risk management are key to attaining good standards of corporate governance practices in a banking environment. The Board oversees the Group’s policies, procedures and controls of measuring, monitoring and controlling risks arising from the banking and related financial service businesses. The day-to-day supervision of major functional areas is delegated to various specialised committees comprising directors and senior management members of the Bank. The unaudited supplementary financial information regarding corporate governance, risk management and other financial information disclosed pursuant to the Supervisory Policy Manual “Financial Disclosure By Locally Incorporated Authorised Institutions” issued by the Hong Kong Monetary Authority provides a detailed report on the Board and senior management oversight and the risk management process.

Directors’ Securities Transactions

The Bank has adopted a code for securities transactions by directors with terms no less exacting than those set out in the Model Code for Securities Transactions by Directors of Listed Issuers under Appendix 10 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Model Securities Transactions Code”). After specific enquiry by the Bank, all of the directors confirmed that, for the financial year ended 31 December 2007, they had complied with the required standards as set out in both the Model Securities Transactions Code and the Bank’s own code in question.

CORPORATE GOVERNANCE REPORT

Board of Directors

As at 31 December 2007, the Board was composed of the following directors. During the year of 2007, six board meetings were held and the attendance of each director is set out as follows:

Name of Director	Number of Board Meetings Attended	Attendance Rate
Executive Directors		
Mr LIU Lit Man, GBS, JP, FIBA <i>(Executive Chairman)</i>	5 / 6	83.33%
Dr LIU Lit Mo, LLD, MBE, JP <i>(Vice Chairman)</i>	6 / 6	100%
Mr LIU Lit Chi <i>(Managing Director and Chief Executive Officer)</i>	6 / 6	100%
Mr Don Tit Shing LIU <i>(Deputy Chief Executive Officer)</i>	6 / 6	100%
Mr LAU Wai Man <i>(Deputy Chief Executive Officer)</i>	6 / 6	100%
Mr Wilfred Chun Ning LIU	3 / 6	50%
Mr Frank Shui Sang JIN	6 / 6	100%
Mr Andrew Chiu Wing TSANG	6 / 6	100%
Mr George Har Kar WONG	6 / 6	100%
Non-executive Directors		
Mr Timothy George FRESHWATER	5 / 6	83.33%
Mr XU Minjie	2 / 3	66.67%
Mr Andrew LIU	3 / 6	50%
Mr Eiichi YOSHIKAWA	2 / 3	66.67%
Mr Christopher Kwun Shing LIU	4 / 6	66.67%
Mr Alfred Cheuk Yu CHOW, JP	6 / 6	100%
Mr WANG Zhi	3 / 6	50%
Independent Non-executive Directors		
Dr Robin Yau Hing CHAN, GBS, LLD, JP	4 / 6	66.67%
Mr Wanchai CHIRANAKHORN	6 / 6	100%
Mr CHENG Yuk Wo	6 / 6	100%
Mr Andrew Chiu Cheung MA	2 / 2	100%

CORPORATE GOVERNANCE REPORT

The Board, constituted in accordance with the Bank's Articles of Association for the time being in force, is the ultimate governing body of the Bank responsible for setting the Bank's strategic goals and policies; monitoring management performance against the achievement of such goals and the compliance with such policies; filling senior management positions and reviewing succession plans for such positions; ensuring that a proper system of internal controls exists; and accounting for the Bank's operations.

The day-to-day operations of the Bank are mainly managed by various specialised committees, as well as different divisions and departments reporting to the Managing Director and Chief Executive Officer, while the Board remains ultimately responsible for the Bank's operations and affairs.

Board meetings are usually scheduled a year in advance. At least 7 days' notice of board meetings is normally given to directors. The Executive Chairman sets the agenda for board meetings. The views of the directors, as expressed in the board meetings, on matters brought to their attention are duly minuted. Minutes of every board meeting are circulated to all directors for comment before they are confirmed at the next board meeting.

Directors are entitled to have access to board papers and any other related materials, and may seek external professional advice, as they see fit, so as to keep themselves abreast of the latest relevant development of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") and other applicable rules and regulations with an eye to ensuring better compliance and meeting better corporate governance standards.

The Bank has received, from each of the independent non-executive directors an annual confirmation of his independence pursuant to Rule 3.13 of the Listing Rules. The Bank considers all of its independent non-executive directors to be independent.

As to the nomination of candidates for appointment to the Board, instead of having a nomination committee in place, any director is entitled to recommend for the consideration and, if thought fit, approval of the Board suitable candidates who can contribute to the Bank, discharge their responsibilities in the interests of the Bank and its shareholders as a whole, and meet the requirements of The Stock Exchange of Hong Kong Limited and the Hong Kong Monetary Authority for appointment as directors.

Chairman and Chief Executive Officer

Mr Liu Lit Man is the Executive Chairman of the Bank and Mr Liu Lit Chi is its Managing Director and Chief Executive Officer. The roles and responsibilities of the Executive Chairman and the Managing Director and Chief Executive Officer are separate. They are assumed by two different individuals. The Executive Chairman is responsible for the management of the Board, while the Managing Director and Chief Executive Officer is charged with the responsibilities to manage the day-to-day business of the Bank.

Auditors' Remuneration

The remuneration paid and payable to the Group's auditors, Messrs Deloitte Touche Tohmatsu, for 2007 amounted to:

	HKD
Audit services	3,500,000
Interim review	383,590
Tax, information technology and regulatory consulting	<u>562,900</u>
Total	<u><u>4,446,490</u></u>

Remuneration Committee

The Remuneration Committee comprises two independent non-executive directors and one non-executive director appointed by the Board.

The Remuneration Committee reviews and makes recommendations to the Board on the remuneration policy applicable to directors and senior management of the Bank, and ensures that the Bank is able to attract, retain, and motivate a high-calibre team of senior executives which is essential to the success of the Bank. The terms of reference of the Remuneration Committee sets out its roles.

The Remuneration Committee meets twice a year. During the year of 2007, two meetings were held and the attendance of each member is set out as follows:

Name of Member	Number of Committee Meetings Attended	Attendance Rate
Mr Wanchai CHIRANAKHORN <i>(Chairman)</i>	2 / 2	100%
Mr CHENG Yuk Wo	2 / 2	100%
Mr Alfred Cheuk Yu CHOW, JP	2 / 2	100%

The Remuneration Committee is provided with sufficient resources to discharge its duties and the following is a summary of the work of the Remuneration Committee during 2007:

- (i) discussion and review of the current remuneration policy and structure applicable to all employees as a whole;
- (ii) discussion and review of the directors' fees; and
- (iii) discussion and review of the benefits in kind, including staff housing loan and group medical benefits to all employees of the Bank.

The emolument payable to directors will depend on their respective contractual terms under employment contracts, if any, and as recommended by the Remuneration Committee. Details of the directors' remuneration are set out in note 12 to the financial statements.

Audit Committee

The Audit Committee comprises two independent non-executive directors and one non-executive director who possess the appropriate professional expertise and experience in financial management and business. The Audit Committee is chaired by Mr Cheng Yuk Wo and the other members are Mr Wanchai Chiranakhorn and Mr Alfred Cheuk Yu Chow.

Under its terms of reference, the Audit Committee is required, among other things, to advise the Board on the appointment and retention of the external auditors, to review the external auditors' independence and objectivity, to oversee the relationship with the external auditors, to review the half-yearly and annual reports and accounts, to review the external auditors' management letter, to hold meetings with the Hong Kong Monetary Authority, to assess the adequacy and effectiveness of the Bank's systems of internal control, to review the internal audit function, and to review and recommend internal procedures to ensure compliance with regulatory requirements and generally accepted accounting standards.

CORPORATE GOVERNANCE REPORT

The Audit Committee shall meet at least twice a year. During the year of 2007, the Audit Committee held four meetings and record of individual attendance of members is set out as follows:

Name of Member	Number of Committee	
	Meetings Attended	Attendance Rate
Mr CHENG Yuk Wo <i>(Chairman)</i>	4 / 4	100%
Mr Wanchai CHIRANAKHORN	4 / 4	100%
Mr Alfred Cheuk Yu CHOW, JP	4 / 4	100%

To discharge its responsibilities, the Audit Committee performed the following major reviews in 2007:

Financial Statements

The Audit Committee met with the external auditors and the executive director in charge of Finance and Treasury Management Division to discuss the accounts for the year ended 31 December 2006 and for the six months ended 30 June 2007. The Audit Committee reviewed and discussed with the external auditors to ensure that the Bank's financial statements had been prepared in accordance with the accounting principles generally accepted in Hong Kong.

Relationship with the External Auditors

The Audit Committee reviewed the independence and objectivity of the external auditors, the scope of audit services and related audit fees payable to the external auditors for the Board's approval. Moreover, the Audit Committee met and discussed with the external auditors on their audit strategy and assessment of the sufficiency of the internal control of the Bank.

Internal Control Review

The Audit Committee also reviewed the internal control issues and the internal audit function of the Bank, covering the annual audit plan, the staffing and resources of Internal Audit Department, the audit findings and recommendations raised in the internal audits undertaken, and the implementation status of related audit recommendations.

INDEPENDENT AUDITOR'S REPORT



TO THE MEMBERS OF CHONG HING BANK LIMITED *(incorporated in Hong Kong with limited liability)*

We have audited the consolidated financial statements of Chong Hing Bank Limited (the “Bank”) and its subsidiaries (collectively referred to as the “Group”) set out on pages 39 to 126, which comprise the consolidated and the Bank balance sheets as at 31 December 2007, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the consolidated financial statements

The directors of the Bank are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Bank and of the Group as at 31 December 2007 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong

5 March 2008

FINANCIAL STATEMENTS

Consolidated Income Statement	39
Consolidated Balance Sheet	40
Balance Sheet	41
Consolidated Statement of Changes in Equity	42
Consolidated Cash Flow Statement	44
Notes to the Financial Statements	46
1. General	46
2. Application of new and revised Hong Kong financial reporting standards (“HKFRSs”)	46
3. New and revised HKFRSs issued but not yet effective	46
4. Significant accounting policies	47
5. Critical accounting judgement and key source of estimation uncertainty	59
6. Business and geographical segments	61
7. Financial risk management	66
8. Net interest income	103
9. Net fee and commission income	103
10. Other operating income	104
11. Operating expenses	104
12. Directors’ and employees’ emoluments	105
13. Taxation	106
14. Dividends	106
15. Earnings per share	107
16. Cash and short-term funds	107
17. Derivative financial instruments	107
18. Investments in securities	108
19. Advances and other accounts	110
20. Investments in subsidiaries	112
21. Interests in jointly controlled entities	113

22. Investment properties	114
23. Property and equipment	115
24. Prepaid lease payments for land	116
25. Deposits from customers	117
26. Loan capital	117
27. Share capital	117
28. Reserves	118
29. Deferred taxation	119
30. Share option scheme	119
31. Loans to officers	120
32. Impairment loss on goodwill	120
33. Impairment loss on available-for-sale securities	120
34. Contingent liabilities and commitments	121
35. Retirement benefits scheme	122
36. Related party transactions	125
37. Comparative figures	126

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

1. Specialised committees	127
2. Management of risks	129
3. Segmental information	130
4. Advances to customers – by industry sectors	130
5. Advances to customers – by geographical areas	131
6. Cross-border claims	132
7. Currency risk	133
8. Overdue and rescheduled assets	134
9. Non-bank mainland exposures	135
10. Liquidity ratio	135
11. Capital charge for credit, market and operational risks	136
12. Risk management	137
13. Basis of consolidation	143

CONSOLIDATED INCOME STATEMENT

for the year ended 31 December 2007

	NOTES	2007 HK\$'000	2006 HK\$'000
Interest income		3,310,484	2,740,518
Interest expense		<u>(2,339,871)</u>	<u>(1,911,979)</u>
Net interest income	8	<u>970,613</u>	<u>828,539</u>
Fee and commission income		326,641	172,301
Fee and commission expense		<u>(43,229)</u>	<u>(4,166)</u>
Net fee and commission income	9	283,412	168,135
Other operating income	10	166,669	133,554
Operating expenses	11	<u>(642,894)</u>	<u>(591,537)</u>
		777,800	538,691
Impairment allowances on loans and advances	19	(82,922)	(59,801)
Net loss on disposal of property and equipment		(64)	(913)
Net gain on disposal of land		2,591	–
Net gain on disposal of investment properties		14,420	–
Net gain on disposal of available-for-sale securities		177,351	54,001
Fair value adjustment on investment properties	22	14,391	5,390
Impairment loss on available-for-sale securities	33	(369,627)	–
Impairment loss on goodwill	32	<u>(30,000)</u>	–
Profit from operations		503,940	537,368
Share of profit of jointly controlled entities		<u>66,074</u>	<u>33,546</u>
Profit before taxation		570,014	570,914
Taxation	13	<u>(64,982)</u>	<u>(67,770)</u>
Profit for the year		<u>505,032</u>	<u>503,144</u>
Dividends	14	<u>282,750</u>	<u>265,350</u>
Earnings per share, basic and diluted	15	<u>HK\$1.16</u>	<u>HK\$1.16</u>

CONSOLIDATED BALANCE SHEET

as at 31 December 2007

	NOTES	2007 HK\$'000	2006 HK\$'000
Assets			
Cash and short-term funds	16	14,763,977	16,256,859
Placements with banks and other financial institutions maturing between one to twelve months		3,084,147	2,638,461
Derivative financial instruments	17	60	4,962
Financial assets at fair value through profit or loss	18	1,134,422	610,811
Available-for-sale securities	18	876,661	1,098,141
Held-to-maturity securities	18	15,607,980	13,903,173
Advances and other accounts	19	32,495,890	27,497,020
Tax recoverable		19,816	–
Interests in jointly controlled entities	21(i)	142,230	99,256
Loan to a jointly controlled entity	21(ii)	5,267	31,000
Investment properties	22	60,241	82,250
Property and equipment	23	446,873	380,825
Prepaid lease payments for land	24	334,231	316,535
Goodwill	32	80,606	110,606
Total assets		69,052,401	63,029,899
Liabilities			
Deposits and balances of banks and other financial institutions		456,858	528,993
Deposits from customers	25	60,327,437	54,675,232
Derivative financial instruments	17	114,546	1,716
Other accounts and accruals		861,619	754,550
Current tax liabilities		35,008	22,463
Loan capital	26	970,871	967,376
Deferred tax liabilities	29	15,274	27,839
Total liabilities		62,781,613	56,978,169
Shareholders' equity			
Share capital	27	217,500	217,500
Reserves		6,053,288	5,834,230
Shareholders' funds		6,270,788	6,051,730
Total liabilities and shareholders' equity		69,052,401	63,029,899

The consolidated financial statements on pages 39 to 126 were approved and authorised for issue by the Board of Directors on 5 March 2008 and signed on its behalf by:

Liu Lit Man, *Executive Chairman*

Liu Lit Mo, *Vice Chairman-Executive Director*

Frank S S Jin, *Executive Director*

Michael K W Yeung, *Company Secretary*

BALANCE SHEET

as at 31 December 2007

	NOTES	2007 HK\$'000	2006 HK\$'000
Assets			
Cash and short-term funds	16	14,713,472	16,208,174
Placements with banks and other financial institutions maturing between one to twelve months		3,084,147	2,638,461
Derivative financial instruments	17	60	4,962
Financial assets at fair value through profit or loss	18	1,134,158	610,388
Available-for-sale securities	18	724,187	916,433
Held-to-maturity securities	18	15,607,980	13,903,173
Advances and other accounts	19	32,093,440	27,201,853
Tax recoverable		19,816	–
Investments in subsidiaries	20(i)	333,323	363,323
Amounts due from subsidiaries	20(ii)	3,407	4,677
Interests in jointly controlled entities	21(i)	56,500	56,500
Loan to a jointly controlled entity	21(ii)	5,267	31,000
Investment properties	22	35,900	64,250
Property and equipment	23	425,599	372,115
Prepaid lease payments for land	24	848,465	842,475
Deferred tax assets	29	2,077	–
Total assets		69,087,798	63,217,784
Liabilities			
Deposits and balances of banks and other financial institutions		456,858	528,993
Deposits from customers	25	60,323,598	54,671,174
Amounts due to subsidiaries	36	658,146	616,592
Derivative financial instruments	17	114,546	1,716
Other accounts and accruals		457,448	435,963
Current tax liabilities		3,333	14,497
Loan capital	26	970,871	967,376
Deferred tax liabilities	29	–	13,317
Total liabilities		62,984,800	57,249,628
Shareholders' equity			
Share capital	27	217,500	217,500
Reserves	28	5,885,498	5,750,656
Shareholders' funds		6,102,998	5,968,156
Total liabilities and shareholders' equity		69,087,798	63,217,784

Approved and authorised for issue by the Board of Directors on 5 March 2008 and signed on its behalf by:

Liu Lit Man, *Executive Chairman*

Liu Lit Mo, *Vice Chairman-Executive Director*

Frank S S Jin, *Executive Director*

Michael K W Yeung, *Company Secretary*

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2007

	Notes	Share capital HK\$'000	Share premium HK\$'000	Goodwill HK\$'000	Investment revaluation reserve HK\$'000	General reserve HK\$'000	Translation reserve HK\$'000	Regulatory reserve HK\$'000	Retained profits HK\$'000	Total HK\$'000
At 1 January 2007		217,500	1,542,817	(182)	142,386	1,388,500	(152)	165,000	2,595,861	6,051,730
Revaluation losses, net		-	-	-	(206,538)	-	-	-	-	(206,538)
Exchange differences arising from translation of foreign operations		-	-	-	-	-	482	-	-	482
Deferred taxation arising from revaluation movement	29	-	-	-	10,556	-	-	-	-	10,556
Net expense recognised directly in equity		-	-	-	(195,982)	-	482	-	-	(195,500)
Profit for the year		-	-	-	-	-	-	-	505,032	505,032
Reversal of reserve upon impairment		-	-	-	369,627	-	-	-	-	369,627
Reversal of reserve upon disposal		-	-	-	(177,351)	-	-	-	-	(177,351)
Total recognised income for the year		-	-	-	(3,706)	-	482	-	505,032	501,808
Interim dividend paid for financial year 2007	14	-	-	-	-	-	-	-	(91,350)	(91,350)
Final dividend paid for financial year 2006	14	-	-	-	-	-	-	-	(191,400)	(191,400)
Earmark of retained profits as regulatory reserve		-	-	-	-	-	-	191,000	(191,000)	-
At 31 December 2007		<u>217,500</u>	<u>1,542,817</u>	<u>(182)</u>	<u>138,680</u>	<u>1,388,500</u>	<u>330</u>	<u>356,000</u>	<u>2,627,143</u>	<u>6,270,788</u>

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2007

	Notes	Share capital HK\$'000	Share premium HK\$'000	Goodwill HK\$'000	Investment revaluation reserve HK\$'000	General reserve HK\$'000	Translation reserve HK\$'000	Regulatory reserve HK\$'000	Retained profits HK\$'000	Total HK\$'000
At 1 January 2006		217,500	1,542,817	(182)	163,125	1,388,500	(1,691)	122,837	2,400,230	5,833,136
Revaluation gains, net		-	-	-	60,387	-	-	-	-	60,387
Exchange differences arising from translation of foreign operations		-	-	-	-	-	1,539	-	-	1,539
Deferred taxation arising from revaluation movement	29	-	-	-	(27,125)	-	-	-	-	(27,125)
Net income recognised directly in equity		-	-	-	33,262	-	1,539	-	-	34,801
Profit for the year		-	-	-	-	-	-	-	503,144	503,144
Reversal of reserve upon disposal		-	-	-	(54,001)	-	-	-	-	(54,001)
Total recognised income for the year		-	-	-	(20,739)	-	1,539	-	503,144	483,944
Interim dividend paid for financial year 2006	14	-	-	-	-	-	-	-	(82,650)	(82,650)
Final dividend paid for financial year 2005	14	-	-	-	-	-	-	-	(182,700)	(182,700)
Earmark of retained profits as regulatory reserve		-	-	-	-	-	-	42,163	(42,163)	-
At 31 December 2006		<u>217,500</u>	<u>1,542,817</u>	<u>(182)</u>	<u>142,386</u>	<u>1,388,500</u>	<u>(152)</u>	<u>165,000</u>	<u>2,595,861</u>	<u>6,051,730</u>

The retained profits of the Group included accumulated profits of HK\$84,571,000 (2006: HK\$18,497,000) retained by the jointly controlled entities of the Group.

The regulatory reserve is set up in compliance with the Hong Kong Monetary Authority's requirements and is distributable to shareholders of the Bank subject to consultation with the Hong Kong Monetary Authority.

The general reserve comprises transfers from previous years' retained profits.

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December 2007

	2007 HK\$'000	2006 HK\$'000
OPERATING ACTIVITIES		
Profit before taxation	570,014	570,914
Adjustments for:		
Net loss on disposal of property and equipment	64	913
Net gain on disposal of investment properties	(14,420)	–
Net gain on disposal of land	(2,591)	–
Net gain on disposal of available-for-sale securities	(177,351)	(54,001)
Impairment allowances on loans and advances	82,922	59,801
Impairment loss on goodwill	30,000	–
Impairment loss on available-for-sale securities	369,627	–
Dividend income from investments	(11,859)	(13,543)
Share of profit of jointly controlled entities	(66,074)	(33,546)
Fair value adjustment on investment properties	(14,391)	(5,390)
Depreciation	36,846	30,535
Amortisation of prepaid lease payments for land	5,710	5,114
Interest income from held-to-maturity securities and available-for-sale securities	(702,669)	(455,581)
Interest expense on loan capital	63,971	2,952
Exchange adjustments	2,871	1,873
Operating cash flows before movements in operating assets and liabilities	172,670	110,041
Increase in interest receivable and other accounts	(153,985)	(322,242)
Increase in other accounts and accruals	107,551	411,166
Increase in placements with banks and other financial institutions with original maturity over three months	(850,625)	(777,531)
Decrease (increase) in exchange fund bills with original maturity over three months	155,580	(127,460)
Decrease (increase) in money at call and short notice with original maturity over three months	624,478	(1,753,156)
Increase in bills receivable	(25,354)	(154,655)
Increase in trade bills	(26,220)	(9,788)
Increase in other advances to customers	(4,880,739)	(2,523,220)
Decrease (increase) in advances to banks and other financial institutions	341	(216)
Decrease in deposits and balances of banks and other financial institutions with original maturity over three months	(79,162)	(19,177)
(Increase) decrease in financial assets at fair value through profit or loss	(523,611)	198,349
Decrease in derivative financial instruments	117,732	42,361
Increase in deposits from customers	5,652,205	13,168,940
Cash generated from operations	290,861	8,243,412
Hong Kong Profits Tax paid	(71,290)	(67,618)
Overseas tax paid	(2,972)	(850)
NET CASH GENERATED FROM OPERATING ACTIVITIES	216,599	8,174,944

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December 2007

	2007 HK\$'000	2006 HK\$'000
INVESTING ACTIVITIES		
Interest received on held-to-maturity securities and available-for-sale securities	706,817	416,922
Dividends received on investments	11,859	13,543
Dividend income from jointly controlled entities	23,100	–
Purchase of held-to-maturity securities	(26,184,962)	(15,680,153)
Purchase of available-for-sale securities	(364,551)	(340,798)
Purchase of property and equipment	(103,050)	(215,748)
Lease prepayment for land	(28,171)	(20,680)
Proceeds from redemption of held-to-maturity securities	24,480,155	10,969,886
Proceeds from sale and redemption of available-for-sale securities	379,493	104,813
Proceeds from disposals of property and equipment	95	233
Proceeds from disposal of land	7,356	–
Proceeds from disposal of investment properties	50,820	–
Repayment of loan from a jointly controlled entity	25,733	–
NET CASH USED IN INVESTING ACTIVITIES	<u>(995,306)</u>	<u>(4,751,982)</u>
CASH USED IN FINANCING ACTIVITIES		
Interest paid on loan capital	(63,333)	–
Net proceeds from issue of loan capital	–	967,000
Dividends paid	(282,750)	(265,350)
NET CASH (USED IN) FROM FINANCING ACTIVITIES	<u>(346,083)</u>	<u>701,650</u>
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS		
	(1,124,790)	4,124,612
CASH AND CASH EQUIVALENTS AT 1 JANUARY	<u>14,115,214</u>	<u>9,990,602</u>
CASH AND CASH EQUIVALENTS AT 31 DECEMBER, represented by		
Cash and balances with banks and other financial institutions	1,833,309	997,461
Money at call and short notice	9,776,851	14,744,553
Exchange fund bills	3,153,817	514,845
Placements with banks and other financial institutions maturing between one to twelve months	3,084,147	2,638,461
Deposits and balances of banks and other financial institutions	(456,858)	(528,993)
Less: Amounts with original maturity over three months	(4,400,842)	(4,251,113)
	<u>12,990,424</u>	<u>14,115,214</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

1. GENERAL

The Bank is a public limited company incorporated in Hong Kong and its shares are listed on the Stock Exchange of Hong Kong Limited. Its parent is Liu Chong Hing Estate Company, Limited and its ultimate holding company is Liu's Holdings Limited. The Bank is engaged in the provision of banking and related financial services. The address of the registered office and principal place of business of the Bank is disclosed in the Annual Report.

The consolidated financial statements are presented in Hong Kong dollars, which is also the functional currency of the Bank.

2. APPLICATION OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS ("HKFRSs")

In the current year, the Group and the Bank have applied, for the first time, a number of new standard, amendment and interpretations ("new HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), which are effective for accounting periods beginning on 1 January 2007.

HKAS 1 (Amendment)	Capital disclosures
HKFRS 7	Financial instruments: Disclosures
HK(IFRIC) - INT 9	Reassessment of embedded derivatives
HK(IFRIC) - INT 10	Interim financial reporting and impairment

The Group has applied the disclosure requirements under HKAS 1 (Amendment) and HKFRS 7 retrospectively. Certain information presented in prior years under the requirements of HKAS 32 has been removed and the relevant comparative information based on the requirements of HKAS 1 (Amendment) and HKFRS 7 has been presented for the first time in the current year.

3. NEW AND REVISED HKFRSs ISSUED BUT NOT YET EFFECTIVE

The Group and the Bank have not early applied the following new and revised standards or interpretations that have been issued but are not yet effective. The directors of the Bank anticipate that the application of these standards or interpretations will have no material impact on the results and the financial position of the Group and the Bank.

HKAS 1 (Revised)	Presentation of financial statements ¹
HKAS 23 (Revised)	Borrowing costs ¹
HKFRS 8	Operating segments ¹
HK(IFRIC) - INT 11	HKFRS 2 - Group and treasury share transactions ²
HK(IFRIC) - INT 12	Service concession arrangements ³
HK(IFRIC) - INT 13	Customer loyalty programmes ⁴
HK(IFRIC) - INT 14	HKAS 19 - The limit on a defined benefit asset, minimum funding requirements and their interaction ³

¹ Effective for annual periods beginning on or after 1 January 2009.

² Effective for annual periods beginning on or after 1 March 2007.

³ Effective for annual periods beginning on or after 1 January 2008.

⁴ Effective for annual periods beginning on or after 1 July 2008.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared on the historical cost basis except for certain properties and financial instruments, which are measured at fair values, as explained in the accounting policies set out below.

The consolidated financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards issued by the HKICPA. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited and by the Companies Ordinance.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and entities (including special purpose entities) controlled by the Bank (or its subsidiaries). Control is achieved where the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Subsidiary companies are companies in which the Group has the power to govern the financial and operating policies to obtain benefits from its activities and this is generally accompanied by a shareholding of more than one half of the voting rights.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Investments in subsidiaries are stated in the Bank's balance sheet at cost less provision for impairment losses. The results of subsidiary companies are accounted for by the Bank on the basis of dividends received or receivable.

Goodwill

Goodwill arising on acquisitions prior to 1 January 2005

Goodwill arising on an acquisition of net assets and operations of another entity for which the agreement date is before 1 January 2005 represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of the relevant acquiree at the date of acquisition.

Goodwill arising on acquisitions of net assets and operations of another entity which have been previously charged directly to reserves prior to 1 January 2005 continues to be held in reserves, and will be charged to the retained earnings at the time when the business to which the goodwill relates is disposed of or when a cash-generating unit to which the goodwill relates becomes impaired.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Goodwill - continued

Goodwill arising on acquisitions on or after 1 January 2005

Goodwill arising on an acquisition of a business for which the agreement date is on or after 1 January 2005 represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of the relevant business at the date of acquisition. Such goodwill is carried at cost less any accumulated impairment losses.

Capitalised goodwill arising on an acquisition of a business is presented separately in the consolidated balance sheet.

For the purposes of impairment testing, goodwill arising from an acquisition is allocated to each of the relevant cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the acquisition. A cash-generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a financial year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that financial year. When the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated to reduce the carrying amount of any goodwill allocated to the unit first, and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. Any impairment loss for goodwill is recognised directly in the consolidated income statement. An impairment loss for goodwill is not reversed in subsequent periods.

On subsequent disposal of the relevant cash-generating unit, the attributable amount of goodwill capitalised is included in the determination of the amount of gain or loss on disposal.

Interests in jointly controlled entities

Joint venture arrangements that involve the establishment of a separate entity in which venturers have joint control over the economic activity of the entity are referred to as jointly controlled entities.

The results and assets and liabilities of jointly controlled entities are incorporated in these consolidated financial statements using the equity method of accounting. Under the equity method, investments in jointly controlled entities are carried in the consolidated balance sheet at cost as adjusted for post-acquisition changes in the Group's share of the net assets of the jointly controlled entities, less any identified impairment loss. When the Group's share of losses of a jointly controlled entity equals or exceeds its interest in that jointly controlled entity, the Group discontinues recognising its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that jointly controlled entity.

When a group entity transacts with a jointly controlled entity of the Group, profits or losses are eliminated to the extent of the Group's interest in the jointly controlled entity, except to the extent that unrealised losses provide evidence of an impairment of the asset transferred, in which case, the full amount of losses is recognised.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Revenue recognition

Interest income and expenses

Interest income and expenses are recognised on a time-proportion basis by reference to the principal outstanding and at the effective interest rate applicable. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, where appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. The calculation includes significant fees and transaction costs that are an integral part of the effective interest rate, and premiums or discounts.

Once a financial asset has been written down as a result of an impairment loss, interest income is recognised using the original rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Fees and commission income

Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, including account servicing fees, investment management fees, sales commission, placement fees and syndication fees, are recognised as the related services are performed. When a loan commitment is not expected to result in the draw-down of a loan, loan commitment fees are recognised on a straight-line basis over the commitment period.

Other fees and commission expenses relates mainly to transaction and service fees, which are expensed as the services are provided.

Dividends

Dividend income from investments including financial assets at fair value through profit or loss is recognised when the shareholders' rights to receive payment have been established.

Property and equipment

Leasehold buildings and equipment are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is provided to write off the cost of leasehold buildings and equipment over their estimated useful lives after taking into account their estimated residual value, using the straight-line method.

An item of property and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the income statement in the year in which the item is derecognised.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Investment properties

Investment properties are properties held to earn rentals or for capital appreciation.

On initial recognition, investment properties are measured at cost, including any directly attributable expenditure. Subsequent to initial recognition, investment properties are measured using the fair value model. Gains or losses arising from changes in the fair value of investment properties are included in profit or loss for the period in which they arise.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use or no future economic benefits are expected from its disposals. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement in the year in which the item is derecognised.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessor

Amounts due from lessees under finance leases are recorded as receivables at the amount of the Group's net investment in the leases. Finance lease income is allocated to accounting periods so as to reflect a constant periodic rate of return on the Group's net investment outstanding in respect of the leases.

Rental income from operating leases is recognised in the consolidated income statement on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised as an expense on a straight-line basis over the lease term.

The Group as lessee

Rentals payable under operating leases are charged to profit or loss on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

Prepaid lease payments for land

Leasehold premises held for own use is split into a lease of land and building in proportion to the relative fair values of the leasehold interests in the land element and the building element of the lease at the inception of the lease. Prepaid lease payments are stated at cost and amortised over the period of the lease.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Foreign currencies

In preparing the financial statements of each individual group entity, transactions in currencies other than the functional currency of that entity (foreign currencies) are recorded in the respective functional currency (i.e. the currency of the primary economic environment in which the entity operates) at the rates of exchanges prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items, are recognised in profit or loss in the period in which they arise, except for exchange differences arising on a monetary item that forms part of the Bank's net investment in a foreign operation, in which case, such exchange differences are recognised in equity in the consolidated financial statements. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity, in which cases, the exchange differences are also recognised directly in equity.

For the purposes of presenting the consolidated financial statements, the assets and liabilities of the Group's foreign operations are translated into the presentation currency of the Group (i.e. Hong Kong dollars) at the rate of exchange prevailing at the balance sheet date, and their income and expenses are translated at the average exchange rates for the year, unless exchange rates fluctuate significantly during the period, in which case, the exchange rates prevailing at the dates of transactions are used. Exchange differences arising, if any, are recognised as a separate component of equity (the translation reserve). Such exchange differences are recognised in income statement in the period in which the foreign operation is disposed of.

Retirement benefit costs

Payments to the defined contribution retirement benefit plans are charged as an expense when employees have rendered service entitling them to the contributions.

For defined benefit retirement benefit plans, the cost of providing benefits is determined using the projected unit credit method, with actuarial valuations being carried out with sufficient regularity. Actuarial gains and losses which exceed 10 per cent of the greater of the present value of the Group's pension obligations and the fair value of plan assets are amortised over the expected average remaining working lives of the participating employees. Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the amended benefits become vested.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Retirement benefit costs - continued

The amount recognised in the consolidated balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised actuarial gains and losses and unrecognised past service cost, and as reduced by the fair value of plan assets. Any asset resulting from this calculation is limited to unrecognised actuarial losses and past service cost, plus the present value of available refunds and reductions in future contributions to the plan.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax base used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Borrowing costs

All borrowing costs are recognised as and included in interest expenses in the consolidated income statement in the period in which they are incurred.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments

Financial assets and financial liabilities are recognised on the balance sheet when a group entity becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in consolidated income statement.

Financial assets

The Group's and the Bank's financial assets are classified into one of the four categories, including financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments and available-for-sale financial assets. All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss has two subcategories, including financial assets held for trading and those designated at fair value through profit or loss on initial recognition.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial assets - continued

Financial assets at fair value through profit or loss - continued

A financial asset other than a financial asset held for trading may be designated as at fair value through profit or loss upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and HKAS 39 permits the entire combined contract (asset or liability) to be designated as at fair value through profit or loss.

At each balance sheet date subsequent to initial recognition, financial assets at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in consolidated income statement in the period in which they arise. The net gain or loss recognised in profit or loss exclude any dividend or interest earned on the financial assets.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. At each balance sheet date subsequent to initial recognition, loans and receivables including cash and short term funds, placements with and advances to banks and other financial institutions, interest receivable, bills receivable, trade bills and loans and advances to customers, loan to a jointly controlled entity and amounts due from subsidiaries are carried at amortised cost using the effective interest method, less any identified impairment losses.

Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. At each balance sheet date subsequent to initial recognition, held-to-maturity investments are measured at amortised cost using the effective interest method, less any identified impairment losses, with revenue recognised on an effective yield basis.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial assets - continued

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated or not classified as any of the other categories (set out above). At each balance sheet date subsequent to initial recognition, available-for-sale financial assets are measured at fair value and losses arising from changes in fair value are recognised directly in the investment revaluation reserve with the exception of impairment losses. Interest income calculated using the effective interest method and foreign exchange gains and losses arising on translation are recognised directly in consolidated income statement. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the investments revaluation reserve is included in profit or loss for the period.

Dividends on available-for-sale equity instruments are recognised in consolidated income statement when the Group's right to receive payments is established.

The fair value of available-for-sale monetary assets denominated in a foreign currency is translated at the spot rate at reporting date. The change in fair value attributable to such translation differences is recognised in profit or loss for the period.

Impairment of financial assets

Financial assets, other than those financial assets at fair value through profit or loss, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been impacted.

For an available-for-sale equity investment, a significant or prolonged decline in the fair value of that investment below its cost is considered to be objective evidence of impairment.

For all other financial assets, objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation.

For certain categories of financial asset, such as loans and receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis.

Individual impairment allowances are assessed by a discounted cash flow method for loans and advances that are individually significant and have objective evidence of impairment. The individual impairment allowances are measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the original effective interest rate.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Impairment of financial assets - continued

On collective impairment, individually insignificant advances or advances where no impairment has been identified individually are assessed on the basis of contractual cash flows and historical loss experience adjusted for current conditions.

For financial assets carried at amortised cost, an impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. When the financial assets are considered to be uncollectible, the amounts are written off against the allowance account. Subsequent recoveries of amounts previously written off are credited to profit or loss. If, in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment losses was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Impairment losses on available-for-sale equity investments will not be reversed in profit or loss in subsequent periods. Any increase in fair value subsequent to impairment loss is recognised directly in equity. For available-for-sale debt investments, impairment losses are subsequently reversed if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment loss.

Financial liabilities and equity

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

An equity instrument is any contract that evidences a residual interest in the assets of the group after deducting all of its liabilities. The Group's financial liabilities are generally classified into financial liabilities at fair value through profit or loss and other financial liabilities.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Interest expense is recognised on an effective interest basis.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial liabilities and equity - continued

Financial liabilities at fair value through profit or loss

At each balance sheet date subsequent to initial recognition, financial liabilities at fair value through profit or loss are measured at fair value, with changes in fair value recognised directly in consolidated income statement in the period in which they arise. The net gain or loss recognised in profit or loss excludes any interest paid on the financial liabilities.

Other financial liabilities

Other financial liabilities are initially measured at fair value, net of transaction costs. Other financial liabilities, including deposits and balances of banks and other financial institutions and deposits from customers, amounts due to subsidiaries and loan capital are subsequently measured at amortised cost using the effective interest method.

Offsetting financial instruments

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

Equity instruments

Equity instruments issued by the Bank are recorded at the proceeds received, net of direct issue costs.

Derivative financial instruments

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each balance sheet date. The resulting gain or loss is recognised in consolidated income statement immediately.

Embedded derivatives

Derivatives embedded in non-derivative host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair value with changes in fair value recognised in profit or loss.

Financial guarantee contracts

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument. A financial guarantee contract issued by the Group and not designed as at fair value through profit or loss is recognised initially at its fair value less transaction costs that are directly attributable to the issue of the financial guarantee contract. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount determined in accordance with HKAS 37 "Provisions, Contingent Liabilities and Contingent Assets"; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 "Revenue".

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the assets expire or the financial assets are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

Impairment on non-financial assets

The Group assesses at each reporting date or more frequently if events or changes in circumstances indicate that the carrying value may be impaired, whether there is an indication that a non-financial asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. Where the carrying amount of an asset (or cash-generating unit) exceeds its recoverable amount, the asset (or cash-generating unit) is considered impaired and is written down to its recoverable amount.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. Impairment losses relating to goodwill cannot be reversed for subsequent increases in its recoverable amount in future periods.

Fiduciary assets

The assets held in trust in a fiduciary capacity are not assets of the Group and accordingly are not included in the financial statements.

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash, balances with banks and other financial institutions, placements with banks and other financial institutions and exchange fund bills.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

5. CRITICAL ACCOUNTING JUDGEMENT AND KEY SOURCE OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in Note 4, management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Key sources of estimation uncertainty

The following are the key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

(a) Impairment allowances on loans and advances

The Group establishes, through charges against profit, impairment allowances in respect of estimated incurred loss in loans and advances. The allowances consist of individual impairment allowances and collective impairment allowances. The overall impairment allowances represent the aggregate amount by which management considers necessary to write down its loan portfolio in order to state it in the balance sheet at its estimated net recoverable value.

In determining individual impairment allowances, management considers objective evidence of impairment. When a loan is impaired, an individual impairment allowance is assessed by a discounted cash flow method, measured at the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the original effective interest rate. The quantum of the allowance is also impacted by the collateral value and this, in turn, may be discounted in certain circumstances to recognise the impact of forced sale or quick liquidation.

In determining collective impairment allowances, management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio.

Details of the impairment allowances movements are disclosed in Note 19.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

5. CRITICAL ACCOUNTING JUDGEMENT AND KEY SOURCE OF ESTIMATION UNCERTAINTY - continued

(b) Fair value of derivatives and other financial instruments

The management of the Group use their judgement in selecting an appropriate valuation technique for financial instruments not quoted in an active market. Valuation techniques commonly used by market practitioners are applied. For derivative financial instruments and structured bonds with embedded derivatives, assumptions are made based on quoted market rates adjusted for specific features of the instrument.

The fair values of unlisted equity investments and bond funds are determined based on the net asset values as reported by fund administrator.

Investments in Structured Investment Vehicles (“SIV”) are included under available-for-sale investments. Due to the non-availability of quoted prices of the SIVs and the lack of market transactions in SIVs in recent months as a consequence of current credit market conditions, the Group estimated their fair values by reference to the net asset value of the respective capital notes of each SIV as provided by sponsoring banks of the SIVs and after making further adjustments, as necessary, to take into account other relevant factors or conditions of the SIVs at the year end. Net asset value as provided by the sponsoring banks is calculated by reference to estimated fair values of the underlying investments made by the SIVs, however, a breakdown of underlying investments is not normally provided to the SIV noteholders. Accordingly, the Group has to rely on the net asset value calculation as provided by sponsoring banks and as a result of the leverage nature of the SIVs, any change in the value of underlying investments will lead to multiple changes in the value of the SIV notes.

Details of the assumptions used are disclosed in Note 7.

(c) Estimated impairment of goodwill

According to HKAS 36, impairment loss is made when the carrying amount of an asset exceeds its recoverable amount, which is calculated at the higher of the fair value less costs to sell and value in use.

Management has reviewed goodwill for impairment by comparing the carrying amount and value in use of an acquired subsidiary (the smallest cash-generating unit) to which the goodwill has been allocated. The acquired subsidiary is involved in insurance business.

The value in use calculations primarily use cash flow projections based on five year financial budgets approved by management and estimated terminal value at the end of the five year period. There are a number of assumptions and estimates involved for the preparation of cash flow projections for the period covered by the approved budget and the estimated terminal value. Key assumptions include the expected growth in revenues and selection of discount rates.

Details of the recoverable amount calculation are disclosed in Note 32.

(d) Impairment of available-for-sale investments

The Group determines that available-for-sale investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement, the Group evaluates among other factors, the duration and extent to which the fair value of the investment is less than its cost. In addition, impairment may be appropriate when there is evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows.

Details of the impairment assessment are disclosed in Note 33.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

5. CRITICAL ACCOUNTING JUDGEMENT AND KEY SOURCE OF ESTIMATION UNCERTAINTY - continued

Critical judgements in applying the entity's accounting policies

The following are the critical judgements, apart from those involving estimations, that the management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the consolidated financial statements.

Held-to-maturity investments

The Group classified certain non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires judgement. In making this judgement, the Group evaluates its intention and ability to hold such investments to maturity. If the Group fails to keep these investments to maturity other than for the specific circumstances - for example, selling an insignificant amount close to maturity - it will be required to reclassify the entire class as available-for-sale. The investments would therefore be measured at fair value not amortised cost.

Details of these assets are set out in Note 18.

6. BUSINESS AND GEOGRAPHICAL SEGMENTS

(a) Business segments

For management purposes, the Group is currently organised into the following operating divisions - corporate and retail banking, treasury, securities dealing and other banking-related services. These divisions are the basis on which the Group reports its primary segment information.

Principal activities are as follows:

The corporate and retail banking services provided by the Group are principally lending and trade finance facilities, consumer financing, overdraft facilities, mandatory provident fund services, provision of fixed deposits, current and savings accounts, credit cards and personal wealth management services. The Group also provides fully automated telephone and internet banking services to its customers. Other banking-related services offered include remittance and money exchange, safe deposit boxes, autopay and direct debit services.

Treasury activities mainly comprise inter-bank placement and deposit transactions, management of overall interest rate risk and liquidity of the Group and centralised cash management. Income from foreign exchange activities is generated from services provided to customers in the form of foreign exchange trading and forward contracts.

Securities dealing activities of the Group include securities trading, stockbroking and futures broking.

Other banking-related services of the Group include investment holding, insurance, other investment advisory services and property investments.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS - continued

(a) Business segments - continued

- (i) Segment information about these businesses for the year ended 31 December 2007 is presented below:

INCOME STATEMENT

	Corporate and retail banking HK\$'000	Treasury activities HK\$'000	Securities dealing HK\$'000	Other banking- related services HK\$'000	Eliminations HK\$'000	Consolidated HK\$'000
Interest income from external customers	1,626,540	1,675,038	8,906	-	-	3,310,484
Interest expense to external customers	(2,228,507)	(111,364)	-	-	-	(2,339,871)
Inter-segment interest income (note)	1,156,760	-	-	-	(1,156,760)	-
Inter-segment interest expense (note)	-	(1,156,760)	-	-	1,156,760	-
Net interest income	554,793	406,914	8,906	-	-	970,613
Fee and commission income	76,659	-	202,794	47,188	-	326,641
Fee and commission expense	(37,162)	-	(1,672)	(4,395)	-	(43,229)
Other operating income	91,384	17,840	(60)	57,505	-	166,669
Total operating income	685,674	424,754	209,968	100,298	-	1,420,694
Operating expenses	(366,304)	(27,222)	(51,471)	(21,919)	-	(466,916)
Impairment allowances on loans and advances	(82,922)	-	-	-	-	(82,922)
Net loss on disposal of property and equipment	(64)	-	-	-	-	(64)
Net gain on disposal of land	2,591	-	-	-	-	2,591
Net gain on disposal of investment properties	-	-	-	14,420	-	14,420
Net gain on disposal of available-for-sale securities	-	-	-	177,351	-	177,351
Fair value adjustment on investment properties	-	-	-	14,391	-	14,391
Impairment loss on available-for-sale securities	-	(369,627)	-	-	-	(369,627)
Impairment loss on goodwill	-	-	-	(30,000)	-	(30,000)
Segment profit	238,975	27,905	158,497	254,541	-	679,918
Unallocated corporate expenses						(175,978)
Profit from operations						503,940
Share of profits of jointly controlled entities				66,074		66,074
Profit before taxation						570,014
Taxation						(64,982)
Profit for the year						505,032

Note: Inter-segment pricing for funding transactions is charged at prevailing customer deposit interest rates.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS - continued

(a) Business segments - continued

- (i) Segment information about these businesses for the year ended 31 December 2007 is presented below: - continued

BALANCE SHEET

	Corporate and retail banking HK\$'000	Treasury activities HK\$'000	Securities dealing HK\$'000	Other banking- related services HK\$'000	Consolidated HK\$'000
Assets					
Segment assets	34,309,585	33,100,358	433,174	803,642	68,646,759
Interests in jointly controlled entities	-	-	-	142,230	142,230
Loan to a jointly controlled entity	-	-	-	5,267	5,267
Unallocated corporate assets					258,145
Consolidated total assets					<u>69,052,401</u>
Liabilities					
Segment liabilities	60,666,292	1,559,890	366,359	37,096	62,629,637
Unallocated corporate liabilities					151,976
Consolidated total liabilities					<u>62,781,613</u>

OTHER INFORMATION

	Corporate and retail banking HK\$'000	Treasury activities HK\$'000	Securities dealing HK\$'000	Other banking- related services HK\$'000	Unallocated HK\$'000	Consolidated HK\$'000
Capital additions	75,166	2,355	28,007	2,528	23,165	131,221
Depreciation	22,446	836	1,819	751	10,994	36,846
Amortisation	<u>2,599</u>	<u>247</u>	<u>373</u>	<u>3</u>	<u>2,488</u>	<u>5,710</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS - continued

(a) Business segments - continued

(ii) Segment information about these businesses for the year ended 31 December 2006 is presented below:

INCOME STATEMENT

	Corporate and retail banking HK\$'000	Treasury activities HK\$'000	Securities dealing HK\$'000	Other banking- related services HK\$'000	Eliminations HK\$'000	Consolidated HK\$'000
Interest income from external customers	1,477,181	1,258,559	4,778	-	-	2,740,518
Interest expense to external customers	(1,852,569)	(59,410)	-	-	-	(1,911,979)
Inter-segment interest income (note)	868,714	-	-	-	(868,714)	-
Inter-segment interest expense (note)	-	(868,714)	-	-	868,714	-
Net interest income	493,326	330,435	4,778	-	-	828,539
Fee and commission income	63,146	-	79,247	29,908	-	172,301
Fee and commission expense	(723)	-	(644)	(2,799)	-	(4,166)
Other operating income	62,812	41,682	-	29,060	-	133,554
Total operating income	618,561	372,117	83,381	56,169	-	1,130,228
Operating expenses	(343,071)	(24,472)	(30,748)	(19,977)	-	(418,268)
Impairment allowances on loans and advances	(59,801)	-	-	-	-	(59,801)
Net loss on disposal of property and equipment	(913)	-	-	-	-	(913)
Net gain on disposal of available-for-sale securities	-	-	-	54,001	-	54,001
Fair value adjustment on investment properties	-	-	-	5,390	-	5,390
Segment profit	<u>214,776</u>	<u>347,645</u>	<u>52,633</u>	<u>95,583</u>	<u>-</u>	710,637
Unallocated corporate expenses						(173,269)
Profit from operations						537,368
Share of profit of jointly controlled entities				<u>33,546</u>		33,546
Profit before taxation						570,914
Taxation						(67,770)
Profit for the year						<u>503,144</u>

Note: Inter-segment pricing for funding transactions is charged at prevailing customer deposit interest rates.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS - continued

(a) Business segments - continued

(ii) Segment information about these businesses for the year ended 31 December 2006 is presented below: - continued

BALANCE SHEET

	Corporate and retail banking HK\$'000	Treasury activities HK\$'000	Securities dealing HK\$'000	Other banking- related services HK\$'000	Consolidated HK\$'000
Assets					
Segment assets	28,544,911	32,929,054	295,609	833,071	62,602,645
Interests in jointly controlled entities	-	-	-	99,256	99,256
Loan to a jointly controlled entity	-	-	-	31,000	31,000
Unallocated corporate assets					296,998
Consolidated total assets					<u>63,029,899</u>
Liabilities					
Segment liabilities	55,006,716	1,498,085	281,035	36,214	56,822,050
Unallocated corporate liabilities					156,119
Consolidated total liabilities					<u>56,978,169</u>

OTHER INFORMATION

	Corporate and retail banking HK\$'000	Treasury activities HK\$'000	Securities dealing HK\$'000	Other banking- related services HK\$'000	Unallocated HK\$'000	Consolidated HK\$'000
Capital additions	139,351	19,729	9,499	2,362	65,487	236,428
Depreciation	16,121	306	1,007	697	12,404	30,535
Amortisation	3,490	-	113	5	1,506	5,114

(b) Geographical segments

Geographical segmentation is analysed by the Group based on the locations of the principal operations of the branches and subsidiary companies responsible for reporting the results or booking the assets. For both years 2006 and 2007, more than 90% of the Group's revenue were generated by customers located in Hong Kong and profit before taxation were generated by assets booked by the principal operations of the branches and subsidiary companies located in Hong Kong. More than 90% of assets were located in Hong Kong and the remaining assets were extended to branches outside Hong Kong, mainly in the Mainland China and America.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

6. BUSINESS AND GEOGRAPHICAL SEGMENTS - continued

(b) Geographical segments - continued

Details of geographical segmentation are set out below:

	2007					
	Total operating income HK\$'000	Profit before taxation HK\$'000	Total assets HK\$'000	Total liabilities HK\$'000	Total contingent liabilities and commitments HK\$'000	Capital expenditure during the year HK\$'000
Hong Kong	1,358,206	485,868	67,041,552	61,410,227	17,442,739	122,962
Asia Pacific (excluding Hong Kong)	39,243	67,039	1,541,043	1,134,006	325,076	8,231
America	23,245	17,107	469,806	237,380	176,433	28
Total	<u>1,420,694</u>	<u>570,014</u>	<u>69,052,401</u>	<u>62,781,613</u>	<u>17,944,248</u>	<u>131,221</u>

	2006					
	Total operating income HK\$'000	Profit before taxation HK\$'000	Total assets HK\$'000	Total liabilities HK\$'000	Total contingent liabilities and commitments HK\$'000	Capital expenditure during the year HK\$'000
Hong Kong	1,061,372	496,045	60,581,313	55,640,229	11,729,612	235,115
Asia Pacific (excluding Hong Kong)	43,248	55,139	1,935,345	1,113,537	274,869	705
America	25,608	19,730	513,241	224,403	147,388	608
Total	<u>1,130,228</u>	<u>570,914</u>	<u>63,029,899</u>	<u>56,978,169</u>	<u>12,151,869</u>	<u>236,428</u>

Note: Total operating income consists of net interest income, net fee and commission income and other operating income.

7. FINANCIAL RISK MANAGEMENT

The Group's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. The Group's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Group's financial performance.

The Group's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to date information systems. The Group regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practice.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Risk management is carried out by the Asset and Liability Management Committee (the “ALCO”) under policies approved by the Board of Directors. ALCO identifies, evaluates and hedges financial risks in close co-operation with the Group’s operating units. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments. In addition, internal audit is responsible for the independent review of risk management and the control environment. The most important types of risks from the use of financial instruments are credit risk, market risk and liquidity risk. Market risk includes currency risk, interest rate and other price risk.

Credit risk

The Group takes on exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Impairment allowances are made for losses that have been incurred at the balance sheet date. Significant changes in the economy, or in the health of a particular industry segment, could result in losses that are different from those provided for at the balance sheet date. Management therefore carefully manages its exposure to credit risk.

Management of credit risk

The Group’s lending policies have been formulated on the basis of its own experience, the Banking Ordinance, the Hong Kong Monetary Authority guidelines and other statutory requirements (in the case of overseas branches and subsidiaries, the relevant local laws and regulations).

The Group’s primary credit approval bodies are the Loans Committee, which comprises senior staff members of the Bank, and the Executive Loans Committee, comprising all the Executive Directors of the Bank. The Executive Loans Committee has overall responsibility for the Group’s credit policies and oversees the credit quality of the Group’s advance portfolio. Under the oversight of the Executive Loans Committee, officers of the Group are authorised to approve credit based on the size of the advance, the collateral provided, the credit standing of the applicant and other prescribed credit guidelines.

The Credit Assessment Department is responsible for reviewing all credit applications. When a customer fills out an advance application or requests a credit line, the branch or lending department account officer collects information through customer interviews, documentation requests and feasibility studies as well as other sources. The account officer then prepares and submits a credit proposal based on the information gathered for the review of the Credit Review Officers. Credit Review Officers are required to check the accuracy of the information submitted and that the credit proposal meets the underwriting standard required, and are required to provide an independent credit evaluation in support of a recommendation for granting or rejecting the advance and subsequent renewal applications.

Credit approval is performed by the Loans Committee in accordance with the delegated lending authority from the Lending Policy of the Bank with reference to a customer’s objective of borrowing, financial strength, repayment ability, past account performance and collateral being offered as security, as appropriate. Approval from the Executive Loans Committee is required as and when the requested amount of the advance exceeds the delegated authority of the Loans Committee.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Management of credit risk - continued

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are typically monitored on a revolving basis and are subject to periodic reviews. Limits on the level of credit risk by product, industry sector and by country are approved annually by the Board.

Exposure to credit risk is managed through regular reviews of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

Risk mitigation policies

Some specific control and mitigation measures are outlined below:

(a) Collateral

The Group implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Mortgages over residential properties;
- Charges over business assets such as premises, inventory and accounts receivable; or
- Charges over financial instruments such as debt securities and equities.

In addition, in order to minimise the credit loss the Group will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

(b) Other risk mitigations

The Group uses guarantees and derivatives as credit risk mitigations. Whilst the Group may accept guarantees from any counterparty, it sets a threshold internally for considering guarantors to be eligible for credit risk mitigation.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Impairment and provisioning policies

Impairment allowances are recognised for financial reporting purposes only for losses that have been incurred at the balance sheet date based on objective evidence of impairment.

The impairment allowances shown in the balance sheet is derived from the five rating grades adopted by the Hong Kong Monetary Authority, with the majority of the impairment allowances arising from the bottom three gradings.

The Group's gross advances to customers (including advances booked in overseas branches and subsidiaries) are analysed and reported by industry sectors according to the usage of the loans and/or business activities of the borrowers as follows:

	31 December 2007				
	Gross loans and advances HK\$'000	Collective impairment allowances HK\$'000	Individual impairment allowances HK\$'000	Loans and advances covered by collateral HK\$'000	Gross impaired advances HK\$'000
Loans for use in Hong Kong					
Industrial, commercial and financial					
- Property development	2,134,798	14,652	-	614,626	-
- Property investment	6,506,746	2,333	-	5,992,508	19,262
- Financial concerns	2,523,724	-	-	888,553	-
- Stockbrokers	347,428	-	516	336,497	516
- Wholesale and retail trade	833,578	2,181	212	673,111	2,136
- Manufacturing	2,224,813	2,830	12,035	1,121,713	4,177
- Transport and transport equipment	630,345	69	-	34,651	-
- Recreational activities	45,335	-	-	1,602	-
- Information technology	187	-	-	184	-
- Others	4,829,971	10,467	84	2,125,324	58,383
Individuals					
- Loans for the purchase of flats in the Home Ownership Scheme, and Tenants Purchase Scheme	680,384	-	430	680,262	3,950
- Loans for the purchase of other residential properties	4,704,769	4,864	284	4,690,081	284
- Credit card advances	133,586	7,475	308	-	353
- Others	1,677,388	9,243	3,003	1,588,352	9,335
	<u>27,273,052</u>	<u>54,114</u>	<u>16,872</u>	<u>18,747,464</u>	<u>98,396</u>
Trade finance	918,496	8,317	-	288,315	3,520
Loans for use outside Hong Kong	3,530,335	54,289	1,004	1,622,618	113,904
	<u>31,721,883</u>	<u>116,720</u>	<u>17,876</u>	<u>20,658,397</u>	<u>215,820</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Impairment and provisioning policies - continued

	31 December 2006				
	Gross loans and advances HK\$'000	Collective impairment allowances HK\$'000	Individual impairment allowances HK\$'000	Loans and advances covered by collateral HK\$'000	Gross impaired advances HK\$'000
Loans for use in Hong Kong					
Industrial, commercial and financial					
- Property development	1,576,165	9,374	1,000	648,696	23,599
- Property investment	6,073,467	20,054	2,313	5,789,072	27,045
- Financial concerns	1,555,454	-	-	198,072	174
- Stockbrokers	420,851	-	-	307,898	-
- Wholesale and retail trade	768,422	4,143	619	637,609	6,017
- Manufacturing	1,114,492	2,888	87	483,248	2,045
- Transport and transport equipment	326,560	28	1	46,317	375
- Recreational activities	15,012	-	-	2,080	-
- Information technology	-	-	-	-	-
- Others	4,868,117	9,682	6,235	3,036,122	63,680
Individuals					
- Loans for the purchase of flats in the Home Ownership Scheme, and Tenants Purchase Scheme	676,673	473	708	675,860	5,408
- Loans for the purchase of other residential properties	3,476,285	4,352	459	3,468,184	8,708
- Credit card advances	127,460	6,962	139	-	4,036
- Others	1,315,471	12,345	4,102	1,242,061	15,898
	<u>22,314,429</u>	<u>70,301</u>	<u>15,663</u>	<u>16,535,219</u>	<u>156,985</u>
Trade finance	823,153	804	3,498	325,366	10,348
Loans for use outside Hong Kong	<u>3,736,956</u>	<u>33,359</u>	<u>13,000</u>	<u>2,328,549</u>	<u>162,327</u>
	<u>26,874,538</u>	<u>104,464</u>	<u>32,161</u>	<u>19,189,134</u>	<u>329,660</u>

The Group's and the Bank's policy requires the review of individual financial assets that are above materiality thresholds at least annually or more regularly when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the incurred loss at balance sheet date on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses collateral held and the anticipated receipts for that individual account.

Collectively assessed impairment allowances are provided for: (i) portfolios of homogenous assets that are individually below materiality thresholds; and (ii) losses that have been incurred but have not yet been identified, by using the available historical experience, experienced judgment and statistical techniques.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Concentration of risks of financial assets with credit risk exposure

Concentration of credit risk exists when changes in geographic or industry factors similarly affect groups of counterparties whose aggregate credit exposure is material in relation to the Group's total exposures.

An analysis of geographical and industry sector concentration of the Group's and the Bank's financial assets is disclosed below.

Geographical locations

	THE GROUP				THE BANK			
	Asia Pacific				Asia Pacific			
	Hong Kong	Hong Kong	Others	Total	Hong Kong	Hong Kong	Others	Total
	excluding			excluding				
	Hong Kong	Hong Kong	Others	Total	Hong Kong	Hong Kong	Others	Total
	HK\$'000							
At 31 December 2007								
Short term funds	4,179,308	3,426,258	6,851,415	14,456,981	4,128,840	3,426,258	6,851,415	14,406,513
Placement with banks and other financial institutions	-	1,120,238	1,963,909	3,084,147	-	1,120,238	1,963,909	3,084,147
Derivative financial instruments	60	-	-	60	60	-	-	60
Financial assets at fair value through profit or loss	413,390	456,896	263,872	1,134,158	413,390	456,896	263,872	1,134,158
Available-for-sale securities	-	-	239,042	239,042	-	-	239,042	239,042
Held-to-maturity securities	1,667,831	5,865,020	8,075,129	15,607,980	1,667,831	5,865,020	8,075,129	15,607,980
Advances and other accounts	29,593,226	1,513,271	1,389,393	32,495,890	29,193,701	1,511,035	1,388,704	32,093,440
Amounts due from subsidiaries	-	-	-	-	3,407	-	-	3,407
Loan to a jointly controlled entity	5,267	-	-	5,267	5,267	-	-	5,267
	<u>35,859,082</u>	<u>12,381,683</u>	<u>18,782,760</u>	<u>67,023,525</u>	<u>35,412,496</u>	<u>12,379,447</u>	<u>18,782,071</u>	<u>66,574,014</u>

	THE GROUP				THE BANK			
	Asia Pacific				Asia Pacific			
	Hong Kong	Hong Kong	Others	Total	Hong Kong	Hong Kong	Others	Total
	excluding			excluding				
	Hong Kong	Hong Kong	Others	Total	Hong Kong	Hong Kong	Others	Total
	HK\$'000							
At 31 December 2006								
Short term funds	820,618	4,067,371	11,045,162	15,933,151	771,972	4,067,371	11,045,163	15,884,506
Placement with banks and other financial institutions	150,000	1,558,925	929,536	2,638,461	150,000	1,558,925	929,536	2,638,461
Derivative financial instruments	4,962	-	-	4,962	4,962	-	-	4,962
Financial assets at fair value through profit or loss	158,539	254,088	197,761	610,388	158,539	254,088	197,761	610,388
Available-for-sale securities	-	-	472,076	472,076	-	-	472,076	472,076
Held-to-maturity securities	2,283,881	4,502,033	7,117,259	13,903,173	2,283,881	4,502,033	7,117,259	13,903,173
Advances and other accounts	24,839,590	1,831,739	825,691	27,497,020	24,546,300	1,830,528	825,025	27,201,853
Amounts due from subsidiaries	-	-	-	-	4,677	-	-	4,677
Loan to a jointly controlled entity	31,000	-	-	31,000	31,000	-	-	31,000
	<u>28,288,590</u>	<u>12,214,156</u>	<u>20,587,485</u>	<u>61,090,231</u>	<u>27,951,331</u>	<u>12,212,945</u>	<u>20,586,820</u>	<u>60,751,096</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Concentration of risks of financial assets with credit risk exposure - continued

Industry sectors

	THE GROUP					Total HK\$'000
	Financial institutions HK\$'000	Central	Public	Corporate entities HK\$'000	Others HK\$'000	
		Government	sector			
		and central banks HK\$'000	entities HK\$'000			
At 31 December 2007						
Short term funds	11,303,164	3,153,817	-	-	-	14,456,981
Placement with banks and other financial institutions	3,084,147	-	-	-	-	3,084,147
Derivative financial instruments	-	-	-	60	-	60
Financial assets at fair value through profit or loss	475,282	118,393	-	535,484	4,999	1,134,158
Available-for-sale securities	208,436	-	-	30,606	-	239,042
Held-to-maturity securities	15,060,293	534,442	11,245	2,000	-	15,607,980
Advances and other accounts	2,928,236	-	-	20,196,779	9,370,875	32,495,890
Loan to a jointly controlled entity	5,267	-	-	-	-	5,267
	<u>33,064,825</u>	<u>3,806,652</u>	<u>11,245</u>	<u>20,764,929</u>	<u>9,375,874</u>	<u>67,023,525</u>
At 31 December 2006						
Short term funds	15,418,306	514,845	-	-	-	15,933,151
Placement with banks and other financial institutions	2,638,461	-	-	-	-	2,638,461
Derivative financial instruments	4,567	263	-	35	97	4,962
Financial assets at fair value through profit or loss	372,463	-	-	50,679	187,246	610,388
Available-for-sale securities	-	-	-	-	472,076	472,076
Held-to-maturity securities	13,384,170	359,143	18,508	141,352	-	13,903,173
Advances and other accounts	2,033,730	-	-	17,605,462	7,857,828	27,497,020
Loan to a jointly controlled entity	31,000	-	-	-	-	31,000
	<u>33,882,697</u>	<u>874,251</u>	<u>18,508</u>	<u>17,797,528</u>	<u>8,517,247</u>	<u>61,090,231</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Concentration of risks of financial assets with credit risk exposure - continued

Industry sectors - continued

	THE BANK					Total HK\$'000
	Financial institutions HK\$'000	Central	Public	Corporate entities HK\$'000	Others HK\$'000	
		Government and central banks HK\$'000	sector entities HK\$'000			
At 31 December 2007						
Short term funds	11,252,696	3,153,817	-	-	-	14,406,513
Placement with banks and other financial institutions	3,084,147	-	-	-	-	3,084,147
Derivative financial instruments	-	-	-	60	-	60
Financial assets at fair value through profit or loss	475,282	118,393	-	535,484	4,999	1,134,158
Available-for-sale securities	208,436	-	-	30,606	-	239,042
Held-to-maturity securities	15,060,293	534,442	11,245	2,000	-	15,607,980
Advances and other accounts	2,928,236	-	-	19,794,853	9,370,351	32,093,440
Amounts due from subsidiaries	2,680	-	-	727	-	3,407
Loan to a jointly controlled entity	5,267	-	-	-	-	5,267
	<u>33,017,037</u>	<u>3,806,652</u>	<u>11,245</u>	<u>20,363,730</u>	<u>9,375,350</u>	<u>66,574,014</u>
At 31 December 2006						
Short term funds	15,369,661	514,845	-	-	-	15,884,506
Placement with banks and other financial institutions	2,638,461	-	-	-	-	2,638,461
Derivative financial instruments	4,567	263	-	35	97	4,962
Financial assets at fair value through profit or loss	372,463	-	-	50,679	187,246	610,388
Available-for-sale securities	-	-	-	-	472,076	472,076
Held-to-maturity securities	13,384,170	359,143	18,508	141,352	-	13,903,173
Advances and other accounts	2,033,730	-	-	17,311,904	7,856,219	27,201,853
Amounts due from subsidiaries	1,999	-	-	2,678	-	4,677
Loan to a jointly controlled entity	31,000	-	-	-	-	31,000
	<u>33,836,051</u>	<u>874,251</u>	<u>18,508</u>	<u>17,506,648</u>	<u>8,515,638</u>	<u>60,751,096</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Maximum exposure to credit risk before collateral held or other credit enhancements

Credit risk exposures relating to on-balance sheet assets are as follows:

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Short-term funds	14,456,981	15,933,151	14,406,513	15,884,506
Placements with banks and other financial institutions	3,084,147	2,638,461	3,084,147	2,638,461
Derivative financial instruments	60	4,962	60	4,962
Financial assets at fair value through profit or loss	1,134,158	610,388	1,134,158	610,388
Available-for-sale securities	239,042	472,076	239,042	472,076
Held-to-maturity securities	15,607,980	13,903,173	15,607,980	13,903,173
Advances and other accounts	32,495,890	27,497,020	32,093,440	27,201,853
Amounts due from subsidiaries	–	–	3,407	4,677
Loan to a jointly controlled entity	5,267	31,000	5,267	31,000
	<u>67,023,525</u>	<u>61,090,231</u>	<u>66,574,014</u>	<u>60,751,096</u>

Credit risk exposures relating to off-balance sheet assets are as follows:

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Financial guarantee and other credit related contingent liabilities	1,239,142	1,567,919	1,239,142	1,567,919
Loan commitments and other credit related commitments	16,606,916	10,284,935	16,606,916	10,284,935
Other commitments	98,190	299,015	95,514	294,310
	<u>17,944,248</u>	<u>12,151,869</u>	<u>17,941,572</u>	<u>12,147,164</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Credit quality

Credit quality of loans and advances to customers and banks are summarised as follows:

	THE GROUP	
	31 December 2007	31 December 2006
	HK\$'000	HK\$'000
Neither past due nor impaired	31,626,817	26,562,291
Past due but not impaired	222,517	307,349
Impaired	<u>215,820</u>	<u>329,660</u>
	32,065,154	27,199,300
Less: allowance for impairment	<u>(134,596)</u>	<u>(136,625)</u>
	<u>31,930,558</u>	<u>27,062,675</u>

	THE BANK	
	31 December 2007	31 December 2006
	HK\$'000	HK\$'000
Neither past due nor impaired	31,625,904	26,560,289
Past due but not impaired	222,517	307,349
Impaired	<u>215,820</u>	<u>329,660</u>
	32,064,241	27,197,298
Less: allowance for impairment	<u>(134,590)</u>	<u>(136,608)</u>
	<u>31,929,651</u>	<u>27,060,690</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Credit quality - continued

(ii) Loans and advances past due but not impaired

Gross amount of loans and advances by class to customers that were past due but not impaired were as follows:

	THE GROUP AND THE BANK							Total
	Overdrafts	Instalment loans	Term loans	Syndication loans	Trade finance	Personal		
						tax loans	Others	
HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
At 31 December 2007								
Past due up to 30 days	2,074	8,380	-	-	13,363	67	-	23,884
Past due from 31 to 90 days	17,503	56,550	1,460	-	35,548	302	2,919	114,282
Past due more than 90 days	15,779	57,468	-	-	11,104	-	-	84,351
Total	<u>35,356</u>	<u>122,398</u>	<u>1,460</u>	<u>-</u>	<u>60,015</u>	<u>369</u>	<u>2,919</u>	<u>222,517</u>
Fair value of collateral	<u>101,395</u>	<u>318,680</u>	<u>332</u>	<u>-</u>	<u>39,219</u>	<u>-</u>	<u>-</u>	<u>459,626</u>
At 31 December 2006								
Past due up to 30 days	-	31,705	-	-	1,886	-	-	33,591
Past due from 31 to 90 days	28,250	85,637	-	-	9,247	43	3,886	127,063
Past due more than 90 days	13,982	105,116	2,800	9,881	14,916	-	-	146,695
Total	<u>42,232</u>	<u>222,458</u>	<u>2,800</u>	<u>9,881</u>	<u>26,049</u>	<u>43</u>	<u>3,886</u>	<u>307,349</u>
Fair value of collateral	<u>93,556</u>	<u>409,013</u>	<u>4,720</u>	<u>-</u>	<u>34,280</u>	<u>-</u>	<u>-</u>	<u>541,569</u>

Upon initial recognition of loans and advances, the fair value of collateral is determined based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated by reference to market price.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Credit quality - continued

(iii) Loans and advances individually impaired

(a) Loans and advances to customers

The breakdown of the gross amount of individually impaired loans and advances by class, along with the fair value of related collateral held by the Group and the Bank as security, are as follows:

	THE GROUP AND THE BANK							
	Overdrafts HK\$'000	Instalment loans HK\$'000	Term loans HK\$'000	Syndication loans HK\$'000	Trade finance HK\$'000	Personal loans/ tax loans HK\$'000	Others HK\$'000	Total HK\$'000
At 31 December 2007								
Individually impaired loans	<u>57,863</u>	<u>18,496</u>	<u>121,816</u>	<u>12,910</u>	<u>3,633</u>	<u>749</u>	<u>353</u>	<u>215,820</u>
Fair value of collateral	<u>162,423</u>	<u>21,501</u>	<u>270,105</u>	<u>23,860</u>	<u>4,038</u>	<u>-</u>	<u>-</u>	<u>481,927</u>
At 31 December 2006								
Individually impaired loans	<u>96,866</u>	<u>32,473</u>	<u>159,404</u>	<u>23,293</u>	<u>13,370</u>	<u>218</u>	<u>4,036</u>	<u>329,660</u>
Fair value of collateral	<u>166,611</u>	<u>43,474</u>	<u>225,918</u>	<u>37,399</u>	<u>13,723</u>	<u>-</u>	<u>-</u>	<u>487,125</u>

(b) Loans and advances to banks

There are no individually impaired loans and advances to banks as at 31 December 2007 and 31 December 2006.

(iv) Loans and advances renegotiated

Restructuring activities include extended payment arrangements, approved external management plans, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgement of local management, indicate that payment will most likely continue. These policies are kept under continuous review.

	THE GROUP AND THE BANK	
	2007 HK\$'000	2006 HK\$'000
Renegotiated loans that would otherwise be past due or impaired	<u>918</u>	<u>55,000</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Debt securities

Financial investments by rating agency designation

The following table presents an analysis of financial securities, other than loans and advances, held by the Group and the Bank by rating agency designation at the balance sheet dates, based on Moody's ratings. Financial securities not rated by Moody's are treated as unrated ones.

	THE GROUP AND THE BANK			
	Financial asset at fair value through profit or loss HK\$'000	Available- for-sale securities (excluding equity securities) HK\$'000	Held-to- maturity securities HK\$'000	Total HK\$'000
At 31 December 2007				
Aaa	71,211	–	1,244,723	1,315,934
Aa1 to Aa3	499,575	39,012	11,842,288	12,380,875
A1 to A3	39,012	–	1,859,745	1,898,757
Lower than A3	–	100,831	296,937	397,768
Unrated	524,360	99,199	364,287	987,846
Total	<u>1,134,158</u>	<u>239,042</u>	<u>15,607,980</u>	<u>16,981,180</u>
At 31 December 2006				
Aaa	22,225	–	1,546,161	1,568,386
Aa1 to Aa3	369,894	38,892	7,973,253	8,382,039
A1 to A3	62,079	–	3,372,304	3,434,383
Lower than A3	–	277,561	308,993	586,554
Unrated	156,190	155,623	702,462	1,014,275
Total	<u>610,388</u>	<u>472,076</u>	<u>13,903,173</u>	<u>14,985,637</u>

Reposessed collateral

During the years indicated, the Group and the Bank obtained assets by taking possession of collateral held as security, as follows:

Nature of assets	THE GROUP AND THE BANK	
	2007 HK\$'000	2006 HK\$'000
Residential properties	63,070	53,910
Others	39,700	53,070

Reposessed assets are sold as soon as practicable with the proceeds used to reduce the outstanding indebtedness.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk

The Group and the Bank take on exposure to market risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads, foreign exchange rates and equity prices. The Group and the Bank separate exposures to market risk into either trading or non-trading portfolios.

Trading portfolios include those positions arising from market-making transactions where the Group and the Bank act as principal with clients or with the market.

Non-trading portfolios primarily arise from the interest rate management of the entity's retail and commercial banking assets and liabilities. Non-trading portfolios also consist of foreign exchange and equity risks arising from the Group's and the Bank's held-to-maturity and available-for-sale investments.

The management of market risk is principally undertaken in treasury function using risk limits approved by the Board of Directors. Limits are set for each portfolio, product and risk type, with market liquidity being a principal factor in determining the level of limits set. The Group has dedicated standards, policies and procedures in place to control and monitor the market risk. The market risks which arise on each business are assessed and managed under the supervision of ALCO.

In addition, the Group uses derivatives to mitigate interest rate and foreign exchange risk.

Management of market risk

Stress tests are carried out to provide an indication of the potential size of losses that could arise in extreme conditions. The results of the stress tests are reviewed by senior management in each business unit and by the Board of Directors. The stress testing is tailored to the business segments and typically uses scenario analysis.

Foreign exchange risk

The Group and the Bank undertake certain transactions denominated in foreign currencies and, hence exposures to exchange rate fluctuations arise. Exchange rate exposures are managed within approved policy parameters utilising forward foreign exchange contracts.

The Group and the Bank do not have any significant foreign exchange risk as foreign exchange dealing is moderate. Structural foreign exchange exposure arising from investments in foreign branches and subsidiaries is accounted for in the reserves account. Day-to-day foreign exchange management is performed by the Treasury Management Department within approved limits.

The Group and the Bank take on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board of Directors sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Foreign exchange risk - continued

The following table indicates the concentration of currency risk at the balance sheet date:

	THE GROUP				
	HK\$	US\$	MOP	Others	Total
Hong Kong dollars equivalents (HK\$'000)					
At 31 December 2007					
Assets					
Cash and short-term funds	9,814,179	3,269,551	85,227	1,595,020	14,763,977
Placements with banks and other financial institutions	959,999	1,630,681	–	493,467	3,084,147
Derivative financial instruments	60	–	–	–	60
Financial assets at fair value through profit or loss	807,088	327,334	–	–	1,134,422
Available-for-sale securities	224,822	647,823	–	4,016	876,661
Held-to-maturity securities	6,061,007	6,128,323	–	3,418,650	15,607,980
Advances to customers	30,256,331	1,248,302	26,973	190,277	31,721,883
Other assets	1,641,222	196,745	170	25,134	1,863,271
Total assets	<u>49,764,708</u>	<u>13,448,759</u>	<u>112,370</u>	<u>5,726,564</u>	<u>69,052,401</u>
Liabilities					
Deposits and balances of banks and other financial institutions	3,116	277,707	–	176,035	456,858
Deposits from customers	42,301,866	12,389,216	62,443	5,573,912	60,327,437
Derivative financial instruments	114,546	–	–	–	114,546
Loan capital	(4,417)	975,288	–	–	970,871
Other liabilities	799,007	77,984	3,843	31,067	911,901
Total liabilities	<u>43,214,118</u>	<u>13,720,195</u>	<u>66,286</u>	<u>5,781,014</u>	<u>62,781,613</u>
Net on-balance sheet position	<u>6,550,590</u>	<u>(271,436)</u>	<u>46,084</u>	<u>(54,450)</u>	<u>6,270,788</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Foreign exchange risk - continued

	HK\$	THE GROUP			Total
		US\$	MOP	Others	
Hong Kong dollars equivalents (HK\$'000)					
At 31 December 2006					
Assets					
Cash and short term funds	8,954,099	4,007,904	71,684	3,223,172	16,256,859
Placements with banks and other financial institutions	2,140,000	388,925	–	109,536	2,638,461
Derivative financial instruments	4,962	–	–	–	4,962
Financial assets at fair value through profit or loss	251,962	358,849	–	–	610,811
Available-for-sale securities	362,256	595,024	–	140,861	1,098,141
Held-to-maturity securities	7,483,646	6,011,026	–	408,501	13,903,173
Advances to customers	24,963,656	1,529,678	35,964	345,240	26,874,538
Other assets	1,558,918	67,835	148	16,053	1,642,954
Total assets	<u>45,719,499</u>	<u>12,959,241</u>	<u>107,796</u>	<u>4,243,363</u>	<u>63,029,899</u>
Liabilities					
Deposits and balances of banks and other financial institutions	95,803	352,218	–	80,972	528,993
Deposits from customers	38,855,766	11,297,915	46,722	4,474,829	54,675,232
Derivative financial instruments	1,716	–	–	–	1,716
Loan capital	(4,624)	972,000	–	–	967,376
Other liabilities	720,559	62,909	3,107	18,277	804,852
Total liabilities	<u>39,669,220</u>	<u>12,685,042</u>	<u>49,829</u>	<u>4,574,078</u>	<u>56,978,169</u>
Net on-balance sheet position	<u>6,050,279</u>	<u>274,199</u>	<u>57,967</u>	<u>(330,715)</u>	<u>6,051,730</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Foreign exchange risk - continued

	HK\$	US\$	THE BANK		Total
			MOP	Others	
Hong Kong dollars equivalents (HK\$'000)					
At 31 December 2007					
Assets					
Cash and short-term funds	9,763,674	3,269,551	85,227	1,595,020	14,713,472
Placements with banks and other financial institutions	959,999	1,630,681	–	493,467	3,084,147
Derivative financial instruments	60	–	–	–	60
Financial assets at fair value through profit or loss	806,824	327,334	–	–	1,134,158
Available-for-sale securities	72,348	647,823	–	4,016	724,187
Held-to-maturity securities	6,061,007	6,128,323	–	3,418,650	15,607,980
Advances to customers	30,255,802	1,248,302	26,973	190,277	31,721,354
Other assets	1,882,537	196,745	170	22,988	2,102,440
Total assets	<u>49,802,251</u>	<u>13,448,759</u>	<u>112,370</u>	<u>5,724,418</u>	<u>69,087,798</u>
Liabilities					
Deposits and balances of banks and other financial institutions	3,116	277,707	–	176,035	456,858
Deposits from customers	42,298,027	12,389,216	62,443	5,573,912	60,323,598
Derivative financial instruments	114,546	–	–	–	114,546
Loan capital	(4,417)	975,288	–	–	970,871
Other liabilities	1,008,179	77,984	3,843	28,921	1,118,927
Total liabilities	<u>43,419,451</u>	<u>13,720,195</u>	<u>66,286</u>	<u>5,778,868</u>	<u>62,984,800</u>
Net on-balance sheet position	<u>6,382,800</u>	<u>(271,436)</u>	<u>46,084</u>	<u>(54,450)</u>	<u>6,102,998</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Foreign exchange risk - continued

	HK\$	US\$	THE BANK		Total
			MOP	Others	
Hong Kong dollars equivalents (HK\$'000)					
At 31 December 2006					
Assets					
Cash and short term funds	8,905,413	4,007,904	71,684	3,223,173	16,208,174
Placements with banks and other financial institutions	2,140,000	388,925	–	109,536	2,638,461
Derivative financial instruments	4,962	–	–	–	4,962
Financial assets at fair value through profit or loss	251,539	358,849	–	–	610,388
Available-for-sale securities	180,547	595,024	–	140,862	916,433
Held-to-maturity securities	7,483,646	6,011,026	–	408,501	13,903,173
Advances to customers	24,961,935	1,529,678	35,964	345,241	26,872,818
Other assets	1,979,414	67,835	148	15,978	2,063,375
Total assets	<u>45,907,456</u>	<u>12,959,241</u>	<u>107,796</u>	<u>4,243,291</u>	<u>63,217,784</u>
Liabilities					
Deposits and balances of banks and other financial institutions	95,803	352,218	–	80,972	528,993
Deposits from customers	38,851,708	11,297,915	46,722	4,474,829	54,671,174
Derivative financial instruments	1,716	–	–	–	1,716
Loan capital	(4,624)	972,000	–	–	967,376
Other liabilities	996,148	62,909	3,107	18,205	1,080,369
Total liabilities	<u>39,940,751</u>	<u>12,685,042</u>	<u>49,829</u>	<u>4,574,006</u>	<u>57,249,628</u>
Net on-balance sheet position	<u>5,966,705</u>	<u>274,199</u>	<u>57,967</u>	<u>(330,715)</u>	<u>5,968,156</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Foreign exchange risk - continued

Foreign currency sensitivity

The Group and the Bank is mainly exposed to US dollars, Renminbi and Macau Pataca. The following table details the Group's and the Bank's sensitivity to a 1 per cent change in Hong Kong dollars against the US dollars, and 10 percent change in Hong Kong dollars against Renminbi and Macau Pataca. The percentage is the rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the possible change in foreign exchange rates. The sensitivity analyses of the Group's and the Bank's exposure to foreign currency risk at the reporting date has been determined based on the change taking place at the beginning of the financial year and held constant throughout the reporting period.

	Change in currency rate					
	US Dollars		Renminbi		Macau Pataca	
	+1%	-1%	+10%	-10%	+10%	-10%
THE GROUP						
Hong Kong dollars equivalents (HK\$'000)						
2007						
Profit before tax	(2,855)	2,855	9,818	(9,818)	4,608	(4,608)
Other equity	46	(46)	-	-	-	-
2006						
Profit before tax	3	(3)	37	(37)	5,797	(5,797)
Other equity	37	(37)	-	-	-	-
THE BANK						
2007						
Profit before tax	(2,855)	2,855	9,818	(9,818)	4,608	(4,608)
Other equity	46	(46)	-	-	-	-
2006						
Profit before tax	3	(3)	37	(37)	5,797	(5,797)
Other equity	37	(37)	-	-	-	-

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Group and the Bank take on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both fair value and cash flow risks. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. Limits are set on the level of mismatch of interest rate repricing that may be undertaken, which is monitored regularly.

The Group and the Bank measures the exposure of its assets and liabilities to fluctuations in interest rates primarily by way of gap analysis which provides the Group and the Bank with a static view of the maturity and re-pricing characteristics of balance sheet positions.

The tables below summarise the Group's and the Bank's exposure to interest rate risks. Included in the tables are the Group's and the Bank's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

	THE GROUP					Total HK\$'000
	Up to 3 months HK\$'000	3 - 12 months HK\$'000	1 - 5 years HK\$'000	Over 5 years HK\$'000	Non- interest bearing HK\$'000	
At 31 December 2007						
Assets						
Cash and short-term funds	14,361,137	51,052	-	-	351,788	14,763,977
Placements with banks and other financial institutions	2,684,574	399,573	-	-	-	3,084,147
Derivative financial instruments	-	-	-	-	60	60
Financial assets at fair value						
through profit or loss	861,059	-	78,023	-	195,340	1,134,422
Available-for-sale securities	239,042	-	-	-	637,619	876,661
Held-to-maturity securities	12,871,862	2,655,195	78,923	-	2,000	15,607,980
Advances to customers	30,561,808	822,886	50,875	2,846	283,468	31,721,883
Other assets	9,733	20,620	26,731	-	1,806,187	1,863,271
Total assets	<u>61,589,215</u>	<u>3,949,326</u>	<u>234,552</u>	<u>2,846</u>	<u>3,276,462</u>	<u>69,052,401</u>
Liabilities						
Deposits and balances of banks and other financial institutions	437,555	-	-	-	19,303	456,858
Deposits from customers	54,953,819	2,355,240	13,216	-	3,005,162	60,327,437
Derivative financial instruments	-	-	-	-	114,546	114,546
Loan capital	970,871	-	-	-	-	970,871
Other liabilities	-	-	-	-	911,901	911,901
Total liabilities	<u>56,362,245</u>	<u>2,355,240</u>	<u>13,216</u>	<u>-</u>	<u>4,050,912</u>	<u>62,781,613</u>
Total interest sensitivity gap	<u>5,226,970</u>	<u>1,594,086</u>	<u>221,336</u>	<u>2,846</u>	<u>(774,450)</u>	<u>6,270,788</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Interest rate risk - continued

	THE GROUP					Total HK\$'000
	Up to 3 months HK\$'000	3 - 12 months HK\$'000	1 - 5 years HK\$'000	Over 5 years HK\$'000	Non- interest bearing HK\$'000	
At 31 December 2006						
Assets						
Cash and short term funds	15,656,479	232,315	–	–	368,065	16,256,859
Placements with banks and other financial institutions	2,453,461	185,000	–	–	–	2,638,461
Derivative financial instruments	–	–	–	–	4,962	4,962
Financial assets at fair value						
through profit or loss	184,439	100,682	220,442	–	105,248	610,811
Available-for-sale securities	417,620	46,677	7,779	–	626,065	1,098,141
Held-to-maturity securities	8,515,698	1,839,437	3,545,844	–	2,194	13,903,173
Advances to customers	25,553,255	801,250	39,650	2,925	477,458	26,874,538
Other assets	56,000	–	–	–	1,586,954	1,642,954
Total assets	<u>52,836,952</u>	<u>3,205,361</u>	<u>3,813,715</u>	<u>2,925</u>	<u>3,170,946</u>	<u>63,029,899</u>
Liabilities						
Deposits and balances of banks and other financial institutions	516,125	–	–	–	12,868	528,993
Deposits from customers	49,081,782	2,911,570	194,021	–	2,487,859	54,675,232
Derivative financial instruments	–	–	–	–	1,716	1,716
Loan capital	967,376	–	–	–	–	967,376
Other liabilities	–	–	–	–	804,852	804,852
Total liabilities	<u>50,565,283</u>	<u>2,911,570</u>	<u>194,021</u>	<u>–</u>	<u>3,307,295</u>	<u>56,978,169</u>
Total interest sensitivity gap	<u>2,271,669</u>	<u>293,791</u>	<u>3,619,694</u>	<u>2,925</u>	<u>(136,349)</u>	<u>6,051,730</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Interest rate risk - continued

	THE BANK					Total HK\$'000
	Up to	3 - 12	1 - 5	Over	Non-	
	3 months HK\$'000	months HK\$'000	years HK\$'000	5 years HK\$'000	interest bearing HK\$'000	
At 31 December 2007						
Assets						
Cash and short-term funds	14,310,731	51,052	-	-	351,689	14,713,472
Placements with banks and other financial institutions	2,684,574	399,573	-	-	-	3,084,147
Derivative financial instruments	-	-	-	-	60	60
Financial assets at fair value through profit or loss	861,060	-	78,023	-	195,075	1,134,158
Available-for-sale securities	239,042	-	-	-	485,145	724,187
Held-to-maturity securities	12,871,862	2,655,195	78,923	-	2,000	15,607,980
Advances to customers	30,561,279	822,886	50,875	2,846	283,468	31,721,354
Other assets	9,733	20,620	26,731	-	2,045,356	2,102,440
Total assets	<u>61,538,281</u>	<u>3,949,326</u>	<u>234,552</u>	<u>2,846</u>	<u>3,362,793</u>	<u>69,087,798</u>
Liabilities						
Deposits and balances of banks and other financial institutions	437,555	-	-	-	19,303	456,858
Deposits from customers	54,949,980	2,355,240	13,216	-	3,005,162	60,323,598
Derivative financial instruments	-	-	-	-	114,546	114,546
Amount due to subsidiaries	650,125	-	-	-	8,021	658,146
Loan capital	970,871	-	-	-	-	970,871
Other liabilities	-	-	-	-	460,781	460,781
Total liabilities	<u>57,008,531</u>	<u>2,355,240</u>	<u>13,216</u>	<u>-</u>	<u>3,607,813</u>	<u>62,984,800</u>
Total interest sensitivity gap	<u>4,529,750</u>	<u>1,594,086</u>	<u>221,336</u>	<u>2,846</u>	<u>(245,020)</u>	<u>6,102,998</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Interest rate risk - continued

	THE BANK					Total HK\$'000
	Up to	3 - 12	1 - 5	Over	Non-	
	3 months HK\$'000	months HK\$'000	years HK\$'000	5 years HK\$'000	interest bearing HK\$'000	
At 31 December 2006						
Assets						
Cash and short term funds	15,607,834	232,315	–	–	368,025	16,208,174
Placements with banks and other financial institutions	2,453,461	185,000	–	–	–	2,638,461
Derivative financial instruments	–	–	–	–	4,962	4,962
Financial assets at fair value through profit or loss	184,439	100,682	220,442	–	104,825	610,388
Available-for-sale securities	417,620	46,677	7,779	–	444,357	916,433
Held-to-maturity securities	8,515,698	1,839,437	3,545,844	–	2,194	13,903,173
Advances to customers	25,551,535	801,250	39,650	2,925	477,458	26,872,818
Other assets	56,000	–	–	–	2,007,375	2,063,375
Total assets	<u>52,786,587</u>	<u>3,205,361</u>	<u>3,813,715</u>	<u>2,925</u>	<u>3,409,196</u>	<u>63,217,784</u>
Liabilities						
Deposits and balances of banks and other financial institutions	516,125	–	–	–	12,868	528,993
Deposits from customers	49,077,855	2,911,570	194,021	–	2,487,728	54,671,174
Derivative financial instruments	–	–	–	–	1,716	1,716
Amounts due to subsidiaries	609,382	–	–	–	7,210	616,592
Loan capital	967,376	–	–	–	–	967,376
Other liabilities	–	–	–	–	463,777	463,777
Total liabilities	<u>51,170,738</u>	<u>2,911,570</u>	<u>194,021</u>	<u>–</u>	<u>2,973,299</u>	<u>57,249,628</u>
Total interest sensitivity gap	<u>1,615,849</u>	<u>293,791</u>	<u>3,619,694</u>	<u>2,925</u>	<u>435,897</u>	<u>5,968,156</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Interest rate risk - continued

Interest rate sensitivity

The sensitivity analyses below have been determined based on the exposure to interest rates at the reporting date and the stipulated change taking place at the beginning of the financial year and held constant throughout the reporting period. A 100 basis point change is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the possible change in interest rates.

	2007		2006	
	Change in basis points		Change in basis points	
	+100	-100	+100	-100
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
THE GROUP				
Profit before tax	45,970	(45,970)	13,822	(13,822)
Other equity	<u>(771)</u>	<u>771</u>	<u>(597)</u>	<u>597</u>
THE BANK				
Profit before tax	45,437	(45,437)	7,564	(7,564)
Other equity	<u>(771)</u>	<u>771</u>	<u>(597)</u>	<u>597</u>

Price risk

The Group and the Bank are exposed to price risk arising from its investment in debt and equity securities. The Group and the Bank do not actively trade these investments. The sensitivity analysis below is determined based on 10% changes in the price of the underlying investments.

Price sensitivity

	2007		2006	
	Change in price		Change in price	
	+10%	-10%	+10%	-10%
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
THE GROUP				
Profit before tax	52,977	(52,977)	7,779	(7,779)
Other equity	<u>39,606</u>	<u>(39,606)</u>	<u>63,679</u>	<u>(63,679)</u>
THE BANK				
Profit before tax	52,977	(52,977)	7,779	(7,779)
Other equity	<u>24,627</u>	<u>(24,627)</u>	<u>45,769</u>	<u>(45,769)</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk

Liquidity risk is the risk that the Group is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfil commitments to lend.

Management of liquidity risk

The ALCO is responsible for monitoring the Group's liquidity position, and does so through the periodic review of the statutory liquidity ratio, the maturity profile of assets and liabilities, loan-to-deposit ratio and inter-bank transactions. Liquidity policy is monitored by the ALCO and reviewed regularly by the Board of Directors of the Group. The Group's policy is to maintain a conservative level of liquid funds on a daily basis so that the Group is prepared to meet its obligations when they fall due in the normal course of business and to satisfy statutory liquidity ratio requirements.

The Bank's Risk Management and Compliance Committee (the "RMCC") recommends internal target levels in respect of the liquidity ratios. The Group's Chief Accountant is responsible for monitoring these ratios and, where a tight liquidity position remains for a prolonged period, the Chief Accountant reports his findings to the ALCO and RMCC who, after consultation with members of the Executive Committee decide the appropriate corrective actions to be taken. The liquidity positions of the overseas branches in Shantou, San Francisco and Macau are monitored through the submission of monthly management accounts and daily cash flow positions to the Bank's head office.

The following table details the Group's and the Bank's remaining contractual maturity for its non-derivative financial liabilities. The tables below have been drawn up based on the contractual maturities of the undiscounted financial liabilities including interest that will accrue to those liabilities except where the Group and the Bank are entitled and intends to repay the liability before its maturity.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Management of liquidity risk - continued

	THE GROUP					
	Less than 1 month HK\$'000	1-3 months HK\$'000	3 months to 1 year HK\$'000	1- 5 years HK\$'000	Over 5 years HK\$'000	Total HK\$'000
	At 31 December 2007					
Deposits and balances of banks and other financial institutions	27,038	429,820	-	-	-	456,858
Deposits from customers	15,597,198	42,618,558	2,090,485	13,569	7,627	60,327,437
Loan capital	-	13,733	41,200	1,140,087	-	1,195,020
Other liabilities	606,433	185,337	84,041	34,130	1,960	911,901
Total undiscounted financial liabilities	<u>16,230,669</u>	<u>43,247,448</u>	<u>2,215,726</u>	<u>1,187,786</u>	<u>9,587</u>	<u>62,891,216</u>
At 31 December 2006						
Deposits and balances of banks and other financial institutions	19,140	509,853	-	-	-	528,993
Deposits from customers	11,783,183	40,279,921	2,518,105	94,023	-	54,675,232
Loan capital	-	15,540	47,311	1,195,020	-	1,257,871
Other liabilities	504,266	178,467	66,565	50,375	5,179	804,852
Total undiscounted financial liabilities	<u>12,306,589</u>	<u>40,983,781</u>	<u>2,631,981</u>	<u>1,339,418</u>	<u>5,179</u>	<u>57,266,948</u>
	THE BANK					
	Less than 1 month HK\$'000	1-3 months HK\$'000	3 months to 1 year HK\$'000	1- 5 years HK\$'000	Over 5 years HK\$'000	Total HK\$'000
At 31 December 2007						
Deposits and balances of banks and other financial institutions	27,038	429,820	-	-	-	456,858
Deposits from customers	15,597,198	42,614,719	2,090,485	13,569	7,627	60,323,598
Loan capital	-	13,733	41,200	1,140,087	-	1,195,020
Other liabilities	528,990	549,466	35,534	4,937	-	1,118,927
Total undiscounted financial liabilities	<u>16,153,226</u>	<u>43,607,738</u>	<u>2,167,219</u>	<u>1,158,593</u>	<u>7,627</u>	<u>63,094,403</u>
At 31 December 2006						
Deposits and balances of banks and other financial institutions	19,140	509,853	-	-	-	528,993
Deposits from customers	11,783,183	40,275,863	2,518,105	94,023	-	54,671,174
Loan capital	-	15,540	47,311	1,195,020	-	1,257,871
Other liabilities	510,910	502,698	43,957	19,115	3,689	1,080,369
Total undiscounted financial liabilities	<u>12,313,233</u>	<u>41,303,954</u>	<u>2,609,373</u>	<u>1,308,158</u>	<u>3,689</u>	<u>57,538,407</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Management of liquidity risk - continued

The following table details the Group's and the Bank's expected maturity for its derivative financial instruments. The table has been drawn up based on the undiscounted net cash inflows/ (outflows) on the derivative instrument that settle on a net basis and the undiscounted gross inflows and (outflows) on those derivatives that require gross settlement. When the amount payable or receivable is not fixed, the amount disclosed has been determined by reference to the projected interest rates as illustrated by the yield curves existing at the reporting date.

	THE GROUP AND THE BANK				
	Less than	3 months		Over	
	1 month	1 - 3 months	to 1 year	1 - 5 years	5 years
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2007					
Derivatives settled net					
Interest rate contracts	<u>5,244</u>	<u>3,743</u>	<u>5,040</u>	<u>(15,283)</u>	<u>–</u>
Derivatives settled gross					
Exchange rate contracts					
- inflow	24,223	4,625	62,808	–	–
- outflow	<u>(24,286)</u>	<u>(3,946)</u>	<u>(64,127)</u>	<u>–</u>	<u>–</u>
	<u>(63)</u>	<u>679</u>	<u>(1,319)</u>	<u>–</u>	<u>–</u>
At 31 December 2006					
Derivatives settled net					
Interest rate contracts	<u>(239)</u>	<u>(1,599)</u>	<u>3,472</u>	<u>1,880</u>	<u>–</u>
Derivatives settled gross					
Exchange rate contracts					
- inflow	379,761	3,820	2,753	55,435	–
- outflow	<u>(378,204)</u>	<u>(2,967)</u>	<u>(1,059)</u>	<u>(52,496)</u>	<u>–</u>
	<u>1,557</u>	<u>853</u>	<u>1,694</u>	<u>2,939</u>	<u>–</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Off-balance sheet items

The dates of the contractual amounts of the Group's and the Bank's off-balance sheet financial instruments that commit it to extending credit to customers and other facilities, financial guarantees, future minimum lease payments under non-cancellable operating leases and capital commitments are summarised in the table below:

	THE GROUP			
	No later than 1 year HK\$'000	1 - 5 years HK\$'000	Over 5 years HK\$'000	Total HK\$'000
At 31 December 2007				
Loan commitments	16,606,916	–	–	16,606,916
Guarantee, acceptances and other financial facilities	1,239,142	–	–	1,239,142
Operating lease commitments	28,150	36,839	275	65,264
Capital commitments	32,926	–	–	32,926
Total	17,907,134	36,839	275	17,944,248
At 31 December 2006				
Loan commitments	10,284,935	–	–	10,284,935
Guarantee, acceptances and other financial facilities	1,567,919	–	–	1,567,919
Operating lease commitments	25,975	43,088	1,985	71,048
Capital commitments	227,967	–	–	227,967
Total	12,106,796	43,088	1,985	12,151,869
	THE BANK			
	No later than 1 year HK\$'000	1-5 years HK\$'000	Over 5 years HK\$'000	Total HK\$'000
At 31 December 2007				
Loan commitments	16,606,916	–	–	16,606,916
Guarantee, acceptances and other financial facilities	1,239,142	–	–	1,239,142
Operating lease commitments	26,288	36,025	275	62,588
Capital commitments	32,926	–	–	32,926
Total	17,905,272	36,025	275	17,941,572
At 31 December 2006				
Loan commitments	10,284,935	–	–	10,284,935
Guarantee, acceptances and other financial facilities	1,567,919	–	–	1,567,919
Operating lease commitments	23,945	40,413	1,985	66,343
Capital commitments	227,967	–	–	227,967
Total	12,104,766	40,413	1,985	12,147,164

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Analysis of assets and liabilities by remaining maturity

The maturity analysis of financial assets and liabilities shown in the balance sheet, based on the remaining period at the balance sheet date to the contractual maturity date in accordance with the guideline issued by the Hong Kong Monetary Authority, is shown below:

	THE GROUP						
	Repayable on demand HK\$'000	Repayable within 3 months or less (except those repayable on demand) HK\$'000	Repayable after 3 months but within 1 year HK\$'000	Repayable after 1 year but within 5 years HK\$'000	Repayable after 5 years HK\$'000	With an indefinite period HK\$'000	Total HK\$'000
At 31 December 2007							
Assets							
Cash and short-term funds	1,910,782	12,803,827	49,368	-	-	-	14,763,977
Placements with banks and other financial institutions	-	2,684,574	399,573	-	-	-	3,084,147
Derivative financial instruments	-	-	-	-	-	60	60
Financial assets at fair value through profit or loss	-	-	54,236	884,846	-	195,340	1,134,422
Available-for-sale securities	-	-	-	121,082	117,960	637,619	876,661
Held-to-maturity securities	-	6,530,013	2,536,112	6,528,610	13,245	-	15,607,980
Advances to customers	2,510,697	4,104,480	4,790,328	10,604,914	9,496,204	215,260	31,721,883
Advances to banks and other financial institutions	1,084	18,000	38,000	-	-	-	57,084
Other assets	468,823	281,538	107,923	1,775	21,914	924,214	1,806,187
Total assets	4,891,386	26,422,432	7,975,540	18,141,227	9,649,323	1,972,493	69,052,401
Liabilities							
Deposits and balances of banks and other financial institutions	27,038	429,820	-	-	-	-	456,858
Deposits from customers	15,597,198	42,618,558	2,090,485	13,569	-	7,627	60,327,437
Derivative financial instruments	-	-	-	-	-	114,546	114,546
Loan capital	-	-	-	-	970,871	-	970,871
Other liabilities	606,433	185,337	84,041	34,130	-	1,960	911,901
Total liabilities	16,230,669	43,233,715	2,174,526	47,699	970,871	124,133	62,781,613
Net liquidity gap	(11,339,283)	(16,811,283)	5,801,014	18,093,528	8,678,452	1,848,360	6,270,788

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Analysis of assets and liabilities by remaining maturity - continued

	THE GROUP						
	Repayable on demand HK\$'000	Repayable within 3 months or less (except those repayable on demand) HK\$'000	Repayable after 3 months but within 1 year HK\$'000	Repayable after 1 year but within 5 years HK\$'000	Repayable after 5 years HK\$'000	With an indefinite period HK\$'000	Total HK\$'000
At 31 December 2006							
Assets							
Cash and short-term funds	1,145,253	14,879,291	232,315	–	–	–	16,256,859
Placements with banks and other financial institutions	–	2,453,461	185,000	–	–	–	2,638,461
Derivative financial instruments	–	–	–	–	–	4,962	4,962
Financial assets at fair value through profit or loss	–	104,825	79,083	426,480	–	423	610,811
Available-for-sale securities	–	76,209	38,897	194,482	162,488	626,065	1,098,141
Held-to-maturity securities	–	4,738,140	2,841,907	6,304,607	18,519	–	13,903,173
Advances to customers	1,486,391	4,410,927	4,243,045	9,007,982	7,349,957	376,236	26,874,538
Advances to banks and other financial institutions	–	19,425	38,000	–	–	–	57,425
Other assets	354,989	269,756	71,225	35,935	3,335	850,289	1,585,529
Total assets	2,986,633	26,952,034	7,729,472	15,969,486	7,534,299	1,857,975	63,029,899
Liabilities							
Deposits and balances of banks and other financial institutions	19,140	509,853	–	–	–	–	528,993
Deposits from customers	11,783,183	40,279,921	2,518,105	94,023	–	–	54,675,232
Derivative financial instruments	–	–	–	–	–	1,716	1,716
Loan capital	–	–	–	–	967,376	–	967,376
Other liabilities	504,266	178,467	66,565	50,375	–	5,179	804,852
Total liabilities	12,306,589	40,968,241	2,584,670	144,398	967,376	6,895	56,978,169
Net liquidity gap	(9,319,956)	(14,016,207)	5,144,802	15,825,088	6,566,923	1,851,080	6,051,730

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Analysis of assets and liabilities by remaining maturity - continued

	THE BANK						
	Repayable on demand HK\$'000	Repayable within 3 months or less (except those repayable on demand) HK\$'000	Repayable after 3 months but within 1 year HK\$'000	Repayable after 1 year but within 5 years HK\$'000	Repayable after 5 years HK\$'000	With an indefinite period HK\$'000	Total HK\$'000
At 31 December 2007							
Assets							
Cash and short-term funds	1,910,683	12,753,421	49,368	-	-	-	14,713,472
Placements with banks and other financial institutions	-	2,684,574	399,573	-	-	-	3,084,147
Derivative financial instruments	-	-	-	-	-	60	60
Financial assets at fair value through profit or loss	-	-	54,237	884,846	-	195,075	1,134,158
Available-for-sale securities	-	-	-	121,082	117,960	485,145	724,187
Held-to-maturity securities	-	6,530,013	2,536,112	6,528,610	13,245	-	15,607,980
Advances to customers	2,510,697	4,104,454	4,790,244	10,604,495	9,496,204	215,260	31,721,354
Advances to banks and other financial institutions	1,084	18,000	38,000	-	-	-	57,084
Other assets	74,478	279,687	106,180	3,853	21,914	1,559,244	2,045,356
Total assets	<u>4,496,942</u>	<u>26,370,149</u>	<u>7,973,714</u>	<u>18,142,886</u>	<u>9,649,323</u>	<u>2,454,784</u>	<u>69,087,798</u>
Liabilities							
Deposits and balances of banks and other financial institutions	27,038	429,820	-	-	-	-	456,858
Deposits from customers	15,597,198	42,614,719	2,090,485	13,569	-	7,627	60,323,598
Derivative financial instruments	-	-	-	-	-	114,546	114,546
Loan capital	-	-	-	-	970,871	-	970,871
Other liabilities	528,990	549,466	35,534	4,937	-	-	1,118,927
Total liabilities	<u>16,153,226</u>	<u>43,594,005</u>	<u>2,126,019</u>	<u>18,506</u>	<u>970,871</u>	<u>122,173</u>	<u>62,984,800</u>
Net liquidity gap	<u>(11,656,284)</u>	<u>(17,223,856)</u>	<u>5,847,695</u>	<u>18,124,380</u>	<u>8,678,452</u>	<u>2,332,611</u>	<u>6,102,998</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Analysis of assets and liabilities by remaining maturity - continued

	THE BANK						
	Repayable on demand HK\$'000	Repayable within 3 months or less (except those repayable on demand) HK\$'000	Repayable after 3 months but within 1 year HK\$'000	Repayable after 1 year 5 years but within 5 years HK\$'000	Repayable after 5 years HK\$'000	With an indefinite period HK\$'000	Total HK\$'000
At 31 December 2006							
Assets							
Cash and short-term funds	1,145,213	14,830,646	232,315	-	-	-	16,208,174
Placements with banks and other financial institutions	-	2,453,461	185,000	-	-	-	2,638,461
Derivative financial instruments	-	-	-	-	-	4,962	4,962
Financial assets at fair value through profit or loss	-	104,825	79,083	426,480	-	-	610,388
Available-for-sale securities	-	76,209	38,897	194,482	162,488	444,357	916,433
Held-to-maturity securities	-	4,738,140	2,841,907	6,304,607	18,519	-	13,903,173
Advances to customers	1,486,390	4,409,208	4,243,045	9,007,982	7,349,957	376,236	26,872,818
Advances to banks and other financial institutions	-	19,425	38,000	-	-	-	57,425
Other assets	66,018	266,921	69,969	35,932	3,335	1,563,775	2,005,950
Total assets	<u>2,697,621</u>	<u>26,898,835</u>	<u>7,728,216</u>	<u>15,969,483</u>	<u>7,534,299</u>	<u>2,389,330</u>	<u>63,217,784</u>
Liabilities							
Deposits and balances of banks and other financial institutions	19,140	509,853	-	-	-	-	528,993
Deposits from customers	11,783,183	40,275,863	2,518,105	94,023	-	-	54,671,174
Derivative financial instruments	-	-	-	-	-	1,716	1,716
Loan capital	-	-	-	-	967,376	-	967,376
Other liabilities	510,910	502,698	43,957	19,115	-	3,689	1,080,369
Total liabilities	<u>12,313,233</u>	<u>41,288,414</u>	<u>2,562,062</u>	<u>113,138</u>	<u>967,376</u>	<u>5,405</u>	<u>57,249,628</u>
Net liquidity gap	<u>(9,615,612)</u>	<u>(14,389,579)</u>	<u>5,166,154</u>	<u>15,856,345</u>	<u>6,566,923</u>	<u>2,383,925</u>	<u>5,968,156</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Fair value of financial assets and liabilities

Except as detailed in the following table, the directors of the Group and the Bank consider that the carrying amounts of financial assets and financial liabilities recorded at amortised cost in the financial statements approximate their fair values.

	THE GROUP AND THE BANK			
	Carrying value		Fair value	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Financial assets				
- Held-to-maturity securities	<u>15,607,980</u>	<u>13,903,173</u>	<u>15,144,333</u>	<u>13,945,888</u>
Financial liabilities				
- Loan capital	<u>970,871</u>	<u>967,376</u>	<u>944,523</u>	<u>985,384</u>

The following table shows an analysis of financial instruments recorded at fair value, between those whose fair value is based on quoted market prices and those involving valuation techniques where all the model inputs are observable in the market.

	THE GROUP		
	Quoted market price	Valuation techniques - market observable inputs	Total
	HK\$'000	HK\$'000	HK\$'000
At 31 December 2007			
Financial assets			
- Derivatives financial instruments	-	60	60
- Financial assets at fair value through profit or loss	264	1,134,158	1,134,422
- Available-for-sale securities	228,869	449,207	678,076
Financial liabilities			
- Derivatives financial instruments	<u>-</u>	<u>114,546</u>	<u>114,546</u>
At 31 December 2006			
Financial assets			
- Derivatives financial instruments	-	4,962	4,962
- Financial assets at fair value through profit or loss	423	610,388	610,811
- Available-for-sale securities	366,125	732,016	1,098,141
Financial liabilities			
- Derivatives financial instruments	<u>-</u>	<u>1,716</u>	<u>1,716</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Fair value of financial assets and liabilities - continued

	Quoted market price HK\$'000	THE BANK Valuation techniques - market observable inputs HK\$'000	Total HK\$'000
At 31 December 2007			
Financial assets			
- Derivatives financial instruments	-	60	60
- Financial assets at fair value through profit or loss	-	1,134,158	1,134,158
- Available-for-sale securities	79,004	446,598	525,602
Financial liabilities			
- Derivatives financial instruments	-	114,546	114,546
At 31 December 2006			
Financial assets			
- Derivatives financial instruments	-	4,962	4,962
- Financial assets at fair value through profit or loss	-	610,388	610,388
- Available-for-sale securities	187,026	729,407	916,433
Financial liabilities			
- Derivatives financial instruments	-	1,716	1,716

Fair values of investment classified as fair value through profit or loss are determined based on prices quoted in the market or by the brokers/issuers or valuation technique (discounted cash flows) with observable market inputs adjusted for specific features of the instrument.

The fair values of unlisted equity investments and bond funds are determined based on net asset values as reported by fund administrator.

Investments in Structured Investment Vehicles ("SIV") are included under available-for-sale investments. Due to the non-availability of quoted prices of the SIVs and the lack of market transactions in SIVs in recent months as a consequence of current credit market conditions, the Group estimated their fair values by reference to the net asset value of the respective capital notes of each SIV as provided by sponsoring banks of the SIVs and after making further adjustments, as necessary, to take into account other relevant factors or conditions of the SIVs at the year end.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Capital management

The group has adopted a policy of maintaining a strong capital base to:

- comply with the capital requirements under the Banking (Capital) Rules of the Banking Ordinance; and
- support the Group's stability and business growth so as to provide reasonable returns for shareholders.

Capital adequacy ratio, computed as a ratio of total regulatory capital to the risk-weighted asset, has remained well above the statutory minimum ratio of 8% for the past five years.

Capital adequacy position and the use of regulatory capital are monitored closely by the Group's management, employing techniques based on the Banking (Capital) Rules. The required information is filed with the Hong Kong Monetary Authority on a quarterly basis in the form of a statistical return.

The Group has an established capital planning process to assess the adequacy of its capital to support current and future activities. The process states the Group's capital adequacy goals in relation to risk, taking into account its strategic focus and business plan. Key factors to consider in this process include additional capital required for future expansion, results of the stress test programme regularly conducted, dividend policy, income recognition and provisioning policies.

Capital Adequacy Ratio

	THE GROUP	
	2007	2006
	%	%
Capital adequacy ratio	<u>14.22</u>	<u>15.59</u>
Core capital ratio	<u>11.52</u>	<u>—</u>

The core capital ratio as at 31 December 2007 calculated in accordance with the Banking (Capital) Rules, which became effective on 1 January 2007, was 11.52%.

Capital adequacy ratio as at 31 December 2007 was compiled in accordance with the Banking (Capital) Rules under section 98A of the Hong Kong Banking Ordinance for the implementation of the "Basel II" capital accord, which became effective on 1 January 2007. In accordance with the Banking (Capital) Rules, the Bank has adopted the "standardized approach" for the calculation of the risk-weighted assets for credit risk and "basic indicator approach" for the calculation of operational risk. The capital adequacy ratio is consolidated, under the Banking (Capital) Rules, with reference to the financial information of the Bank, Chong Hing Finance Limited, Liu Chong Hing Banking Corporation, Cayman, Right Way Investments Limited, Gallbraith Limited, Chong Hing Information Technology Limited and Card Alliance Company Limited.

The capital adequacy ratio as at 31 December 2006 was compiled in accordance with the Third Schedule of the Banking Ordinance under the "Basel I" capital accord.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

7. FINANCIAL RISK MANAGEMENT - continued

Capital base

The capital base after deductions used in the calculation of the above capital adequacy ratios as at 31 December and reported to the Hong Kong Monetary Authority is analysed as follows:

	THE GROUP	
	2007 HK\$'000	2006 HK\$'000
Core capital		
Paid up ordinary share capital	217,500	217,500
Share premium	1,542,817	1,542,817
Published reserves	3,231,676	3,225,758
Profit and loss account	56,732	168,048
Less: Net deferred tax assets	(2,079)	–
Total core capital	<u>5,046,646</u>	<u>5,154,123</u>
Other deductions from core capital	(418,739)	–
Core capital after deductions	<u>4,627,907</u>	<u>5,154,123</u>
Supplementary capital		
Reserves attributable to fair value gains on revaluation of holdings of land and buildings	5,755	27,835
Reserves attributable to fair value gains on revaluation of holdings of available-for-sale equities and debt securities	10,062	39,572
Unrealised fair value gains arising from holdings of equities and debt securities designated at fair value through profit or loss	45,807	2,796
Regulatory reserve for general banking risks	356,000	165,000
Collective impairment allowances	116,720	104,464
Term subordinated debt	970,871	967,376
Total supplementary capital	<u>1,505,215</u>	<u>1,307,043</u>
Other deductions from supplementary capital	(418,740)	–
Supplementary capital after deductions	<u>1,086,475</u>	<u>1,307,043</u>
Total deductions from capital base	–	(633,406)
Total capital base after deductions	<u><u>5,714,382</u></u>	<u><u>5,827,760</u></u>

The calculation of the capital base as at 31 December 2007 above is based on the Banking (Capital) Rules effective from 1 January 2007. The calculation of the capital base as at 31 December 2006 was based on Third Schedule to the Banking Ordinance. The comparatives of the components of the core capital and supplementary capital were not restated on the ground that different approaches were used to calculate its regulatory capital in the years ended 31 December 2007 and 2006.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

8. NET INTEREST INCOME

	2007 HK\$'000	2006 HK\$'000
Interest income		
Short term funds and placements	978,648	802,350
Investments in securities	718,519	470,184
Loans and advances	<u>1,613,317</u>	<u>1,467,984</u>
	<u>3,310,484</u>	<u>2,740,518</u>
Interest expense		
Deposits and balances from banks and customers	(2,275,900)	(1,909,027)
Loan capital in issue	<u>(63,971)</u>	<u>(2,952)</u>
	<u>(2,339,871)</u>	<u>(1,911,979)</u>
Net interest income	<u>970,613</u>	<u>828,539</u>
Included within interest income		
Interest income on impaired loans and advances	<u>19,417</u>	<u>3,061</u>

Included within interest income and interest expense are HK\$3,294,634,000 (2006: HK\$2,725,915,000) and HK\$2,339,871,000 (2006: HK\$1,911,979,000) for financial assets and financial liabilities that are not at fair value through profit or loss, respectively.

9. NET FEE AND COMMISSION INCOME

	2007 HK\$'000	2006 HK\$'000
Fees and commission income		
Securities dealings	202,794	79,247
Credit lines	7,618	7,845
Trade finance	15,397	14,042
Credit card services	42,106	30,358
Agency services	47,187	29,908
Others	<u>11,539</u>	<u>10,901</u>
Total fees and commission income	326,641	172,301
Less: Fees and commission expense	<u>(43,229)</u>	<u>(4,166)</u>
Net fees and commission income	<u>283,412</u>	<u>168,135</u>
of which:		
Net fee income, other than amounts included in determining the effective interest rate, arising from financial assets or financial liabilities that are not held for trading nor designated at fair value		
- fee income	70,936	58,410
- fee expense	<u>(37,051)</u>	<u>(25,462)</u>
	<u>33,885</u>	<u>32,948</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

10. OTHER OPERATING INCOME

	2007	2006
	HK\$'000	HK\$'000
Dividend income		
Listed investments	8,979	10,538
Unlisted investments	2,880	3,005
Net gains on dealing in foreign currencies	29,859	26,589
Net gains on financial assets at fair value through profit or loss		
- designated at fair value through profit or loss	127,980	12,348
- deemed held for trading	(117,608)	192
Gross rents from properties	11,910	4,550
Less: Outgoings	(961)	(992)
Net rental income	10,949	3,558
Safe deposit box rentals	25,064	23,431
Insurance underwriting profit	10,130	12,190
Other banking services income	41,595	39,460
Actuarial gain on retirement scheme	21,914	–
Others	4,927	2,243
	<u>166,669</u>	<u>133,554</u>

11. OPERATING EXPENSES

	2007	2006
	HK\$'000	HK\$'000
Amortisation of prepaid lease payments for land	5,710	5,114
Auditor's remuneration	3,579	3,291
Staff costs		
Salaries and other costs	355,624	299,992
Retirement benefits scheme contributions	26,620	22,609
Total staff costs	382,244	322,601
Depreciation	36,846	30,535
Premises and equipment expenses, excluding depreciation/amortisation		
Rentals and rates for premises	35,747	46,610
Others	17,842	16,177
Other operating expenses	160,926	167,209
	<u>642,894</u>	<u>591,537</u>

Included in the premises and equipment expenses are minimum lease payments under operating lease of HK\$31,246,000 (2006: HK\$42,455,000).

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

12. DIRECTORS' AND EMPLOYEES' EMOLUMENTS

The emoluments paid or payable to each of the directors were as follows:

	2007				2006			
	Fees	Salaries and other benefits	Contribution to retirement benefits scheme	Total	Fees	Salaries and other benefits	Contribution to retirement benefits scheme	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Executive directors (Hong Kong)								
Liu Lit Man	120	5,454	350	5,924	100	5,431	350	5,881
Liu Lit Mo	70	488	45	603	50	492	45	587
Liu Lit Chi	70	8,328	224	8,622	50	8,099	210	8,359
Don Tit Shing Liu	70	2,198	217	2,485	50	1,960	192	2,202
Lau Wai Man	70	2,053	205	2,328	50	1,791	178	2,019
Wilfred Chun Ning Liu	70	2,215	163	2,448	50	2,150	157	2,357
Frank Shui Sang Jin	70	1,977	196	2,243	50	1,762	166	1,978
Andrew Chiu Wing Tsang	70	1,845	155	2,070	50	1,621	128	1,799
George Har Kar Wong	70	1,827	131	2,028	50	1,643	109	1,802
Total executive directors	<u>680</u>	<u>26,385</u>	<u>1,686</u>	<u>28,751</u>	<u>500</u>	<u>24,949</u>	<u>1,535</u>	<u>26,984</u>
Non-executive directors (Hong Kong)								
Timothy George Freshwater	100	80	-	180	80	80	-	160
Sun Jiakang	37	-	-	37	50	-	-	50
Xu Minjie	33	-	-	33	-	-	-	-
Andrew Liu	70	11	-	81	50	4	-	54
Toshiaki Arai	37	-	-	37	50	-	-	50
Eiichi Yoshikawa	33	-	-	33	-	-	-	-
Christopher Kwun Shing Liu	70	-	-	70	50	-	-	50
Alfred Cheuk Yu Chow	100	-	-	100	80	-	-	80
Wang Zhi	70	-	-	70	50	-	-	50
Total non-executive directors	<u>550</u>	<u>91</u>	<u>-</u>	<u>641</u>	<u>410</u>	<u>84</u>	<u>-</u>	<u>494</u>
Independent non-executive directors (Hong Kong)								
Robin Yau Hing Chan	100	-	-	100	80	-	-	80
Wanchai Chiranakhorn	100	-	-	100	80	-	-	80
Cheng Yuk Wo	100	-	-	100	80	-	-	80
Andrew Chiu Cheung Ma	40	-	-	40	-	-	-	-
Total independent non-executive directors	<u>340</u>	<u>-</u>	<u>-</u>	<u>340</u>	<u>240</u>	<u>-</u>	<u>-</u>	<u>240</u>
Total	<u>1,570</u>	<u>26,476</u>	<u>1,686</u>	<u>29,732</u>	<u>1,150</u>	<u>25,033</u>	<u>1,535</u>	<u>27,718</u>

The five highest paid individuals in the Group in 2007 and 2006 were all directors of the Bank and details of their emoluments are included in note 12 above.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

13. TAXATION

	2007 HK\$'000	2006 HK\$'000
The tax charge comprises:		
Hong Kong Profits Tax		
- current year	63,824	68,831
- overprovision in prior years	<u>(557)</u>	<u>(10,797)</u>
	63,267	58,034
Overseas taxation	3,724	2,573
Deferred tax (note 29)	<u>(2,009)</u>	<u>7,163</u>
	<u>64,982</u>	<u>67,770</u>

Hong Kong Profits Tax is calculated at 17.5% (2006: 17.5%) of the estimated assessable profit for the year.

Taxation arising in other jurisdictions is calculated at the rates prevailing in the relevant jurisdictions.

The tax charge for the year can be reconciled to the Group's profit per the consolidated income statement as follows:

	2007 HK\$'000	2006 HK\$'000
Profit before taxation	<u>570,014</u>	<u>570,914</u>
Tax at the domestic income tax rate of 17.5% (2006: 17.5%)	99,752	99,910
Tax effect of share of profit of jointly controlled entities	(11,563)	(5,871)
Tax effect of expenses not deductible for tax purpose	6,316	94
Tax effect of income not taxable for tax purpose	(27,133)	(14,273)
Utilisation of tax losses previously not recognised	(437)	(510)
Overprovision in prior years	(557)	(10,797)
Effect of different tax rates of subsidiaries operating in other jurisdictions	(1,541)	(221)
Others	<u>145</u>	<u>(562)</u>
Tax charge for the year	<u>64,982</u>	<u>67,770</u>

14. DIVIDENDS

	2007 HK\$'000	2006 HK\$'000
Dividends recognised as distribution during the year:		
2007 Interim - HK\$0.21 (2006: HK\$0.19) per share	91,350	82,650
2006 Final - HK\$0.44 (2005: HK\$0.42) per share	<u>191,400</u>	<u>182,700</u>
	<u>282,750</u>	<u>265,350</u>

The final dividend of HK\$0.44 per share in respect of the current financial year (2006: HK\$0.44) has been proposed by the directors and is subject to approval by the shareholders in general meeting.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

15. EARNINGS PER SHARE

The calculation of basic and diluted earnings per share is based on the profit attributable to shareholders of HK\$505,032,000 (2006: HK\$503,144,000) and on 435,000,000 (2006: 435,000,000) ordinary shares in issue during the year.

16. CASH AND SHORT-TERM FUNDS

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Cash and balances with banks and other financial institutions	1,833,309	997,461	1,833,210	997,421
Money at call and short notice	9,776,851	14,744,553	9,726,445	14,695,908
Exchange fund bills	3,153,817	514,845	3,153,817	514,845
	<u>14,763,977</u>	<u>16,256,859</u>	<u>14,713,472</u>	<u>16,208,174</u>

17. DERIVATIVE FINANCIAL INSTRUMENTS

	THE GROUP AND THE BANK					
	2007			2006		
	Notional amount	Fair values		Notional amount	Fair values	
HK\$'000	Assets	Liabilities	HK\$'000	Assets	Liabilities	
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Derivatives held for trading						
- Foreign currency related contracts	36,051	60	276	513,269	1,726	128
- Interest rate swaps	1,019,568	-	112,746	345,014	1,553	1,588
- Currency swaps	55,840	-	1,524	52,240	1,683	-
		<u>60</u>	<u>114,546</u>		<u>4,962</u>	<u>1,716</u>

The replacement costs and credit risk weighted amounts of the derivatives exposures are as follows:

	THE GROUP AND THE BANK					
	2007			2006		
	Notional amount	Replacement cost	Credit risk weighted amount	Notional amount	Replacement cost	Credit risk weighted amount
HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
Exchange rate contracts	91,891	60	626	565,509	3,409	2,195
Interest rate contracts	1,019,568	-	1,529	345,014	1,553	710
		<u>60</u>	<u>2,155</u>		<u>4,962</u>	<u>2,905</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

17. DERIVATIVE FINANCIAL INSTRUMENTS - continued

The derivative financial instruments including exchange rate contracts and interest rate contracts have been recognised on balance sheet at fair value.

The derivative financial instruments do not qualify for hedge accounting for financial reporting but are managed in conjunction with the financial instruments designated at fair value through profit or loss.

Replacement cost is the cost of replacing all contracts that have a positive value when marked to market (should the counterparty default on its obligations) and is obtained by marking contracts to market. Replacement cost is a close approximation of the credit risk for these contracts at the balance sheet dates.

As at 31 December 2007, the credit risk weighted amount is the amount which has been calculated in accordance with the Banking (Capital) Rules, which came into operation on 1 January 2007, and the guidelines issued by the Hong Kong Monetary Authority.

As at 31 December 2006, the credit risk weighted amounts are the amounts that have been calculated in accordance with the Third Schedule of the Banking Ordinance and guidelines issued by the Hong Kong Monetary Authority. The amounts calculated are dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

18. INVESTMENTS IN SECURITIES

	THE GROUP					THE BANK				
	Financial assets at fair value through profit or loss					Financial assets at fair value through profit or loss				
	Deemed held for trading	Designated at fair value	Held-to-maturity securities	Available-for-sale securities	Total	Deemed held for trading	Designated at fair value	Held-to-maturity securities	Available-for-sale securities	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
2007										
Equity securities:										
Listed in Hong Kong	264	-	-	220,255	220,519	-	-	-	70,390	70,390
Listed overseas	-	-	-	8,614	8,614	-	-	-	8,614	8,614
	264	-	-	228,869	229,133	-	-	-	79,004	79,004
Unlisted	-	-	-	408,750	408,750	-	-	-	406,141	406,141
	264	-	-	637,619	637,883	-	-	-	485,145	485,145
Debt securities:										
Certificates of deposit	-	-	1,484,139	-	1,484,139	-	-	1,484,139	-	1,484,139
Other debt securities - Unlisted	-	1,134,158	14,123,841	239,042	15,497,041	-	1,134,158	14,123,841	239,042	15,497,041
	-	1,134,158	15,607,980	239,042	16,981,180	-	1,134,158	15,607,980	239,042	16,981,080
Total:										
Listed in Hong Kong	264	-	-	220,255	220,519	-	-	-	70,390	70,390
Listed overseas	-	-	-	8,614	8,614	-	-	-	8,614	8,614
Unlisted	-	1,134,158	15,607,980	647,792	17,389,930	-	1,134,158	15,607,980	645,183	17,387,321
	264	1,134,158	15,607,980	876,661	17,619,063	-	1,134,158	15,607,980	724,187	17,466,325
Market value of listed securities:										
Listed in Hong Kong	264	-	-	220,255	220,519	-	-	-	70,390	70,390
Listed overseas	-	-	-	8,614	8,614	-	-	-	8,614	8,614
	264	-	-	228,869	229,133	-	-	-	79,004	79,004
As analysed by issuing entities:										
Central government and central banks	-	118,393	534,442	-	652,835	-	118,393	534,442	-	652,835
Public sector entities	-	-	11,245	-	11,245	-	-	11,245	-	11,245
Bank and other financial institutions	56	475,282	15,060,293	272,315	15,807,946	-	475,282	15,060,293	210,326	15,745,901
Corporate entities	208	535,484	2,000	198,204	735,896	-	535,484	2,000	107,719	645,203
Others	-	4,999	-	406,142	411,141	-	4,999	-	406,142	411,141
	264	1,134,158	15,607,980	876,661	17,619,063	-	1,134,158	15,607,980	724,187	17,466,325

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

18. INVESTMENTS IN SECURITIES - continued

Included in financial assets designated at fair value through profit or loss are primarily:

- i) bonds (classified as “other debt securities” above) which contain embedded derivatives that would otherwise have been separately accounted for; and
- ii) bond funds (classified as “other debt securities” above) are designated at fair value through profit or loss because they are managed and evaluated on a fair value basis, in accordance with investment strategy. Information about the bond funds is provided internally on that basis to the Group’s key management personnel.

Included in available-for-sale securities are financial instruments issued by Structured Investment Vehicles with gross investment cost of approximately HK\$568,212,000 (2006: HK\$433,131,000). Impairment losses of HK\$369,627,000 (2006: HK\$Nil) has been recognised for these investments. All other available-for-sale securities and investments in securities are neither past due nor impaired.

Details of the impairment assessment are disclosed in Note 33.

Certain held-to-maturity certificates of deposit of approximately HK\$25,170,000 (2006: HK\$24,479,000) held by the San Francisco Branch of the Bank have been pledged to the State of California of the United States of America in compliance with the requirements of the California Financial Code.

	THE GROUP					THE BANK				
	Financial assets at fair value through profit or loss					Financial assets at fair value through profit or loss				
	Deemed held for trading	Designated at fair value	Held-to-maturity securities	Available-for-sale securities	Total	Deemed held for trading	Designated at fair value	Held-to-maturity securities	Available-for-sale securities	Total
HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
2006										
Equity securities:										
Listed in Hong Kong	423	-	-	359,134	359,557	-	-	-	180,035	180,035
Listed overseas	-	-	-	6,991	6,991	-	-	-	6,991	6,991
	423	-	-	366,125	366,548	-	-	-	187,026	187,026
Unlisted	-	-	-	259,940	259,940	-	-	-	257,331	257,331
	423	-	-	626,065	626,488	-	-	-	444,357	444,357
Debt securities:										
Certificates of deposit	-	-	1,863,937	-	1,863,937	-	-	1,863,937	-	1,863,937
Other debt securities - Unlisted	-	610,388	12,039,236	472,076	13,121,700	-	610,388	12,039,236	472,076	13,121,700
	-	610,388	13,903,173	472,076	14,985,637	-	610,388	13,903,173	472,076	14,985,637
Total:										
Listed in Hong Kong	423	-	-	359,134	359,557	-	-	-	180,035	180,035
Listed overseas	-	-	-	6,991	6,991	-	-	-	6,991	6,991
Unlisted	-	610,388	13,903,173	732,016	15,245,577	-	610,388	13,903,173	729,407	15,242,968
	423	610,388	13,903,173	1,098,141	15,612,125	-	610,388	13,903,173	916,433	15,429,994
Market value of listed securities:										
Listed in Hong Kong	423	-	-	359,134	359,557	-	-	-	180,035	180,035
Listed overseas	-	-	-	6,991	6,991	-	-	-	6,991	6,991
	423	-	-	366,125	366,548	-	-	-	187,026	187,026
As analysed by issuing entities:										
Central government and central banks	-	-	359,143	-	359,143	-	-	359,143	-	359,143
Public sector entities	-	-	18,508	-	18,508	-	-	18,508	-	18,508
Banks and other financial institutions	53	372,463	13,384,170	85,518	13,842,204	-	372,463	13,384,170	66,083	13,822,716
Corporate entities	199	50,679	141,352	246,749	438,979	-	50,679	141,352	120,942	312,973
Others	171	187,246	-	765,874	953,291	-	187,246	-	729,408	916,654
	423	610,388	13,903,173	1,098,141	15,612,125	-	610,388	13,903,173	916,433	15,429,994

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

19. ADVANCES AND OTHER ACCOUNTS

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Advances to customers				
Bills receivable	509,729	484,375	509,729	484,375
Trade bills	164,557	138,337	164,557	138,337
Other advances to customers	<u>31,047,597</u>	<u>26,251,826</u>	<u>31,047,068</u>	<u>26,250,106</u>
	31,721,883	26,874,538	31,721,354	26,872,818
Interest receivable	286,187	267,337	285,803	267,055
Impairment allowances				
- Individually assessed	(17,876)	(32,161)	(17,876)	(32,161)
- Collectively assessed	<u>(116,720)</u>	<u>(104,464)</u>	<u>(116,714)</u>	<u>(104,447)</u>
	31,873,474	27,005,250	31,872,567	27,003,265
Advances to banks and other financial institutions	<u>57,084</u>	<u>57,425</u>	<u>57,084</u>	<u>57,425</u>
	31,930,558	27,062,675	31,929,651	27,060,690
Other accounts	<u>565,332</u>	<u>434,345</u>	<u>163,789</u>	<u>141,163</u>
	<u>32,495,890</u>	<u>27,497,020</u>	<u>32,093,440</u>	<u>27,201,853</u>

Included in the “Advances to customers” of the Group and the Bank are aggregate amounts of approximately HK\$Nil (2006: HK\$77,785,000) due from companies having significant influence on the Group.

Included in the “Advances to banks and other financial institutions” of the Group and the Bank is an amount of approximately HK\$57,084,000 (2006: HK\$57,425,000) placed as reserve funds with the financial institutions in the People’s Republic of China by the Shantou Branch of the Bank in compliance with the requirements of Regulations Governing Foreign Financial Institutions of the People’s Republic of China.

Included in the “other accounts” of the Group and the Bank is retirement benefits scheme assets of HK\$21,914,000 (2006: HK\$Nil) due to the excess of scheme assets over defined benefit obligations, as disclosed in Note 35.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

19. ADVANCES AND OTHER ACCOUNTS - continued

Impairment allowances on advances:

	THE GROUP			THE BANK		
	Individual	Collective	Total	Individual	Collective	Total
	assessment	assessment		assessment	assessment	
HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
Balance at 1 January 2007	32,161	104,464	136,625	32,161	104,447	136,608
Increase in impairment allowances	99,889	12,238	112,127	99,889	12,249	112,138
Amounts reversed	(29,205)	-	(29,205)	(29,205)	-	(29,205)
Recoveries of advances written off in previous years	21,458	-	21,458	21,458	-	21,458
Unwinding effect of discount rate	(19,417)	-	(19,417)	(19,417)	-	(19,417)
Amounts written off	(87,010)	-	(87,010)	(87,010)	-	(87,010)
Exchange difference	-	18	18	-	18	18
Balance at 31 December 2007	<u>17,876</u>	<u>116,720</u>	<u>134,596</u>	<u>17,876</u>	<u>116,714</u>	<u>134,590</u>

	THE GROUP			THE BANK		
	Individual	Collective	Total	Individual	Collective	Total
	assessment	assessment		assessment	assessment	
HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	
Balance at 1 January 2006	54,640	131,933	186,573	54,640	131,901	186,541
Increase in impairment allowances	141,403	-	141,403	141,376	-	141,376
Amounts reversed	(54,115)	(27,487)	(81,602)	(54,115)	(27,472)	(81,587)
Recoveries of advances written off in previous years	47,453	-	47,453	47,453	-	47,453
Unwinding effect of discount rate	(3,061)	-	(3,061)	(3,061)	-	(3,061)
Amounts written off	(154,159)	-	(154,159)	(154,132)	-	(154,132)
Exchange difference	-	18	18	-	18	18
Balance at 31 December 2006	<u>32,161</u>	<u>104,464</u>	<u>136,625</u>	<u>32,161</u>	<u>104,447</u>	<u>136,608</u>

Details of the impaired loans are as follows:

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Gross impaired loans	215,820	329,660	215,820	329,660
Less: Impairment allowances under individual assessment	(17,876)	(32,161)	(17,876)	(32,161)
Net impaired loans	<u>197,944</u>	<u>297,499</u>	<u>197,944</u>	<u>297,499</u>
Gross impaired loans as a percentage of gross advances to customers	<u>0.68%</u>	<u>1.23%</u>	<u>0.68%</u>	<u>1.23%</u>
Market value of collateral pledged	<u>210,897</u>	<u>313,786</u>	<u>210,897</u>	<u>313,786</u>

In addition to the individually assessed loan impairment allowance, the Group has also provided collectively assessed loan impairment allowance for loans that are individually insignificant or advances where no impairment has been identified individually.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

19. ADVANCES AND OTHER ACCOUNTS - continued

Advances to customers of the Group include receivables under finance leases as follows:

	Minimum lease payments		Present value of minimum lease payments	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Within one year	–	97	–	94
In the second to fifth year inclusive	–	–	–	–
	–	97	–	94
Less: Unearned finance income	–	(4)	–	–
Present value of minimum lease payments receivable	–	93	–	94
Analysed as:				
Non-current finance lease receivables (recoverable after 12 months)			–	–
Current finance lease receivables (recoverable within 12 months)			–	94
			–	94

20. INVESTMENTS IN SUBSIDIARIES

(i)

	2007	2006
	HK\$'000	HK\$'000
Unlisted shares, at cost	333,323	363,323

Details of the principal subsidiaries as at 31 December 2007 are as follows:

Name of company	Place of incorporation/ operation	Issued and fully paid ordinary share capital	Percentage of issued share capital directly held	Principal activities
Chong Hing (Nominees) Limited	Hong Kong	HK\$100,000	100%	Provision of nominee services
Chong Hing Finance Limited	Hong Kong	HK\$25,000,000	100%	Deposit-taking and lending
Chong Hing Information Technology Limited	Hong Kong	HK\$100,000	100%	Provision of electronic data processing services
Liu Chong Hing Banking Corporation, Cayman	Cayman Islands/ Hong Kong	US\$10,000,000	100%	General merchant banking
Chong Hing Securities Limited	Hong Kong	HK\$10,000,000	100%	Stockbroking
Chong Hing Commodities and Futures Limited	Hong Kong	HK\$5,000,000	100%	Investment holding and commodities and futures broking
Gallbraith Limited	Hong Kong	HK\$16,550,000	100%	Property investment
Card Alliance Company Limited	Hong Kong	HK\$18,000,000	100%	Credit card management
Chong Hing Insurance Company Limited	Hong Kong	HK\$50,000,000	100%	Insurance underwriting

None of the subsidiaries had any debt security subsisting at the end of the year or at any time during the year.

(ii) Amounts due from subsidiaries

	2007	2006
	HK\$'000	HK\$'000
Amounts due from subsidiaries	3,407	4,677

The amounts due from subsidiaries are unsecured, non-interest bearing and, in the opinion of the directors, are repayable within three months.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

21. INTERESTS IN JOINTLY CONTROLLED ENTITIES

(i)	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Unlisted shares, at cost	–	–	56,500	56,500
Share of increases in net assets, net of dividends received	142,230	99,256	–	–
	<u>142,230</u>	<u>99,256</u>	<u>56,500</u>	<u>56,500</u>

The directors consider the Bank has joint control over these jointly controlled entities.

As at 31 December 2007, the Group had interests in the following jointly controlled entities:

Name of company	Place of incorporation and operation	Class of share held	Ownership interest	Proportion of voting power	Nature of business
Bank Consortium Holding Limited	Hong Kong	Ordinary	13.3%	14.3%	Investment holding and provision of trustee, administration and custodian services for retirement schemes
BC Reinsurance Limited	Hong Kong	Ordinary	21.0%	21.0%	Reinsurance
Hong Kong Life Insurance Limited	Hong Kong	Ordinary	16.7%	16.7%	Life insurance underwriting
Net Alliance Co., Limited	Hong Kong	Ordinary	17.6%	15.0%	Provision of internet services

The summarised financial information in respect of Group's jointly controlled entities which are accounted for using equity method is set out below:

	2007	2006
	HK\$'000	HK\$'000
Assets	573,233	426,031
Liabilities	(431,003)	326,775
Income	105,521	68,006
Expense	<u>(39,447)</u>	<u>(34,460)</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

21. INTERESTS IN JOINTLY CONTROLLED ENTITIES - continued

(ii) Loan to a jointly controlled entity

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Loan to a jointly controlled entity	<u>5,267</u>	<u>31,000</u>	<u>5,267</u>	<u>31,000</u>

The loan to a jointly controlled entity, Bank Consortium Holding Limited, amounting to HK\$5,267,000 (2006: HK\$31,000,000), is unsecured, non-interest bearing, and will be repayable on 28 December 2008.

During the year, HK\$25,733,000 was received from Bank Consortium Holdings Limited as partial repayment of the above mentioned loan.

22. INVESTMENT PROPERTIES

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 1 January	82,250	76,860	64,250	58,860
Net increase in fair value recognised in the income statement	14,391	5,390	8,050	5,390
Disposals	<u>(36,400)</u>	—	<u>(36,400)</u>	—
At 31 December	<u>60,241</u>	<u>82,250</u>	<u>35,900</u>	<u>64,250</u>

Investment properties owned by the Group and by the Bank were revalued at 31 December 2007 on an open market value basis by Vigers Hong Kong Limited, independent professionally qualified valuers.

The investment properties are rented out under operating leases.

The carrying amount of investment properties of the Group and the Bank comprises:

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Leasehold properties				
Held in Hong Kong on long-term lease (over 50 years unexpired)	14,500	10,250	14,500	10,250
Held in Hong Kong on medium-term lease (10 - 50 years unexpired)	21,400	54,000	21,400	54,000
Held outside Hong Kong on medium-term lease (10 - 50 years unexpired)	<u>24,341</u>	<u>18,000</u>	—	—
	<u>60,241</u>	<u>82,250</u>	<u>35,900</u>	<u>64,250</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

23. PROPERTY AND EQUIPMENT

	THE GROUP			THE BANK		
	Buildings HK\$'000	Equipment HK\$'000	Total HK\$'000	Buildings HK\$'000	Equipment HK\$'000	Total HK\$'000
COST						
At 1 January 2007	284,080	351,348	635,428	284,080	316,559	600,639
Additions	24,265	78,785	103,050	20,465	66,816	87,281
Disposals	-	(4,962)	(4,962)	-	(4,828)	(4,828)
Exchange adjustments	-	4	4	-	4	4
At 31 December 2007	<u>308,345</u>	<u>425,175</u>	<u>733,520</u>	<u>304,545</u>	<u>378,551</u>	<u>683,096</u>
ACCUMULATED DEPRECIATION						
At 1 January 2007	21,562	233,041	254,603	21,562	206,962	228,524
Provided for the year	6,079	30,767	36,846	6,072	27,569	33,641
Eliminated on disposals	-	(4,803)	(4,803)	-	(4,669)	(4,669)
Exchange adjustments	-	1	1	-	1	1
At 31 December 2007	<u>27,641</u>	<u>259,006</u>	<u>286,647</u>	<u>27,634</u>	<u>229,863</u>	<u>257,497</u>
CARRYING AMOUNTS						
At 31 December 2007	<u>280,704</u>	<u>166,169</u>	<u>446,873</u>	<u>276,911</u>	<u>148,688</u>	<u>425,599</u>

	THE GROUP				THE BANK			
	Buildings HK\$'000	Equipment HK\$'000	Construction in progress HK\$'000	Total HK\$'000	Buildings HK\$'000	Equipment HK\$'000	Construction in progress HK\$'000	Total HK\$'000
COST								
At 1 January 2006	80,511	308,643	40,454	429,608	80,511	278,556	-	359,067
Additions	14,407	52,633	148,708	215,748	14,407	45,317	189,162	248,886
Disposals	-	(9,924)	-	(9,924)	-	(7,310)	-	(7,310)
Transfer from construction in progress to buildings	189,162	-	(189,162)	-	189,162	-	(189,162)	-
Exchange adjustments	-	(4)	-	(4)	-	(4)	-	(4)
At 31 December 2006	<u>284,080</u>	<u>351,348</u>	<u>-</u>	<u>635,428</u>	<u>284,080</u>	<u>316,559</u>	<u>-</u>	<u>600,639</u>
ACCUMULATED DEPRECIATION								
At 1 January 2006	19,498	213,350	-	232,848	19,498	187,462	-	206,960
Provided for the year	2,064	28,471	-	30,535	2,064	25,843	-	27,907
Eliminated on disposals	-	(8,778)	-	(8,778)	-	(6,341)	-	(6,341)
Exchange adjustments	-	(2)	-	(2)	-	(2)	-	(2)
At 31 December 2006	<u>21,562</u>	<u>233,041</u>	<u>-</u>	<u>254,603</u>	<u>21,562</u>	<u>206,962</u>	<u>-</u>	<u>228,524</u>
CARRYING AMOUNTS								
At 31 December 2006	<u>262,518</u>	<u>118,307</u>	<u>-</u>	<u>380,825</u>	<u>262,518</u>	<u>109,597</u>	<u>-</u>	<u>372,115</u>

The above items of property and equipment are depreciated on a straight-line basis at the following rates per annum:

Leasehold buildings	Over the shorter of the term of the lease or 2%
Equipment	10% -20%

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

23. PROPERTY AND EQUIPMENT - continued

The carrying amount of buildings shown above comprise:

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Leasehold properties				
Held in Hong Kong on long-term lease (over 50 years unexpired)	212,036	201,337	211,885	201,337
Held in Hong Kong on medium-term lease (10-50 years unexpired)	65,450	60,299	61,808	60,299
Held outside Hong Kong on medium-term lease (10-50 years unexpired)	3,218	882	3,218	882
	<u>280,704</u>	<u>262,518</u>	<u>276,911</u>	<u>262,518</u>

24. PREPAID LEASE PAYMENTS FOR LAND

The Group's prepaid lease payments comprise:

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
COST				
In Hong Kong held on:				
Leases of over 50 years	125,548	126,035	650,932	651,975
Leases of between 10 to 50 years	204,592	183,952	193,442	183,952
Outside Hong Kong held on:				
Leases of between 10 to 50 years	4,091	6,548	4,091	6,548
	<u>334,231</u>	<u>316,535</u>	<u>848,465</u>	<u>842,475</u>
Net book value at 1 January	316,535	300,969	842,475	217,931
Additions	28,171	20,680	17,071	630,226
Amortisation of prepaid operating lease payments	(5,710)	(5,114)	(6,316)	(5,682)
Disposals	(4,765)	–	(4,765)	–
	<u>334,231</u>	<u>316,535</u>	<u>848,465</u>	<u>842,475</u>
Analysed as:				
Current portion	5,710	5,114	6,316	5,682
Non-current portion	328,521	311,421	842,149	836,793
Total	<u>334,231</u>	<u>316,535</u>	<u>848,465</u>	<u>842,475</u>

The allocation of lease payments between leasehold land and building elements was performed by Vigers Hong Kong Limited, independent professionally qualified valuers.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

25. DEPOSITS FROM CUSTOMERS

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Demand deposits and current accounts	2,992,184	2,479,907	2,992,184	2,479,907
Savings deposits	12,584,043	9,377,813	12,584,043	9,377,813
Time, call and notice deposits	44,751,210	42,817,512	44,747,371	42,813,454
	<u>60,327,437</u>	<u>54,675,232</u>	<u>60,323,598</u>	<u>54,671,174</u>

Included in the balances is an aggregate amount of approximately HK\$174,430,000 (2006: HK\$127,187,000) representing deposits of companies and their subsidiaries having significant influence on the Bank.

26. LOAN CAPITAL

	THE GROUP AND THE BANK	
	2007	2006
	HK\$'000	HK\$'000
US\$125 million callable floating rate subordinated notes due 2016	<u>970,871</u>	<u>967,376</u>

On 15 December 2006 the Bank issued subordinated notes qualifying as tier 2 capital with face value of US\$125,000,000.

The above subordinated notes will mature on 16 December, 2016 and are redeemable at the option of the Group in December 2011 at their principal amount.

The floating rate notes bear interest at the rate of three month LIBOR plus 0.93 per cent, payable quarterly from the issue date to the call option date. Thereafter, if the notes are not redeemed on the call option date, the interest rate will be reset to three month LIBOR plus 1.93 per cent, payable quarterly.

27. SHARE CAPITAL

	2007 & 2006
	HK\$'000
Authorised:	
600,000,000 shares of HK\$0.50 each	<u>300,000</u>
Issued and fully paid:	
435,000,000 shares of HK\$0.50 each	<u>217,500</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

28. RESERVES

	Share premium HK\$'000	Investment revaluation reserve HK\$'000	General reserve HK\$'000	Translation reserve HK\$'000	Regulatory reserve HK\$'000	Retained profits HK\$'000	Total HK\$'000
THE BANK							
At 1 January 2007	1,542,817	73,491	1,378,500	98	165,000	2,590,750	5,750,656
Revaluation losses, net	-	(328,073)	-	-	-	-	(328,073)
Exchange differences arising from translation of foreign operations	-	-	-	237	-	-	237
Deferred taxation arising from revaluation movement (Note 29)	-	8,423	-	-	-	-	8,423
Net expense recognised directly in equity	-	(319,650)	-	237	-	-	(319,413)
Profit for the year	-	-	-	-	-	440,334	440,334
Reversal of reserves upon impairment	-	369,627	-	-	-	-	369,627
Reversal of reserves upon disposal	-	(72,956)	-	-	-	-	(72,956)
Total recognised income for the year	-	(22,979)	-	237	-	440,334	417,592
Interim dividend paid	-	-	-	-	-	(91,350)	(91,350)
Final dividend paid	-	-	-	-	-	(191,400)	(191,400)
Earmark of retained profits as regulatory reserve	-	-	-	-	191,000	(191,000)	-
At 31 December 2007	<u>1,542,817</u>	<u>50,512</u>	<u>1,378,500</u>	<u>335</u>	<u>356,000</u>	<u>2,557,334</u>	<u>5,885,498</u>
At 1 January 2006	1,542,817	139,735	1,378,500	(127)	122,837	2,418,118	5,601,880
Revaluation losses, net	-	(23,787)	-	-	-	-	(23,787)
Exchange differences arising from translation of foreign operations	-	-	-	225	-	-	225
Deferred taxation arising from revaluation movement (Note 29)	-	(12,600)	-	-	-	-	(12,600)
Net expense recognised directly in equity	-	(36,387)	-	225	-	-	(36,162)
Profit for the year	-	-	-	-	-	480,145	480,145
Reversal of reserves upon disposal	-	(29,857)	-	-	-	-	(29,857)
Total recognised income for the year	-	(66,244)	-	225	-	480,145	414,126
Interim dividend paid	-	-	-	-	-	(82,650)	(82,650)
Final dividend paid	-	-	-	-	-	(182,700)	(182,700)
Earmark of retained profits as regulatory reserve	-	-	-	-	42,163	(42,163)	-
At 31 December 2006	<u>1,542,817</u>	<u>73,491</u>	<u>1,378,500</u>	<u>98</u>	<u>165,000</u>	<u>2,590,750</u>	<u>5,750,656</u>

The Bank's reserves available for distribution to shareholders as at 31 December 2007 comprised retained profits of HK\$2,557,334,000 (2006: HK\$2,590,750,000) and general reserve of HK\$1,378,500,000 (2006: HK\$1,378,500,000).

The regulatory reserve is set up in compliance with the Hong Kong Monetary Authority's requirements and is distributable to shareholders of the Bank subject to consultation with the Hong Kong Monetary Authority.

The general reserve is comprised of transfers from previous years' retained profits.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

29. DEFERRED TAXATION

The following are the major deferred tax liabilities (assets) recognised and movements thereon during the current and prior reporting year:

	Accelerated tax depreciation HK\$'000	Collectively assessed impairment allowance HK\$'000	Investment properties HK\$'000	Revaluation of available- for-sale securities HK\$'000	Total HK\$'000
THE GROUP					
At 1 January 2007	10,403	(17,263)	7,574	27,125	27,839
Charge (credit) to consolidated income statement for the year (Note 13)	1,879	(2,463)	(1,425)	–	(2,009)
Credit to equity for the year	–	–	–	(10,556)	(10,556)
At 31 December 2007	<u>12,282</u>	<u>(19,726)</u>	<u>6,149</u>	<u>16,569</u>	<u>15,274</u>
At 1 January 2006	9,353	(22,433)	6,631	–	(6,449)
Charge to consolidated income statement for the year (Note 13)	1,050	5,170	943	–	7,163
Charge to equity for the year	–	–	–	27,125	27,125
At 31 December 2006	<u>10,403</u>	<u>(17,263)</u>	<u>7,574</u>	<u>27,125</u>	<u>27,839</u>
THE BANK					
At 1 January 2007	10,403	(17,260)	7,574	12,600	13,317
Credit to income statement for the year	(1,120)	(2,465)	(3,386)	–	(6,971)
Credit to equity for the year	–	–	–	(8,423)	(8,423)
At 31 December 2007	<u>9,283</u>	<u>(19,725)</u>	<u>4,188</u>	<u>4,177</u>	<u>(2,077)</u>
At 1 January 2006	9,353	(22,427)	6,631	–	(6,443)
Charge to income statement for the year	1,050	5,167	943	–	7,160
Charge to equity for the year	–	–	–	12,600	12,600
At 31 December 2006	<u>10,403</u>	<u>(17,260)</u>	<u>7,574</u>	<u>12,600</u>	<u>13,317</u>

30. SHARE OPTION SCHEME

The Bank's share option scheme (the "Scheme") was adopted pursuant to a resolution passed on 25 April 2002 for the primary purpose of providing incentives to directors and eligible employees, and will expire on 24 April 2012. Under the Scheme, the Board of Directors of the Bank may grant options to eligible employees, including directors of the Bank and its subsidiaries, to subscribe for shares in the Bank. Additionally, the Bank may, from time to time, grant share options to outside third parties for settlement in respect of goods or services provided to the Bank.

The total number of shares in respect of which options may be granted under the Scheme is not permitted to exceed 10% of the shares of the Bank in issue at the date of approval of the Scheme, without prior approval from the Bank's shareholders. The number of shares in respect of which options may be granted to any individual is not permitted to exceed 1% of the shares of the Bank in issue at any point in time, without prior approval from the Bank's shareholders.

Options granted must be taken up within 28 days of the date of offer, upon payment of HK\$10 per option. Options may be exercised at any time from the date of grant of the share option to the fifth anniversary of the date of grant. The exercise price is determined by the Board of Directors of the Bank, and will be the highest of the closing price of the Bank's shares on the date of offer, the average closing price of the shares for the five trading days immediately preceding the date of offer and the nominal value of the shares.

No options have been granted under the above-mentioned scheme since the Scheme was adopted.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

31. LOANS TO OFFICERS

The aggregate relevant loans to officers, included in “advances to customers” in Note 19, and disclosed pursuant to Section 161B of the Companies Ordinance are as follows:

	THE GROUP AND THE BANK	
	2007	2006
	HK\$'000	HK\$'000
Aggregate balance of all relevant loans outstanding at the balance sheet date	<u>85,172</u>	<u>90,865</u>
Maximum aggregate balance of relevant loans during the year	<u>172,658</u>	<u>163,699</u>

The loans have no fixed repayment terms and the applicable interest rate ranges from 0% to prime rate plus 10%. Included in the loans to officers are loans of HK\$83,683,000 (2006: HK\$89,369,000) with collateral.

32. IMPAIRMENT LOSS ON GOODWILL

In prior years, the Group acquired 100% of issued share capital of Chong Hing Insurance Company Limited. The amount of goodwill arising as a result of acquisition was HK\$110,606,000.

For the year ended 31 December 2007, management has reviewed the goodwill for impairment purposes. The review comprised a comparison of the carrying amount and value in use of an acquired subsidiary (the smallest cash-generating unit) to which the goodwill has been allocated. The acquired subsidiary is involved in insurance business.

The value in use calculations primarily use cash flow projections based on five year financial budgets approved by management and estimated terminal value at the end of the five year period. There are a number of assumptions and estimates involved for the preparation of cash flow projections for the period covered by the approved budget and the estimated terminal value. Key assumptions include the expected growth in revenues and selection of discount rates.

Value in use is derived at by discounting the expected future cash flows at 12% discount rate. Management's financial model assumes an overall growth in gross written premium of 5% per annum during the first 5 years. Cash flows beyond five years are extrapolated using a terminal growth rate of 3.5%. A goodwill impairment loss of HK\$30,000,000 (2006: HK\$Nil), representing the excess of the carrying amount above the value in use, has been recognised for the year ended 31 December 2007.

33. IMPAIRMENT LOSS ON AVAILABLE-FOR-SALE SECURITIES

As of 31 December 2007, the Group investment portfolio contained capital or income notes issued by Structured Investment Vehicles (“SIVs”), which were categorised as available-for-sale investments in 2006 and 2007.

These investments are considered illiquid based upon the fact that there were no open market bids for them as of 31 December 2007. As such, the fair value of these investments was estimated to approximate net asset value as reported by the SIVs investment managers unless market conditions warrant a different valuation method.

The total amounts invested in these SIVs are HK\$568,212,000 (2006: HK\$433,131,000). The Group evaluates these available-for-sale investments for impairment on a regular basis. Impairment losses of HK\$369,627,000 (2006: HK\$Nil) has been recognised for the year ended 31 December 2007 primarily due to downgrade of credit ratings and increase of funding costs for the SIVs.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

34. CONTINGENT LIABILITIES AND COMMITMENTS

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Contingent liabilities and commitments				
- contractual amounts				
Direct credit substitutes	643,264	1,221,388	643,264	1,221,388
Trade - related contingencies	595,878	346,531	595,878	346,531
Forward asset purchases	32,926	227,967	32,926	227,967
Other commitments:				
Which are unconditionally cancellable without prior notice	5,761,482	4,082,935	5,761,482	4,082,935
With an original maturity of one year and under	8,632,587	4,602,428	8,632,587	4,602,428
With an original maturity of over one year	2,212,847	1,599,572	2,212,847	1,599,572
Lease commitments	65,264	71,048	62,588	66,343
	<u>17,944,248</u>	<u>12,151,869</u>	<u>17,941,572</u>	<u>12,147,164</u>

At the balance sheet dates, the Group had commitments for future minimum lease payments under these non-cancellable operating leases which fall due as follows:

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Within one year	28,150	25,975	26,288	23,945
In the second to fifth years inclusive	36,839	43,088	36,025	40,413
Over five years	275	1,985	275	1,985
	<u>65,264</u>	<u>71,048</u>	<u>62,588</u>	<u>66,343</u>

Operating lease payments represent rental payable by the Group for certain of its office properties. Leases are negotiated for an average term of three years and rentals are fixed.

Capital commitments outstanding at the balance sheet dates are as follows:

	THE GROUP		THE BANK	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Capital expenditure contracted for but not provided in the financial statements in respect of:				
- property and equipment	32,926	77,725	32,926	77,725
- investments in funds	-	150,242	-	150,242
	<u>32,926</u>	<u>227,967</u>	<u>32,926</u>	<u>227,967</u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

34. CONTINGENT LIABILITIES AND COMMITMENTS - continued

The credit risk weighted amount of contingent liabilities and commitments is HK\$3,321,625,000 (2006: HK\$3,329,570,000).

At the balance sheet date, the Group and the Bank as lessor had contracted with tenants for the following future minimum lease payments:

	THE GROUP AND THE BANK	
	2007	2006
	HK\$'000	HK\$'000
Within one year	2	6
In the second to fifth years inclusive	—	2
	<u>2</u>	<u>8</u>

35. RETIREMENT BENEFITS SCHEME

At the balance sheet date, the Group had three retirement schemes in operation, a contributory scheme and a defined benefit scheme which were registered under the Occupational Retirement Scheme Ordinance (the "ORSO Scheme") in 1995 and a Mandatory Provident Fund Scheme (the "MPF Scheme") established under the Mandatory Provident Fund Ordinance in December 2000. Employees who were members of the ORSO Scheme prior to the establishment of the MPF Scheme stayed within the ORSO Scheme or switched to the MPF Scheme, whereas all new employees joining the Group on or after December 2000 are required to join the MPF Scheme. Most of the employees enrolled in the MPF Scheme in replacement of the ORSO Scheme (the "participating members"). The assets of the schemes are held separately from those of the Group, in funds under the control of trustees. Under the MPF Scheme, the employee contributes 5% of the relevant payroll to the MPF Scheme while the Group contributes from 5% to 10% of the relevant payroll to the MPF Scheme depending on the years of service completed.

The Group operates the ORSO (Defined benefit) Scheme for qualifying employees. Under the ORSO Scheme (Defined benefit), the employees are entitled to retirement benefits varying between 0 and 100 percent of total contributions on attainment of a retirement age of 55. Upon retirement, the employees are entitled to monthly pension until death varying between 0 and 100 percent of final salary depending on years of service completed at the time of retirement.

The most recent actuarial valuation of the ORSO (Defined benefit) Scheme was carried out as at 31 December 2007 by the qualified actuaries of Watson Wyatt Hong Kong Limited. The accrued liabilities and future costs were measured using the Projected Unit Credit method.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

35. RETIREMENT BENEFITS SCHEME - continued

At the date of the latest formal independent actuarial valuation made at 31 December 2007, the market value of the ORSO (Defined benefit) Scheme was HK\$47,035,000.

Net benefit income:

	HK\$'000
Current service cost	(84)
Interest cost on benefit obligation	(1,014)
Expected return on plan assets	1,956
Actuarial gains recognised in the year	<u>9,343</u>
Net benefit income	<u><u>10,201</u></u>

The amount included in the consolidated balance sheet arising from Group's defined benefit retirement benefit plan is as follows:

	HK\$'000
Present value of defined benefit obligation	(25,121)
Fair value of plan assets	<u>47,035</u>
Retirement benefit asset	<u><u>21,914</u></u>

Changes in the present value of the defined benefit obligation are as follows:

	HK\$'000
Opening defined benefit obligation	28,742
Interest cost	1,014
Current service cost	84
Actuarial gains on obligations	(2,211)
Benefits paid	<u>(2,508)</u>
Closing defined benefit obligation	<u><u>25,121</u></u>

Changes in fair value of plan assets are as follows:

	HK\$'000
Opening fair value of plan assets	40,455
Expected return	1,956
Actuarial gains on plan assets	7,132
Benefits paid	<u>(2,508)</u>
Closing fair value of plan assets	<u><u>47,035</u></u>

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

35. RETIREMENT BENEFITS SCHEME - continued

The Bank does not expect to make contributions to its defined benefit plan as the market value of Scheme assets was sufficient to cover the Aggregate Vested Liability and Aggregate Past Service Cost.

The major categories of plan assets as a percentage of the fair value of total plan assets are as follows:

	%
Cash	29
Equities	71

The overall expected rates of return on assets is determined based on the market prices including published brokers' forecasts prevailing on the date of valuation, applicable to the period over which the obligation is to be settled.

The actual return on plan assets for 2007 was HK\$9,088,000.

The amounts of assets of the Scheme invested in the Bank's own financial instruments as at 31 December 2007 were:

	HK\$'000
Deposits with the Bank	13,270

The principal assumptions used in determining pension obligations for the Bank's plan are shown below:

	%
Discount rate	3.5
Expected rate of return on plan assets	5.0
Expected rate of salary increase	3.0

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

36. RELATED PARTY TRANSACTIONS

During the year, the Group and the Bank entered into the following material transactions with related parties:

	Interest, commission and rental income		Interest and rental expenses	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Investing enterprises having significant influence on the Bank and their subsidiaries	<u>11,033</u>	<u>4,580</u>	<u>16,769</u>	<u>16,663</u>
Jointly controlled entities	<u>13,480</u>	<u>8,387</u>	<u>12,901</u>	<u>11,728</u>
Directors and their associates	<u>20,100</u>	<u>43,562</u>	<u>26,638</u>	<u>24,869</u>

The above transactions were carried out at market rates.

At the balance sheet date, the Group and the Bank had the following material outstanding balances with related parties:

	Amounts due from related parties		Amounts due to related parties	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Investing enterprises having significant influence on the Bank and subsidiaries	<u>–</u>	<u>77,785</u>	<u>174,430</u>	<u>127,187</u>
Jointly controlled entities	<u>5,267</u>	<u>31,000</u>	<u>277,015</u>	<u>147,701</u>
Directors and their associates	<u>991,440</u>	<u>1,006,461</u>	<u>603,806</u>	<u>618,282</u>

The above outstanding balances bear interest at rates similar to those made available to non-related parties.

The Group's lending to related parties are under terms and conditions similar to those made available to non-related parties.

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2007

36. RELATED PARTY TRANSACTIONS - continued

During the year, the Bank entered into the following material transactions with subsidiaries:

	Interest, commission and rental income		Interest and rental expenses		Computer service expense		Dividend income		Purchase of land and building	
	2007	2006	2007	2006	2007	2006	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Subsidiaries	<u>8,852</u>	<u>2,773</u>	<u>21,314</u>	<u>19,102</u>	<u>27,700</u>	<u>26,877</u>	<u>230,000</u>	<u>100,000</u>	<u>-</u>	<u>650,000</u>

The above transactions were carried out at market rates.

At the balance sheet date, the Bank had the following material outstanding balances with subsidiaries:

	Amounts due from		Amounts due to	
	2007	2006	2007	2006
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Subsidiaries	<u>3,407</u>	<u>4,677</u>	<u>658,146</u>	<u>616,592</u>

The above outstanding balances are unsecured, non-interest bearing and, in the opinion of the directors, are repayable within three months.

Compensation of key management personnel

The remuneration of directors and other members of key management during the year was as follows:

	THE GROUP AND THE BANK	
	2007	2006
	HK\$'000	HK\$'000
Short-term benefits	49,787	44,048
Post employment benefits	<u>3,324</u>	<u>2,892</u>
	<u>53,111</u>	<u>46,940</u>

The remuneration of directors and key management is reviewed by Remuneration Committee having regard to the performance of individuals and market trends.

37. COMPARATIVE FIGURES

Net fee and commission income and other operating income have been reclassified to conform with the current year's presentation.

The unaudited supplementary financial information regarding corporate governance, risk management and other financial information disclosed pursuant to the Banking (Disclosure) Rules issued by the Hong Kong Monetary Authority is as follows :

1. SPECIALISED COMMITTEES

The Board of Directors of the Bank (the “Board”) is constituted in accordance with the Bank’s Articles of Association and is the ultimate governing body. In order to ensure that matters arising between meetings of the Board are handled properly and timely, the Board delegates the day-to-day supervision of major functional areas to the following specialised committees. These committees are established with clearly defined objectives, authorities, responsibilities and tenure. Written terms of reference are approved by the Board and are up-dated appropriately.

(i) Executive Committee

The Executive Committee comprises all executive directors of the Bank.

It is authorised by the Board to exercise all such powers and do all such acts as may be exercised, done or approved by Board, thus relieving the full Board of detailed review of information and operational activities. The Executive Committee steers the Group’s policy and operational decisions on a day-to-day basis, and attends to matters that require the review and supervision of the Board between regular board meetings. Moreover, it also coordinates the work of other committees as it sees fit.

(ii) Executive Management Committee

Members of the Executive Management Committee, comprising the Managing Director and Chief Executive Officer and certain other executive directors and division heads, are responsible for managing the day-to-day business and the affairs of the Bank group. The Executive Management Committee holds regular meetings twice a week to discuss and formulate operation and management policies, discuss significant daily operational issues, review key business performance, and discuss business opportunities arising from changing market and competitive conditions. In performing its functions, the Executive Management Committee shall act in accordance with the directions and requirements as may from time to time be stipulated by the Board.

(iii) Executive Loans Committee

The Executive Loans Committee comprises all executive directors of the Bank.

The Executive Loans Committee is established to guide and review the operations of, and to delegate proper authorities as it deems appropriate from time to time to the Loans Committee. It also approves large and certain specific new loan applications and applications for renewal and amendment of existing loans, having due regard to the Group’s Lending Policy and the relevant laws and regulations.

1. SPECIALISED COMMITTEES - continued

(iv) Loans Committee

Members of the Loans Committee are appointed by the Board. It comprises senior staff members of the Bank including the executive director in charge of the Credit Control Division.

The Loans Committee ensures that the Group's Lending Policy is adequate, and issues guidelines from time to time to guide lending activities of the Group. It also directs the Credit Risk Management Department to monitor loans portfolio quality through identifying problems early and taking timely corrective actions such as implementing debt-restructuring schemes and maintaining adequate provisions for loan losses. The Loans Committee members meet regularly to evaluate loan applications and make credit decisions. The monitoring of compliance with statutory lending limits, the assessment and approval of new loan products, the implementation of policies and instructions set by the Executive Loans Committee are other key functions of the Loans Committee.

(v) The Asset and Liability Management Committee (the "ALCO")

Members of the ALCO are appointed by the Board. It comprises senior staff members representing major divisions of the Bank.

The ALCO is established to facilitate the oversight of the Board in the management of the assets and liabilities of the Group from the perspective of containing the pertinent liquidity, interest rate, foreign exchange and other market risks. The assessment of the impact of the current economic and business climate on the Group's balance sheet, the formulation of the corresponding strategies and plans, and the evaluation of non-credit related products also come under other key functions of the ALCO.

(vi) The Risk Management and Compliance Committee (the "RMCC")

Members of the RMCC are appointed by the Board. It comprises senior staff members who are responsible for risk management, compliance issues and operations of the Bank.

The RMCC is established to facilitate the oversight of the Board concerning risk management and compliance issues of the Bank. The RMCC discharges its responsibilities by identifying and analysing major risk management and compliance issues, and by approving and overseeing the implementation of the risk management and compliance policies and procedures. The RMCC also takes charge of coordinating and monitoring the implementation of the recommendations made by the regulators. Regular reports as prepared by the RMCC are submitted to the Board.

Details concerning composition and functions of Audit Committee and Remuneration Committee are set out in Corporate Governance Report.

2. MANAGEMENT OF RISKS

The Group has established policies, procedures, and controls for measuring, monitoring and controlling risks arising from the banking and related financial services business. These policies, procedures, and controls are implemented by various committees and departments of the Group and are regularly reviewed by the Board. The internal auditors also play an important role in the risk management process by performing regular, as well as sporadic compliance audits.

The management of assets and liabilities of the Group is conducted under the guidance of the ALCO. The ALCO holds weekly meetings, and more frequent meetings when required, to review and direct the relevant policies, and to monitor the bank-wide positions. The day-to-day management of the liquidity, foreign exchange, interest rate and other market risks, and the compliance with the ALCO and RMCC policies are monitored by the Treasury Management and the Finance Departments with the assistance of various qualitative and quantitative analyses.

In addition to complementing the ALCO in the management of assets and liabilities, the RMCC also oversees the implementation of the policies and procedures established for managing the Group's operational, legal, and reputation risks and compliance requirements.

(i) Operational and legal risk

Operational risk is the risk of unexpected losses attributable to human error, systems failures, fraud, or inadequate internal controls and procedures.

Executive directors, department heads, in-house legal counsels, and internal auditors collaborate to manage operational and legal risks through proper human resources policies, delegation of authorities, segregation of duties, and timely and accurate management information. Senior management and the Audit Committee are accountable to the Board for maintaining a strong and disciplined control environment to provide reasonable assurance that the operational and legal risks are prudently managed.

A comprehensive contingency plan is available to ensure that key business functions continue and normal operations are restored effectively and efficiently in the event of business interruption.

(ii) Reputation risk

Reputation risk is the risk to earnings or capital arising from negative public opinion.

Reputation risk is managed by ensuring proper and adequate communications and public relation efforts to foster the reputation of the Group. A risk management mechanism guided by the senior management including executive directors and senior managers has been established to manage the media exposure, handle customers' and other relevant parties' complaints and suggestions, and to ensure that new business activities and agents acting on our behalf do not jeopardise our reputation.

Details of the Group's capital management, credit risk, liquidity risk, market risk, foreign exchange risk, interest rate risk management policies and measures are set out in Note 7 to the consolidated financial statements.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

3. SEGMENTAL INFORMATION

The Group's information concerning geographical analysis has been classified by the location of the principal operations of the branches and subsidiary companies responsible for reporting the results or booking the assets. Details are set out in Note 6 to the consolidated financial statements.

4. ADVANCES TO CUSTOMERS - BY INDUSTRY SECTORS

The Group's gross advances to customers (including advances booked in overseas branches and subsidiaries) are analysed and reported by industry sectors according to the usage of the loans and/or business activities of the borrowers. Details are set out in Note 7 (Credit Risk) to the consolidated financial statements.

The Group's collective impairment allowances, individual impairment allowances, gross impaired advances, new impairment allowances and advances written off during the year in respect of industry sectors which constitute not less than 10 per cent of gross advances to customers are analysed as follows:

	31 December 2007						
	Gross loans and advances HK\$'000	Collective impairment allowances HK\$'000	Individual impairment allowances HK\$'000	Gross impaired advances HK\$'000	New impairment allowances during the year HK\$'000	Advances written off during the year HK\$'000	
Loans for use in Hong Kong							
Industrial, commercial and financial							
- Property investment	6,506,746	2,333	-	19,262	3,065	3,000	
- Others	4,829,971	10,467	84	58,383	16,166	16,065	
Individuals							
- Loans for the purchase of other residential properties	4,704,769	4,864	284	284	254	103	
Loans for use outside Hong Kong	3,530,335	54,289	1,004	113,904	32,621	35,500	
	31 December 2006						
	Gross loans and advances HK\$'000	Collective impairment allowances HK\$'000	Individual impairment allowances HK\$'000	Gross impaired advances HK\$'000	New impairment allowances during the year HK\$'000	Advances written off during the year HK\$'000	
Loans for use in Hong Kong							
Industrial, commercial and financial							
- Property investment	6,073,467	20,054	2,313	27,045	108	4,221	
- Others	4,868,117	9,682	6,235	63,680	35,053	22,652	
Individuals							
- Loans for the purchase of other residential properties	3,476,285	4,352	459	8,708	471	567	
Loans for use outside Hong Kong	3,736,956	33,359	13,000	162,327	31,684	32,311	

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

5. ADVANCES TO CUSTOMERS - BY GEOGRAPHICAL AREAS

The Group's gross advances to customers by countries or geographical areas after taking into account any risk transfers are as follows:

	31 December 2007				
	Total advances HK\$'000	Advances overdue for over three months HK\$'000	Impaired advances HK\$'000	Individual impairment allowance HK\$'000	Collective impairment allowance HK\$'000
Hong Kong	29,035,137	201,750	118,916	16,872	98,593
People's Republic of China	185,861	96,904	96,904	1,004	2,450
Macau	1,183,673	-	-	-	10,215
America	327,637	-	-	-	5,462
Others	989,575	-	-	-	-
	<u>31,721,883</u>	<u>298,654</u>	<u>215,820</u>	<u>17,876</u>	<u>116,720</u>

	31 December 2006				
	Total advances HK\$'000	Advances overdue for over three months HK\$'000	Impaired advances HK\$'000	Individual impairment allowance HK\$'000	Collective impairment allowance HK\$'000
Hong Kong	24,417,811	320,852	204,854	31,161	82,383
People's Republic of China	271,592	124,806	124,806	1,000	1,447
Macau	1,460,076	-	-	-	13,684
America	356,916	-	-	-	5,518
Others	368,143	-	-	-	1,432
	<u>26,874,538</u>	<u>445,658</u>	<u>329,660</u>	<u>32,161</u>	<u>104,464</u>

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

6. CROSS-BORDER CLAIMS

The Group's cross-border claims by countries or geographical areas which constitutes 10% or more of the relevant disclosure item after taking into account any risk transfers are as follows:

	2007			
	Banks and other financial institutions HK\$'000	Public sector entities HK\$'000	Others HK\$'000	Total HK\$'000
Asia Pacific excluding Hong Kong	11,066,557	83,332	1,288,720	12,438,609
- of which - Australia	3,550,345	1,625	1,888	3,553,858
North America	2,475,330	16,684	1,434,847	3,926,861
Europe	13,133,599	2,433	769,382	13,905,414
- of which - United Kingdom	2,753,192	1,008	307,940	3,062,140
- of which - Germany	<u>2,704,841</u>	<u>1,304</u>	<u>3,754</u>	<u>2,709,899</u>
	2006			
	Banks and other financial institutions HK\$'000	Public sector entities HK\$'000	Others HK\$'000	Total HK\$'000
Asia Pacific excluding Hong Kong	10,101,438	65,696	1,339,099	11,506,233
- of which - Australia	3,929,675	2,138	995	3,932,808
North America	2,811,117	17,569	1,278,823	4,107,509
Europe	16,004,492	2,902	725,986	16,733,380
- of which - United Kingdom	3,741,074	1,478	310,507	4,053,059
- of which - Germany	<u>3,471,632</u>	<u>1,278</u>	<u>3,980</u>	<u>3,476,890</u>

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

7. CURRENCY RISK

The Group's foreign currency exposures arising from non-trading and structural position which constitute 10% or more of the total net position in all foreign currencies are as follows:

	2007		Total
	US\$	AUD	
Equivalent in thousands of HK\$			
Spot assets	14,600,807	2,475,049	17,075,856
Spot liabilities	(14,571,481)	(2,475,105)	(17,046,586)
Forward purchases	69,167	12,740	81,907
Forward sales	(78,616)	(9,297)	(87,913)
Net long position	<u>19,877</u>	<u>3,387</u>	<u>23,264</u>
		RMB	MOP
Net structural position		<u>107,230</u>	<u>48,545</u>

	2006			Total
	US\$	MOP	RMB	
Equivalent in thousands of HK\$				
Spot assets	13,633,746	59,251	286,962	13,979,959
Spot liabilities	(13,359,547)	(49,829)	(283,551)	(13,692,927)
Forward purchases	185,772	–	2,192	187,964
Forward sales	(455,999)	–	–	(455,999)
Net long position	<u>3,972</u>	<u>9,422</u>	<u>5,603</u>	<u>18,997</u>
				MOP
Net structural position				<u>48,545</u>

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

8. OVERDUE AND RESCHEDULED ASSETS

	2007	
	Gross amount of advances HK\$'000	Percentage to total advances %
Advances overdue for		
- 6 months or less but over 3 months	22,180	0.1
- 1 year or less but over 6 months	12,697	0.1
- over 1 year	<u>263,777</u>	<u>0.8</u>
Total overdue advances	<u>298,654</u>	<u>1.0</u>
Rescheduled advances	<u>183,825</u>	<u>0.6</u>
Individual impairment allowances made in respect of overdue loans and advances	<u>4,898</u>	

	2006	
	Gross amount of advances HK\$'000	Percentage to total advances %
Advances overdue for		
- 6 months or less but over 3 months	59,715	0.2
- 1 year or less but over 6 months	29,325	0.1
- over 1 year	<u>356,618</u>	<u>1.3</u>
Total overdue advances	<u>445,658</u>	<u>1.6</u>
Rescheduled advances	<u>257,203</u>	<u>1.0</u>
Individual impairment allowances made in respect of overdue loans and advances	<u>26,012</u>	

The value of the security of the above overdue advances is analysed as follows:

	2007 HK\$'000	2006 HK\$'000
Covered portion of overdue loans and advances	290,558	430,789
Uncovered portion of overdue loans and advances	<u>8,096</u>	<u>14,869</u>
	<u>298,654</u>	<u>445,658</u>
Market value of collateral held against covered portion of overdue loans and advances	<u>805,823</u>	<u>704,123</u>

There were no advances to banks and other financial institutions or other assets which were overdue for over 3 months as at 31 December 2007 and 31 December 2006, nor were there any rescheduled advances to banks and other financial institutions.

Repossessed assets held by the Group as at 31 December 2007 amounted to HK\$87,570,000 (2006: HK\$103,480,000).

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

9. NON-BANK MAINLAND EXPOSURES

	31 December 2007			
	On-balance sheet exposure HK\$'000	Off-balance sheet exposure HK\$'000	Total HK\$'000	Individual impairment allowance HK\$'000
Types of counterparties				
Mainland entities	746,276	390,346	1,136,622	–
Companies and individuals outside Mainland where the credit is granted for use in Mainland	2,490,540	1,591,485	4,082,025	1,000
Other counterparties the exposures to whom are considered to be non-bank Mainland exposures	2,221	–	2,221	–
	<u>3,239,037</u>	<u>1,981,831</u>	<u>5,220,868</u>	<u>1,000</u>

	31 December 2006			
	On-balance sheet exposure HK\$'000	Off-balance sheet exposure HK\$'000	Total HK\$'000	Individual impairment allowance HK\$'000
Types of counterparties				
Mainland entities	603,657	390,199	993,856	10,000
Companies and individuals outside Mainland where the credit is granted for use in Mainland	1,696,688	707,562	2,404,250	12,658
Other counterparties the exposures to whom are considered to be non-bank Mainland exposures	2,742	–	2,742	142
	<u>2,303,087</u>	<u>1,097,761</u>	<u>3,400,848</u>	<u>22,800</u>

10. LIQUIDITY RATIO

	2007 %	2006 %
Average liquidity ratio for the year	<u>55.82</u>	<u>55.65</u>

The average liquidity ratio is calculated as the ratio, expressed as a percentage, of the average of each calendar month's average ratio, as specified in the Fourth Schedule of the Banking Ordinance, with reference to the financial information of the Bank, Chong Hing Finance Limited, Liu Chong Hing Banking Corporation, Cayman, Right Way Investments Limited and Gallbraith Limited.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

11. CAPITAL CHARGE FOR CREDIT, MARKET AND OPERATIONAL RISKS

The capital requirements for each class of exposures are summarized below. This disclosure is made by multiplying the Group's risk-weighted amount derived from the relevant computation method by 8%, not the Group's actual regulatory capital.

(i) Capital charge for credit risk

	Capital requirement
	2007
	HK\$'000
Sovereign exposures	1,775
Public sector entity exposures	16,647
Bank exposures	502,133
Securities firm exposures	29,082
Corporate exposures	1,563,442
Cash items	8,308
Regulatory retail exposures	18,468
Residential mortgage loans	296,859
Other exposures which are not past due exposures	297,349
Past due exposures	40,780
Total capital charge for on-balance sheet exposures	<u>2,774,843</u>
Direct credit substitutes	41,339
Trade-related contingencies	8,710
Forward asset purchases	2,634
Other commitments	213,047
Exchange rate contracts	50
Interest rate contracts	122
Total capital charge for off-balance sheet exposures	<u>265,902</u>
Total capital charge for credit risk	<u><u>3,040,745</u></u>

11. CAPITAL CHARGE FOR CREDIT, MARKET AND OPERATIONAL RISKS - continued

(ii) Capital charge for market risk

The Group has an exemption from the calculation of market risk under section 22(1) of the Banking (Capital) Rules. However, the Group is required to provide details concerning market risk to the Hong Kong Monetary Authority annually based on the year-end position. The market risk capital charge set out below relates to net open positions of the Group's foreign exchange exposures as at 31 December 2007. There are no other market risk exposures as at that date.

	Capital charge
	2007
	HK\$'000
Foreign exchange exposures (including gold and options)	<u>781</u>
Capital charge for market risk	<u>781</u>

(iii) Capital charge for operational risk

	2007
	HK\$'000
Capital charge for operational risk	<u>174,595</u>

The Group uses the Basic Indicator Approach for calculating operational risk.

12. RISK MANAGEMENT

(i) Credit risk

(a) Credit risk exposures

Moody's Investors Service is the external credit assessment institution (the "ECAI") that the Group has used in relation to each class of exposures set out below. The process used to map ECAI issuer ratings to exposures booked in the banking book is a process as prescribed in Part 4 of the Banking (Capital) Rules.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

12. RISK MANAGEMENT - continued

(i) Credit risk - continued

(a) Credit risk exposures - continued

Class of exposures	2007							
	Total exposures HK\$'000	Exposures after recognised credit risk mitigation		Risk-weighted amounts		Total risk- weighted amounts HK\$'000	Total exposure covered by recognised collateral HK\$'000	Total exposure covered by recognised guarantees HK\$'000
		Rated HK\$'000	Unrated HK\$'000	Rated HK\$'000	Unrated HK\$'000			
A. On-balance Sheet								
1. Sovereign	3,685,859	3,685,859	-	22,189	-	22,189	-	-
2. Public sector entity	250,545	316,028	651,065	77,870	130,213	208,083	-	-
3. Bank	27,930,418	27,382,251	548,167	6,074,768	201,889	6,276,657	-	-
4. Securities firm	1,001,706	697,790	274,836	226,106	137,418	363,524	29,080	-
5. Corporate	22,033,348	2,336,292	18,821,264	721,755	18,821,264	19,543,019	875,793	554,366
6. Cash items	318,069	-	1,755,182	-	103,854	103,854	-	-
7. Regulatory retail	337,052	-	307,798	-	230,848	230,848	29,254	-
8. Residential mortgage loan	7,697,740	-	6,956,459	-	3,710,735	3,710,735	24,733	716,548
9. Other exposures which are not past due exposures	4,195,111	-	3,716,858	-	3,716,858	3,716,858	478,252	-
10. Past due exposures	502,047	-	502,047	-	509,746	509,746	472,481	5,093
B. Off-balance Sheet								
1. Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	3,628,307	67,000	3,561,307	32,000	3,289,625	3,321,625	173,418	52,000
2. OTC derivative transactions	<u>5,936</u>	<u>4,598</u>	<u>1,338</u>	<u>1,317</u>	<u>838</u>	<u>2,155</u>	<u>-</u>	<u>-</u>
Exposures deducted from Capital Base	<u>837,479</u>							

12. RISK MANAGEMENT - continued

(i) Credit risk - continued

(a) Credit risk exposures - continued

Properties and cash deposits are recognised collateral for past due exposures and other exposures respectively. Recognised guarantees are guarantees issued by banks and the Government of the HKSAR. The Group has also taken properties and listed shares as collateral pledged as security against loans totalling HK\$17,841,134,000 and HK\$1,597,705,000 respectively.

(b) Counter-party credit risk exposures

The Group enters into OTC derivative transactions, mainly exchange and interest rate contracts, for hedging customers' and own positions. The methodology used to assign internal capital and credit limits for counter-party credit exposures is based on Banking (Capital) Rules. Counter-parties of these OTC derivative transactions are reputable banks and security firms and collateral is not normally required.

The following table summarises the Group's credit exposures arising from OTC derivative transactions. There are no repo-style transactions or credit derivative contracts outstanding as at 31 December 2007.

	OTC derivative transactions 2007 HK\$'000
OTC derivative	
Gross total positive fair value	<u>60</u>
Credit equivalent amount	<u>5,936</u>
Risk weighted amounts	<u>2,155</u>

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

12. RISK MANAGEMENT - continued

(i) Credit risk - continued

(b) Counter-party credit risk exposures - continued

The breakdown of the credit equivalent amounts and the risk-weighted amount is summarised as follows:

	OTC derivative transactions 2007 HK\$'000
Notional amounts:	
- Banks	678,594
- Security firms	405,000
- Corporates	5,631
- Others	<u>22,234</u>
	<u>1,111,459</u>
Credit equivalent amounts:	
- Banks	3,698
- Security firms	1,900
- Corporates	116
- Others	<u>222</u>
	<u>5,936</u>
Risk-weighted amounts:	
- Banks	1,137
- Security firms	680
- Corporates	116
- Others	<u>222</u>
	<u>2,155</u>

12. RISK MANAGEMENT - continued**(i) Credit risk - continued****(c) Credit risk mitigation**

The Group generally accepts collateral pledged as security and financial guarantees to support loans and advances made to customers. However, on-balance sheet and off-balance sheet netting and credit derivative contracts are not used for credit risk mitigation purposes.

Main types of recognised collateral include cash deposits and properties, whereas main types of recognised guarantees include financial guarantees issued by banks and the Government of the HKSAR.

The Group only accepts collateral pledged as security:

- when it is readily realizable;
- when it has stable value that can be quantified or supported by valuation; and
- the title of which can be verified and legally assigned to the Group.

Loan to value (collateral value) ratios are prescribed by the Lending Policy of the Group for various types of loan. At loan inception and renewal, collateral to be pledged as security is valued by reference to its market value. Collateral is subject to re-valuation on a regular basis and at times of significant price fluctuations of the underlying assets. Physical custody of title documents such as title deeds of properties and deposit certificates of cash deposits are required to be placed with the Group. Completion of registration of charges on the collateral pledged as security with the relevant authorities is a condition precedent for granting secured loans.

(ii) Asset Securitisation

The Group uses the standardized (securitization) approach to calculate the credit risk for securitization exposures, and is an investing institution for all classes of exposures set out below.

Moody's Investors Services is the ECAI that the Group has used in relation to the rated securitization exposures set out below.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

12. RISK MANAGEMENT - continued

(ii) Asset Securitisation - continued

Securitization exposures	Outstanding amounts HK\$'000	THE GROUP 2007 Exposures deducted from its	
		Core Capital HK\$'000	Supplementary Capital HK\$'000
Traditional securitisations			
Structured Investment			
Vehicles	<u>198,586</u>	<u>99,293</u>	<u>99,293</u>

(iii) Equity exposures in banking book

The Group adopts a policy of holding equity securities for long-term investment purposes. Equity holdings taken for strategic reasons are primarily joint venture operations that complement directly the Group's banking and other financial services business.

Equity securities are accounted for as available for sale financial assets, the accounting policy of which is set out in note 4 to the financial statements on pages 47 to 58. At the balance sheet date, listed equity securities are stated at fair value which is determined by reference to prices quoted in the respective stock markets. Unlisted equity securities are valued at cost, as adjusted to reflect earning multiples for comparable listed companies if the investee companies are performing at or above expectation. When deemed necessary, equity securities are carried at written down value to reflect the impairment in value of those investee companies.

	2007 HK\$'000
Net realised gains from sales/liquidations	<u>177,351</u>
Net unrealised revaluation gains:	
- Amount included in reserves but not through income statement	<u>138,680</u>
- Amount included in supplementary capital	<u>9,914</u>

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2007

12. RISK MANAGEMENT - continued

(iv) Interest rate exposures in banking book

Note 7 to the financial statements on pages 86 to 90 sets out the nature and the frequency of measurement of the interest rate risk. In measuring the interest rate exposures, the Group assumes that past contractual re-pricing behaviour will continue in the same manner over the next 12 months.

Variations in earnings for significant upward and downward interest rate movements in accordance with the method the Group uses for stress-testing, broken down by major currencies are set out below:

	2007			Total
	HK\$	US\$	Others	
Interest rate risk shock				
Equivalents in thousands of HK\$				
- Variations in earnings				
(+100 basis points)	<u>59,770</u>	<u>(13,221)</u>	<u>(579)</u>	<u>45,970</u>
- Variations in earnings				
(-100 basis points)	<u>(59,770)</u>	<u>13,221</u>	<u>579</u>	<u>(45,970)</u>

13. BASIS OF CONSOLIDATION

The consolidated financial statements covers the consolidated financial information of the Bank and all its subsidiaries and included the attributable share of interest in the Group's jointly controlled entities.

In preparing the capital adequacy ratio and liquidity ratio of the Group, they are prepared according to the basis of consolidation for regulatory purposes. The main difference between the consolidation basis for accounting and regulatory purposes is that the former includes the Bank, all its subsidiaries and the attributable share of interests in the Group's jointly controlled entities whereas the latter includes the Bank and only some of the Group's subsidiaries which mainly conduct banking business or other businesses incidental to banking business.

HEAD OFFICE, BRANCHES, PRINCIPAL SUBSIDIARIES AND AFFILIATES

as at 5 March 2008

		Telephone
HEAD OFFICE	24 Des Voeux Road Central, Hong Kong	3768 1111
HONG KONG ISLAND BRANCHES		
Aberdeen	166-168 Aberdeen Main Road	2553 9472
Causeway Bay	488 Jaffe Road	2893 6225
Happy Valley	1-9 Yuk Sau Street	2575 3201
North Point	376 King's Road	2570 0585
Sai Ying Pun	81-85 Des Voeux Road West	2547 6513
Shau Kei Wan	203-205 Shau Kei Wan Road	2560 6277
Sheung Wan	163 Wing Lok Street	2543 0653
Wan Chai	265-267 Hennessy Road	2511 3931
Wan Tsui Estate	Shop No. G11A, G/F, Wan Tsui Shopping Centre Wan Tsui Estate, Chai Wan	2976 0880
Western	347-349 Des Voeux Road West	2547 3809
KOWLOON BRANCHES		
Castle Peak Road	285-287 Castle Peak Road	2387 2421
Cho Yiu Chuen	G/F, Block C, King Cho Road	2742 2211
Ho Man Tin	Shop Nos. 7 & 8, G/F, Ho Man Tin Plaza 80 Fat Kwong Street, Ho Man Tin	2242 0681
Hoi Lai Estate	Shop No. 112, Hoi Lai Shopping Centre Hoi Lai Estate, Sham Shui Po	3514 6477
How Ming Street	114 How Ming Street	2342 6386
Jordan	G/F, 120 Woosung Street, Jordan	2735 8559
Kowloon Bay	Shop Unit 8, G/F, Chevalier Commercial Centre 8 Wang Hoi Road, Kowloon Bay	2750 8838
Kowloon City	31-33 Nga Tsin Wai Road	2382 7392
Kwong Tin Estate	No. 205, Shopping Centre, Kwong Tin Estate	2717 2414
Kwun Tong	31-33 Mut Wah Street	2342 7328
Lai Chi Kok Road	139 Lai Chi Kok Road	2391 1573
Lei Yue Mun	LG1, Lower Ground Floor, Lei Yue Mun Plaza, Yau Tong	2772 6320
Mongkok	591 Nathan Road	3768 0001
Po Tat Estate	Shop No. 203B-204, 2/F, Po Tat Shopping Centre Po Tat Estate, Kwun Tong	2190 4110
San Po Kong	55-57 Yin Hing Street	2325 5303
Sham Shui Po	144-148 Tai Po Road	2777 4441
Shun Lee Estate	Lee Yat House, Shun Lee Estate	2342 7141
Tak Tin Estate	No. 207, Shopping Centre, Tak Tin Estate	2775 1175
To Kwa Wan	34-34A Tam Kung Road	2711 4404
Tsim Sha Tsui	16 Granville Road	2369 4091
Tsz Wan Shan	60-64 Sheung Fung Street	2327 0913

HEAD OFFICE, BRANCHES, PRINCIPAL SUBSIDIARIES AND AFFILIATES

		Telephone
NEW TERRITORIES BRANCHES		
Butterfly Estate	Shop Nos. 131-134, Level 1, Tip Ling House Butterfly Shopping Centre, Butterfly Estate Tuen Mun	2463 9263
Cheung Fat Estate	Shop Nos. 304 & 311, Level 3 Cheung Fat Shopping Centre Cheung Fat Estate, Tsing Yi	2495 7697
Fanling	2 Wo Lung Street, Luen Wo Market, Fanling	2675 6203
Fu Tai Estate	Shop 101, Level 1, Fu Tai Shopping Centre Fu Tai Estate, Tuen Mun	2453 7630
Heng On Estate	Level 3, Commercial Centre, Heng On Estate Ma On Shan, Sha Tin	2641 1911
Kwai Chung Estate	Shop 111, Podium Level 1 Kwai Chung Shopping Centre Kwai Chung Estate, Kwai Chung	2279 4161
On Ting Estate	Shop No. 103, Level 1, Restaurant Block On Ting Shopping Centre, On Ting Estate Tuen Mun	2441 7117
Sheung Shui	71 San Fung Avenue, Sheung Shui	2670 6295
Sheung Tak Estate	Shop No. 237, Sheung Tak Shopping Centre Sheung Tak Estate, Tseung Kwan O	2178 1203
Tin Chak Estate	Shop 112, 1/F, Tin Chak Shopping Centre Tin Chak Estate, Tin Shui Wai	2486 3423
Tin Tsz Estate	Shop No. 110, 1/F, Tin Tsz Shopping Centre Tin Tsz Estate, Tin Shui Wai	2616 4618
Tsuen Wan	Jade Plaza, 298 Sha Tsui Road, Tsuen Wan	2408 7481
Tuen Mun Glorious Garden	Shop No. 82, Glorious Garden, 45 Lung Mun Road Tuen Mun	2453 0181
Wan Tau Tong Estate	Shop Nos. 11-12A, Wan Loi House Wan Tau Tong Estate, Tai Po	2656 4313
Yat Tung Estate	Shop Nos. 1 & 2, G/F, Yat Tung Shopping Centre Yat Tung Estate, Tung Chung	3141 7115
Yuen Long	99-109 Castle Peak Road, Yuen Long	2475 5307

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Telephone

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PRINCIPAL SUBSIDIARIES

Card Alliance Company Limited
Chong Hing Commodities and Futures Limited
Chong Hing Finance Limited
Chong Hing Information Technology Limited
Chong Hing Insurance Company Limited
Chong Hing (Nominees) Limited
Chong Hing Securities Limited
Gallbraith Limited
Liu Chong Hing Banking Corporation, Cayman

AFFILIATES

Liu Chong Hing Investment Limited
COSCO (Hong Kong) Group Limited
The Bank of Tokyo-Mitsubishi UFJ, Ltd