

2017 ANNUAL REPORT



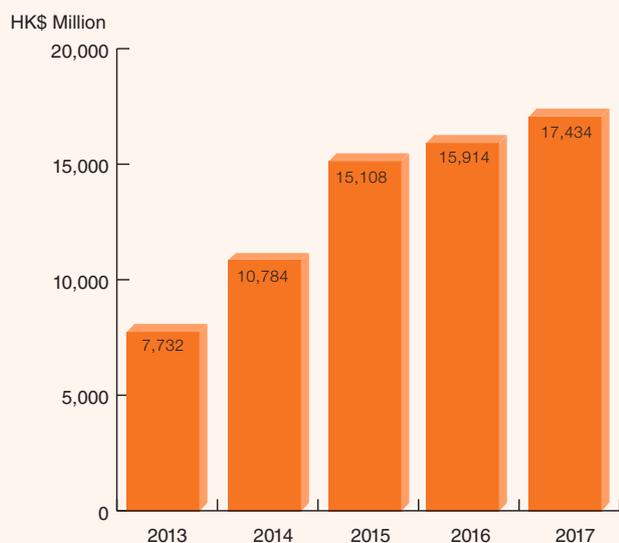
2	Five-year Financial Summary
3	Corporate Information
5	Biographical Details of Directors and Senior Management
13	Abridged Corporate Structure
14	Shareholders' Calendar
15	Chairman's Statement
18	Chief Executive's Statement
33	Directors' Report
45	Corporate Governance Report
65	Independent Auditor's Report
71	Financial Statements – Contents
73	Consolidated Income Statement
74	Consolidated Statement of Comprehensive Income
75	Consolidated Statement of Financial Position
76	Consolidated Statement of Changes in Equity
78	Consolidated Statement of Cash Flows
80	Notes to the Consolidated Financial Statements
210	Unaudited Supplementary Financial Information
232	Head Office, Branches, Sub-Branches, Representative Offices, Principal Subsidiaries and Associates

FIVE-YEAR FINANCIAL SUMMARY

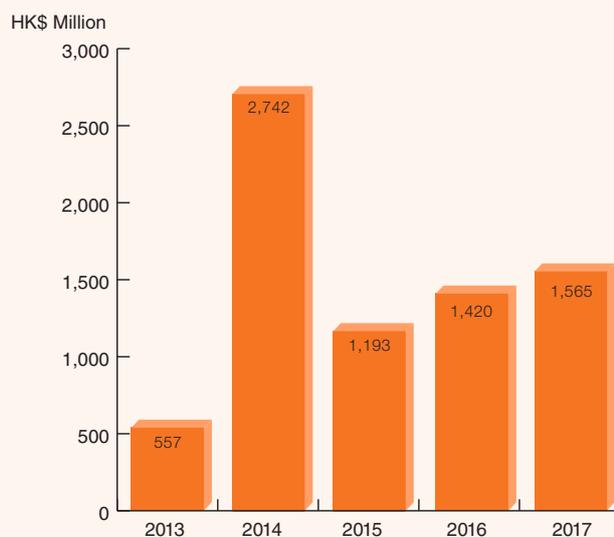
Total Advances To Customers / Total Customers' Deposits / Total Assets



Total Equity



Profit Attributable To Equity Owners



BOARD OF DIRECTORS**Executive Directors**

Mrs LEUNG Ko May Yee Margaret SBS, JP
(Deputy Chairman and Managing Director)
 Mr ZONG Jianxin
(Deputy Managing Director and Chief Executive)
 Mr LAU Wai Man *(Deputy Managing Director)*

Non-executive Directors

Mr ZHANG Zhaoxing *(Chairman)*
 Mr ZHU Chunxiu
 Mr WANG Shuhui
 Mr LI Feng
 Mr CHOW Cheuk Yu Alfred BBS, JP

Independent Non-executive Directors

Mr CHENG Yuk Wo
 Mr MA Chiu Cheung Andrew
 Mr LEE Ka Lun
 Mr YU Lup Fat Joseph

BOARD COMMITTEES**Audit Committee**

Mr CHENG Yuk Wo *(Chairman)*
 Mr WANG Shuhui
 Mr CHOW Cheuk Yu Alfred BBS, JP
 Mr LEE Ka Lun
 Mr YU Lup Fat Joseph

Connected Party Transactions Committee

Mr MA Chiu Cheung Andrew *(Chairman)*
 Mr CHOW Cheuk Yu Alfred BBS, JP
 Mr CHENG Yuk Wo
 Mr CHAN Kam Ki Vincent *(Chief Financial Officer)*
 Mr HSU Rockson *(Chief Risk Officer)*

Nomination Committee

Mr YU Lup Fat Joseph *(Chairman)*
 Mr ZHANG Zhaoxing
 Mr ZHU Chunxiu
 Mr CHENG Yuk Wo
 Mr MA Chiu Cheung Andrew

Remuneration Committee

Mr YU Lup Fat Joseph *(Chairman)*
 Mr ZHANG Zhaoxing
 Mr CHOW Cheuk Yu Alfred BBS, JP
 Mr MA Chiu Cheung Andrew
 Mr LEE Ka Lun

Risk Committee

Mr LEE Ka Lun *(Chairman)*
 Mr ZHU Chunxiu
 Mr LI Feng
 Mr CHENG Yuk Wo
 Mr YU Lup Fat Joseph

SENIOR MANAGEMENT

Mr FUNG Siu Ming *(Deputy Managing Director)*
 Mr CHAN Kam Ki Vincent *(Chief Financial Officer)*
 Mr HSU Rockson *(Chief Risk Officer)*
 Mr CHIU Tak Wah Edward *(Chief Operating Officer)*
 Mrs NG Yu Kam Ping Alice *(Head of Personal Banking)*
 Ms CHAN Yun Ling *(Head of Financial Markets)*
 Ms MA Yuen Lai Barbara *(Head of Hong Kong Corporates)*
 Mr SIN Tat Wo *(Head of China Corporates)*
 Ms CHAN Oi Hung Blanche *(Head of Human Resources)*
 Ms LAI Wing Nga *(Company Secretary)*

CORPORATE INFORMATION

as of 29 March 2018

REGISTERED OFFICE

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



Smartphone quick website access code

PRINCIPAL LEGAL ADVISERS

Deacons
Kwan & Chow
Mayer Brown JSM
Robertsons

AUDITOR

PricewaterhouseCoopers

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 (1) shares, (2) subordinated notes due 2020, (3) undated non-cumulative subordinated additional tier 1 capital securities and (4) tier 2 subordinated notes due 2027 are (1) 01111 (CHONG HING BANK), (2) 04327 (CH BANK N2011), (3) 05804 (CH BANK UCS) and (4) 05249 (CH BANK N2707) respectively.

BOARD OF DIRECTORS



Front (from left to right): LAU Wai Man, LEUNG Ko May Yee Margaret, ZHANG Zhaoxing, ZHU Chunxiu, ZONG Jianxin
Back (from left to right): LI Feng, MA Chiu Cheung Andrew, CHOW Cheuk Yu Alfred, YU Lup Fat Joseph, CHENG Yuk Wo, LEE Ka Lun, WANG Shuhui

Executive Directors

Mrs LEUNG Ko May Yee Margaret SBS, JP

aged 65, has been appointed an Executive Director, the Deputy Chairman and the Managing Director of the Bank since February 2014 and acted as the Chief Executive of the Bank from May 2016 to April 2017. Mrs Leung has been appointed an Executive Director, the Vice-chairman and the Chief Executive of Yuexiu Financial Holdings Limited (the immediate holding company of the Bank) ("Yuexiu Financial Holdings") since February 2014. She is also the Chairman of Chong Hing Finance Limited ("CH Finance"), a wholly-owned subsidiary of the Bank. Mrs Leung is an Independent Non-executive Director of each of First Pacific Company Limited (Stock Code: 00142), Li & Fung Limited (Stock Code: 00494), Sun Hung Kai Properties Limited (Stock Code: 00016) and Hong Kong Exchanges and Clearing Limited (Stock Code: 00388), all of which are companies listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). Mrs Leung was an Independent Non-executive Director of China Construction Bank Corporation, a company listed on the Stock Exchange (Stock Code: 00939), until June 2016, and was an Independent Non-executive Director of QBE Insurance Group Limited, a company listed on the Australian Securities Exchange (Stock Code: QBE), until March 2017. Mrs Leung is a council member, Treasurer, the Chairman of the Finance Committee, a member of the Human Resources Policy Committee and the Business School Board of Directors of The University of Hong Kong; a member of the Business School Advisory Board of The Hong Kong University of Science and Technology; a Steward of The Hong Kong Jockey Club; and a member of the National Committee of the Chinese People's Political Consultative Conference and the Guangzhou Municipal Committee of the Chinese People's Political Consultative Conference. She was a member of the Standing Committee of the Henan Provincial Committee of the Chinese People's Political Consultative Conference until January 2018. Prior to joining the Bank, Mrs Leung was the Vice Chairman and the Chief Executive of Hang Seng Bank Limited (Stock Code: 00011), and the Group General Manager of HSBC Holdings plc (Stock Code: 00005), both of which are companies listed on the Stock Exchange.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

as of 29 March 2018

Mr ZONG Jianxin

aged 51, has been appointed Deputy Managing Director and Head of China Business of the Bank since May 2015, an Executive Director of the Bank since September 2015 and the Chief Executive of the Bank since April 2017. He acted as Alternate Chief Executive of the Bank from May 2016 to April 2017. Mr Zong has been an Executive Director and Alternate Chief Executive of Yuexiu Financial Holdings since November 2015 and June 2016 respectively. He has been a Director and the Chief Executive of CH Finance since August 2017. Mr Zong has more than 20 years of banking experience, specialising in corporate banking, international business and investment banking business. He was an Executive Director and Alternate Chief Executive of Industrial and Commercial Bank of China (Asia) Limited (“ICBC Asia”) from October 2010 to May 2015, and was also a Director of various subsidiaries of ICBC Asia from December 2010 to May 2015. Mr Zong held various positions in Industrial and Commercial Bank of China Limited, Shenzhen Branch from October 1999 to December 2009, with his last position as the Vice President of the Branch from June 2006 to December 2009. Mr Zong holds a Master Degree in Business Administration awarded by Shanghai Jiao Tong University.

Mr LAU Wai Man

aged 59, has been appointed an Executive Director of the Bank since August 2001 and was appointed as Deputy Managing Director and re-designated as Alternate Chief Executive of the Bank in May 2016. He has been an Executive Director and Alternate Chief Executive of Yuexiu Financial Holdings since February 2014. He is also a Director of all the subsidiaries of the Bank. Mr Lau holds a Bachelor of Law degree and a Master of Business Administration degree. He is a Vice President of the Council of the Hong Kong Institute of Bankers, a Certified Financial Planner^{CM} and a member of the Hong Kong Institute of Certified Public Accountants. He was a fellow of the Association of Chartered Certified Accountants and a senior associate of the Australian Institute of Bankers. Mr Lau joined the Bank as the Chief Auditor in 1988, and was Deputy Chief Executive Officer from July 2007 to March 2013 and Chief Executive Officer from March 2013 to May 2016. Before joining the Bank, he had worked for an international bank and a global accounting firm.

Non-executive Directors

Mr ZHANG Zhaoxing

aged 54, has been appointed the Chairman and a Non-executive Director of the Bank since February 2014. Mr Zhang is the Chairman of Guangzhou Yue Xiu Holdings Limited (“GZYX Holdings”), Yue Xiu Enterprises (Holdings) Limited (“YX Enterprises”) and Yuexiu Financial Holdings. He is also an Executive Director and the Chairman of Yuexiu Property Company Limited (“Yuexiu Property”) (Stock Code: 00123), a company listed on the Stock Exchange. Mr Zhang holds an Executive Master of Business Administration degree awarded by Huazhong University of Science and Technology and possesses the qualification of senior accountant in China. He has extensive experience in the financial management, industrial operation, capital operation and corporate culture development of large enterprises. Prior to joining YX Enterprises in 2008, Mr Zhang was the Director and General Manager of Guangzhou Radio Group Co., Ltd., Chairman and General Manager of Haihua Electronics Enterprise (China) Corporation, Chairman of Guangzhou Guangdian Real Estate Development Co., Ltd. and a Director of GRG Banking Equipment Co., Ltd. (Stock Code: 002152), a company listed on the Shenzhen Stock Exchange. He was also the Chairman and an Executive Director of Yuexiu Transport Infrastructure Limited (“Yuexiu Transport”) (Stock Code: 01052), a company listed on the Stock Exchange, from July 2008 to March 2014 and General Manager of Yuexiu Property from July 2008 to March 2014. Mr Zhang is a deputy to the 12th National People’s Congress of the People’s Republic of China.

Mr ZHU Chunxiu

aged 55, has been appointed a Non-executive Director of the Bank since February 2014. Mr Zhu is the Vice-chairman and General Manager of GZYX Holdings and YX Enterprises, and is also a Non-executive Director of Yuexiu Financial Holdings. He is the Chairman and an Executive Director of Yuexiu Transport (Stock Code: 01052) and the Vice-chairman and an Executive Director of Yuexiu Property (Stock Code: 00123), both of which are listed on the Stock Exchange. Mr Zhu was a Director of Guangzhou Rural Commercial Bank (formerly known as Guangzhou Rural Credit Union). Prior to joining YX Enterprises in 2013, Mr Zhu was the Vice-chairman and General Manager of Guangzhou Finance Holdings Group Co., Ltd. (formerly known as Guangzhou International Holding Group Co., Ltd.). Mr Zhu was awarded the Degree in Executive Master of Business Administration by Sun Yat-Sen University, and holds the economist qualification in China. Mr Zhu has extensive experience in the operation and management of large financial institutions and banks. He is a deputy to the 14th and 15th sessions of the Guangzhou City People's Congress.

Mr WANG Shuhui

aged 46, has been appointed a Non-executive Director of the Bank since February 2014. He is a Non-executive Director of Yuexiu Financial Holdings, and a Director of Guangzhou Yuexiu Financial Holdings Group Co., Ltd. ("GZYX Financial Holdings") (formerly known as Guangzhou Friendship Group Co., Ltd.), a company listed on the Shenzhen Stock Exchange (Stock Code: 000987). Mr Wang was an Executive Director of Yuexiu Transport, a company listed on the Stock Exchange (Stock Code: 01052), from November 2009 to March 2014, and was a Director and a Deputy General Manager of GZYX Holdings and YX Enterprises. Mr Wang graduated from the School of Finance of the Southwestern University of Finance and Economics and holds a Master degree in Monetary Economics and Banking and an economist qualification from Jinan University. Before joining YX Enterprises in May 2006, Mr Wang had over 13 years of experience in Guangzhou Securities Co., Ltd. and had held various senior management positions (including the Project Manager of the Securities Issuance Consultancy Department, Manager of the Research and Development Department, Director of the Office of the CEO, General Manager of the Human Resource Department and the Assistant to the CEO, Board Secretary, Vice President) within the company. Mr Wang has solid knowledge and extensive professional experiences in financial industry and is familiar with the practice in the financial markets of Mainland China and the practice of listed company business operation.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

as of 29 March 2018

Mr LI Feng

aged 49, has been appointed a Non-executive Director of the Bank since February 2014. Mr Li is the Chief Capital Officer of GZYZ Holdings and YX Enterprises, managing the Capital Department, Customer Resource Management and Synergy Department and Information Centre of GZYZ Holdings and YX Enterprises, mainly responsible for formulating and implementing major capital management plans, organizing and coordinating the investor relationship of listed companies, optimizing and upgrading the customer resource management and synergy, and facilitating and enhancing the development of information technology, etc. Mr Li is also a Director of Guangzhou City Construction & Development Co., Ltd. He is an Executive Director of Yuexiu Property (Stock Code: 00123), a company listed on the Stock Exchange; a Non-executive Director of Yuexiu REIT Asset Management Limited (the Manager of Yuexiu Real Estate Investment Trust (Stock Code: 00405), which is listed on the Stock Exchange); and a Director of GZYZ Financial Holdings (formerly known as GuangZhou Friendship Group Co., Ltd.), a company listed on the Shenzhen Stock Exchange (Stock Code: 000987). Mr Li graduated from the Faculty of Naval Architecture and Ocean Engineering of South China University of Technology majoring in Naval Architecture, and obtained a Master of Business Administration degree from Jinan University. He holds the qualification of a Senior Engineer in China and the certificate in Major Administrative Decision-Making and Argumentation (廣州市重大行政決策論證專家) conferred by the Guangzhou Municipal Government. Mr Li joined YX Enterprises in December 2001 and has successively held positions in GZYZ Holdings and YX Enterprises, including the Assistant to General Manager, Assistant Manager of Corporate Management Department, Assistant to General Manager of Supervision and Auditing Department, Deputy General Manager of Capital Department, and Deputy General Manager of Yue Xiu International Development Limited. Mr Li is familiar with business of listed companies and the operations of capital markets. Since 2008, he has participated in all of the major capital operation projects of GZYZ Holdings and YX Enterprises; before that, he was also involved in the successful listing of Yuexiu Real Estate Investment Trust, and has extensive practical experience in capital operations.

Mr CHOW Cheuk Yu Alfred BBS, JP

aged 67, has been a Board member of the Bank since February 2003, and was re-designated from Independent Non-executive Director to Non-executive Director of the Bank in September 2004. Mr Chow has been a Non-executive Director of Yuexiu Financial Holdings since February 2014. He is also the Chairman and a Non-executive Director of Chong Hing Insurance Company Limited ("CH Insurance"), a wholly-owned subsidiary of the Bank. 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 30 years as a solicitor, Mr Chow is presently the senior partner of Kwan & Chow, Solicitors in Hong Kong. He is also a China-Appointed Attesting Officer. Mr Chow is a director and legal advisor of Hong Kong Chiu Chow Chamber of Commerce Limited and Federation of HK Chiu Chow Community Organizations Limited; and legal advisor to Jao Tsung-I Petite Ecole Fan Club and various community bodies. He was the Chairman of the HKSAR Passports Appeal Board and Chief Adjudicator of the Registration of Persons Tribunal, and currently serves on other statutory boards.

Independent Non-executive Directors

Mr CHENG Yuk Wo

aged 57, has been appointed an Independent Non-executive Director of the Bank since September 2004. He has also been an Independent Non-executive Director of Yuexiu Financial Holdings since February 2014. He has been an Independent Non-executive Director of CH Insurance since May 2017. 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 Professional Accountants of Canada. Mr Cheng has more than 30 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.

In addition to his directorship in the Bank, Mr Cheng is also an Independent Non-executive Director of a number of companies listed on the Stock Exchange, including CSI Properties Limited (Stock Code: 00497), HKC (Holdings) Limited (Stock Code: 00190), C.P. Lotus Corporation (Stock Code: 00121), Goldbond Group Holdings Limited (Stock Code: 00172), CPMC Holdings Limited (Stock Code: 00906), Top Spring International Holdings Limited (Stock Code: 03688), Liu Chong Hing Investment Limited (Stock Code: 00194), Chia Tai Enterprises International Limited (Stock Code: 03839), DTXS Silk Road Investment Holdings Company Limited (formerly known as UDL Holdings Limited) (Stock Code: 00620), Miricor Enterprises Holdings Limited (Stock Code: 08358), Somerley Capital Holdings Limited (Stock Code: 08439) and Kidsland International Holdings Limited (Stock Code: 02122). Besides, Mr Cheng was an Independent Non-executive Director of Imagi International Holdings Limited (Stock Code: 00585), a company listed on the Stock Exchange, from July 2010 to January 2016.

Mr MA Chiu Cheung Andrew

aged 76, has been appointed an Independent Non-executive Director of the Bank since August 2007. He has also been an Independent Non-executive Director of Yuexiu Financial Holdings since February 2014. He has been an Independent Non-executive Director of CH Insurance since January 2018. Mr Ma is a founder and former director of AMA CPA Limited (formerly known as Andrew Ma DFK (CPA) Limited). He is presently a Director of Mayee Management Limited and also a Director of several other private companies. Mr Ma has more than 40 years' experience in the fields of accounting, auditing 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 and Wales, the Hong Kong Institute of Certified Public Accountants, The Hong Kong Institute of Directors and The Taxation Institute of Hong Kong.

In addition to his directorship in the Bank, Mr Ma is also an Independent Non-executive Director of a number of companies listed on the Stock Exchange, including Asia Financial Holdings Limited (Stock Code: 00662), China Resources Power Holdings Company Limited (Stock Code: 00836), C.P. Pokphand Co. Ltd. (Stock Code: 00043), Asiaray Media Group Limited (Stock Code: 01993) and C-MER Eye Care Holdings Limited (Stock Code: 03309). Mr Ma was an Independent Non-executive Director of Southwest Securities International Securities Limited (formerly known as Tanrich Financial Holdings Limited) (Stock Code: 00812), a company listed on the Stock Exchange, from April 2005 to January 2015.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

as of 29 March 2018

Mr LEE Ka Lun

aged 63, has been appointed an Independent Non-executive Director of the Bank since February 2014. Mr Lee has been an Independent Non-executive Director of Yuexiu Financial Holdings since November 2013. He is also an Independent Non-executive Director of Yuexiu Property (Stock Code: 00123), Chow Sang Sang Holdings International Limited (Stock Code: 00116), REXLot Holdings Limited (Stock Code: 00555), Medicskin Holdings Limited (Stock Code: 08307) and Ever Harvest Group Holdings Limited (Stock Code: 01549), all of which are listed on the Stock Exchange. Mr Lee is an accountant by profession and is a Fellow of the Association of Chartered Certified Accountants in the UK. He has over 20 years of experience in banking and auditing.

Mr YU Lup Fat Joseph

aged 70, has been appointed an Independent Non-executive Director of the Bank since August 2015. Mr Yu has been an Independent Non-executive Director of Yuexiu Financial Holdings since August 2015. He is also an Independent Non-executive Director of Yuexiu Property (Stock Code: 00123), a company listed on the Stock Exchange. Mr Yu holds a Master Degree in Applied Finance from Macquarie University in Australia, a Diploma of Management Studies from The University of Hong Kong and a Diploma from the Association of International Bond Dealers. Mr Yu was the Founding President of the Hong Kong Forex Club from 1974 to 1975. Mr Yu was also the Founding Deputy Chairman of the Hong Kong Capital Markets Association and Asia Chairman of the Association of International Bond Dealers. Mr Yu has held numerous senior managerial and advisory positions and has more than 40 years of experience in investment, banking and finance.

Note: The directorships held by the Directors in the subsidiaries of the Bank (where applicable) are set out in the “List of names of the directors of Chong Hing Bank Limited and its subsidiaries” posted on the Bank’s website (www.chbank.com/en/about-ch-bank/investor-relations/directors-list/index.shtml).

SENIOR MANAGEMENT

Mr FUNG Siu Ming

aged 65, has been appointed Deputy Managing Director of the Bank since September 2017 and an Alternate Chief Executive of the Bank since December 2017. He has been an Alternate Chief Executive of Yuexiu Financial Holdings and CH Finance since December 2017 and February 2018 respectively. Prior to joining the Bank, Mr Fung was the Executive Director, Alternate Chief Executive and Chief Risk Officer of the Hong Kong subsidiary of a large-size China banking group until his retirement in April 2014, and served as an advisor of that Banking Group from September 2014 to September 2017 and the Compliance Officer of the Hong Kong Branch of the same Group from April 2015 to September 2017. Except for a brief period, Mr Fung had been a Non-executive Director of a China-incorporated bank of the same Group operating in Shenzhen since October 2011 until September 2017. Mr Fung holds a Bachelor's Degree in Social Sciences from The University of Hong Kong. He has more than 40 years of local banking experience specialised in bank lending and credit risk management.

Mr CHAN Kam Ki Vincent

aged 55, General Manager, has been appointed Chief Financial Officer of the Bank since April 2017. Mr Chan graduated from The Chinese University of Hong Kong and obtained a Master Degree in Applied Finance from Macquarie University, Australia. He is a fellow of the Hong Kong Institute of Certified Public Accountants and a member of the Institute's Banking Regulatory Advisory Panel, a member of the American Institute of Certified Public Accountants, a designation holder of the Chartered Institute of Management Accountants and a Certified Internal Auditor of The Institute of Internal Auditors. Mr Chan has more than 30 years of auditing and financial controllership experience in the financial services industry. He worked for an international accounting firm and held regional roles in major cities of several international banks and senior positions in regional and local banks prior to joining the Bank.

Mr HSU Rockson

aged 48, General Manager, has been appointed Chief Risk Officer of the Bank since September 2015. Mr Hsu has more than 25 years of risk management experience in foreign and local banks and possesses sound knowledge in credit risk management in China and various business segments. Prior to joining the Bank, he was Deputy Risk Officer of a local bank. Mr Hsu graduated from New York University, USA and obtained a Bachelor of Science degree in Finance and International Business.

Mr CHIU Tak Wah Edward

aged 55, General Manager, has been appointed Chief Operating Officer of the Bank since May 2017. He is also a Director of various subsidiaries of the Bank. He graduated from Kings College London, University of London, and obtained a Master (Econ) degree from London School of Economics and Political Science, University of London. Mr Chiu has more than 28 years' experience in banking, financial services and management consultancy in the Asia Pacific region, Europe and China while working for several leading financial institutions. Prior to joining the Bank, he was a General Manager, Head of Operations of a leading Chinese bank, and held different senior positions in major financial institutions.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

as of 29 March 2018

Mrs NG Yu Kam Ping Alice

aged 57, General Manager and Head of Personal Banking. She is also a Director of Card Alliance Company Limited, a wholly-owned subsidiary of the Bank. She holds a Master Degree of Business and Administration from the University of Adelaide, Australia. Mrs Ng is also a Certified Financial Planner (CFP^{CM}), Associate of the Institute of Financial Services, United Kingdom (Aifs) and Associate of the Hong Kong Institute of Bankers (AHKIBTM). She possesses more than 30 years of experience in retail banking, and has held different senior positions with major international banks in managing retail and private banking teams. Mrs Ng has specialty in wealth management business development and has rich experience in operation control, quality assurance, cost control and project management. Mrs Ng joined the Bank in August 2014.

Ms CHAN Yun Ling

aged 51, General Manager and Head of Financial Markets since April 2015. She holds a Bachelor of Arts degree from The Chinese University of Hong Kong, and had pursued studies in France and the UK. With specialty in financial markets business, Ms Chan has worked in major financial hubs including Hong Kong, Tokyo, Singapore, Shanghai and Taiwan, in charge of financial markets related activities in various financial institutions.

Ms MA Yuen Lai Barbara

aged 51, General Manager, joined the Bank in March 2017 as Deputy Head of Hong Kong Corporates and has been appointed Head of Hong Kong Corporates since March 2018. Ms Ma has more than 25 years of experience in corporate banking with UK, US and local financial institutions and has worked in London, New York and Hong Kong. Over her career, she has possessed experience in managing a broad spectrum of clients from a wide range of industries. Ms Ma obtained a Bachelor of Science (Economics) degree in International Relations from The London School of Economics and Political Science.

Mr SIN Tat Wo

aged 48, General Manager and Head of China Corporates. Mr Sin graduated from Hong Kong Baptist University with Bachelor Degree in Business Administration. He has more than 20 years of experience in the banking industry in Hong Kong and China. He worked for a number of major Chinese Banks in their corporate, commercial and investment banking departments. Mr Sin joined the Bank in December 2015.

Ms CHAN Oi Hung Blanche

aged 53, General Manager and Head of Human Resources. Ms Chan is a seasoned human resources practitioner with over 25 years of experience and held senior and head positions with international, regional and local banks in Hong Kong. Ms Chan received a Bachelor of Social Sciences degree in Economics from The University of Hong Kong and a MBA degree from The Chinese University of Hong Kong. Ms Chan joined the Bank in July 2016.

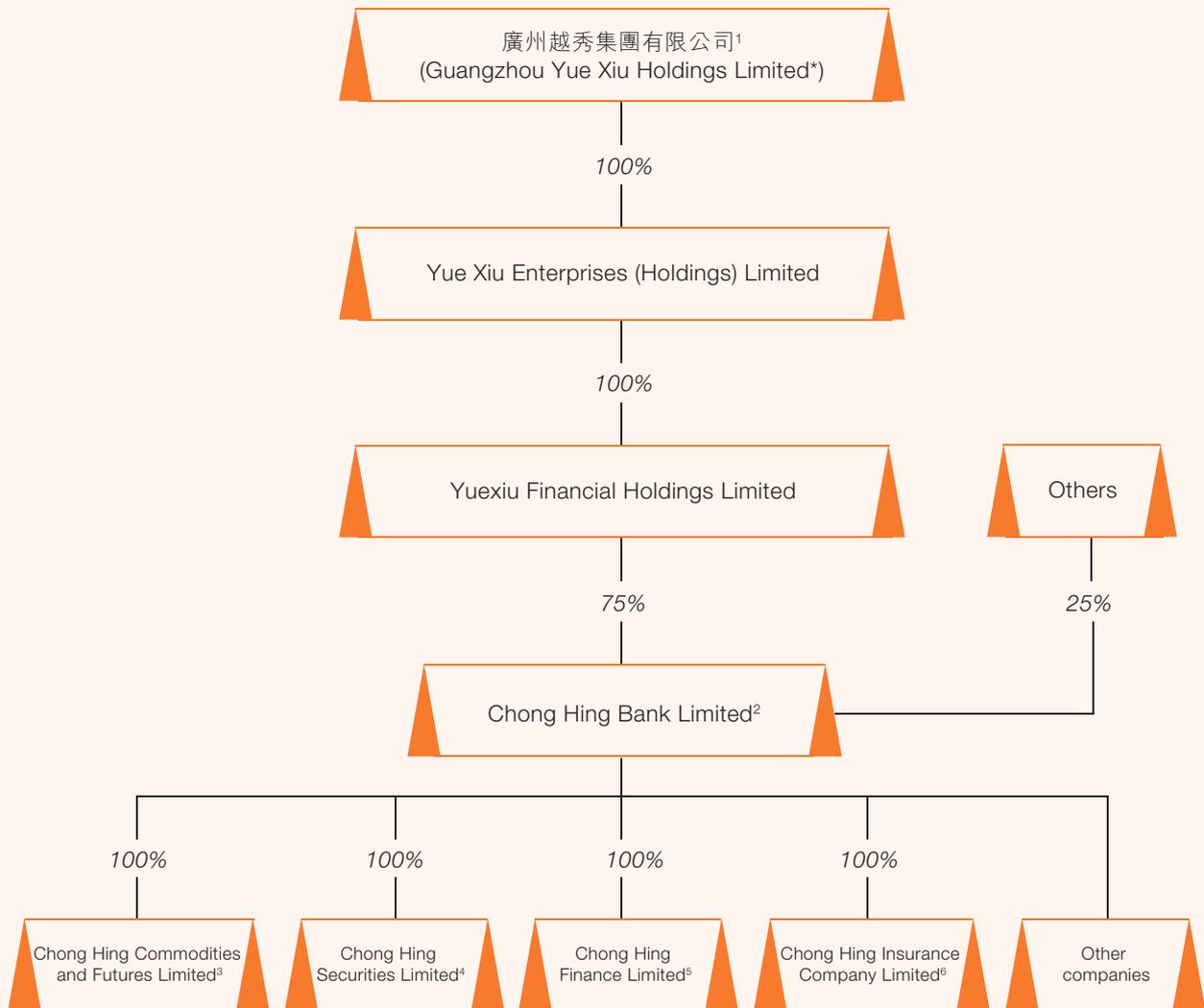
Ms LAI Wing Nga

aged 53, General Manager, has been appointed Company Secretary of the Bank since August 2015. Ms Lai has had over 25 years of working experience in the corporate secretarial and governance areas of sizable listed companies and financial institutions. Prior to joining the Bank, Ms Lai was the company secretary of AIA Group Limited from April 2010 to July 2015, which is a company listed on the Stock Exchange (Stock Code: 01299). She was the company secretary of Standard Chartered Bank (Hong Kong) Limited from April 2005 to March 2010 and before that was the company secretary of Industrial and Commercial Bank of China (Asia) Limited from April 2000 to April 2005. Ms Lai obtained a master of business degree from The University of Newcastle in Australia. She also obtained a postgraduate diploma in corporate finance from The Hong Kong Polytechnic University. Ms Lai is a fellow of the Hong Kong Institute of Chartered Secretaries and the Institute of Chartered Secretaries and Administrators in the UK.

Note: The directorships held by the Senior Management in the subsidiaries of the Bank (where applicable) are set out in the "List of names of the directors of Chong Hing Bank Limited and its subsidiaries" posted on the Bank's website (www.chbank.com/en/about-ch-bank/investor-relations/directors-list/index.shtml).

ABRIDGED CORPORATE STRUCTURE

as of 29 March 2018



¹ Wholly state-owned enterprise under the supervision of the State-owned Assets Supervision and Administration Commission of the Guangzhou Municipal People's Government

² Listed on The Stock Exchange of Hong Kong Limited

³ Registered with The Hong Kong Futures Exchange Limited as a participant

⁴ Registered with The Stock Exchange of Hong Kong Limited as a participant

⁵ Licensed under the Hong Kong Banking Ordinance as a deposit-taking company

⁶ Licensed under the Insurance Ordinance as an insurance company

* for identification purpose only

SHAREHOLDERS' CALENDAR

as of 29 March 2018

25 August 2017	Interim results for the first half of 2017 announced
<hr/>	
25 September 2017	Interim cash dividend for 2017 of HK\$0.15 per share paid
<hr/>	
29 March 2018	Final results for the year of 2017 announced
<hr/>	
14 to 17 May 2018 (both days inclusive)	Register of Members will be closed for the purpose of ascertaining entitlements to attend and vote at the 2018 Annual General Meeting
<hr/>	
18 May 2018	2018 Annual General Meeting will be held
<hr/>	
25 to 29 May 2018 (both days inclusive)	Register of Members will be closed for the purpose of ascertaining entitlements to receive the final cash dividend for 2017
<hr/>	
5 June 2018	If approved by Shareholders at the 2018 Annual General Meeting, the final cash dividend for 2017 of HK\$0.39 per share will be payable to Shareholders whose names appear on the Register of Members of the Bank on 29 May 2018
<hr/>	



Mr Zhang Zhaoxing

Chairman

In line with its core values of “Exceed Excel”, Chong Hing Bank continued to implement its various optimisation reforms during the year as part of its five-year strategic plan to improve quality and enhance efficiency with the aim of building a solid foundation for the Bank’s long-term development. Chong Hing Bank is seeking to further expand its business scope and raise its service quality so as to take advantage of new opportunities presented in the development of both Guangdong and Hong Kong. With the corporate vision of becoming “an integrated commercial bank with cross-border expertise” in sight, the Bank endeavours to become a century-old brand in the minds of people in Hong Kong.

I am pleased to announce that, in 2017, Chong Hing Bank’s core business lines and overall financial health remained strong, asset quality was sound and profitability from core business had increased. Operating profit after impairment allowances amounted to HK\$983 million. Profit attributable to equity owners amounted to HK\$1,565 million, an improvement of 10.2% from last year, and earnings per share was HK\$2.17 (2016: HK\$1.94 per share). The Board has considered that it is prudent to preserve the Bank’s capital so as to better satisfy the new requirement under “Basel III”. Hence, the Board has recommended the payment of the final cash dividend of HK\$0.39 per share for the year. The total dividend payout for the year as a percentage of this adjusted profit attributable to equity owners less distribution paid on the additional equity instruments will be 38.46% (2016: 35.06%).

The major financial ratios for 2017 are as follows:

- Return on shareholders' equity: 9.89%
- Average liquidity maintenance ratio: 40.73%
- Total capital ratio: 17.60% as of 31 December 2017
- Tier 1 capital ratio: 13.30% as of 31 December 2017
- Loan to deposit ratio: 70.85% as of 31 December 2017

China's "13th Five-Year Plan" further strengthens Hong Kong's role as a global offshore Renminbi business hub and international asset management centre. Driven by innovation as an important pillar of the industry's development strategy, finance and technology will be more interrelated and the fusion between them will be the focus of future financial services in the long run. Chong Hing Bank keeps pace with the times by devoting resources to build a dedicated digital transformation team and upgrade its electronic platforms, as well as participate in various digital and innovative projects. At the same time, by developing financial technology to enhance customer experience, the Bank stands ready for further business development and transformation.

China's economic growth is on a steady track with a year-on-year GDP growth of 6.9%, marking a new benchmark of RMB80 trillion in 2017. Guangzhou is among the top cities in China's provincial development in terms of GDP, and the financial industry is one of Guangzhou's ten pillar industries. In 2017, the Fortune Global Forum was held in Guangzhou, where Fortune 500 companies, multinational corporations, governmental bodies and social celebrities congregated and exchanged views on the structural formulation of the new global economy. The event focused the world's attention on Guangzhou and helped promote innovation and development in the city.

As a core member of the financial sector of the Guangzhou-based Yuexiu Group, Chong Hing Bank has continued to take advantage of the Yuexiu Group's resources in establishing the strategic position of the Guangzhou Branch to oversee its branch network in Mainland China. It also sought to deepen the regional synergies between Guangdong and Hong Kong, as well as expand its Mainland operations to attract high-quality Mainland customers, thereby establishing its unique role in the Pearl River Delta region. With new business opportunities associated with China's Belt and Road Initiative, the Framework Agreement on Deepening Guangdong-Hong Kong-Macao Cooperation in the Development of the Bay Area and the free trade zones in Guangdong, the financial cooperation between Guangdong, Hong Kong and Macau will be strengthened further. Leveraging its advantageous positions in Guangdong and Hong Kong as well as its comprehensive integrated financial services system, Chong Hing Bank will be able to cater to the financial services needs on both sides and better capture cross-border business opportunities following on from the national policies. The Bank will continue to take a prudent and proactive approach towards achieving the vision of becoming "an integrated commercial bank with cross-border expertise".

In 2017, Chong Hing Bank established a customised corporate culture accountability structure and philosophy in line with the “Bank Culture Reform” guidelines issued by the Hong Kong Monetary Authority, bearing in mind the banking industry’s specifics and the Bank’s strategic proposition. The concept of Core Values, Vision and Mission determines Chong Hing Bank’s value orientation and strategic objectives, while the Management Concepts, Enterprise Spirit and Corporate Style of the Bank make up the underlying concept of its corporate culture and formulate the basis for its code of conduct. Chong Hing Bank is committed to implementing its philosophy in its business operation and management, and will endeavour to consolidate its team through high-quality corporate culture, so that it may work together as one to expand its business further.

There are quite a few challenges that Chong Hing Bank has to overcome while facing the fast-changing business environment. I would like to express my gratitude to all the Directors for their valuable guidance and advice on the Bank’s sustainable growth; and, on behalf of the Board, I would also like to convey my sincere appreciation to our shareholders, customers and business partners for their long-term support and trust. Finally, I sincerely appreciate the Bank’s management team and staff members of all levels for their continuous collaborations and persistent dedication, which is instrumental in moving Chong Hing Bank forward on its path of pursuing excellence.

Zhang Zhaoxing

Chairman

Hong Kong, 29 March 2018



Mr Zong Jianxin

Chief Executive

GLOBAL ECONOMY

In 2017, the global economy experienced a steady recovery. With continuous economic expansion, and driven by the growth in consumer spending, business investment and exports, the US gross domestic product (GDP) recorded a year-on-year increase of 2.3%. The US Federal Reserve Board (FRB) announced its plan of balance sheet reduction in September, marking a step forward in the normalisation of monetary policy. Concurrently, the FRB announced its third rate hike for 2017 at the rate-fixing meeting held in December. This was the fifth rate hike since the start of the new round of the US-initiated rate hike cycle in December 2015. Furthermore, the US Congress passed the first massive tax reform bill in thirty years, slashing the top corporate tax rate from 35% to 21%. This move may have an impact on global capital flows. Despite the economic uncertainties brought on by the Brexit issue, the Eurozone maintained robust economic growth, with a 2.5% year-on-year increase of GDP for the year. The European Central Bank began a reduction in its monthly asset purchases at the beginning of 2018.

Asian economies delivered a strong performance throughout the year. The Japanese economy has also seen significant improvement. Nevertheless, as the Bank of Japan continued an accommodative monetary policy and maintained its deposit interest rate at -0.1%, it was expected that the pace of economic recovery would continue to be moderate. In China, the economy stabilised with an improved outlook, with an economic growth of 6.9% for the year due to higher corporate earnings and a further optimised economic structure. According to the report of the 19th National Congress of the Communist Party of China, China's economy has been transitioning from rapid growth to high-quality development. China is at a pivotal stage of transforming its growth model, improving its economic structure and fostering new drivers of growth. Core cities in the Pearl River Delta region achieved a satisfactory economic performance as a whole. Instilled with a new growth momentum and steady improvement in both quality and efficiency, Guangzhou recorded a year-on-year GDP growth of 7% for the year. Shenzhen recorded a year-on-year GDP growth of 8.8% for the year, with emerging industries maintaining sound growth. The People's Bank of China implemented a steady, neutral monetary policy, which guided the "deleveraging" process in the banking system. The China Banking Regulatory Commission gradually introduced a series of guiding opinions for "strengthening regulation", "resolving chaos" and "preventing risks", aiming to enhance risk management in the financial system. The CNY/USD exchange rate resumed its uptrend in 2017, with the Renminbi onshore price (CNY) and offshore price (CNH) appreciating by a total of 6.71% and 6.53% respectively during the year, the highest increases since 2008.

Riding on the stable economic development in China and the favourable external economic environment, Hong Kong's economy is moving ahead strongly with a GDP growth of 3.8% in real terms for 2017. Benefiting from a broad-based upturn in the global economic and trading environment, Hong Kong's total exports and trade recorded increases of 8% and 8.4% respectively for the year. Under an accommodative monetary environment, major banks in Hong Kong did not follow the US rate hikes. The total money supply (M3) at the end of December increased by 10% as compared with the same period last year. With rising credit demand, total loans and advances from authorised institutions at the end of December achieved a year-on-year growth of 16.1%. During the year, the booming Hong Kong property market has contributed to a 21-month continuous growth in the private domestic housing price index as of December, the most persistent growth ever recorded. The number of property registrations in the entire market for the year increased by 14.8% to 83,815 as compared with the previous year, reaching a five-year high. Fuelled by a favourable global economy and capital inflows from China and foreign countries, the Hong Kong stock market surged for eight consecutive months from January 2017 and broke through the 30,000 mark in November, hitting a ten-year high. The Hang Seng Index ended the year at 29,919 points, with an accumulated increase of 36% for the year. The Shanghai-Hong Kong Stock Connect and the Shenzhen-Hong Kong Stock Connect also achieved record high turnovers.

CHIEF EXECUTIVE'S STATEMENT

RESULTS ANNOUNCEMENT AND PROFIT ANALYSIS

The results for the financial year of 2017 of the Bank, on a consolidated basis, are summarised below:

Key Financial Data	31 December (12 months)		Variance %
	2017 HK\$'000	2016 HK\$'000	
1. Operating profit after impairment allowances	983,413	1,475,871	-33.37
2. Profit attributable to equity owners	1,564,867	1,419,704	+10.22
3. Net interest income	2,317,128	2,044,800	+13.32
4. Net fee and commission income	327,471	259,584	+26.15
5. Net (loss) income from trading and investments	(93,938)	230,059	-140.83
6. Other operating income	158,895	139,853	+13.62
7. Operating expenses	1,353,633	1,227,552	+10.27
8. Net (charge) reversal of impairment allowances on loans and advances	(371,591)	40,198	-1,024.40
	As of 31 December 2017 HK\$'000	As of 31 December 2016 HK\$'000	Variance %
9. Total loans and advances to customers	86,698,372	70,689,155	+22.65
10. Total customer deposits	118,758,674	102,880,629	+15.43
11. Investments in securities	39,153,501	29,727,952	+31.71
12. Total assets	163,747,114	137,772,051	+18.85

CHIEF EXECUTIVE'S STATEMENT

Key Financial Data	31 December (12 months)		Variance %
	2017 HK\$'000	2016 HK\$'000	
13. Return on shareholders' equity ⁽¹⁾	9.89%	9.61%	+0.28
14. Earnings per share ⁽²⁾	HK\$2.17	HK\$1.94	+11.86
15. Net interest margin	1.52%	1.66%	-0.14
16. Cost to income ratio	49.96%	45.90%	+4.06
17. Average liquidity maintenance ratio	40.73%	40.59%	+0.14
	As of 31 December 2017 HK\$'000	As of 31 December 2016 HK\$'000	Variance %
18. Impaired loan ratio	0.46%	0.07%	+0.39
19. Non-performing loan ratio	0.56%	0.64%	-0.08
20. Provision coverage of impaired loans and advances	181.87%	602.98%	-421.11
21. Loan to deposit ratio	70.85%	67.40%	+3.45
22. Net asset value per share (excluding additional equity instruments and before the final dividend)	HK\$23.18	HK\$20.85	+11.18
23. Total capital ratio	17.60%	16.32%	+1.28
24. Tier 1 capital ratio	13.30%	14.16%	-0.86
25. Common Equity Tier 1 capital ratio	11.30%	11.81%	-0.51

Notes:

- (1) Return on shareholders' equity took into consideration the coupon of the additional equity instruments relevant for the period.
- (2) Earnings per share was calculated after deducting the distribution paid on the additional equity instruments in the year.

CHIEF EXECUTIVE'S STATEMENT

ANALYSIS OF KEY FINANCIAL DATA

In 2017, profit attributable to equity owners of the Bank increased by 10.2% year-on-year to HK\$1,565 million.

Net interest income increased by 13.3% to HK\$2,317 million. The improvement in net interest income was achieved mainly through the growth of loans and advances and investment in debt securities. The increase in interest expenses was mainly attributable to the increase in deposits from customers. Net interest margin at 1.52% was 14 basis points less than the same period last year. After excluding penalty cost factor, year over year net interest margin dropped 7 basis points.

Net fee and commission income improved by 26.2% to HK\$327 million, which was mainly attributable to a 33.1% increase in commission income arising from securities dealings as the stock market turnover was much higher than the same period last year.

Net loss from trading and investments at HK\$94 million was due to the RMB appreciation resulting in a translation loss of HK\$195 million. The increase in net gains on disposal of the available-for-sale debt securities of HK\$97 million partly offset the RMB translation loss.

The Bank strived for operation enhancement and at the same time invested in talents and systems to support business growth and expansion into the Mainland.

To optimise the use of resources, certain assets that were not considered essential to the core business lines had been sold, and a net gain of HK\$657 million was recorded in 2017.

Total loans and advances to customers increased by HK\$16 billion to HK\$86.7 billion, with noticeable growth in term loans and syndication loans. With careful management on the exposure of credit risk, asset quality of loans and advances continued to be good with impaired loan ratio at 0.46%, non-performing loan ratio at 0.56% and provision coverage of impaired loans and advances at 182%.

Total customer deposits increased by 15.4% to HK\$118.8 billion. The Bank continued to maintain a stable deposit base, allowing the Bank to balance loan growth and investment in debt securities, as well as wealth management and cross-border financial business needs.

Total assets increased by 18.9% to HK\$163.7 billion. As at 31 December 2017, 87.7% of the Bank's assets was based in Hong Kong.

As a result of proactive management of assets and liabilities, the Bank's liquidity remained stable, the loan to deposit ratio was 70.85%, and the liquidity maintenance ratio was an average of 40.73%.

Total capital ratio was at 17.60%, the Tier 1 capital ratio was at 13.30% and the Common Equity Tier 1 capital ratio was at 11.30%.

Overall, the Bank's core business lines, financial positions and asset quality are strong, while impaired loan ratio remains low with high provision coverage. Capital adequacy ratio and liquidity maintenance ratio are above the relevant statutory requirements.

DIVIDEND

To properly balance sharing of success with preserving capital for future growth, the Board has recommended the payment of the final cash dividend of HK\$0.39 per share for the financial year of 2017 (2016 final cash dividend: HK\$0.39 per share). Subject to the approval of shareholders at the forthcoming annual general meeting of the Bank, the final cash dividend will be paid on Tuesday, 5 June 2018 to the shareholders whose names appear on the register of members of the Bank on Tuesday, 29 May 2018. Total dividends for the financial year of 2017, including the interim cash dividend of HK\$0.15 per share paid on 25 September 2017 (2016 interim cash dividend: HK\$0.15 per share), amounted to HK\$0.54 per share (2016 total dividends: HK\$0.54 per share).

ISSUANCE OF TIER 2 SUBORDINATED NOTES

To raise funds for Basel III-compliant Tier 2 capital, the Bank settled and closed a US\$382,903,000 Tier 2 Subordinated Notes (the "New Notes") offering on 26 July 2017. The New Notes are 10-year non-call 5-year fixed rate notes, with a fixed coupon rate of 3.876% per annum, payable semi-annually for the first five years; the interest rate will be reset on 26 July 2022.

The aggregate principal amount of the New Notes is US\$382,903,000. This includes US\$22,903,000 of "New Exchange Notes" (being the New Notes issued pursuant to the exchange offer by the Bank to the holders of its US\$225 million 6.000% Subordinated Notes due 2020) and US\$360 million of "New Money Notes". The final deal size is the largest ever international bond offering transaction by the Bank and is also the first Basel III-compliant transaction by the Bank. In line with the Bank's prudent and stable development approach, the proceeds from the offering will be used to strengthen the Bank's capital base and fund the growth of its operations and development. The New Notes have been listed on the Stock Exchange of Hong Kong under Stock Code of 05249 on 27 July 2017.

BUSINESS REVIEW

Corporate Banking

By strengthening its capability in offering professional services and facilitating customer-oriented product innovation, Chong Hing Bank is committed to providing a one-stop banking services platform for our corporate customers in Hong Kong and the Mainland. The Bank also fully supports Hong Kong Mortgage Corporation Limited's "SME Financing Guarantee Scheme" in addition to participating in the Hong Kong Government's "SME Loan Guarantee Scheme" to foster the development of SMEs.

In recent years, the Bank has strived to develop its loan syndication business, which recorded a satisfactory performance. In 2017, the Bank completed 42 syndicated loans and acted as the lead arranger for six of them. Moreover, the Bank proceeded to book-run its first ever syndicated loan with another bank in the region's loan syndication market. This is a milestone in loan syndication business for the Bank. By virtue of its syndicated and bilateral loans, the Bank was able to maintain growth in total corporate loans in 2017, while non-interest income from business also improved as compared with the same period in 2016.

Being an integrated commercial bank offering cross-border expertise and leveraging on its competitive edge in network interaction between Hong Kong and Mainland China, the Bank provides various cross-border financial products and services to accommodate customers' funding requirements in Hong Kong and Mainland China, and effectively manages their interest rate and exchange risks through its treasury product portfolio.

Personal Banking

The Bank provides its personal banking customers with various personal financial management services, including deposits, mortgage loans, consumer finance, wealth management and private banking, etc. Apart from enhancing communication with existing customers, our personal banking team continues to expand its customer base in financial management, focusing its attention on product development and improving service quality, and promoting its products through a variety of activities. The team will remain committed to delivering quality banking services and products for Hong Kong and cross-border personal customers in Guangdong and Hong Kong.

The personal banking business continued to maintain stable business growth in 2017:

- As the investment market was strong during the year, a certain amount of customers' deposits was channelled into securities and related investment products. Through a series of promotional activities and efforts to expand the customer base, total deposits in personal customers recorded a steady growth of 6.98%. Advances to personal banking customers steadily grew by 4.14% without compromising loan quality, while the loan quality stayed at a healthy level. In addition, the Bank recruited a good number of quality customers during the year, creating a solid foundation for further business expansion.
- The Bank proactively promoted the development of its wealth management business, with the sales of investment products maintaining a strong growth momentum. Coupled with heightened investment sentiment in the market, the commission income grew more than 64% year-on-year, marking a strong double-digit growth for three consecutive years. The Bank launched a number of new services during the year, including the "Online Fund Search" tool and the enhanced foreign currency trading channels to improve customer experience and optimise transaction procedures. On the sales of life insurance products, the Bank adjusted its marketing strategies and offered diverse products to suit different customers. The Bank will continually drive its online trading platform development and expand its working partners of wealth management products in order to meet Hong Kong and cross-border customers' wealth management needs.
- In the area of credit card business, the Bank launched various customer reward programmes and market promotions to attract new customers and improve the credit card utilisation rate. The Bank also devoted efforts to developing its merchant-acquiring business. Meanwhile, commission income from the merchant-acquiring business increased by over 43% year-on-year.

創興私人貸款 助您實現更多可能

私人貸款

郵輪假期 子女海外升學 夢想置業 家居裝修

實際年利率 3.75%起
 貸款最高額 HK\$1,000,000
 或月薪12倍*

成功申請 還款靈活可選* 專業及迅速服務

忠告：穩定吸債？還清到先好嘢！

申請請向 請即行動

24小時網上查詢
 3768 6899 | www.chbank.com

創興銀行
 Chung King Bank

助您部署未來大計 成就豐盛退休生活

退休理財策劃

專業財富管理分析 個人化理財保障計劃

精英理財團隊 進駐全線分行 為您服務

客戶服務熱線：3768 6888 | www.chbank.com

創興銀行
 Chung King Bank

連繫創富機遇 助您部署未來大計

創興投資理財

創興銀行
 Chung King Bank

策略組合

基金認購費低至1%
 外幣出對存款額外利率1%

創興銀行
 Chung King Bank

The Bank provides comprehensive banking products and services to cater to market needs and better serve its customers.

Financial Markets Business

With regard to its treasury business, the Bank optimised the balance sheet by effectively utilising various financial instruments while strictly complying with the established risk controls. At the same time, the Bank adjusted its investment management strategies to successfully enhance asset quality and return on investment. Despite the narrowing spread in 2017, the returns on the Bank's bond and credits portfolio recorded positive results.

Mainland Operations

Mainland business is the Bank's strategic priority. The Bank endeavoured to accelerate its business development, optimise organisational structure, strengthen risk controls as well as drive the development of the information system and the personnel team in order to lay a solid foundation and platform for sustainable and efficient operations.

Business Development

In 2017, the Mainland branches and sub-branches have been growing steadily in their scale of operation, while core businesses are also seeing healthy growth. Profitability rose steadily and asset quality remained sound. The customer base has expanded and the product range remained comprehensive.

The Bank's loan business has seen a new breakthrough. As the government's public finance deposits increased steadily, new sources of funds were secured, and qualifications were granted for government agency business.

The Mainland branches and sub-branches continued to focus on serving the real economy. In response to the national strategies on industrial upgrading and supply-side structural reform, they focused on supporting high quality manufacturers and service enterprises in China. With the implementation of the Belt and Road Initiative and the Guangdong-Hong Kong-Macao Greater Bay Area Initiative, the Bank leveraged on opportunities in various businesses to build up a comprehensive cross-border and regional financial service system, while proactively optimising product structures and enhancing the market competitiveness of the assets business. Mainland branches and sub-branches also joined forces to optimise their loan structure through regulating the deployment of loans.

Furthermore, continuous growth is also seen in the interbank financial business. Interest income surged significantly and the Bank has attained several interbank business qualifications. Both the Guangzhou Branch and the Shenzhen Branch have become bond market members of the National Interbank funding centre. The Guangzhou Branch was also admitted as a foreign currency lending member and RMB/FX spot member of the National Interbank funding centre. These moves served to lay a solid foundation for business development.

The cross-border business continued to grow with more product lines made available for our customers. In addition, we successfully launched onshore guarantees for offshore loans, direct Renminbi cross-border loans and Renminbi cross-border cash pooling, etc.

CHIEF EXECUTIVE'S STATEMENT

Infrastructure

In accordance with the requirements of the regulatory bodies in the Mainland and Hong Kong, the Bank persisted in optimising its organisational structure, further enhancing its risk management regime, improving its procedures and workflows, and uplifting the supporting capability of its various systems.

Credit Risk Management – Facing the economic “new normal”, the Bank’s Mainland branches and sub-branches strengthened their risk controls and maintained good asset quality with zero non-performing loans. They also established a centralised management mechanism to oversee the whole process of loan granting, covering the pre-approval, in-process and post-approval stages, realising sound risk management. They also strengthened market and liquidity risk management by further solidifying the liquidity control indexing system and preparing a contingency plan for managing liquidity risk in case of risk events.

Information System – In order to continuously improve the customer experience, during the year the Bank upgraded its information infrastructure and proceeded with the development of new Internet banking. To better cater for business development and fulfil regulatory requirements, the Bank accelerated the interfacing between its internal and external systems. In addition, a new interbank foreign currency trading system, bond system and electronics commercial draft system are being developed to strengthen business growth.

Compliance – Compliance control and the crime prevention regime were further heightened in the year, with the establishment of systems covering the Mainland branches, and more frequent and thorough internal checking on compliance in order to prevent violation of regulations and criminal conduct.

Chong Hing Securities Limited

In 2017, the Hong Kong stock market was on a bullish course, with strong turnover that was in line with the robust performance of overseas stock markets. The overall turnover of Chong Hing Securities was 61.3% higher than last year, significantly outperforming the 31.9% year-on-year growth in the overall trading volume of the Hong Kong stock market, whereas its total profit before taxation grew by 102.1%. In 2018, backed by the Stock Connects between Mainland China and Hong Kong, the southbound capital from Mainland China is expected to continue to support the performance of the Hong Kong stock market. The Bank maintains a cautiously optimistic outlook for our stock brokerage business.

Chong Hing Insurance Company Limited

In 2017, notwithstanding the intense competition in the Hong Kong insurance industry and decline in overall underwriting profit, Chong Hing Insurance still recorded a 14% year-on-year increase in investment return as driven by market sentiments.

Affected by several typhoons in 2017, Chong Hing Insurance registered lower profits for its property damage insurance business. Nevertheless, the overall business performance continued to improve.

Chong Hing Insurance will continue to leverage on the bancassurance model to explore new business opportunities, and seek to realise the full potential of its strong business network. The Bank will also explore new business opportunities in order to achieve better performance and results.

Future Development

The Bank continues to invest for its sustainable development. The year 2017 was the foundation year of the Bank's customer resource management and efforts to promote synergy. In addition to establishing the relevant systems and mechanisms, the Bank adopted a two-pronged approach of enhancing synergy with the Yuexiu Group as well as synergy within the Bank, and as a result, initial business connections and the expected outcome were achieved.

The Bank is also committed to building a modern operation platform, accelerating bank restructuring and process improvement, and further enhancing customer experience and cost-effectiveness, including the establishment of a centralised trading service team to strengthen the productivity of branches and customer managers. In order to further consolidate and optimise internal resources, the Bank established a digital transformation team to promote innovation and the transformation to digital banking. In addition, the Bank's centralised treasury receipt and payment system was officially launched during the year, and land security deposit system was also completed by early 2018, signifying a new phase in the expansion of the Bank's business in the Mainland.

The successive launch of various IT systems in 2017 was instrumental in enhancing the Bank's capacity to serve its customers and monitor risks.

CORPORATE CULTURE

During the year, the Bank officially established its corporate culture, which comprises six key elements, namely Core Values, Vision, Mission, Management Concepts, Enterprise Spirit and Corporate Style. The Bank hopes to create an excellent corporate culture by making sustainable and long-term efforts to optimise governance and enhance cohesion. The formulation of the corporate culture is also in response to the "Bank Culture Reform" guidelines issued by the Hong Kong Monetary Authority to all banks in March 2017.

In order to put the new corporate values into practice, the Bank has launched a new performance management system to reward employees whose performances are in line with the corporate culture. The Bank has also established core competencies and related behavioural indicators to make objective assessments and assist our employees in developing career plans.

CORPORATE RESPONSIBILITY

Established in 1948, Chong Hing Bank is dedicated to providing comprehensive banking services for people from all walks of life. The Bank currently operates a network of 39 branches in Hong Kong, 3 branches and 4 sub-branches in the Mainland, and 1 branch in Macau.

Having the community at heart, the Bank gives back to society through active participation in volunteer activities, charitable donations and supporting community and art events held by charity organisations and art groups. It also sponsors projects to show its care for needy groups.

CHIEF EXECUTIVE'S STATEMENT

Community Events

- In January, the Bank donated to the “Green Power Hike for a Green Future”, held by Green Power, and the “Charity Cycling Marathon”.
- In May and July, the Bank sponsored the social skill classes for children with special needs held by the Hong Kong Association of the Deaf. Visits to the association were also organised for staff members to participate in a creative light clay workshop with the hearing-impaired children, helping them integrate into society.



- In June, the Bank participated in the “Financial Education Workshop” jointly held by The Hong Kong Association of Banks and The Salvation Army to share tips on financial management with participants.



- In December, the Bank visited the Hong Kong Playground Association's Tsing Yi Centre to share knowledge on saving money with primary school students in the district.



Through the Bank's branch network and cooperation with numerous charity organisations such as the Tung Wah Group of Hospitals, Yan Chai Hospital and Médecins Sans Frontières, the Bank organised a variety of community fund-raising activities, including selling raffle tickets and collecting donations from flag bags on flag-selling day. Furthermore, to contribute to public welfare, the Bank inserted promotional leaflets of charity organisations into its bank mailers sent to customers.

Art Events

- In July, the Bank sponsored "Heritage Showtime on LOK KU ROAD", a local art and cultural event.
- In October, the Bank sponsored "Fine Art Asia", a fair showcasing a wide range of collectable fine art from Asia and the West.
- In December, the Bank sponsored "Ink Asia", featuring contemporary ink art.

The Bank seeks to promote and foster the development of art and culture through sponsoring events as well as expositions held by different art groups.

Achievements under Corporate Responsibility

The Bank is committed to giving back to society and protecting the environment in a variety of ways to fulfil our social responsibility. For its achievements in this regard, the Bank gained recognition from various sectors.

- The Bank was granted a "10 Years Plus Caring Company" logo by the Hong Kong Council of Social Service. It was a recognition that the Bank has continuously participated in community events to serve and care for society.



- The Bank's branch network assisted the Tung Wah Group of Hospitals in selling raffle tickets to raise funds, achieving great success. In 2017, the Bank was awarded the title of "Runner-up in the Commercial and Industrial Institutes and Groups Category in the Charity Raffle Tickets Selling Competition" and received the "Raffle Tickets Selling Award" from the Tung Wah Group of Hospitals.



CHIEF EXECUTIVE'S STATEMENT

- In order to help minimise the light nuisance and energy wastage that may be caused by external lighting installations, the Bank realised its pledge to switch off external lights at the pre-set time in response to the “Charter on External Lighting” organised by the Environment Bureau of the Hong Kong SAR Government. Many branches complied with the lighting requirements, and the Bank was presented with the “Platinum Award” for its efforts.
- The Bank was awarded “The Employer of Choice Award” by JobMarket in recognition of its superior talent management strategies and practices.



CORPORATE GOVERNANCE

The Bank fully appreciates that compliance with the relevant statutory and regulatory requirements and maintaining good corporate governance standards are imperative to its sustainable development. The Bank has deployed considerable resources and implemented the relevant measures to ensure that the statutory and regulatory requirements are fully complied with, and that a high standard of corporate governance is maintained.

For details of the Bank's corporate governance practices, please refer to the section entitled “Corporate Governance Report” of this Annual Report.

AWARDS

The Bank aims to offer quality banking services to its customers. In 2017, it achieved excellent results in different fields and received awards and recognition from different organisations.

In May 2017, the Bank received the “Straight Through Processing (STP) Award” from the Bank of New York Mellon for the ninth consecutive year. This award recognised the Bank’s outstanding performance in payment formatting and a high STP rate of over 95% in fully-automated US dollar payment processing without manual intervention.



The Bank works closely with SMEs with the goal of achieving mutual growth while providing them with diversified banking services. This support has been widely recognised by the industry. In June, the Bank received the “Best SME’s Partner Award” from the Hong Kong General Chamber of Small and Medium Business for the ninth time.



In November, the Bank received the “STP Award” from CitiBank Asia Pacific for the first time as an indication that the rate of fully-automated STP exceeded 97% and as recognition of the Bank’s quality services.



In December, the Bank received for the first time the “Five Stars Honor Award”, the highest award at the “Distinguished Banks of the Year” competition hosted by Hong Kong Life Insurance, indicating that the remarkable performance of the Bank was widely recognised.



OUTLOOK

Hong Kong and the Mainland are connected geographically and many aspects of their developments are complementary. Under China's Belt and Road Initiative and the Guangdong-Hong Kong-Macao Greater Bay Area Initiative, Hong Kong will be able to further cement our pivotal role as a hub for infrastructure financing, trading and investment.

The Bank will seize the opportunities brought about by the closer integration of Hong Kong with the Mainland, in particular the regional linkage, and target cross-border financial services as its core development direction. The branches in Hong Kong and the branch and sub-branch network throughout the core Pearl River Delta region of the Bank have established a platform for the provision of cross-border services. Leveraging on its diversified cross-border banking products, and being equipped with a customer-oriented and innovative mindset, the Bank created a solid business foundation for cross-border business. The Bank will continue to provide quality banking services to customers from both Hong Kong and the Mainland through deepening synergy with the business of the Yuexiu Group, and fulfil its vision of becoming an "integrated commercial bank with cross-border expertise".

Having our roots in Hong Kong for decades, Chong Hing Bank has established a remarkable brand, assembled a professional management team and developed loyal customers. The Bank will adhere to its solid and prudent operating principles, continuously exploit and seize opportunities in various fields, drive its sustainable and healthy development and endeavour to achieve satisfactory results in order to accomplish its corporate mission: "To benefit Customers, Employees, Shareholders and Community".

APPRECIATION

In 2017, with the hard work of all staff members of Chong Hing Bank, the efficiency of both the management and operations of the Bank received a boost while its core competence gained constant enhancement. I would like to thank all the Directors on the Board for their wise counsel and support. I would also like to express my gratitude to the management team and all our staff members for their tireless contributions. I also take this opportunity to convey my appreciation to our shareholders and customers for their long-standing support and trust. Chong Hing Bank was established in 1948, and is currently marking its 70th year with a solid foundation and a progressive spirit. Looking forward, the Bank will proactively grasp the opportunity to achieve quality, sustained growth and accomplish outstanding results on our path to excellence.

Zong Jianxin

Chief Executive

Hong Kong, 29 March 2018

The Directors are pleased to present their annual report and the audited consolidated financial statements for the year ended 31 December 2017.

PRINCIPAL ACTIVITIES AND BUSINESS REVIEW

The Bank is engaged in the provision of banking and related financial services. The principal activities and other particulars of its principal subsidiaries are set out in note 22 to the consolidated financial statements.

Further discussion and analysis of these activities as required by Schedule 5 to the Hong Kong Companies Ordinance (the "CO"), including a fair review of the business and a description of the principal risks and uncertainties facing the Bank and its subsidiaries (the "Group"), particulars of important events affecting the Group that have occurred since the end of the financial year 2017 (if any), as well as indication of likely future development in the Group's business are set out in the sections headed "Chairman's Statement", "Chief Executive's Statement" and "Notes to the Consolidated Financial Statements" contained in this Annual Report. Discussions on the environmental policies and performance, compliance by the Group with the relevant laws and regulations that have a significant impact on the Group and an account of the key relationships of the Group with its stakeholders are contained in the "2017 Environmental, Social and Governance Report" (the "ESG Report"), which is an online report available on the websites of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") and the Bank. The abovementioned sections and the ESG Report form part of this Report.

BUSINESS PERFORMANCE

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:

	2017 <i>HK\$'000</i>	2016 <i>HK\$'000</i>
Corporate and retail banking	2,262,667	1,723,027
Financial markets activities	426,779	687,200
Securities dealing business	154,834	115,029
Others	(134,724)	149,040
	2,709,556	2,674,296

The corporate and retail banking services provided by the Group are principally lending and trade finance facilities, auto financing, 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 services offered include remittance and money exchange, safe deposit boxes, autopay and direct debit services.

Financial markets 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, and from the Bank's cash management activities through foreign currency funding swaps.

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

Others comprise 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 other operating income of the Group for the year.

RESULTS AND APPROPRIATIONS

The results of the Group for the year ended 31 December 2017 are set out in the consolidated income statement and the consolidated statement of comprehensive income on pages 73 and 74.

An interim cash dividend of HK\$0.15 per share was paid to the shareholders during the year. The Board has recommended the payment of a final cash dividend for the year ended 31 December 2017 of HK\$0.39 per share (2016: HK\$0.39 per share) to the shareholders whose names appear on the register of members of the Bank on 29 May 2018.

DISTRIBUTABLE RESERVES

The distributable reserves are shown in note 41 to the consolidated financial statements.

PRINCIPAL PROPERTIES

The Group's investment properties were revalued during the year. The net increase in fair value arising on the revaluation, which has been credited directly to the consolidated income statement, amounted to HK\$12,632,000. Details of the investment properties of the Group are set out in note 25 to the consolidated financial statements.

Details of the movements in the property and equipment of the Group during the year are set out in note 26 to the consolidated financial statements.

SHARE CAPITAL

Details of the share capital of the Bank are set out in note 32 to the consolidated financial statements. There was no movement in the share capital of the Bank during the year.

DEBENTURES ISSUED

On 26 July 2017, the Bank completed the issue of US\$382,903,000 Tier 2 Subordinated Notes due 2027 (the "New Notes"), with a fixed coupon rate of 3.876% per annum payable semi-annually for the first five years. The interest rate will be reset on 26 July 2022 to the sum of the then prevailing 5-year U.S. Treasury Rate and the initial spread. The New Notes, which are listed on the Stock Exchange (Stock Code: 05249), were issued to strengthen the Bank's capital base and fund the growth of the Bank's operations and development.

Pursuant to the exchange offer by the Bank to the holders of its US\$225,000,000 6.000% Subordinated Notes due 2020 (Stock Code: 04327) (the "Existing Notes") to exchange their Existing Notes for the New Notes (the "Exchange Offer"), US\$22,903,000 out of US\$382,903,000 in aggregate principal amount of the New Notes was issued in exchange for US\$20,976,000 in aggregate principal amount of the Existing Notes. Following the settlement of the Exchange Offer, US\$204,024,000 in aggregate principal amount of the Existing Notes remains outstanding.

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

Save for the Exchange Offer as disclosed above under the heading "DEBENTURES ISSUED", neither the Bank nor any of its subsidiaries purchased, sold or redeemed any of the Bank's listed securities during the year.

EQUITY-LINKED AGREEMENTS

Other than the share option scheme as set out in note 35 to the consolidated financial statements, no equity-linked agreements were entered into by the Bank during the year or subsisted at the end of the year. No options have been granted under the said scheme since its adoption in 2012.

DIRECTORS

The Directors of the Bank during the year and up to the date of this Report are:

Executive Directors

Mrs LEUNG Ko May Yee Margaret SBS, JP	<i>(Deputy Chairman and Managing Director)</i>
Mr ZONG Jianxin	<i>(Deputy Managing Director and Chief Executive)</i>
Mr LAU Wai Man	<i>(Deputy Managing Director)</i>

Non-executive Directors

Mr ZHANG Zhaoxing	<i>(Chairman)</i>
Mr ZHU Chunxiu	
Mr WANG Shuhui	
Mr LI Feng	
Mr CHOW Cheuk Yu Alfred BBS, JP	

Independent Non-executive Directors

Mr CHIRANAKHORN Wanchai	<i>(Passed away on 23 January 2017)</i>
Mr CHENG Yuk Wo	
Mr MA Chiu Cheung Andrew	
Mr LEE Ka Lun	
Mr YU Lup Fat Joseph	

Article 100 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, Mrs Leung Ko May Yee Margaret, Mr Chow Cheuk Yu Alfred, Mr Cheng Yuk Wo and Mr Ma Chiu Cheung Andrew shall retire at the forthcoming annual general meeting to be held on 18 May 2018 (the "2018 AGM"). Except for Mrs Leung who has informed the Bank that she will not stand for re-election at the 2018 AGM, each of the other three retiring Directors will offer themselves for re-election at the 2018 AGM.

Each of Messrs Cheng Yuk Wo and Ma Chiu Cheung Andrew has served as an Independent Non-executive Director of the Bank for more than nine years. During their tenure, both Mr Cheng and Mr Ma have not engaged in any executive management of the Bank and have demonstrated their ability to provide an independent view to the Bank's matters. In addition, Mr Cheng and Mr Ma have declared their independence by submitting the annual confirmation of independence to the Board pursuant to Rule 3.13 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). The Board believes that they are independent and comply with the independence requirements under Rule 3.13 of the Listing Rules.

Details of the three Directors to be re-elected at the 2018 AGM are set out in the circular to the shareholders sent together with this Annual Report.

DIRECTORS' REPORT

None of the three Directors proposed for re-election at the 2018 AGM has a service contract with the Bank and/or any of its subsidiaries which is not determinable by the Bank within one year without payment of compensation (other than statutory compensation).

STATUS OF INDEPENDENT NON-EXECUTIVE DIRECTORS

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 still considers all the Independent Non-executive Directors to be independent.

DIRECTORS OF SUBSIDIARIES

Listed below are the names of all the Directors who have served on the boards of the Bank's subsidiaries during the year and up to the date of this Report:

CHAN Hoi Kit Frederick ⁽²⁾	LAU Wai Man
CHAN Man Mei Michael	LEE Ka Shing
CHAN Tai On	LEUNG Chan Keung
CHENG Yuk Wo	LEUNG Ko May Yee Margaret
CHIRANAKHORN Wanchai ⁽¹⁾	MA Chiu Cheung Andrew
CHIU Tak Wah Edward	MA Wai Leung
CHIU Yau Sim	TSANG Chiu Wing ⁽²⁾
CHOW Cheuk Yu Alfred	WONG Wan Hong
CHU Shiu Man	YU Kam Ping Alice
CHU Wai Hung Kevin ⁽²⁾	ZONG Jianxin
CHUN Ka Wing	

Notes:

- (1) Mr Chiranakhorn Wanchai passed away on 23 January 2017.
- (2) Resigned/ceased as a Director of the relevant subsidiary(ies) of the Bank as of 31 December 2017.

A list setting out specifically the directorship of each individual subsidiary of the Bank is updated whenever there are directorate changes and is posted on the Bank's website (www.chbank.com/en/about-ch-bank/investor-relations/directors-list/index.shtml).

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

As of 31 December 2017, the interests and short positions of the Directors (including the Chief Executive) in the shares, underlying shares and debentures of the Bank and its associated corporations (within the meaning of 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 (the "Register"), or as otherwise notified to the Bank and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers under Appendix 10 to the Listing Rules (the "Model Code"), were as follows:

Interests in shares

Name of Director	Associated Corporation	Long/short position	Number of ordinary shares held			Total interests	Percentage of issued share capital ⁽¹⁾
			Personal interests	Spousal interests	Corporate interests		
Li Feng	Yuexiu Property Company Limited	Long	172,900	–	–	172,900	0.001
Lee Ka Lun	Yuexiu Property Company Limited	Long	3,200,000	–	–	3,200,000	0.026
Yu Lup Fat Joseph	Yuexiu Property Company Limited	Long	4,000,000	–	–	4,000,000	0.032

Note:

(1) Based on 12,401,306,631 shares of Yuexiu Property Company Limited issued as at 31 December 2017.

Save as disclosed above, as of 31 December 2017, none of the Directors (including the Chief Executive) had or was deemed to have any other interests or short positions in any shares, underlying shares or debentures of the Bank or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the Register or as otherwise notified to the Bank and the Stock Exchange pursuant to the Model Code. Moreover, as of 31 December 2017, none of the Directors (including the Chief Executive), their spouses or children under 18 years of age was granted, or exercised, any right to subscribe for shares in or debentures of the Bank or any of its associated corporations (within the meaning of Part XV of the SFO).

At no time during the year was the Bank or any of its holding companies, its subsidiaries or its fellow subsidiaries a party to any arrangement 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, with the exception of the share option scheme as described under the heading “EQUITY-LINKED AGREEMENTS” of this Report.

DIRECTORS' INTERESTS IN TRANSACTIONS, ARRANGEMENTS AND CONTRACTS OF SIGNIFICANCE

Other than those interests disclosed below under the heading “CONNECTED TRANSACTIONS”, no transactions, arrangements and contracts of significance in relation to the Group’s business to which the Bank or any of its holding companies, its subsidiaries or its fellow subsidiaries was a party and in which a Director of the Bank or an entity connected with a Director (within the meaning of Section 486 of the CO) had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

None of the Directors is interested in any business which competes or is likely to compete, either directly or indirectly, with the business of the Bank.

DISCLOSURE OF CHANGES IN DIRECTORS' INFORMATION

Changes in Directors' information since the date of the 2017 Interim Report which are required to be disclosed pursuant to Rule 13.51B(1) of the Listing Rules are set out below:

Name of Director	Change
Mrs LEUNG Ko May Yee Margaret SBS, JP <i>Executive Director</i>	<ul style="list-style-type: none"> Extended her service agreement with the Bank for the period from 14 February 2018 to 18 May 2018 (being the date of the 2018 AGM). Her emolument package remains unchanged, with the annual base salary of HK\$12,800,000 (subject to pro-rata adjustment for an incomplete year), discretionary bonus and other benefits Will retire as Executive Director, Deputy Chairman and Managing Director of the Bank with effect from the conclusion of the Bank's 2018 AGM
Mr ZONG Jianxin <i>Executive Director</i>	<ul style="list-style-type: none"> Appointed as Deputy Chairman of the Bank, which will become effective on 18 May 2018
Mr ZHU Chunxiu <i>Non-executive Director</i>	<ul style="list-style-type: none"> Appointed as Deputy Chairman of the Bank, which will become effective on 18 May 2018
Mr CHENG Yuk Wo <i>Independent Non-executive Director</i>	<ul style="list-style-type: none"> Appointed as Independent Non-executive Director of Kidsland International Holdings Limited* (Stock Code: 02122) with effect from 20 October 2017
Mr MA Chiu Cheung Andrew <i>Independent Non-executive Director</i>	<ul style="list-style-type: none"> Appointed as Independent Non-executive Director of C-MER Eye Care Holdings Limited# (Stock Code: 03309) with effect from 13 December 2017 Appointed as Independent Non-executive Director of Chong Hing Insurance Company Limited with effect from 25 January 2018

* Listed on the Stock Exchange on 10 November 2017

Listed on the Stock Exchange on 15 January 2018

The emoluments of the Directors of the Bank on a named basis are set out in note 42 to the consolidated financial statements. Starting from 1 January 2018, the annual fees for the Chairman and members of the Audit Committee, Connected Party Transactions Committee (the "CPT Committee"), Nomination Committee, Remuneration Committee, Risk Committee and Special Board Committee (for an IT Project) (the "SBC") are as follows:

	Audit Committee	CPT Committee	Nomination Committee	Remuneration Committee	Risk Committee	SBC
Chairman	HK\$100,000	HK\$80,000	HK\$80,000	HK\$80,000	HK\$80,000	HK\$100,000
Member	HK\$20,000	HK\$20,000 ⁽¹⁾	HK\$20,000	HK\$20,000	HK\$20,000	HK\$20,000 ⁽²⁾

Notes:

- (1) Chief Financial Officer and Chief Risk Officer of the Bank, both being members of the CPT Committee, are not entitled to receive the abovementioned membership fee.
- (2) The three Executive Directors of the Bank, all being members of the SBC, are not entitled to receive the abovementioned membership fee. The remaining members of the SBC are Mr LEE Ka Lun (who serves as the SBC's Chairman) and Mr LI Feng.

Other than the information disclosed above, there is no other information required to be disclosed pursuant to Rule 13.51B(1) of the Listing Rules.

REMUNERATION POLICY

The Bank has set up the Remuneration Committee, responsibilities of which include reviewing and approving the performance-based remuneration packages payable to Directors and Senior Management, if any, by reference to the Bank's corporate goals and objectives.

PERMITTED INDEMNITY

Pursuant to the Bank's Articles of Association, every Director or other officer of the Bank shall be entitled to be indemnified out of the assets of the Bank against any liability (to the extent permitted by the CO) incurred by them or any of them as the holder of any such office or appointment to a person other than the Bank or any of its holding companies, its subsidiaries or its fellow subsidiaries. The Bank has taken out insurance against any liability associated with defending any proceedings which may be brought against the Directors and other officers of the Bank.

SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS

As of 31 December 2017, the register required to be kept under Section 336 of the SFO showed that the following parties had interests and short positions in the shares and underlying shares of the Bank:

Interests in shares

Name	Long/short position	Capacity	Number of ordinary shares	Percentage of issued share capital ⁽¹⁾
Yuexiu Financial Holdings Limited ⁽²⁾	Long	Beneficial owner	489,375,000	75
Yue Xiu Enterprises (Holdings) Limited ("YX Enterprises")	Long	Interest of a controlled corporation	489,375,000	75
廣州越秀集團有限公司 (Guangzhou Yue Xiu Holdings Limited*) ("GZYX Holdings")	Long	Interest of a controlled corporation	489,375,000	75

Notes:

- (1) Based on 652,500,000 shares of the Bank issued as at 31 December 2017.
- (2) Yuexiu Financial Holdings Limited is wholly-owned by YX Enterprises, and YX Enterprises is wholly-owned by GZYX Holdings.

* for identification purpose only

Save as disclosed above, the Bank had not been notified of any other interests and short positions in its shares and underlying shares as of 31 December 2017 which were required to be recorded in the register kept under Section 336 of the SFO.

PUBLIC FLOAT

As at the date of this Report, the Bank has maintained the prescribed public float under the Listing Rules, based on the information that is publicly available to the Bank and within the knowledge of the Directors of the Bank.

CONNECTED TRANSACTIONS

- i. The connected transactions between the Group and GZYX Holdings and its associates (as defined under Chapter 14A of the Listing Rules) (collectively referred to as the "Yue Xiu Group") during the year under review were as follows:
 - A. The Bank handled routine banking transactions for the members of the Yue Xiu Group. Services provided by the Bank included cheque clearing, accepting deposits, extending credit facilities, foreign exchange transactions, remittances and other banking and financial services. Such transactions were conducted on normal commercial terms and in the ordinary and usual course of business of the Bank, and are exempt from the relevant disclosure requirements under Chapter 14A of the Listing Rules.
 - B. As set out in the Bank's announcement dated 25 October 2017, the Bank and Guangzhou Yuexiu Financial Technology Co., Ltd. ("Yuexiu Financial Technology") (an associate of GZYX Holdings) entered into an information technology framework agreement (the "IT Framework Agreement") on 25 October 2017 which governs the provision of various information technology related services (the "IT Services") by the Yuexiu Financial Technology and its subsidiaries (the "Yuexiu Financial Technology Group") to the Group. The term of the IT Framework Agreement commenced on 25 October 2017 and shall end on 31 August 2020 (both dates inclusive). The fees charged by the Yuexiu Financial Technology Group for the IT Services to be supplied to the Group under the IT Framework Agreement will be determined with reference to the expected costs to be incurred in the course of provision of the IT Services to the Group, volume and duration of the IT Services required, and the prevailing market prices of the same or similar services offered by independent third parties.

During the period from 25 October 2017 to 31 December 2017, the total fees incurred in respect of the IT Services provided by the Yuexiu Financial Technology Group to the Group were HK\$8,668,995, which was within the annual cap of HK\$35,376,000 for the period as announced on 25 October 2017.

- C. As set out in the Bank's announcement dated 29 November 2016, the Bank and Yuexiu Property Company Limited ("Yuexiu Property") (an associate of YX Enterprises) entered into a foreign exchange transactions framework agreement (the "FX Framework Agreement") on 29 November 2016 which governs the foreign exchange transactions (the "FX Transactions") to be entered into between the Group and Yuexiu Property and its subsidiaries (the "Yuexiu Property Group"). The term of the FX Framework Agreement commenced on 29 November 2016 and shall end on 31 December 2018 (both dates inclusive). The FX Transactions between the Group and the Yuexiu Property Group will adopt the prevailing market prices or rates normally applicable to similar transactions conducted with independent third parties.

Messrs Zhang Zhaoxing, Zhu Chunxiu, Li Feng, Lee Ka Lun and Yu Lup Fat Joseph, being common directors of the Bank and Yuexiu Property on the date of the FX Framework Agreement, abstained from voting on the resolutions approving the FX Framework Agreement and the FX Transactions. Save as disclosed above, none of the Directors has any material interest in the FX Framework Agreement and the FX Transactions.

As of 31 December 2017, the aggregate absolute amount of fair value at inception of the FX Transactions recorded as assets/liabilities was HK\$6,748,338, which was within the annual cap of HK\$17 million for the financial year 2017 as announced on 29 November 2016.

- D. As set out in the Bank's announcement dated 17 June 2016, the Bank and GZYX Holdings entered into a foreign exchange and financial markets transactions framework agreement (the "Framework Agreement") on 17 June 2016 which governs the foreign exchange transactions and financial markets transactions (the "FX and FM Transactions") to be entered into between the Group and GZYX Holdings and its non-listed subsidiaries (the "Yuexiu Holdings Private Group"). The term of the Framework Agreement commenced from the date of the Framework Agreement and shall end on 31 December 2018 (both dates inclusive). The FX and FM Transactions between the Group and the Yuexiu Holdings Private Group will adopt the prevailing market prices or rates normally applicable to similar transactions conducted with independent third parties.

Messrs Zhang Zhaoxing, Zhu Chunxiu and Wang Shuhui, being common directors of the Bank and GZYX Holdings on the date of the Framework Agreement, abstained from voting on the resolutions approving the Framework Agreement and the FX and FM Transactions. Save as disclosed above, none of the Directors has any material interest in the Framework Agreement and the FX and FM Transactions.

As set out in the Bank's announcement dated 13 July 2016, the annual caps for the financial years 2016, 2017 and 2018 in respect of the FX and FM Transactions were revised. As of 31 December 2017, the aggregate absolute amount of fair value at inception of the FX and FM Transactions recorded as assets/liabilities was HK\$913,453, which was within the revised annual cap of HK\$60 million for the financial year 2017 as announced on 13 July 2016.

- E. As set out in the Bank's announcement dated 30 November 2015, the Bank and Guangzhou City Construction & Development Co. Ltd. ("Guangzhou City Construction") (an associate of YX Enterprises) entered into a tenancy agreement (the "Tenancy Agreement") on 30 November 2015 for the lease of Rooms 01-16, 50/F Yuexiu Financial Tower, 28 Zhujiang East Road, Tianhe District, Guangzhou, the People's Republic of China (the "YX Tower Property") for its Guangzhou Branch at a monthly rent of RMB627,578 from 1 December 2015 to 30 November 2016, RMB665,233 from 1 December 2016 to 30 November 2017 and RMB705,147 from 1 December 2017 to 30 November 2018. The Bank was entitled to a rent concession period from 1 December 2015 to 29 February 2016 (the "Rent Concession Period") for rent concession of RMB209,192 from 1 December 2015 to 31 January 2016 and RMB209,194 from 1 February 2016 to 29 February 2016. If the Tenancy Agreement is terminated before its expiry date for reasons not related to Guangzhou City Construction, the Bank will no longer be entitled to such rent concession and the original rent (i.e. RMB627,578) will apply in respect of the Rent Concession Period.

On 30 November 2015, the Bank and Guangzhou Yue Xiu City Construction Jones Lang LaSalle Property Services Co., Ltd. ("GZYX Jones Lang") (an associate of YX Enterprises) entered into a property management agreement (the "PM Agreement") for the provision of management services in relation to the YX Tower Property at a monthly management fee of RMB99,568.

The total rents and management fees incurred during the financial year 2017 were within the annual cap of RMB9,469,000 as announced on 30 November 2015.

Starting from 1 June 2016, the Bank's Guangzhou Branch replaced the Bank as the tenant of the YX Tower Property and entered into relevant supplemental agreements to the Tenancy Agreement and the PM Agreement with Guangzhou City Construction (as landlord) and GZYX Jones Lang (as property manager) respectively. From 1 August 2017 onwards, Guangzhou Jingyao Real Estate Company Limited (a wholly-owned subsidiary of Guangzhou City Construction) replaced Guangzhou City Construction as the landlord of the YX Tower Property and entered into a supplemental agreement with Guangzhou Branch.

- F. As set out in the Bank's announcement dated 23 June 2014, the Bank and Guangzhou Yue Xiu City Construction International Finance Centre Co., Ltd. (the "IFC Landlord") (an associate of YX Enterprises) entered into a tenancy agreement (the "Original Tenancy Agreement") on 23 June 2014 for the lease of Unit 103, 1/F Podium, Guangzhou International Finance Centre, House 160, 5 Zhujiang West Road, Tianhe District, Guangzhou, the People's Republic of China and Unit 203, 2/F Podium, Guangzhou International Finance Centre, House 260, 5 Zhujiang West Road, Tianhe District, Guangzhou, the People's Republic of China (the "IFC Property") at a monthly rent of RMB233,068 from 1 July 2014 to 30 June 2016 and RMB244,722 from 1 July 2016 to 30 June 2017. The Bank was entitled to a rent concession in the total amount of RMB699,204 for the period from 1 July 2014 to 31 October 2014. If the Original Tenancy Agreement is terminated by the Bank before the expiry of the tenancy, the Bank is required to pay back the same amount to the IFC Landlord.

On 23 June 2014, the Bank and GZYX Jones Lang entered into a property management agreement (the "Original PM Agreement") for the provision of management services in relation to the IFC Property at a monthly management fee of RMB34,720.

The total rents and management fees incurred during the period from 1 January 2017 to 30 June 2017 were within the annual cap of RMB1,746,000 as announced on 23 June 2014.

On 30 June 2017, both of the Original Tenancy Agreement and the Original PM Agreement expired.

As set out in the Bank's announcement dated 30 June 2017, Guangzhou Tianhe Sub-Branch of the Bank and the IFC Landlord entered into a new tenancy agreement (the "New Tenancy Agreement") on 30 June 2017 for the lease renewal of the IFC Property at a monthly rent (inclusive of 5% VAT) of RMB128,338.33 from 1 July 2017 to 31 August 2017 (with a monthly rent concession of RMB128,338.33 (tax inclusive) granted by the IFC Landlord), RMB256,675.65 from 1 September 2017 to 30 June 2018, RMB128,338.33 from 1 July 2018 to 31 August 2018 (with a monthly rent concession of RMB128,338.33 (tax inclusive) granted by the IFC Landlord), RMB256,675.65 from 1 September 2018 to 30 June 2019 and RMB269,508.75 from 1 July 2019 to 30 June 2020. If the New Tenancy Agreement is terminated before its expiry date for reasons not related to the IFC Landlord, Guangzhou Tianhe Sub-Branch will no longer be entitled to the rent concession granted by the IFC Landlord as described above and will be immediately required to repay the IFC Landlord all the rents payable during the relevant periods.

On 30 June 2017, Guangzhou Tianhe Sub-Branch and GZYX Jones Lang entered into a new property management agreement for the provision of management services in relation to the IFC Property at a monthly management fee of RMB34,720.

The total rents and management fees incurred during the period from 1 July 2017 to 31 December 2017 were within the annual cap of RMB2,115,000 as announced on 30 June 2017.

- ii. The connected transactions between the Bank and its Directors and their associates during the year under review were as follows:

The Bank handled routine banking transactions for its Directors and their associates, including cheque clearing, accepting deposits, extending credit facilities, foreign exchange transactions, remittances and other banking and financial services. Such transactions were conducted under terms and conditions normally applicable to customers of comparable standing, and are exempt from the relevant disclosure requirements under Chapter 14A of the Listing Rules.

The transactions described in sub-section (i) (comprising items A to F) and sub-section (ii) above are collectively referred to as the "Continuing Connected Transactions" entered into by the Group.

The Bank's external auditor was engaged to report on the Continuing Connected Transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 (Revised) "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. The auditor has issued an unqualified letter containing its findings and conclusions in respect of the Continuing Connected Transactions in accordance with Rule 14A.56 of the Listing Rules. A copy of the auditor's letter has been provided by the Bank to the Stock Exchange. The Independent Non-executive Directors have reviewed the Continuing Connected Transactions and the auditor's letter and have confirmed that those transactions have been entered into in the ordinary and usual course of business of the Group, on normal commercial terms, and in accordance with the respective agreements governing such transactions on terms that are fair and reasonable and in the interests of shareholders of the Bank as a whole.

Certain related party transactions (the "RPT Transactions") as disclosed under note 39 to the consolidated financial statements constituted connected transactions or continuing connected transactions under the Listing Rules. Such RPT Transactions are either disclosed in sub-section (i) above or exempt from the disclosure requirements under Chapter 14A of the Listing Rules because they are (1) below the de minimis threshold under Rule 14A.76(1) of the Listing Rules or (2) fallen within the exemptions under Rules 14A.87 and 14A.90 of the Listing Rules.

MANAGEMENT CONTRACTS

Save for the service contracts, no other contracts concerning the management and/or administration of the whole or any substantial part of the business of the Bank were entered into or subsisting during the year.

DONATIONS

During the year, the Group made charitable and other donations amounting to approximately HK\$12,000 (2016: HK\$16,000).

CORPORATE GOVERNANCE

Details of the Bank's corporate governance practices are set out in the "Corporate Governance Report" in this Annual Report.

AUDITOR

Messrs PricewaterhouseCoopers shall retire and, being eligible, offer itself for re-appointment as the Bank's auditor at the 2018 AGM.

On behalf of the Board

Zhang Zhaoxing

Chairman

Hong Kong, 29 March 2018

CORPORATE GOVERNANCE PRACTICES

Chong Hing Bank Limited (the “Bank”) is an authorised institution supervised by the Hong Kong Monetary Authority (the “HKMA”) under the Hong Kong Banking Ordinance (the “Banking Ordinance”). The Bank is committed to maintaining high standards of corporate governance, with a view to safeguarding the interests of shareholders, customers, employees and other stakeholders.

The Bank has applied the principles in the Corporate Governance Code set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) and the module on “Corporate Governance of Locally Incorporated Authorised Institutions” (“CG-1”) under the Supervisory Policy Manual (“SPM”) issued by the HKMA to its corporate governance structure and practices.

Throughout the year ended 31 December 2017, the Bank complied with all the applicable code provisions set out in the Corporate Governance Code, except for deviations from the following code provisions:

1. Code Provision A.4.1 provides that non-executive directors should be appointed for a specific term, subject to re-election. None of the Non-executive Directors of the Bank was appointed for a specific term; however, all of them are subject to retirement by rotation and re-election at the annual general meeting of the Bank (“AGM”) in accordance with the Bank’s Articles of Association (the “Articles of Association”).
2. Rule 3.25 of the Listing Rules and Code Provision A.5.1 of the Corporate Governance Code provide that the remuneration committee and the nomination committee should comprise a majority of independent non-executive directors. Following the passing away of Mr Chiranakhorn Wanchai, the then Independent Non-executive Director of the Bank, on 23 January 2017, only half of the members of both the Remuneration Committee and the Nomination Committee of the Bank were Independent Non-executive Directors. The Board conducted a holistic review and put in place the new composition of the Remuneration Committee and the Nomination Committee with effect from 16 February 2017 in order to comply with the respective requirements under Rule 3.25 of the Listing Rules and Code Provision A.5.1 of the Corporate Governance Code.

The Bank has adopted its own code for securities transactions by Directors on 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 Listing Rules (the “Model Code”). All the Directors confirmed, following specific enquiry by the Bank, that they have complied with the required standards set out in the Model Code and the Bank’s own code for securities transactions by Directors throughout the year ended 31 December 2017.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

BOARD OF DIRECTORS

Roles and Responsibilities

The Board is ultimately responsible for the sustainable performance of the Bank and its subsidiaries (the “Group”), including the consistent achievement of business plans and compliance with statutory and corporate obligations. It is the ultimate decision-making body for all matters considered material to the Group and operates under defined Terms of Reference. The Board is also responsible for laying down strategic directions of the Group and overseeing their implementation by Senior Management, reviewing the operational and financial performance, and providing oversight to ensure that effective systems of risk management and internal control of the Group are in place.

While the Board delegates the day-to-day operations and administration of the Bank’s business to Senior Management, specific matters are reserved for the Board’s consideration and decision under its Terms of Reference, including but not limited to the Group’s long-term objectives and strategies, annual business plan and budget, capital planning and management policies, annual and interim financial reporting, major acquisitions and disposals, overall risk management strategy and framework, and corporate governance matters covering the development, implementation and monitoring of the corporate governance policies and practices.

During the year under review, the Board conducted a robust review of the Group’s corporate governance framework and updated its Terms of Reference and other Board Committees’ Terms of Reference to reflect best practices. The Board also adopted various policies as recommended by the Risk Committee, Remuneration Committee and Executive Committee and reviewed the Bank’s compliance with the Corporate Governance Code and the SPMs issued by the HKMA including the necessary disclosures in its reports to the shareholders of the Bank (the “Shareholders”).

Chairman and Chief Executive

The roles of the Chairman and the Chief Executive of the Bank are separate, with a clear division of responsibilities as set out in the Board’s Terms of Reference.

The Chairman of the Board, who is a Non-executive Director, is responsible for the leadership and effective running of the Board and for ensuring that decisions of the Board are taken on a sound and well-informed basis and in the best interest of the Group.

The Chief Executive, who is an Executive Director, is responsible for implementing the strategies and policies as established by the Board, including all day-to-day operations and administration, within the framework of the Group’s policies, reserved powers and routine reporting requirements.

Board Composition

As of 31 December 2017, the Board was made up of 12 members, comprising three Executive Directors, five Non-executive Directors and four Independent Non-executive Directors. There is a strong independent element on the Board that ensures the independence and objectivity of the decisions of the Board, as well as the thoroughness and impartiality of the Board's oversight of the management.

The composition of the Board is well balanced with each Director having sound board level experience and a diverse range of business, banking and professional expertise relevant to the business operations and development of the Group. Biographies of the Directors, which include relationships with the members of the Board, Senior Management and substantial shareholders (as defined in the Listing Rules) of the Bank, are set out in the "Biographical Details of Directors and Senior Management" section on pages 5 to 12 of this Annual Report.

The Bank has received from each of the Independent Non-executive Directors an annual confirmation of his independence. Following the assessment of the independence of the Independent Non-executive Directors in accordance with the guidelines set out in Rule 3.13 of the Listing Rules, the Board confirmed that all Independent Non-executive Directors continue to be independent.

All Directors are expressly identified by reference to their roles and functions and whether they are Executive Directors, Non-executive Directors and Independent Non-executive Directors in all corporate communications of the Bank that disclose their names. An updated list of the Directors (including their roles and functions) is available on the websites of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") and the Bank.

Appointment and Re-election of Directors

The Bank adopts a formal procedure in the selection of new Directors and nomination of retiring Directors for re-election by the Shareholders at general meetings.

The prospective director will first be assessed by the Nomination Committee, taking into account the balance of skills, knowledge, experience and diversity on the Board. Upon receiving the recommendation from the Nomination Committee, the proposed appointment will be considered and approved by the Board after due deliberation.

In accordance with the requirement under the Banking Ordinance, approval from the HKMA will be obtained for the appointment of new Directors.

All new Directors are subject to re-election by the Shareholders at the next AGM. None of the Non-executive Directors of the Bank was appointed for a specific term; however, all Directors are subject to retirement by rotation at the AGM at least once every three years in accordance with the Articles of Association. The retiring Directors shall be eligible for re-election.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

Board Process

Board meetings shall be held at least four times a year and no less than once every quarter. Additional Board meetings will be held as and when warranted.

Notice of meetings will be given to all Directors at least 14 days before each regular meeting to give them an opportunity to attend. Meeting agenda and accompanying board papers are sent to all Directors a week before the intended date of a Board meeting.

The Board has a standing agenda of items to ensure that matters relating to overall strategies, business plans, interim and annual results, corporate governance review, risk management and compliance are covered in its meetings at appropriate intervals.

Apart from those regular financial and business performance reports submitted to the Board for deliberation at the regular meetings, the Management provides monthly updates to the Board members with information on the Bank's latest financial performance and any material variance from its annual business plan to enable them to discharge their responsibilities. Management also submits to the Board members regular reports regarding auditor's and regulators' findings and recommendations as well as loans and advances to connected parties for regular review and monitoring, where appropriate.

During the year under review, there were six Board meetings, all of which were convened in accordance with the Articles of Association and attended by the Directors either in person or through electronic means of communication. In addition to the formal Board meetings, the Chairman has regular gatherings with Directors, occasionally without the presence of the Executive Directors and Senior Management, to consider issues in an informal setting. During 2017, a total of 13 Board lunches and dinners were held, and the Chairman held a meeting that was attended only by Non-executive Directors and Independent Non-executive Directors.

All Directors are entitled to have access to board papers and related materials. Where queries are raised by Non-executive Directors, steps will be taken to respond as promptly and fully as possible. Any concerns raised or dissenting views expressed by the Directors in respect of any matter discussed at a Board meeting will be reflected clearly in the minutes. Full minutes are being kept by the Company Secretary and such minutes are open for inspection at any time during office hours on reasonable notice by any Director.

All Directors are entitled to seek independent professional advice for the purpose of discharging their duties at the Bank's expense.

Non-executive Directors have devoted sufficient time and attention to the affairs of the Bank.

The Bank has put in place procedures to deal with Directors' conflict of interest. Directors are required to declare their direct/indirect interests, if any, in any proposed transactions to be considered by the Board and, where appropriate, they should abstain from voting on the proposed transactions and should not be counted in the quorum.

Appropriate Directors' and Officers' liability insurance cover has been arranged to indemnify the Directors and Officers against liabilities arising out of corporate activities. The coverage and the sum insured for 2017/2018 was reviewed and renewed.

Attendance Records

The attendance records of individual Directors at the Board, Board Committee meetings and 2017 AGM held in 2017 are as follows:

Names of Directors	2017							2017 AGM
	Number of Meetings Attended/Required Meetings to Attend							
	Board	Audit Committee	Transactions Committee	Executive Committee	Nomination Committee	Remuneration Committee	Risk Committee	
Connected Party								
Chairman and Non-executive Director								
Mr ZHANG Zhaoxing	5/6	-	-	-	2/2	4/4	-	1/1
Executive Directors								
Mrs LEUNG Ko May Yee Margaret ⁽¹⁾	6/6	-	-	13/13	-	-	1/1	1/1
Mr ZONG Jianxin	6/6	-	-	13/13	-	-	-	1/1
Mr LAU Wai Man	6/6	-	-	12/13	-	-	-	1/1
Non-executive Directors								
Mr ZHU Chunxiu	5/6	-	-	-	2/2	-	3/5	0/1
Mr WANG Shuhui	6/6	3/5	-	-	-	-	-	1/1
Mr LI Feng	6/6	-	-	-	-	-	5/5	1/1
Mr CHOW Cheuk Yu Alfred ⁽²⁾	6/6	5/5	2/2	-	-	4/4	1/1	1/1
Independent Non-executive Directors								
Mr CHIRANAKHORN Wanchai ⁽³⁾	-	-	-	-	-	-	-	-
Mr CHENG Yuk Wo ⁽⁴⁾	6/6	5/5	2/2	-	2/2	-	4/4	1/1
Mr MA Chiu Cheung Andrew ⁽⁵⁾	5/6	-	2/2	-	1/1	4/4	-	0/1
Mr LEE Ka Lun ⁽⁶⁾	5/6	5/5	-	-	1/1	3/3	4/4	1/1
Mr YU Lup Fat Joseph ⁽⁷⁾	6/6	5/5	-	-	1/1	4/4	5/5	1/1

Notes:

- (1) Mrs Leung ceased to act as a member of the Risk Committee on 16 February 2017.
- (2) Mr Chow ceased to act as the deputy chairman of the Risk Committee on 16 February 2017 and was appointed as a member of the Audit Committee on the same day.
- (3) Mr Chiranakhorn passed away on 23 January 2017.
- (4) Mr Cheng was appointed as a member of the Risk Committee on 16 February 2017.
- (5) Mr Ma ceased to act as a member of the Audit Committee on 16 February 2017 and was appointed as a member of the Nomination Committee on the same day.
- (6) Mr Lee ceased to act as a member of the Nomination Committee on 16 February 2017 and was appointed as a member of the Remuneration Committee and the chairman of the Risk Committee on the same day.
- (7) Mr Yu was appointed as the chairman of the Nomination Committee on 16 February 2017.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

Board Effectiveness

During the year ended 31 December 2017, the Board conducted an annual review of its effectiveness by way of an evaluation survey (the "Survey") and received responses from all Directors. The scope of the Survey required Directors to consider the performance and effectiveness of the Board and its Board Committees including the composition, structure, dynamics, operation and diversity. The overall feedback was positive and encouraging. The evaluation revealed that the Board and all the Board Committees continue to perform well with a strong composition and operate to a high standard.

Induction and Ongoing Development

The Bank provides each Director with personalized induction, training and development. On appointment, each new Director receives a comprehensive and tailored induction covering, among others, information about the Group's operations and business, the roles and responsibilities of the Board and its key Board Committees, the Bank's governance structure and practices, and the ambit of the internal audit and risk management functions.

On an ongoing basis, all Directors are provided with briefings and trainings in order to keep them continually updated on the Group's business and the latest developments of the Listing Rules and other applicable laws, rules and regulations to ensure the continued enhancement of their knowledge and skills. Such briefings and trainings are provided at the Bank's expense.

During the year, the Bank organized a Board Strategy Day and provided a number of trainings and briefings to the Directors which covered such topics as internal capital targets, IFRS 9 "Financial Instruments", corporate culture of the Bank and latest regulatory updates. Certain Directors also visited several branches and back-end offices in Hong Kong where Directors had an in-depth review of the Bank's business operations.

All Directors are required to provide their training records to the Bank on an annual basis. The training received by the Directors during the year under review is summarized as follows:

Names of Directors	Regulatory Updates	Articles/Seminars/Conferences relevant to the Bank's business and corporate governance
Chairman and Non-executive Director		
Mr ZHANG Zhaoxing	√	√
Executive Directors		
Mrs LEUNG Ko May Yee Margaret	√	√
Mr ZONG Jianxin	√	√
Mr LAU Wai Man	√	√
Non-executive Directors		
Mr ZHU Chunxiu	√	√
Mr WANG Shuhui	√	√
Mr LI Feng	√	√
Mr CHOW Cheuk Yu Alfred	√	√
Independent Non-executive Directors		
Mr CHENG Yuk Wo	√	√
Mr MA Chiu Cheung Andrew	√	√
Mr LEE Ka Lun	√	√
Mr YU Lup Fat Joseph	√	√

Policy Statement on Board Diversity

The Bank recognizes and embraces the benefits of having a Board composed of a diverse range of experience, which is an essential element in supporting the attainment of the Bank's strategic objectives and achieving sustainable commercial success of the Bank.

Board diversity has been considered from various aspects in designing the Board's composition, including gender, age, cultural and educational background, industry or related experience, ethnicity, professional experience, skills, knowledge and length of service. All Board appointments will be based on meritocracy, and candidates will be considered against objective criteria, having due regard for the benefits of diversity on the Board.

The diverse culture helps promote critical thinking and foster constructive debate, thereby enabling the Board to provide strategic direction to the management and to ensure the decision-making process is fair and balanced. All of these are essential in achieving a sustainable and balanced development of the Group.

This policy statement is not intended to, and does not, either enlarge or diminish the responsibilities of the Directors under the Articles of Association and such other relevant laws, rules, regulations, codes, guidelines, practice notes, circulars and the like. This policy statement is, however, intended to serve as a source of guiding principles for Directors to take appropriate actions to achieve the aims of board diversity as outlined above. The Board will review and, where appropriate, revise from time to time this policy statement in light of experience, evolving standards of corporate governance and any other changing circumstances.

Company Secretary

All Directors have access to the advice and services of the Company Secretary. The Company Secretary is responsible for ensuring the Board policies and procedures are followed and for facilitating information flows and communications among Directors as well as with Shareholders and Management.

The Company Secretary's biography is set out in the "Biographical Details of Directors and Senior Management" section on page 12 of this Annual Report. During the year of 2017, the Company Secretary undertook over 15 hours of professional training to update her skills and knowledge.

BOARD COMMITTEES

The Board has delegated its authorities to various committees, namely the Audit Committee, the Connected Party Transactions Committee, the Executive Committee, the Nomination Committee, the Remuneration Committee and the Risk Committee which operate under defined Terms of Reference. Composition and Terms of Reference of the Board Committees are reviewed and updated regularly to ensure that they remain appropriate and in line with the Group's business and changes in governance practices.

Terms of Reference of the respective Board Committees are available on the websites of the Stock Exchange and the Bank.

Each Board Committee has been provided with sufficient resources to discharge its duties.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

Audit Committee

The Audit Committee currently consists of five members, including three Independent Non-executive Directors and two Non-executive Directors.

Under its Terms of Reference, the Audit Committee is required, among other things, to make recommendations to the Board on the appointment, reappointment and removal of the external auditor, to review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process in accordance with the applicable standards, to review any engagement of external auditor for the provision of non-audit services, to review the half-year and annual reports and accounts before submission to the Board, to receive audit reports and review the external auditor's management letter, to review the HKMA's on-site examination reports and bring major findings to the attention of the Board, and to assess and consider the adequacy and effectiveness of the Group's systems of internal control, financial reporting and controls, risk management and regulatory compliance.

Five committee meetings were held in 2017 and the attendance records of the Audit Committee members are set out on page 49 of this Annual Report. The major work performed by the Audit Committee during the year included:

- (i) met with the external auditor and the Bank's senior executives in charge of Finance and Capital Management to discuss the financial statements for the year ended 31 December 2016 and for the six months ended 30 June 2017;
- (ii) reviewed and discussed with the external auditor to ensure that the Group's financial statements had been prepared in accordance with the accounting principles generally accepted in Hong Kong;
- (iii) reviewed the independence and objectivity of the external auditor and the scope of audit services;
- (iv) reviewed the audit fees payable to the external auditor and recommended to the Board for approval, and reviewed the non-audit services provided by the external auditor to the Group and the related fees;
- (v) met and discussed with the external auditor on the audit strategy and assessment of the sufficiency of the internal control of the Group;
- (vi) reviewed the internal control issues and the internal audit function of the Group, covering the annual internal audit plan, the staffing, resources and performance of Internal Audit Department, the audit findings and recommendations raised in the internal audits undertaken, and the implementation status of related audit recommendations;
- (vii) approved the revised Internal Audit Policy;
- (viii) reviewed the Bank's proposed procedure for implementing the quarterly regulatory disclosure pursuant to the amended Banking (Disclosure) Rules and recommended to the Board for adopting the procedure;
- (ix) reviewed the Bank's progress for the adoption of HKFRS 9; and
- (x) reviewed and updated its Terms of Reference.

Auditors' Remuneration

The remuneration paid and payable to the Group's auditor, PricewaterhouseCoopers, for 2017 amounted to:

	<i>HK\$'000</i>
Audit services and interim review	6,263
Tax service	504
Other service	413
Total	<u>7,180</u>

Connected Party Transactions Committee

The Connected Party Transactions Committee currently consists of five members, including one Non-executive Director, two Independent Non-executive Directors, the Chief Financial Officer and the Chief Risk Officer of the Bank.

Under its Terms of Reference, the Connected Party Transactions Committee is responsible for reviewing the robustness of the Bank's control framework to ensure proper compliance with all legal and regulatory requirements, Listing Rules together with accounting requirements (promulgated in Hong Kong and other jurisdictions) as may be applicable and approving significant connected transactions.

Two committee meetings were held in 2017 and the attendance records of the three Connected Party Transactions Committee members who are also Directors are set out on page 49 of this Annual Report.

During the year, the Connected Party Transactions Committee reviewed and recommended to the Board for approval various connected transactions between the Group and the members of Guangzhou Yue Xiu Holdings Limited, including the renewal of tenancy agreement and property management agreement, and the entering into the information technology framework agreement.

Executive Committee

The Executive Committee currently consists of nine members, including three Executive Directors and other senior executives of the Bank.

The Executive Committee exercises its powers, authorities and discretions as delegated by the Board to manage the day-to-day operations of the Group in accordance with its Terms of Reference and such other policies and directives as the Board may determine from time to time.

The Executive Committee has established the Asset and Liability Management Committee, the Disciplinary Committee, the Information Technology Committee and the Risk Management Committee with defined Terms of Reference that are in line with best practices. The above specialized sub-committees report directly to the Executive Committee and are responsible for overseeing assets and liabilities, staff disciplinary-related issues, overall information technology strategy as well as major risk and compliance issues of the Group.

13 committee meetings were held in 2017 and the attendance records of the Executive Directors are set out on page 49 of this Annual Report.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

Nomination Committee

The Nomination Committee currently consists of five members, including three Independent Non-executive Directors and two Non-executive Directors.

Under its Terms of Reference, the Nomination Committee is responsible for, among others, reviewing and making recommendations to the Board on the structure, size and composition of the Board and identifying potential candidate suitably qualified to become director of the Bank.

Two committee meetings were held in 2017 and the attendance records of the Nomination Committee members are set out on page 49 of this Annual Report. The primary duties performed by the Nomination Committee during the year included:

- (i) recommended to the Board on the renewal of the service agreement of Mrs Leung Ko May Yee Margaret and the re-designation of the roles and responsibilities for Mrs Leung and Mr Zong Jianxin;
- (ii) recommended to the Board on the new hiring of Deputy Managing Director and the appointment of Chief Financial Officer and Chief Operating Officer;
- (iii) reviewed the structure, size and composition (including the skills, knowledge, experience and diversity) of the Board and its committees and made recommendations to the Board;
- (iv) reviewed the efficiency and effectiveness of the functioning of the Board and its committees;
- (v) assessed and confirmed the independence of the Independent Non-executive Directors of the Bank;
- (vi) nominated candidates to the Board for it to recommend the candidates to stand for re-election as Directors by Shareholders at the 2017 AGM; and
- (vii) reviewed and updated its Terms of Reference.

Remuneration Committee

Authority and Responsibility

The Bank has established a Remuneration Committee with specific Terms of Reference to entrust it with the authority and responsibilities for, among others, making recommendation and reviewing the Remuneration Policy of the Group by taking into account the pay and conditions across the Group's individual remuneration packages for Directors, Senior Management and Key Personnel as well as those in positions of significant influence and those having an impact on the Group's risk profile; ensuring that the remuneration frameworks and decisions shall be developed in a manner that is in line with the Group's risk appetite, risk culture and long-term interests; ensuring that no individual Director, Chief Executive or any of their associates will be involved in deciding his/her own remuneration; and assisting the Board in carrying out the Bank Corporate Culture-related duties.

The Remuneration Committee currently consists of five members, including three Independent Non-executive Directors and two Non-executive Directors.

Remuneration Structure

The remuneration system of the Group is composed mainly of fixed remuneration (cash-based) with performance based variable remuneration (in cash-based discretionary performance-related bonus and/or incentive) which not only conforms with the risk appetite and aligns with the long-term value creation and time horizon of risk of the Group to grow steadily and prudently by encouraging long-term performance rather than short-term risk taking, but also motivates, recognizes, rewards and retains both outstanding individual contribution and sound team performance. The proportion and amount of fixed and variable remuneration shall be of an appropriate balance and vary according to an employee's seniority, role and responsibilities within the Group, also the market benchmarking and trend.

Performance Management

The Group uses a Balanced Scorecard (the "Scorecard") approach to measure and manage performance at the levels of the Group, business/functional units and individual employees. With reference to corporate goals and objectives at the beginning of financial year and when necessary, the Remuneration Committee reviews the Key Performance Indicators ("KPIs") and the corresponding target levels of the Group and recommends to the Board for approval. The annual targets of the Group will be cascaded down under the Balanced Scorecard Framework whereby the performance would be assessed from the dimensions of financial, customer, internal process and people management.

Each dimension of the Scorecard is comprised of a set of KPIs to assess the performance according to the specific areas of responsibility of the Group, business/functional units and individual employees; both financial and non-financial performance indicators are required to ensure a balanced evaluation. To ensure independence, financial KPIs should not be applicable to those risk control unit/personnel whose performance should be evaluated by their performance objectives and independent of the performance of the business areas which they oversee. Under the current performance management system, apart from evaluating individuals' KPIs, the assessment of Core Competency has been incorporated. The Group has developed six Core Competencies and their related behavioral descriptors so as to ensure employees clearly understand the required attitude and behaviors to achieve the defined core values and corporate culture of the Group.

To put the principle of aligning performance and remuneration with risk into practice, on top of the mentioned KPIs and Core Competencies, a Risk/Compliance & Control Modifier is in place in the performance management system to take into account any risk factors, control and compliance event, also its severity and impact to be fully reflected on the performance rating of the Group, business/functional units and individual employees.

In respect of risk management, the Bank has developed a complete Risk Appetite Statement and Key Risk Indicators as the basis for monitoring, assessing and controlling the Group's risk profile. In the Risk Modifier Framework of the Corporate Scorecard for 2017, seven major areas including credit risk, market risk, interest rate risk, liquidity risk, operational risk, compliance risk and risk culture are taken into account when computing a Corporate Scorecard Risk Modifier.

The Compliance and Risk Control assessment at individual level covers the employee's compliance, risk control and ethical standard. This includes, but is not limited to, the performance of the assessed employee in controlling various risks (e.g. credit, compliance, operations and reputation etc.), the risk management ratings, compliance reports or audit reports related to the performance of the assessed employee, verbal or written warnings etc.

Risk/Compliance & Control Modifier can be applied to adjust the annual performance score in response to any relevant performance. Poor performance can result in a deduction of the total score, which in turn affects the magnitude and amount of variable remuneration.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

Award of Variable Remuneration

The size of the overall variable bonus pool of the Group is determined according to the risk/compliance adjusted performance of the Group together with the consideration of all necessary factors (including capital position, market and peers business conditions, market competitiveness, material or potential risks involved in the business, and the extent to which the risks affect the Group as a whole), as recommended by Remuneration Committee to the Board for approval and is subject to the Board's discretion.

The subsequent allocation of variable bonus to each business/functional unit and an individual employee is based on the overall performance of the relevant business/functional unit, as well as the performance of the individual employee; while the performance assessment of the units and employees is based on the final risk-adjusted performance rating in the Scorecards.

Poor performance (either financial or non-financial) will result in a reduction or elimination of variable bonus at any level. Adverse performance in non-financial factors, where appropriate, should override outstanding financial achievements. The overall performance (including compliance and risk control factors) of a business/functional unit or an individual employee could be thoroughly assessed, rather than solely relying on its/his/her financial performance. This ultimately helps mitigate risk to the Group and align with its long-term value creation.

To ensure independence, the remuneration of risk control personnel is determined in accordance with their performance objectives and commensurate with their key role in the Group. To avoid possible undue influence from business units, risk control personnel are compensated in a manner that is independent of the performance of the business unit which they oversee.

Deferral Arrangements

The award of variable bonus to employee is subject to deferment in such a manner as determined by the Remuneration Committee. Deferral of the payment of a portion of variable bonus will allow employees' performance, including the associated risks, to be observed and validated over a period of time before the payment is actually made. In general, the overall level of their variable bonus as a multiple of their fixed salary is subject to deferment. Deferral period can last for 3 years the longest.

The award of deferred bonus is subject to a minimum vesting period and pre-defined vesting conditions as determined by the Remuneration Committee and communicated to all relevant employees. Deferred bonus is awarded in such a manner so as to align the relevant employees' variable awards with long-term value creation and the time horizons of risk. The future performance (both financial and non-financial) of the Group, relevant business/functional units, and individual employees are taken into consideration when approving the vesting arrangement. In circumstances where it is later established that any performance measurement for a pre-defined year was based on data that is later proven to have been manifestly misstated, or it is later established that the relevant employee has committed fraud, malfeasance, or a violation of internal control policies, any unvested portions of the deferred variable bonus (relating to that particular year in question) should be forgone, either in part or in whole, as determined by the Remuneration Committee.

External Remuneration Consultant

Appointed by the Board, the Remuneration Committee is authorised to obtain professional advice as it deems appropriate and is responsible for the selection and appointment of consultants to advise it on all aspects of remuneration.

In order to effectively realize the concept of Pay for Performance, the Group appointed Willis Towers Watson (“WTW”) to review and analyze the current status of the Group and set out the recommendations and actions forward in the pay for performance management system for consideration.

Summary of Work

Four committee meetings were held in 2017 and the attendance records of the Remuneration Committee members are set out on page 49 of this Annual Report. The major works performed by the Remuneration Committee during the year included:

- (i) reviewed the performance indicators of the Corporate Scorecard of the Bank for 2017 and the estimated achievement of targets; reviewed the proposal for the 2017 bonus pool available for distribution and recommended to the Board for approval;
- (ii) reviewed the salary adjustment proposal for 2017 and the variable bonus payment for 2016 for the Executive Directors, Senior Management and Key Personnel and recommended to the Board;
- (iii) reviewed the Bank-level 2015 deferred bonus vesting arrangement and the 2018 annual salary review proposal and recommended to the Board;
- (iv) reviewed the new China remuneration structure;
- (v) reviewed the annual Directors’ Fees of the Bank and recommended to the Board;
- (vi) reviewed the “Chong Hing Bank Corporate Culture” philosophy and implementation plan and recommended to the Board for approval;
- (vii) reviewed the update of the Bank’s Remuneration Policy and its Appendix with regard to the HKMA guideline of Bank Culture Reform, the SPM Module CG-1 (version 3) and the annual review and recommended to the Board for approval;
- (viii) received the reports on Independent Review against HKMA’s SPM Module “CG-5 Guideline on a Sound Remuneration System” (“CG-5”) by WTW and the project progress update on “Grading Structure Design” and “Pay for Performance Review”; and
- (ix) reviewed and updated its Terms of Reference.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

The emolument payable to Directors will depend on their respective contractual terms under employment contracts, if any, and the recommendations made by the Remuneration Committee. Details of the Directors' emolument are set out in note 42 to the consolidated financial statements. According to CG-5 and defined in the Remuneration Policy of the Group, Senior Management refers to Executive Directors, Deputy Managing Director and the Chief Functional Officers; Key Personnel refers to individual positions whose duties or activities involve the assumption of material risk or the taking on of material exposures on behalf of the Group and Heads of control functions. There are currently 7 and 9 employees categorised as Senior Management and Key Personnel respectively. The aggregate payouts for these senior executives for 2016 and 2017 are shown in the table below in accordance with the disclosure requirement under paragraph 3.2.3 of CG-5 issued by the HKMA on 12 March 2015.

The remuneration for the Senior Management and Key Personnel for the years ended 31 December 2016 and 2017, which was entirely paid in cash, is as follows:

Senior Management	Year ended 31 December 2017		Year ended 31 December 2016	
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	Non-deferred	Deferred	Non-deferred	Deferred
Fixed remuneration:	38,291	–	35,390	–
– Cash	38,291	–	35,390	–
– Shares and share-linked instrument	N/A	N/A	N/A	N/A
– Others	N/A	N/A	N/A	N/A
Number of beneficiaries	9	–	7	–
Variable remuneration:	429	–	6,930	940
– Cash	429	–	6,930	940
– Shares and share-linked instrument	N/A	N/A	N/A	N/A
– Others	N/A	N/A	N/A	N/A
Number of beneficiaries	3	–	5	2
– Vested	–	940	–	776
– Unvested	–	–	–	–
– Awarded	–	–	–	–
– Paid out	–	–	–	–
– Reduced through performance adjustments	–	–	–	–

Remarks:

There was a transition of Chief Operating Officers (“COO”) in the Group on 22 May 2017. The above disclosed figures consist of the total remuneration of the former and current COOs for their service tenures.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

Key Personnel	Year ended 31 December 2017		Year ended 31 December 2016	
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
	Non-deferred	Deferred	Non-deferred	Deferred
Fixed remuneration:	23,633	–	18,025	–
– Cash	23,633	–	18,025	–
– Shares and share-linked instrument	N/A	N/A	N/A	N/A
– Others	N/A	N/A	N/A	N/A
Number of beneficiaries	10	–	8	–
Variable remuneration:	2,621	200	3,182	328
– Cash	2,621	200	3,182	328
– Shares and share-linked instrument	N/A	N/A	N/A	N/A
– Others	N/A	N/A	N/A	N/A
Number of beneficiaries	7	1	6	2
– Vested	–	588	–	–
– Unvested	–	–	–	–
– Awarded	–	–	–	–
– Paid out	–	–	–	–
– Reduced through performance adjustments	–	–	–	–

Remarks:

There were additional positions categorized as Key Personnel in 2017. The above disclosed figures for 2017 consist of the remuneration of the additional positions.

	Year ended 31 December 2017	Year ended 31 December 2016
	HK\$'000	HK\$'000
Guaranteed Bonus	0	0
Number of beneficiaries	0	0
Sign-on Awards/Buy-out Payment	1,906	100
Number of beneficiaries	3	1
Severance Payment/Long Service Payment	0	521
Number of beneficiaries	0	2

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

The Remuneration Committee will continue to review and enhance the Group's Remuneration Policy in accordance with the principles and spirit of CG-1 & CG-5, with particular attention paid to risk adjustments to performance assessment; also alongside with the development of labor market, especially in the financial services sector, to evaluate and refine the remuneration provision so as to ensure that the rewards are competitive for the retention of talents.

Risk Committee

The Risk Committee currently consists of five members, including three Independent Non-executive Directors and two Non-executive Directors.

Under its Terms of Reference, the Risk Committee is required, among other things, to advise the Board on the overall risk appetite/tolerance and risk management strategies of the Group, and to oversee senior management's implementation of those strategies that are established and approved by the Board and aligned with the Bank's overall business objectives. In performing its role, the Risk Committee is supported by the Bank's Risk Management Committee and its specialized sub-committees.

Five committee meetings were held in 2017 and the attendance records of the Risk Committee members are set out on page 49 of this Annual Report. The major duties performed by the Risk Committee during the year included:

- (i) reviewed the overall risk management strategies and risk appetite/tolerance statement(s) of the Group and recommended to the Board for approval and received regularly the risk level rating for each risk type;
- (ii) reviewed and assessed regularly the adequacy and effectiveness of the Group's risk management framework, internal control systems and risk management policies, procedures and systems, and monitored their effective operation, implementation and maintenance;
- (iii) monitored the implementation progress of the risk management module under the substantial upgrade of the Bank's information technology system;
- (iv) monitored the implementation progress of the rectification measures taken by the Bank in response to the findings of the thematic examinations on risk-related matters conducted by the HKMA;
- (v) reviewed the governance structure of the Bank;
- (vi) reviewed the revised Liquidity Risk Management Policy of the Bank and recommended to the Board for approval;
- (vii) reviewed the 2017 Business Continuity Planning Policy of the Bank;
- (viii) received the Bank's progress for the adoption of HKFRS 9 and the assessment conducted under the Cyber Resilience Assessment Framework of the HKMA;

- (ix) provided oversight on the independence of staff members responsible for implementing risk management systems and controls;
- (x) reported significant risk management issues to the Board as set out in its Terms of Reference; and
- (xi) reviewed and updated its Terms of Reference.

During the year under review, the Risk Committee held meetings with the risk management function and the Bank's Chief Risk Officer separately without the Executive Directors present. The Committee also met with the representatives of the HKMA to maintain a regular dialogue with the regulator and to keep posted of the HKMA's general views of its supervisory focus.

ACCOUNTABILITY AND AUDIT

Financial Reporting

The Board is responsible for presenting a balanced, clear and comprehensible assessment of the Group's performance, financial results and prospects to Shareholders and other stakeholders in a timely manner. The annual and interim results and other discloseable financial information of the Bank are published in accordance with the requirements of the Listing Rules and other applicable regulations and industry best practice.

Management provides the Board with sufficient explanation and information to enable it to make an informed assessment of the Group's financial and other information put before it for approval.

The Directors also receive monthly financial and business updates with information on the Bank's latest financial performance and any material variance from its annual business plan to enable them to discharge their duties and responsibilities.

The Directors acknowledge their responsibility for preparing the Bank's consolidated financial statements and ensuring that the preparation of the Bank's consolidated financial statements is in accordance with the relevant requirements and applicable standards. As at 31 December 2017, the Directors were not aware of any material uncertainties relating to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern.

The statement of the Bank's external auditor concerning its reporting responsibilities on the Bank's consolidated financial statements and the key audit matters identified in its audit are set out in the "Independent Auditor's Report" on pages 65 to 70 of this Annual Report.

Risk Management and Internal Control

The Board acknowledges that it is responsible for the Group's risk management and internal control systems and reviewing their effectiveness. Although such systems are designed to manage rather than eliminate the risk of failure to achieve business objectives and to provide reasonable but not absolute assurance against material misstatement or loss, the Bank is committed to establishing and maintaining appropriate and effective risk management and internal control systems so as to safeguard Shareholders' investment and the Bank's assets.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

The Bank's risk governance framework is substantiated by the clearly defined three lines of defence which are independent from each other. In short, the first line of defence is provided by the business units where risks are taken. The second line of defence is provided by the risk management and compliance functions that are responsible for overseeing the Bank's risk-taking activities and ensuring compliance with laws and regulations. The third line of defence is provided by the Internal Audit Department which is responsible for providing assurance on the effectiveness of the Bank's risk management framework.

The risk management and internal control systems of the Group comprise comprehensive policies and standards under a well-established organisational structure:

- Policies and procedures have been designed for safeguarding assets against unauthorised use or disposition; for maintaining proper accounting records; for ensuring the reliability of financial information used within the business or for publication; and for ensuring compliance with applicable laws, rules and regulations. Systems and procedures are also in place to identify, evaluate, manage and report on the major types of risks, including credit, liquidity, market, operational, legal and reputational risks. All these policies and systems are regularly reviewed to reflect changes in markets, products and best practices.
- Areas of responsibilities of each business/functional unit are clearly defined to ensure effective checks and balances. Each unit is responsible for the assessment of individual types of risks arising under its areas of responsibilities, the management of the risks in accordance with the established risk management procedures, and the reporting on such risk management issues.
- Specialised committees are established for the oversight and monitoring of major risk areas. Regular risk management reports prepared by relevant business and functional units are submitted to the Asset and Liability Management Committee, the Risk Management Committee, the Executive Committee and the Risk Committee, and ultimately to the Board for oversight and monitoring of the respective types of risks on an ongoing basis. The Bank's risk management policies and major control limits are reviewed and recommended by the relevant specialised committees to the Board for approval, and are monitored and reviewed regularly according to established policies and procedures.
- The Internal Audit Department's role as the third line of defence is independent of the first and second lines of defence, with the Bank's Chief Auditor reporting directly to the Audit Committee. Pursuant to a risk-based approach, the Internal Audit Department conducts independent and objective assessment of the design and implementation of the risk management and control mechanisms of the Bank's business and functional units in order to identify any inadequacy. Results of audit work are reported regularly to the Audit Committee.
- The Bank has established a whistleblowing policy which encourages employees to raise concerns, in confidence, about possible improprieties in any matter related to the Bank. The Bank treats all information received confidentially and protects the identity and the interests of all whistleblowers.

The Board has, through the Audit Committee and the Risk Committee, monitored the performance of the Group's risk management and internal control systems on an ongoing basis and also completed the 2017 annual review of their effectiveness, which covered such material aspects as financial, operational and compliance controls. The Board has received a confirmation from management on the effectiveness of the Group's risk management and internal control systems and is satisfied that such systems, including the resources, staff qualifications and experience, training programmes and budget of the Group's accounting, internal audit and financial reporting functions, are effective and adequate.

COMMUNICATIONS WITH SHAREHOLDERS

Effective Communication

The Bank recognizes the importance of communication and undertakes to maintain an ongoing dialogue with the Shareholders through general meetings, press releases, announcements and corporate communications such as annual report, interim report and circulars. The Board is committed to the timely disclosure of information. The latest information regarding the Bank's activities, announcements, circulars, press releases and corporate communications is made available on the Bank's website at www.chbank.com in a timely manner. The Shareholders' calendar containing important dates for Shareholders is set out on page 14 of this Annual Report for the Shareholders' reference.

A Shareholders' Communication Policy was adopted by the Board and such policy will be reviewed on a regular basis to ensure its effectiveness. Shareholders and other stakeholders may at any time send their enquires and concerns to the Board by addressing them to the Chief Financial Officer by post to the Bank's registered office at Ground Floor, Chong Hing Bank Centre, 24 Des Voeux Road Central, Hong Kong or by email to info@chbank.com.

General Meetings

The Bank aims at maintaining an ongoing dialogue with the Shareholders and, in particular, using AGMs or other general meetings as a forum for effective communication with the Shareholders. The Chairman of the Board and Chairmen of the Board Committees are available to answer questions from the Shareholders in relation to the performance of the Bank at the AGMs. In addition, the external auditor of the Bank is invited to attend the AGMs to answer questions about the conduct of the audit, the preparation and content of the auditor's report, the accounting policies and the auditor's independence. Separate resolutions are proposed at general meetings on each substantial issue, including the election and re-election (as the case may be) of individual Directors.

The Bank held its 2017 AGM on 18 May 2017. Poll results in respect of the resolutions proposed at the 2017 AGM were published on the websites of the Stock Exchange and the Bank on the same day.

The 2018 AGM will be held on 18 May 2018, and the relevant details are set out in the circular to the Shareholders sent together with this Annual Report.

Voting Procedures at General Meetings

All resolutions put to vote at the general meetings of the Bank (other than on procedural and administrative matters) must be taken by poll. At each general meeting, an explanation of the detailed procedures of conducting a poll will be provided to the Shareholders, and questions from the Shareholders regarding voting by poll will also be answered to ensure that Shareholders are familiar with such procedures. The poll results will be posted on the websites of the Stock Exchange and the Bank on the same day following the general meeting.

Shareholders' Rights

1. General Meeting

Shareholder(s) may request to call a general meeting. If such request is made by Shareholder(s) representing 5% of the total voting rights of all the Shareholders having a right to vote at general meetings, such general meeting must be called. Such request, either in hard copy form or in electronic form and being authenticated by the person or persons making it, must be deposited at the registered office of the Bank at Ground Floor, Chong Hing Bank Centre, 24 Des Voeux Road Central, Hong Kong or sent by email to info@chbank.com for the attention of the Company Secretary. Shareholder(s) shall make reference to the provisions under Sections 566 to 568 of the Companies Ordinance for requesting to call a general meeting.

CORPORATE GOVERNANCE REPORT

as of 29 March 2018

2. **Putting Forward a Resolution at an Annual General Meeting**

Pursuant to Section 615 of the Companies Ordinance, a request to put forward a resolution which may properly be moved at an AGM may be submitted by Shareholder(s) representing at least 2.5% of the total voting rights of all the Shareholders who have a right to vote on the resolution at the AGM to which the request relates, or by at least 50 Shareholders who have a right to vote on the resolution at the AGM to which the request relates. Such request must identify the resolution of which notice is to be given, be either in hard copy form or in electronic form, be authenticated by the person or persons making it, and be received by the Bank not later than six weeks before the AGM to which the request relates or, if later, the time at which notice is given of that AGM. The request must be deposited at the registered office of the Bank at Ground Floor, Chong Hing Bank Centre, 24 Des Voeux Road Central, Hong Kong or sent by email to info@chbank.com for the attention of the Company Secretary. Shareholder(s) should make reference to Sections 580 and 615 of the Companies Ordinance for the relevant procedures to put forward a resolution at an AGM.

3. **Proposing a Person for Election as a Director**

Shareholders can propose a person (other than a retiring Director or himself/herself) for election as a director at a general meeting of the Bank. Relevant procedures are available on the Bank's website at www.chbank.com.

Investor Relations and Information Disclosure

The Bank has put in place a Disclosure Policy for the disclosure of material information (including inside information) relating to its businesses, state of affairs, profit or loss and capital adequacy ratio to its stakeholders and the public in compliance with the disclosure obligations required by the Listing Rules, the Banking Ordinance, the Securities and Futures Ordinance and other applicable laws, rules and regulations.

The Disclosure Policy sets out the procedures and internal controls for the handling and dissemination of such information in a timely manner so as to enable the stakeholders and the public to appraise the latest position of the Group. The Disclosure Policy and its effectiveness are subject to review on a regular basis according to the established procedures.

CONSTITUTIONAL DOCUMENTS

During the year ended 31 December 2017, no change was made to the Articles of Association of the Bank, the latest version of which is available on the websites of the Stock Exchange and the Bank.

By Order of the Board

Lai Wing Nga

Company Secretary

Hong Kong, 29 March 2018

TO THE MEMBERS OF CHONG HING BANK LIMITED

(Incorporated in Hong Kong with limited liability)

Opinion

What we have audited

The consolidated financial statements of Chong Hing Bank Limited (the "Bank") and its subsidiaries (the "Group") set out on pages 73 to 209, which comprise:

- the consolidated statement of financial position as at 31 December 2017;
- the consolidated income statement for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Our opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2017, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and have been properly prepared in compliance with the Hong Kong Companies Ordinance.

Basis for Opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing ("HKSA") issued by the HKICPA. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

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

Independence

We are independent of the Group in accordance with the HKICPA's Code of Ethics for Professional Accountants ("the Code"), and we have fulfilled our other ethical responsibilities in accordance with the Code.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current year. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matters identified in our audit are summarised as follows:

- Valuation and impairment allowances of advances to customers
- Disclosure in relation to the new accounting standard, HKFRS 9 – Expected credit losses ("ECL")

Key Audit Matter

How our audit addressed the Key Audit Matter

Valuation and impairment allowances of advances to customers

As at 31 December 2017, the Group had individual impairment allowances and collective impairment allowances amounting to HK\$394 million and HK\$330 million respectively. The calculations of both individual and collective impairment allowances are inherently judgemental for the Group.

The individual impairment allowances calculation is judgemental because it requires the determination of when an impairment event has occurred and then to estimate the expected future cash flows related to that specific loan.

The collective impairment allowances are calculated using a collective impairment assessment model which requires significant management judgement to determine the key assumptions used in the key parameters (including loss factor, macro-economic factor and emergence period factor) and also management overlays applied.

The disclosures about the key sources of estimation uncertainty are set out in note 5(a), and the impairment allowances movement of advances to customers are detailed in note 21 to the consolidated financial statements.

We performed the following procedures in addressing valuation and impairment allowances of advances to customers:

1. Tested controls over management's identification of non-performing loans, which include controls over regular credit review and compilation and review of early warning list;
2. Evaluated, on a sample basis, the level of individual impairment allowances recorded for specific loans by challenging management on the judgement applied in the expected future cash flows estimation and re-performing the mathematical accuracy of management's discounted cash flow calculation; and
3. Evaluated the consistency in the application of the collective impairment assessment model and the key parameters. We also tested, on a sample basis, the accuracy and completeness of input data via re-performance. We further evaluated the management judgement applied in determining the assumption used in the key parameters and management overlays by comparing them to evidence obtained through external sources, our industry knowledge and market experience.

Based on the procedures we performed, we considered the impairment allowances of advances to customers were supportable by available evidence.

Key Audit Matter

How our audit addressed the Key Audit Matter

Disclosure in relation to the new accounting standard, HKFRS 9 – Expected credit losses ('ECL')

The accounting standard HKAS 8 requires disclosure of the reasonably estimable information relevant to assessing the possible impact that application of new accounting standards issued but not yet effective. HKFRS 9 took effect from 1 January 2018 and its application is considered as a highly complex process and requires considerable judgements and interpretations. In particular, our audit focused on the new models developed by the Group for estimating ECL on loans and advances to customers measured at amortised cost which is considered to be material to the Group's consolidated financial statements. New data inputs from systems that have not been used previously for the preparation of the accounting records will also be used in the new ECL models. In some cases where data is unavailable, judgements are applied in seeking reasonable alternatives to enable ECL calculations to be performed.

Management estimated the possible impact on ECL due to the initial application of HKFRS 9, which is disclosed in note 3 to the consolidated financial statements.

We performed the following procedures to assess the reasonableness of the Group's disclosed possible impact of the initial application of HKFRS 9:

1. Obtained an understanding and performed an assessment of the major modelling methodologies and assumptions with the assistance of our modelling specialists on portfolios producing material ECL amounts;
2. Tested the accuracy and completeness of key ECL model data inputs through testing the relevant key data input controls, tracing a sample population of key data to their source documents and data records maintained in various systems involved in the ECL computation; and
3. Assessed the management's review and challenge assessment on the ECL result. We also discussed the reasonableness of the best estimate with management and the Audit Committee.

Based on the procedures we performed, we considered the disclosure of estimated transitional impact of ECL was supportable.

INDEPENDENT AUDITOR'S REPORT

Other Information

The directors of the Bank are responsible for the other information. The other information comprises all of the information included in the annual report other than the consolidated financial statements and our auditor's report thereon, which we obtained prior to the date of this auditor's report, and the Unaudited Supplementary Financial Information and the Regulatory Disclosure for the year ended 31 December 2017, which are expected to be made available to us after the date of this auditor's report.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

When we read the Unaudited Supplementary Financial Information and the Regulatory Disclosure for the year ended 31 December 2017, if we conclude that there is a material misstatement therein, we are required to communicate the matter to the Audit Committee and take appropriate action considering our legal rights and obligations.

Responsibilities of Directors and the Audit Committee for the Consolidated Financial Statements

The directors of the Bank are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA and the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

The Audit Committee is responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, in accordance with Section 405 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. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with HKSAAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

INDEPENDENT AUDITOR'S REPORT

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Ms. Ng, Wai Ying.

PricewaterhouseCoopers

Certified Public Accountants

Hong Kong, 29 March 2018

73	Consolidated Income Statement
74	Consolidated Statement of Comprehensive Income
75	Consolidated Statement of Financial Position
76	Consolidated Statement of Changes in Equity
78	Consolidated Statement of Cash Flows
80	Notes to the Consolidated Financial Statements
80	1. General
80	2. Application of new and revised Hong Kong Financial Reporting Standards (“HKFRSs”)
80	3. New and revised HKFRSs issued but not yet effective
83	4. Significant accounting policies
104	5. Critical accounting judgements and key sources of estimation uncertainty
107	6. Segment information
114	7. Financial risk management
152	8. Financial assets and financial liabilities subject to offsetting, enforceable master netting arrangements and similar agreements
160	9. Net interest income
161	10. Net fee and commission income
162	11. Net (loss) income from trading and investments
163	12. Other operating income
164	13. Operating expenses
165	14. Taxation
166	15. Dividends
166	16. Earnings per share – basic and diluted
166	17. Cash and short-term funds
167	18. Derivative financial instruments
169	19. Investments in securities
172	20. Transfer of financial assets
173	21. Advances and other accounts
176	22. Subsidiaries
177	23. Interests in associates
178	24. Assets held for sale
179	25. Investment properties
181	26. Property and equipment
184	27. Prepaid lease payments for land

FINANCIAL STATEMENTS – CONTENTS

184	28. Financial assets sold under repurchase agreements
185	29. Deposits from customers
185	30. Certificates of deposit and debt securities issued
186	31. Loan capital
188	32. Share capital
188	33. Additional equity instruments
189	34. Deferred taxation
190	35. Share option scheme
191	36. Intangible assets
192	37. Contingent liabilities and commitments
194	38. Retirement benefits scheme
199	39. Related party transactions
201	40. Capital management
202	41. Statement of financial position and reserve movement of the Bank
206	42. Benefits and interests of directors
209	43. Immediate and ultimate holding companies

Unaudited Supplementary Financial Information

210	1. Major specialised committees
211	2. Management of risks
212	3. Capital adequacy ratios, leverage ratio and liquidity ratios
213	4. Other financial information
213	5. Segmental information
214	6. Advances to customers – by industry sectors
215	7. Advances to customers – by geographical areas
216	8. International claims
217	9. Currency risk
218	10. Overdue and rescheduled assets
220	11. Mainland activities exposures
222	12. Capital charge for credit, market and operational risks
224	13. Risk management
231	14. Basis of consolidation

CONSOLIDATED INCOME STATEMENT

for the year ended 31 December 2017

	Notes	2017 HK\$'000	2016 HK\$'000
Interest income		3,800,391	3,001,170
Interest expense		(1,483,263)	(956,370)
Net interest income	9	2,317,128	2,044,800
Fee and commission income		424,545	344,494
Fee and commission expenses		(97,074)	(84,910)
Net fee and commission income	10	327,471	259,584
Net (loss) income from trading and investments	11	(93,938)	230,059
Other operating income	12	158,895	139,853
Operating expenses	13	(1,353,633)	(1,227,552)
Operating profit before impairment allowances		1,355,923	1,446,744
Net (charge) reversal of impairment allowances on loans and advances	21	(371,591)	40,198
Impairment loss on investments in securities		(919)	(11,071)
Operating profit after impairment allowances		983,413	1,475,871
Net gains on disposal of assets held for sale		2,878	–
Net gains on disposal of property and equipment		654,619	24,757
Net gains on disposal of other investments	19	–	160,729
Net gains on disposal of and fair value adjustments on investment properties	25	12,632	2,026
Impairment loss on goodwill	36	–	(11,000)
Share of profits of associates	23	55,723	31,617
Profit before taxation		1,709,265	1,684,000
Taxation	14	(144,398)	(264,296)
Profit for the year			
– Attributable to equity owners of the Bank		1,564,867	1,419,704
Earnings per share – basic and diluted	16	HK\$2.17	HK\$1.94

The notes on pages 80 to 209 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December 2017

	2017 HK\$'000	2016 HK\$'000
Profit for the year	1,564,867	1,419,704
Other comprehensive income		
Items that may not be reclassified subsequently to profit or loss:		
Surplus on transfer of land and buildings to investment properties	–	16,229
Surplus on remeasurement of retirement benefit	5,647	–
Income tax effect relating to retirement benefit	(932)	–
Items that may be reclassified subsequently to profit or loss:		
Exchange differences arising on translation	249,271	(168,225)
Fair value gains of available-for-sale securities arising during the year	354,316	202,037
Amount reclassified to the profit or loss upon impairment of available-for-sale securities	290	11,071
Amount reclassified to the profit or loss upon disposal of available-for-sale securities	(113,937)	(178,309)
Income tax effect relating to disposal of available-for-sale securities	18,800	29,421
Income tax effect relating to fair value change of available-for-sale securities	(58,419)	(35,869)
Share of other comprehensive income of associates	4,647	497
Other comprehensive income for the year (net of tax)	459,683	(123,148)
Total comprehensive income for the year	2,024,550	1,296,556
Total comprehensive income attributable to:		
Equity owners of the Bank	2,024,550	1,296,556

The notes on pages 80 to 209 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

at 31 December 2017

	Notes	2017 HK\$'000	2016 HK\$'000
Assets			
Cash and short-term funds	17	25,164,641	30,521,281
Placements with banks maturing between one to twelve months		6,359,004	1,616,540
Derivative financial instruments	18	556,793	424,845
Investments in securities	19	39,153,501	29,727,952
Advances and other accounts	21	90,949,787	74,081,605
Tax recoverable		–	3,128
Assets held for sale	24	–	2
Interests in associates	23	301,337	262,565
Investment properties	25	298,765	282,927
Property and equipment	26	590,746	633,604
Prepaid lease payments for land	27	2,134	2,201
Deferred tax assets	34	–	4,672
Intangible assets	36	370,406	210,729
Total assets		163,747,114	137,772,051
Liabilities			
Deposits and balances of banks		3,051,932	2,696,681
Financial assets sold under repurchase agreements	28	12,002,989	9,845,753
Deposits from customers	29	118,758,674	102,880,629
Derivative financial instruments	18	882,279	553,614
Other accounts and accruals		1,577,588	1,243,889
Current tax liabilities		434,818	356,298
Certificates of deposit	30	3,217,451	812,329
Debt securities issued	30	1,796,069	1,663,774
Loan capital	31	4,541,380	1,792,267
Deferred tax liabilities	34	50,136	13,245
Total liabilities		146,313,316	121,858,479
Equity attributable to owners of the Bank			
Share capital	32	5,435,904	5,435,904
Additional equity instruments	33	2,312,030	2,312,030
Reserves		9,685,864	8,165,638
Total equity		17,433,798	15,913,572
Total liabilities and equity		163,747,114	137,772,051

The notes on pages 80 to 209 form an integral part of these consolidated financial statements.

Approved and authorised for issue by the Board of Directors on 29 March 2018 and signed on its behalf by:

Zhang Zhaoxing
Chairman

Leung Ko May Yee Margaret
Deputy Chairman and Managing Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2017

	Note	Share capital HK\$'000	Additional equity instruments HK\$'000	Goodwill HK\$'000	Investment revaluation reserve HK\$'000	Land and building 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 2017		5,435,904	2,312,030	(182)	169,620	174,247	1,388,500	(183,255)	739,000	5,877,708	15,913,572
Profit for the year		-	-	-	-	-	-	-	-	1,564,867	1,564,867
Exchange differences arising on translation		-	-	-	-	-	249,271	-	-	-	249,271
Surplus on remeasurement of retirement benefits		-	-	-	-	-	-	-	-	5,647	5,647
Income tax effect relating to retirement benefits		-	-	-	-	-	-	-	-	(932)	(932)
Fair value gains of available-for-sale securities arising during the year		-	-	-	354,316	-	-	-	-	-	354,316
Amount reclassified to the profit or loss upon impairment of available-for-sale securities		-	-	-	290	-	-	-	-	-	290
Amount reclassified to the profit or loss upon disposal of available-for-sale securities		-	-	-	(113,937)	-	-	-	-	-	(113,937)
Income tax effect relating to disposal of available-for-sale securities		-	-	-	18,800	-	-	-	-	-	18,800
Income tax effect relating to fair value change of available-for-sale securities		-	-	-	(58,419)	-	-	-	-	-	(58,419)
Share of other comprehensive income of associates		-	-	-	4,647	-	-	-	-	-	4,647
Other comprehensive income		-	-	-	205,697	-	249,271	-	-	4,715	459,683
Total comprehensive income for the year		-	-	-	205,697	-	249,271	-	-	1,569,582	2,024,550
Distribution payment for additional equity instruments		-	(151,974)	-	-	-	-	-	-	-	(151,974)
Transfer from retained profits		-	151,974	-	-	-	-	-	-	(151,974)	-
Interim dividend paid	15	-	-	-	-	-	-	-	-	(97,875)	(97,875)
Final dividend paid	15	-	-	-	-	-	-	-	-	(254,475)	(254,475)
Earmark of retained profits as regulatory reserve		-	-	-	-	-	-	-	77,000	(77,000)	-
At 31 December 2017		5,435,904	2,312,030	(182)	375,317	174,247	1,388,500	66,016	816,000	6,865,966	17,433,798

The notes on pages 80 to 209 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2017

	Note	Share capital HK\$'000	Additional equity instruments HK\$'000	Goodwill HK\$'000	Investment revaluation reserve HK\$'000	Land and building 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 2016		5,435,904	2,312,030	(182)	140,772	158,018	1,388,500	(15,030)	663,000	5,024,729	15,107,741
Profit for the year		-	-	-	-	-	-	-	-	1,419,704	1,419,704
Exchange differences arising on translation		-	-	-	-	-	-	(168,225)	-	-	(168,225)
Surplus on transfer of land and buildings to investment properties		-	-	-	-	16,229	-	-	-	-	16,229
Fair value gains of available-for-sale securities arising during the year		-	-	-	202,037	-	-	-	-	-	202,037
Amount reclassified to the profit or loss upon impairment of available-for-sale securities		-	-	-	11,071	-	-	-	-	-	11,071
Amount reclassified to the profit or loss upon disposal of available-for-sale securities		-	-	-	(178,309)	-	-	-	-	-	(178,309)
Income tax effect relating to disposal of available-for-sale securities		-	-	-	29,421	-	-	-	-	-	29,421
Income tax effect relating to fair value change of available-for-sale securities		-	-	-	(35,869)	-	-	-	-	-	(35,869)
Share of other comprehensive income of associates		-	-	-	497	-	-	-	-	-	497
Other comprehensive income		-	-	-	28,848	16,229	-	(168,225)	-	-	(123,148)
Total comprehensive income for the year		-	-	-	28,848	16,229	-	(168,225)	-	1,419,704	1,296,556
Distribution payment for additional equity instruments		-	(151,425)	-	-	-	-	-	-	-	(151,425)
Transfer from retained profits		-	151,425	-	-	-	-	-	-	(151,425)	-
Interim dividend paid	15	-	-	-	-	-	-	-	-	(97,875)	(97,875)
Final dividend paid	15	-	-	-	-	-	-	-	-	(241,425)	(241,425)
Earmark of retained profits as regulatory reserve		-	-	-	-	-	-	-	76,000	(76,000)	-
At 31 December 2016		5,435,904	2,312,030	(182)	169,620	174,247	1,388,500	(183,255)	739,000	5,877,708	15,913,572

The retained profits of the Group included retained profits of HK\$171,372,000 (2016: retained profits of HK\$130,859,000) retained by the associates 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 "HKMA").

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

The notes on pages 80 to 209 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

for the year ended 31 December 2017

	Note	2017 HK\$'000	2016 HK\$'000
OPERATING ACTIVITIES			
Profit before taxation		1,709,265	1,684,000
Adjustments for:			
Net interest income	9	(2,317,128)	(2,044,800)
Net charge (reversal) of impairment allowances on loans and advances		371,591	(40,198)
Net gains on disposal of assets held for sale		(2,878)	–
Net gains on disposal of property and equipment		(654,619)	(24,757)
Net gains on disposal of available-for-sale securities		(113,937)	(178,309)
Net gains on disposal of and fair value adjustments on investment properties		(12,632)	(2,026)
Share of profits of associates	23	(55,723)	(31,617)
Net gains on fair value hedge		(1,423)	(6,989)
Dividend received from investments	12	(8,211)	(11,790)
Depreciation	13	79,969	58,447
Release of prepaid lease payments for land	27	66	66
Impairment loss on goodwill		–	11,000
Impairment loss on loan and receivable securities		629	–
Impairment loss on available-for-sale securities		290	11,071
Exchange adjustments		376,428	(241,943)
Operating cash flows before movements in operating assets and liabilities		(628,313)	(817,845)
(Increase) decrease in operating assets:			
Money at call and short notice with original maturity over three months		232,620	929,473
Exchange fund bills with original maturity over three months		(256,978)	152,457
Placements with banks with original maturity over three months		(1,405,100)	5,994,434
Financial assets at fair value through profit or loss		(24)	30
Advances to customers		(15,951,609)	(7,030,729)
Advances to banks		388,427	(496,256)
Other accounts		(1,511,532)	(1,152,637)
Increase (decrease) in operating liabilities:			
Deposits and balances of banks		355,251	(3,031,632)
Financial assets sold under repurchase agreements		2,157,236	6,523,070
Deposits from customers		15,878,045	3,488,265
Certificates of deposit		2,405,122	460,367
Derivative financial instruments		312,004	181,489
Other accounts and accruals		39,940	133,848
Cash generated from operations		2,015,089	5,334,334
Hong Kong profits tax paid		(31,741)	(12,199)
Overseas tax paid		(30,857)	(31,087)
Interest received		2,691,838	2,104,067
Interest paid		(1,073,550)	(899,264)
NET CASH GENERATED FROM OPERATING ACTIVITIES		3,570,779	6,495,851

CONSOLIDATED STATEMENT OF CASH FLOWS

for the year ended 31 December 2017

	Note	2017 HK\$'000	2016 HK\$'000
INVESTING ACTIVITIES			
Interest received from available-for-sale securities and held-to-maturity securities		891,566	828,537
Dividends received on investments	12	8,211	11,790
Dividends received from associates		19,890	17,450
Purchase of held-to-maturity securities		(19,263)	–
Purchase of available-for-sale securities		(18,997,483)	(15,883,224)
Purchase of loan and receivable securities		(63,432)	–
Purchase of property and equipment		(133,276)	(82,389)
Purchase of intangible assets		(155,509)	(166,941)
Proceeds from redemption of held-to-maturity securities		1,933,433	3,093,664
Proceeds from sale and redemption of available-for-sale securities		7,992,916	14,502,715
Proceeds from disposal of assets held for sale		2,880	–
Proceeds from disposal of property and equipment		753,801	33,166
NET CASH (USED IN) GENERATED FROM INVESTING ACTIVITIES		(7,766,266)	2,354,768
FINANCING ACTIVITIES			
Net proceeds from issue of loan capital	31	2,816,997	–
Net proceeds from issue of debt securities		–	1,740,244
Interest paid on loan capital	31	(102,471)	(67,769)
Interest paid on debt securities issued	30	(58,349)	(1,188)
Dividends paid to ordinary shareholders	15	(352,350)	(339,300)
Distribution paid on additional equity instruments	33	(151,974)	(151,425)
NET CASH GENERATED FROM FINANCING ACTIVITIES		2,151,853	1,180,562
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS		(2,043,634)	10,031,181
CASH AND CASH EQUIVALENTS AT 1 JANUARY		29,053,408	19,022,227
CASH AND CASH EQUIVALENTS AT 31 DECEMBER		27,009,774	29,053,408
Represented by:			
Cash and balances with central bank and banks		9,593,548	4,009,869
Money at call and short notice with original maturity of three months or less		11,170,870	23,182,828
Exchange fund bills with original maturity of three months or less		2,097,187	1,049,906
Placements with banks maturing between one to twelve months with original maturity of less than three months		4,148,169	810,805
		27,009,774	29,053,408

The notes on pages 80 to 209 form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

1. GENERAL

Chong Hing Bank Limited (the “Bank”) is a public limited company incorporated in Hong Kong and its shares are listed on The Stock Exchange of Hong Kong Limited.

The Bank is engaged in the provision of banking and related financial services. The address of the registered office of the Bank is Ground Floor, Chong Hing Bank Centre, 24 Des Voeux Road Central, Hong Kong.

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

The following amendments to standards have been adopted by the Group for the first time for the financial year beginning on or after 1 January 2017 and are relevant to the Group:

- The amendments to Hong Kong Accounting Standard (“HKAS”) 12 “Income taxes” are on the recognition of deferred tax assets for unrealised losses and clarify how to account for deferred tax assets related to debt instruments measured at fair value.
- The amendments to HKAS 7 “Statement of cash flows” introduce an additional disclosure that will enable users of financial statements to evaluate changes in liabilities arising from financing activities.

There are also amendments to a standard effective for the accounting period beginning on or after 1 January 2017 but do not have material financial impact. Therefore, these amendments are not analysed in details.

3. NEW AND REVISED HKFRSs ISSUED BUT NOT YET EFFECTIVE

A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after 1 January 2017, and have not been applied in preparing these consolidated financial statements. None of these is expected to have a significant effect on the consolidated financial statements of the Group, except the following set out below:

HKFRS 9 Financial Instruments

Nature of change

HKFRS 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities, introduces new rules for hedge accounting and a new impairment model for financial assets.

Impact

The Group has reviewed its financial assets and liabilities and is expecting the following impact from the adoption of the new standard on 1 January 2018:

The Group’s debt instruments that are currently classified as held-to-maturity/loans and receivables which will continue to be measured at amortised cost under HKFRS 9, except for certain debt instruments will be reclassified to financial assets at fair value through other comprehensive income (“FVOCI”), the related fair value gains of HK\$41,109,000 will be recognised in the opening balance of equity on 1 January 2018.

The Group has assessed that for debt instruments that are currently classified as available-for-sale (“AFS”) will satisfy the conditions for classification as FVOCI and hence there will be no change to the accounting for these assets.

3. NEW AND REVISED HKFRSs ISSUED BUT NOT YET EFFECTIVE - continued

HKFRS 9 Financial Instruments - continued

Impact - continued

For equity instruments that are currently classified as AFS, the Group irrevocably elects to designate these securities as FVOCI, the gains or losses realised on the sale of such securities will no longer be transferred to profit or loss on sale, but instead reclassified below the line from the FVOCI reserve to retained earnings. For equity instruments currently measured at fair value through profit or loss, which will continue to be measured on the same basis under HKFRS 9.

There will be no impact on the Group's accounting for financial liabilities, as the new requirements only affect the accounting for financial liabilities that are designated at fair value through profit or loss and the Group does not have any such liabilities. The derecognition rules have been transferred from HKAS 39 Financial Instruments: Recognition and Measurement and have not been changed.

The new hedge accounting rules will align the accounting for hedging instruments more closely with the Group's risk management practices. As a general rule, more hedge relationships might be eligible for hedge accounting, as the standard introduces a more principles-based approach. HKFRS 9 provides a choice of accounting policy to be remained with HKAS 39 hedge accounting.

The new impairment model requires the recognition of impairment provisions based on expected credit losses ("ECL") rather than only incurred credit losses as is the case under HKAS 39. The impact of the changes to the recognition and measurement of overall credit loss impairment for the Group on initial application of HKFRS 9 is estimated to result in a reduction in the retained earnings of less than 2% as at 1 January 2018. The overall credit loss impairment under HKFRS 9 mainly consist of the estimated impairment allowance for its advances to customers measured at amortised cost.

The new standard also introduces expanded disclosure requirements and changes in presentation. These are expected to change the nature and extent of the Group's disclosures about its financial instruments particularly in the year of the adoption of the new standard.

Date of adoption

HKFRS 9 is effective for annual periods beginning on or after 1 January 2018 on a retrospective basis. The Group plans to use the exemption from restating comparative information and will recognise any transition adjustments against the opening balance of equity at 1 January 2018.

HKFRS 16 Leases

Nature of change

HKFRS 16 was issued in January 2016. It will result in almost all leases being recognised on the statement of financial position, as the distinction between operating and finance leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The only exceptions are short-term and low-value leases.

The accounting for lessors will not significantly change.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

3. NEW AND REVISED HKFRSs ISSUED BUT NOT YET EFFECTIVE - continued HKFRS 16 Leases - continued

Impact

The standard will affect primarily the accounting for the Group's operating leases.

However, the Group has not yet assessed what adjustments, if any, are necessary for example because of the change in the definition of the lease term and the different treatment of variable lease payments and of extension and termination options. It is therefore not yet possible to estimate the amount of right-of-use assets and lease liabilities that will have to be recognised on adoption of the new standard and how this may affect the Group's profit or loss and classification of cash flows going forward.

Date of adoption

Application is mandatory for financial years commencing on or after 1 January 2019. At this stage, the Group does not intend to adopt the standard before its effective date. The Group intends to apply the simplified transition approach and will not restate comparative amounts for the year prior to first adoption.

There are no other standards that are not yet effective and that would be expected to have a material impact on the entity in the current or future reporting periods and on foreseeable future transactions.

4. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with HKFRSs 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 Hong Kong Companies Ordinance.

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.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/or disclosure purposes in these consolidated financial statements is determined on such a basis, except for share-based payment transactions that are within the scope of HKFRS 2, leasing transactions that are within the scope of HKAS 17, and measurements that have some similarities to fair value but are not fair value, such as value in use in HKAS 36.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

The principal accounting policies are set out below. These policies have been consistently applied in all years presented, unless otherwise stated.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and entities controlled by the Bank and its subsidiaries. Control is achieved when the Bank:

- has power over the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Bank reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

Consolidation of a subsidiary begins when the Bank obtains control over the subsidiary and ceases when the Bank loses control of the subsidiary. Specifically, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated income statement from the date the Bank gains control until the date when the Bank ceases to control the subsidiary.

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies.

All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

Investments in subsidiaries

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

Impairment testing of the investments in subsidiaries is required upon receiving a dividend from these investments if the dividend exceeds the total comprehensive income of the subsidiary in the period the dividend is declared or if the carrying amount of the investment in the separate financial statements exceeds the carrying amount in the consolidated financial statements of the investee's net assets including goodwill.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Intangible assets

Goodwill

Goodwill arising on an acquisition of a business 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 statement of financial position.

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 combination.

A cash-generating unit to which goodwill has been allocated is tested for impairment annually, or more frequently whenever there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a reporting period, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that reporting period. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment losses are allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit on a pro rata basis based on the carrying amount of each asset in the unit. Any impairment losses for goodwill is recognised directly in the consolidated income statement. An impairment losses recognised for goodwill is not reversed in subsequent periods.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Computer software and internally developed software

Costs associated with maintaining computer software and internally developed software are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Group are recognised as intangible assets when the following criteria are met:

- It is technically feasible to complete the software product so that it will be available for use;
- Management intends to complete the software product and use or sell it;
- There is an ability to use or sell the software product;
- It can be demonstrated how the software product will generate probable future economic benefits;
- Adequate technical, financial and other resources to complete the development and to use or sell the software product are available; and
- The expenditure attributable to the software product during its development can be reliably measured.

Directly attributable costs that are capitalised as part of the software product include the software development employee costs and an appropriate portion of relevant overheads.

Development costs recognised as assets are amortised over their estimated useful lives, which does not exceed fifteen years.

Other development expenditures that do not meet these criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period.

Interests in associates

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in the consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are initially recognised in the consolidated statement of financial position at cost and adjusted thereafter to recognise the Group's share of the profit or loss and other comprehensive income of the associates. When the Group's share of losses of an associate exceeds the Group's interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate), the Group discontinues recognising its share of further losses. Additional losses are recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Interests in associates - continued

An investment in an associate is accounted for using the equity method from the date on which the investee becomes an associate. On acquisition of the investment in an associate, any excess of the cost of the investment over the Group's share of the net fair value of the identifiable assets and liabilities of the investee is recognised as goodwill, which is included within the carrying amount of the investment. Any excess of the Group's share of the net fair value of the identifiable assets and liabilities over the cost of the investment, after reassessment, is recognised immediately in the income statement in the period in which the investment is acquired.

The requirements of HKAS 39 are applied to determine whether it is necessary to recognise any impairment losses with respect to the Group's investment in an associate. When necessary, the entire carrying amount of the investment (including goodwill) is tested for impairment in accordance with HKAS 36 "Impairment of assets" as a single asset by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount. Any impairment losses recognised forms part of the carrying amount of the investment. Any reversal of that impairment losses are recognised in accordance with HKAS 36 to the extent that the recoverable amount of the investment subsequently increases.

When a group entity transacts with its associate, profits and losses resulting from the transactions with the associate are recognised in the Group's consolidated financial statements only to the extent of interests in the associate that are not related to the Group.

Investments in associates are stated in the Bank's statement of financial position at cost less provision for impairment losses. The results of associates are accounted for by the Bank on the basis of dividends received or receivable.

Interest income and expenses

Interest income and expense for all interest-bearing financial instruments are recognised within "interest income" and "interest expense" in the income statement using the effective interest method.

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 on initial recognition. The calculation includes significant fees and transaction costs that are an integral part of the effective interest rate, and premiums or discounts.

Once an impairment loss of a financial asset has been recognised, subsequent interest income is recognised using the rate of interest used to discount the future cash flows measuring the impairment losses.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Non-interest income revenue recognition

Fees and commission income

Fees and commission income that are integral to the effective interest rate on a financial asset 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.

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 (provided that it is probable that the economic benefits will flow to the Group and the amount of revenue can be measured reliably).

Service income

Service income (including safe deposit box rentals and other banking services income) is recognised when services are provided.

Property and equipment

Property and equipment including land and buildings, which mainly comprise of branches and offices are stated in the statements of financial position at cost less subsequent accumulated depreciation and accumulated impairment losses, if any.

Depreciation is recognised so as to write off the cost of items of property and equipment over their estimated useful lives after taking into account their estimated residual value, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis.

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 gains or losses arising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

Leasehold land classified as finance lease commences amortisation from the time when the land interest becomes available for its intended use. Amortisation on leasehold land classified as finance lease and depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives.

Property and equipment will be reclassified to investment property when it is evidenced by end of owner occupation and commencement of an operating to another party.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Property and equipment - continued

Depreciation is calculated on a straight-line basis at the following useful lives:

Leasehold land	Over the remaining term of the lease
Buildings	Over its estimated useful life of 50 years or over the remaining term of lease of the leasehold land, whichever is the shorter
Equipment	5-15 years

Non-current assets held for sale

Non-current assets are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the asset is available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such asset and its sale is highly probable. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Non-current assets classified as held for sale are measured at the lower of their previous carrying amount and fair value less costs of disposal.

Investment properties

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

Investment properties are initially measured at cost, including any directly attributable expenditure. Subsequent to initial recognition, investment properties are measured at their fair values representing open market value determined at each reporting date by external valuers. Gains or losses arising from changes in the fair value of investment property are included in the income statement for the period in which they arise.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from the disposals. Any gains or losses 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 period in which the item is derecognised.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

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

Rental income from operating leases is recognised in the income statement on a straight-line basis over the term of the relevant lease.

The Group as lessee

Operating lease payments are recognised as an expense on a straight-line basis over the term of the lease.

Leasehold land and building

When a lease includes both land and building elements, the Group assesses the classification of each element as a finance or an operating lease separately based on the assessment as to whether substantially all the risks and rewards incidental to ownership of each element have been transferred to the Group, unless it is clear that both elements are operating leases in which case the entire lease is classified as an operating lease. Specifically, the minimum lease payments (including any lump-sum upfront payments) are allocated between the land and the building elements in proportion to the relative fair values of the leasehold interests in the land element and building element of the lease at the inception of the lease.

To the extent the allocation of the lease payments can be made reliably, interest in leasehold land that is accounted for as an operating lease is presented as “prepaid lease payments for land” in the statements of financial position and is released over the lease term on a straight-line basis except for those that are classified and accounted for as investment properties under the fair value model.

Foreign currencies

Functional and presentation currency

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. The consolidated financial statements are presented in thousands of units of Hong Kong Dollars (HK\$'000), which is the Bank's functional currency and the Group's presentation currency.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Foreign currencies - continued

Transactions and balances

Foreign currency transactions that are transactions denominated, or that require settlement, in a foreign currency are translated into the functional currency using the exchange rates prevailing at the dates of the transactions.

Monetary items denominated in foreign currency are translated with the closing rate as at the reporting date. Non-monetary items measured at historical cost denominated in a foreign currency are translated with the exchange rate as at the date of initial recognition; non-monetary items in a foreign currency that are measured at fair value are translated using the exchange rates at the date when the fair value was determined.

Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at exchange rates at statement of financial position dates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

All foreign exchange gains and losses recognised in the income statement are presented net in the income statement within the corresponding item. Foreign exchange gains and losses on other comprehensive income items are presented in other comprehensive income within the corresponding item.

In the case of changes in the fair value of monetary assets denominated in foreign currency classified as available-for-sale, a distinction is made between translation differences resulting from changes in amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in the amortised cost are recognised in the income statement, and other changes in the carrying amount, except impairment, are recognised in other comprehensive income.

Translation differences on non-monetary financial instruments, such as equity securities classified as held for trading, are reported as part of the fair value gain or loss. Translation differences on non-monetary financial instruments, such as equity securities classified as available-for-sale securities, are included in other comprehensive income.

Group companies and overseas branches

The results and financial position of all the Group's entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- Assets and liabilities for each statement of financial position presented are translated at the closing rate at the date of that statement of financial position;
- Income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- All resulting exchange differences are recognised in other comprehensive income.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Retirement benefit costs

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

For defined retirement benefit plans, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out regularly such that the amounts recognised in the financial statements do not differ materially from the amounts that would be determined at the end of reporting period.

Remeasurement, comprising actuarial gains and losses, the effect of the changes to the asset ceiling (if applicable) and the return on plan assets (excluding interest), is reflected immediately in the statement of financial position with a charge or credit recognised in other comprehensive income in the period in which they occur. Remeasurement recognised in other comprehensive income is reflected immediately in retained profits and will not be reclassified to the income statement. Past service cost is recognised in the income statement in the period of a plan amendment. Net interest is calculated by applying the discount rate at the beginning of the period to the net defined benefit liability or asset. Defined benefit costs are categorised as follows:

- service cost (including current service cost, past service cost, as well as gains and losses on curtailments and settlements), recognised in the income statement;
- net interest expense or income, recognised in the income statement; and
- remeasurement, recognised in the other comprehensive income.

The net retirement benefit liability/asset recognised in the statements of financial position represents the actual deficit or surplus in the Group's defined benefit plans. Any surplus resulting from this calculation is limited to the present value of any economic benefits available in the form of refunds from the plans or reductions in future contributions to the plans.

Bonus plans

Liabilities for bonus plans due wholly within twelve months after the end of the reporting period are recognised when the Group has a present or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

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 before taxation” 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 end of the reporting period.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit. 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.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and interest in associates, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of the reporting period 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 assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset is realised, based on tax rate (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

For the purposes of measuring deferred tax liabilities or deferred tax assets for investment properties that are measured using the fair value model, the carrying amounts of such properties are presumed to be recovered entirely through sale, unless the presumption is rebutted. The presumption is rebutted when the investment property is depreciable and is held within a business model whose objective is to consume substantially all of the economic benefits embodied in the investment property over time, rather than through sale. If the presumption is rebutted, deferred tax liabilities and deferred tax assets for such investment properties are measured in accordance with the above general principles set out in HKAS 12 (i.e. based on the expected manner as to how the properties will be recovered).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Taxation - continued

Current and deferred tax is recognised in the income statement, except when it relates to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred tax are also recognised in other comprehensive income or directly in equity respectively. Where current tax or deferred tax arises from the initial accounting for a business combination, the tax effect is included in the accounting for the business combination.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Financial instruments

Financial assets and financial liabilities are recognised in the statements of financial position 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 issue of financial liabilities at fair value through profit or loss are recognised immediately in the income statement.

Financial assets

The Group'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. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. 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 and 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 to the net carrying amount on initial recognition.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial assets - continued

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss have 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 incurred principally for the purpose of selling in the near future; or
- on initial recognition, it is a part of a portfolio of identified 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.

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 at fair value through profit or loss.

Financial assets at fair value through profit or loss are measured at fair values, with changes in fair values arising from remeasurement recognised directly in the income statement in the period in which they arise. The net gains or losses recognised in the income statement does not include any dividends or interest earned on these assets as these are recognised in accordance with the policies set out in Dividends and Interest income and expenses, respectively.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. 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 other advances to customers, other accounts and amounts due from subsidiaries are carried at amortised cost using the effective interest method, less any identified impairment losses (see accounting policy on impairment of financial assets below).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial assets - continued

Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity dates that the Group's management has the positive intention and ability to hold to maturity other than those that meet the definition of loans and receivables. Subsequent to initial recognition, held-to-maturity investments are measured at amortised cost using the effective interest method, less any identified impairment losses (see accounting policy on impairment of financial assets below).

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated or not classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity investments.

Equity and debt securities held by the Group that are classified as available-for-sale financial assets and are traded in an active market are measured at fair value at the end of each reporting period. Changes in the carrying amount of available-for-sale monetary financial assets relating to interest income calculated using the effective interest method and dividends on available-for-sale equity investments are recognised in the income statement. Other changes in the carrying amount of available-for-sale financial assets are recognised in other comprehensive income and accumulated under the heading of investment revaluation reserve. When the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously accumulated in the investment revaluation reserve is reclassified to the income statement (see the accounting policy in respect of impairment of financial assets below).

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

Available-for-sale equity investments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are measured at cost less any identified impairment losses at the end of the reporting period (see accounting policy on impairment of financial assets below).

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Impairment of financial assets

Financial assets, other than those at fair value through profit or loss, are assessed for indicators of impairment at the end of the reporting period. Financial assets are considered to be 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 affected.

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
- breach of contract, default or delinquency in interest or principal payments; or
- it is probable that the borrower will enter bankruptcy or financial re-organisation; or
- disappearance of an active market for that financial asset because of financial difficulties.

For financial asset carried at amortised cost, such as advances to customers, assets that are assessed not to be impaired individually are, in addition, 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 CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Impairment of financial assets - continued

Individually insignificant advances or advances where no objective evidence of impairment exists for an individually assessed financial assets are assessed for collective impairment by considering the historical loss experience of advances with similar credit risk characteristics adjusted for current conditions.

For financial assets carried at amortised cost, the amount of the impairment losses recognised is the difference between the financial asset's carrying amount and the present value of the estimated future cash flows discounted at the financial asset's original effective interest rate.

For financial assets carried at cost, the amount of the impairment losses is measured as the difference between the financial asset's carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses will not be reversed in subsequent periods.

The carrying amount of the financial asset is reduced through the use of an allowance account. 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 the income statement.

For financial assets measured at amortised cost, if, in a subsequent period, the amount of impairment loss decrease and the decrease can be related objectively to an event occurring after the impairment loss was recognised, the previously recognised impairment losses are reversed through the income statement to the extent that the carrying amount of the financial asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

When an available-for-sale financial asset carried at fair value is considered to be impaired, cumulative losses previously recognised in other comprehensive income are reclassified to the income statement in the period in which the impairment takes place.

Impairment losses on available-for-sale equity investments carried at fair value will not be reversed through the income statement in subsequent periods. Any increase in fair value subsequent to impairment losses are recognised directly in other comprehensive income and accumulated in investment valuation reserve. For available-for-sale debt investments, impairment losses are subsequently reversed through the income statement if an increase in the fair value of the investment can be objectively related to an event occurring after the recognition of the impairment losses.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial liabilities and equity instruments

Financial liabilities

Financial liabilities and equity instruments issued by a group entity are classified as either financial liabilities or equity instruments in accordance with the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

Equity instruments

Equity instruments (including ordinary shares and additional equity instruments) are any contracts that evidence a residual interests in the assets of a group entity after deducting all of its liabilities. Equity instruments issued by the Bank are recognised at the proceeds received, net of direct issuance costs.

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 (including all fees and 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 liability, or, where appropriate, a shorter period to the net carrying amount on initial recognition.

Interest expense is recognised on an effective interest basis.

Financial liabilities at fair value through profit or loss

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

A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of repurchasing in the near future; or
- on initial recognition, it is a part of a portfolio of identified 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.

Financial liabilities at fair value through profit or loss are measured at fair values, with changes in fair values arising from remeasurement recognised directly in the income statement in the period in which they arise. The net gains or losses exclude any interest paid on the financial liabilities and are included in interest expense in the income statement.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Financial liabilities and equity instruments - continued

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, financial assets sold under repurchase agreements, deposits from customers, other accounts and accruals, amounts due to subsidiaries, certificates of deposit and loan capital are subsequently measured at amortised cost using the effective interest method.

Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the statements of financial position 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 financial asset and settle the financial liability simultaneously. The legal enforceable right must not be contingent on future events and must be enforceable in the normal course of business and in the event of default, insolvency or bankruptcy of the Bank or the counterparty.

Derivative financial instruments and hedging

Derivatives are initially recognised at fair values at the date derivative contracts are entered into and are subsequently remeasured to their fair values at the end of each reporting period. The resulting gains or losses are recognised in the income statement immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in the income statement depends on the nature of hedge relationship.

Embedded derivatives

Derivatives embedded in non-derivative host contracts are treated as separate derivatives when they meet the definition of a derivative, their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair values with changes in fair values recognised in the income statement.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Hedge accounting

The Group designates certain derivatives as hedges of the fair value of available-for-sale securities and fixed-rate subordinated note (fair value hedges).

At the inception of the hedging relationship, the entity documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Group documents whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting the changes in fair values of the hedged item.

Fair value hedges

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recognised in the income statement immediately, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The change in the fair value of the hedging instrument and the change in the fair value of the hedged item attributable to the hedged risk are recognised in the income statement in the line item relating to the hedged item.

Hedge accounting is discontinued when the Group revokes the hedging relationship, when the hedging instrument expires or is sold, terminated, or exercised, or when it no longer qualifies for hedge accounting.

Financial guarantee contracts

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for losses 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 designated 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 of obligation under the contract, as 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 the revenue recognition standard.

Any increase in the liability relating to guarantees is reported in the income statement.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Derecognition

The Group derecognises financial assets only when the contractual rights to the cash flows from the financial assets expire, or when it transfers the financial assets and substantially all the risks and rewards of ownership of the financial asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred financial asset, the Group continues to recognise the financial asset to the extent of its continuing involvement and recognises an associated liability. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset in its entirety, the difference between the financial asset's carrying amount and the sum of the consideration received and receivable and the cumulative gains or losses that had been recognised in other comprehensive income and accumulated in equity is recognised in the income statement.

On derecognition of a financial asset other than in its entirety, the Group allocates the previous carrying amount of the financial asset between the part it continues to recognise, and the part it no longer recognises on the basis of the relative fair values of those parts on the date of the transfer. The difference between the carrying amount allocated to the part that is no longer recognised and the sum of the consideration received for the part no longer recognised and any cumulative gain or loss allocated to it that had been recognised in other comprehensive income is recognised in the income statement. A cumulative gain or loss that had been recognised in other comprehensive income is allocated between the part that continues to be recognised and the part that is no longer recognised on the basis of the relative fair values of those parts.

The Group derecognises financial liabilities when, and only when the Group's obligations specified in the relevant contract are discharged, cancelled or expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in the income statement.

Repurchase agreements

Financial assets sold subject to repurchase agreements continue to be recognised and recorded in the statement of financial position. The corresponding liability is included in the financial assets sold under repurchase agreements.

The difference between purchase and sale price is recognised as interest expense in the income statement over the life of the agreements using the effective interest method.

4. SIGNIFICANT ACCOUNTING POLICIES - continued

Financial instruments - continued

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation, and a reliable estimate can be made of the amount of obligation. Provisions are measured at the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (where the effect of the time value of money is material).

Impairment of non-financial assets (other than goodwill)

At the end of the reporting period, the Group reviews the carrying amounts of its non-financial assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment losses, if any. When it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised immediately in the income statement.

Where impairment losses subsequently reverse, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment losses been recognised for the asset in prior years. A reversal of impairment losses is recognised as income immediately.

Cash and cash equivalents

For the purposes of the consolidated statement of cash flows, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash and balances with central bank and banks, money at call and short notice, exchange fund bills as well as placements with banks.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES 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 underlying 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 end of the reporting period, 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 losses 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 statements of financial position 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 on a collective basis for loans and advances with similar credit risk characteristics to assess the impairment loss. More details are set out in note 7.

Details of the impairment allowance movements are disclosed in note 21.

5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY - continued

Key sources of estimation uncertainty - continued

(b) *Fair value of derivatives and other financial instruments*

The management of the Group uses its 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 products with embedded derivatives, assumptions are made based on quoted market rates adjusted for specific features of the instruments.

Details of the assumptions used are disclosed in note 7.

(c) *Estimated impairment of goodwill*

According to HKAS 36 "Impairment of Assets", impairment losses are 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 fair value less cost to sell of an acquired subsidiary (the smallest cash-generating unit) to which the goodwill has been allocated. The acquired subsidiary is involved in insurance business. Details of the recoverable amount calculation are disclosed in note 36.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES 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 Group's accounting policies and that have the most significant effect on the amounts recognised in the consolidated financial statements.

Deferred taxation on investment properties

For the purposes of measuring deferred tax liabilities or deferred tax assets arising from investment properties that are measured using the fair value model, the directors have reviewed the Group's investment property portfolios in Hong Kong and the Government of the People's Republic of China (the "Mainland") and concluded that the Group's investment properties are not held under a business model whose objective is to consume substantially all of the economic benefits embodied in the investment properties over time. Therefore, in measuring the Group's deferred taxation on investment properties, the directors have determined that the presumption that the carrying amounts of investment properties measured using the fair value model are recovered entirely through sale is not rebutted. As a result, the Group has not recognised any deferred taxes on changes in fair value of investment properties located in Hong Kong as the Group is not subject to any income taxes on disposal of these investment properties. As at 31 December 2017, the Group has recognised the deferred tax of HK\$13,156,000 (2016: HK\$8,473,000) on the change in fair value of investment property in the Mainland.

Deferred taxation in respect of temporary differences attributed to the accumulated profits of the Mainland branches

The directors have determined that the Bank is able to control the timing of the reversal of the temporary differences attributable to accumulated profits of the Mainland branches amounting to HK\$561,562,000 (2016: HK\$455,797,000) and that it is probable that the temporary differences will not reverse in the foreseeable future. Accordingly, deferred taxation relating to such temporary differences is not provided.

6. SEGMENT INFORMATION

(a) Operating segments

The Group's operating segments, which are also the reportable segments, based on information regularly reviewed by the chief operating decision maker (Executive Committee of the Group) for the purpose of allocating resources to segments and assessing their performance on business divisions of the Group, are as follows:

The corporate and personal banking services provided by the Group are principally lending and trade finance facilities, auto financing, 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 automated telephone and internet banking services to its customers. Other banking services offered include remittance and money exchange, safe deposit boxes, autopay and direct debit services.

Financial markets 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, and from the Bank's cash management activities through foreign currency funding swaps.

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

Others comprise investment holding, insurance, other investment advisory services and property investments.

No operating segments identified by the chief operating decision maker have been aggregated in arriving at the reportable segments of the Group.

The operating segment information allocation basis was changed for better assessment of the segment's performance for the year ended 31 December 2017. Comparative figures have not been restated as it is impractical to reallocate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

6. SEGMENT INFORMATION - continued

(a) Operating segments - continued

(i) Operating segment information for the year ended 31 December 2017 is presented below:

Operating segment revenues and results

	Corporate and personal banking HK\$'000	Financial markets activities HK\$'000	Securities business HK\$'000	Others HK\$'000	Eliminations HK\$'000	Consolidated HK\$'000
Interest income from external customers	2,604,867	1,183,701	8,429	3,394	-	3,800,391
Interest expense to external customers	(1,228,746)	(254,392)	(125)	-	-	(1,483,263)
Inter-segment interest income (Note 1)	515,731	-	-	-	(515,731)	-
Inter-segment interest expense (Note 1)	-	(515,731)	-	-	515,731	-
Net interest income	1,891,852	413,578	8,304	3,394	-	2,317,128
Fee and commission income	281,089	-	143,456	-	-	424,545
Fee and commission expenses	(96,870)	-	(204)	-	-	(97,074)
Net income (loss) from trading and investments	64,333	12,658	2,560	(173,489)	-	(93,938)
Other operating income	122,263	543	718	35,371	-	158,895
Segment revenue						
Total operating income	2,262,667	426,779	154,834	(134,724)	-	2,709,556
Comprising:						
- Segment revenue from external customers	1,746,936	942,510	154,834	(134,724)		
- Inter-segment transactions	515,731	(515,731)	-	-		
Operating expenses (Note 2)	(1,057,535)	(97,187)	(96,576)	(64,869)	-	(1,316,167)
Net charge of impairment allowances on loans and advances	(371,591)	-	-	-	-	(371,591)
Net gains on disposal of asset held for sale	-	-	-	2,878	-	2,878
Net (losses) gains on disposal of property and equipment	(19)	-	30,350	624,288	-	654,619
Net gains on disposal of and fair value adjustments on investment properties	-	-	-	12,632	-	12,632
Impairment loss on available-for-sale securities	-	-	-	(290)	-	(290)
Impairment loss on loan and receivable securities	(629)	-	-	-	-	(629)
Segment profit	832,893	329,592	88,608	439,915	-	1,691,008
Unallocated corporate expenses						(37,466)
Share of profits of associates						55,723
Profit before taxation						1,709,265

Notes: 1. Inter-segment pricing for funding transactions is charged at prevailing customer deposits interest rates.

2. The difference between the operating expenses in the consolidated income statement and the operating expenses in the operating segments is the unallocated corporate expenses.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

6. SEGMENT INFORMATION - continued

(a) Operating segments - continued

- (i) Operating segment information for the year ended 31 December 2017 is presented below: –
continued

Operating segment assets and liabilities as at 31 December 2017

	Corporate and personal banking HK\$'000	Financial markets activities HK\$'000	Securities business HK\$'000	Others HK\$'000	Consolidated HK\$'000
Assets					
Segment assets	99,078,528	62,763,543	436,863	437,901	162,716,835
Interests in associates					301,337
Unallocated corporate assets					728,942
Consolidated total assets					163,747,114
Liabilities					
Segment liabilities	119,202,062	25,925,751	243,751	112,447	145,484,011
Unallocated corporate liabilities					829,305
Consolidated total liabilities					146,313,316

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

6. SEGMENT INFORMATION - continued

(a) Operating segments - continued

- (i) Operating segment information for the year ended 31 December 2017 is presented below: – continued

Other information – amounts included in the measure of segment results and segment assets

	Corporate and personal banking HK\$'000	Financial markets activities HK\$'000	Securities business HK\$'000	Others HK\$'000	Unallocated HK\$'000	Consolidated HK\$'000
Capital expenditure during the year	83,191	1,248	2,357	73	206,084	292,953
Depreciation	58,347	1,816	2,120	412	21,442	84,137
Release of prepaid lease payments for land	66	-	-	-	-	66

All direct costs incurred by different segments are grouped under respective segments. Indirect costs and support functions' costs are allocated to various segments and products based on effort and time spent while segments' other operating income is allocated depending on the nature of costs incurred. Indirect costs and support functions' costs and income related to corporate activities that cannot be reasonably allocated to segments or products are grouped as unallocated corporate expenses and unallocated corporate income respectively. This is the measure reported to the chief operating decision maker for the purposes of resource allocation and assessment of performance.

There is no operating income with a single external customer amounting to or exceeding 10% of the Group's and the Bank's total operating income.

Assets and liabilities related to corporate activities that cannot be reasonably allocated to segments, products and support functions are grouped as unallocated corporate assets and liabilities. All direct segment assets and liabilities are grouped under respective segments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

6. SEGMENT INFORMATION - continued

(a) Operating segments - continued

(ii) Operating segment information for the year ended 31 December 2016 is presented below:

Operating segment revenues and results

	Corporate and personal banking HK\$'000	Financial markets activities HK\$'000	Securities business HK\$'000	Others HK\$'000	Eliminations HK\$'000	Consolidated HK\$'000
Interest income from external customers	1,781,977	1,212,094	5,843	1,256	-	3,001,170
Interest expense to external customers	(686,345)	(270,025)	-	-	-	(956,370)
Inter-segment interest income (Note 1)	357,719	-	-	-	(357,719)	-
Inter-segment interest expense (Note 1)	-	(357,719)	-	-	357,719	-
Net interest income	1,453,351	584,350	5,843	1,256	-	2,044,800
Fee and commission income	235,260	-	109,234	-	-	344,494
Fee and commission expenses	(84,862)	-	(48)	-	-	(84,910)
Net income from trading and investments	949	102,850	-	126,260	-	230,059
Other operating income	118,329	-	-	21,524	-	139,853
Segment revenue						
Total operating income	1,723,027	687,200	115,029	149,040	-	2,674,296
Comprising:						
- Segment revenue from external customers	1,365,308	1,044,919	115,029	149,040		
- Inter-segment transactions	357,719	(357,719)	-	-		
Operating expenses (Note 2)	(721,421)	(59,991)	(67,835)	(24,954)	-	(874,201)
Net reversal of impairment allowances on loans and advances	40,198	-	-	-	-	40,198
Net (losses) gains on disposal of property and equipment	(67)	-	2	24,822	-	24,757
Net gains on disposal of other investments	-	46,337	-	114,392	-	160,729
Net gains on disposal of and fair value adjustments on investment properties	-	-	-	2,026	-	2,026
Impairment loss on available-for-sale securities	-	-	-	(11,071)	-	(11,071)
Impairment loss on goodwill	-	-	-	(11,000)	-	(11,000)
Segment profit	1,041,737	673,546	47,196	243,255	-	2,005,734
Unallocated corporate expenses						(353,351)
Share of profits of associates						31,617
Profit before taxation						1,684,000

Notes: 1. Inter-segment pricing for funding transactions is charged at prevailing customer deposits interest rates.

2. The difference between the operating expenses in the consolidated income statement and the operating expenses in the operating segments is the unallocated corporate expenses.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

6. SEGMENT INFORMATION - continued

(a) Operating segments - continued

- (ii) Operating segment information for the year ended 31 December 2016 is presented below: –
continued

Operating segment assets and liabilities as at 31 December 2016

	Corporate and personal banking HK\$'000	Financial markets activities HK\$'000	Securities business HK\$'000	Others HK\$'000	Consolidated HK\$'000
Assets					
Segment assets	77,287,514	59,003,434	288,494	454,148	137,033,590
Interests in associates					262,565
Unallocated corporate assets					475,896
Consolidated total assets					137,772,051
Liabilities					
Segment liabilities	103,641,993	17,452,642	139,485	119,599	121,353,719
Unallocated corporate liabilities					504,760
Consolidated total liabilities					121,858,479

Other information – amounts included in the measure of segment results and segment assets

	Corporate and personal banking HK\$'000	Financial markets activities HK\$'000	Securities business HK\$'000	Others HK\$'000	Unallocated HK\$'000	Consolidated HK\$'000
Capital expenditure during the year	48,920	2,826	2,066	22	199,678	253,512
Depreciation	42,373	1,536	1,913	504	16,303	62,629
Release of prepaid lease payments for land	66	-	-	-	-	66

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

6. SEGMENT INFORMATION - continued

(b) Geographical information

Geographical information (including geographical analysis of total segment revenue) is analysed by the Group based on the locations of the principal operations of the branches and subsidiaries which are responsible for reporting the results or booking the assets. Non-current assets presented below are based on the location of the entities' country of domicile which is the same as the location of the non-current assets.

Details of geographical information are set out below:

	2017						
	Total operating income	Profit before taxation	Capital expenditure during the year	Total assets	Total liabilities	Total contingent liabilities and commitments	Non-current assets
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong	2,308,139	1,567,409	223,707	143,575,786	129,936,255	26,237,373	1,367,414
Macau and Mainland China	401,417	141,856	69,246	20,171,328	16,377,061	12,071,618	195,974
Total	2,709,556	1,709,265	292,953	163,747,114	146,313,316	38,308,991	1,563,388

	2016						
	Total operating income	Profit before taxation	Capital expenditure during the year	Total assets	Total liabilities	Total contingent liabilities and commitments	Non-current assets
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong	2,414,138	1,583,927	222,423	118,135,827	108,326,735	21,852,799	1,283,254
Macau and Mainland China	260,158	100,073	31,089	19,636,224	13,531,744	3,735,358	108,706
Total	2,674,296	1,684,000	253,512	137,772,051	121,858,479	25,588,157	1,391,960

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

Non-current assets consist of interests in associates, investment properties, property and equipment, prepaid lease payments for land (non-current portion) and intangible assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT

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

Risk management functions are carried out by the Asset and Liability Management Committee (the "ALCO") under policies approved by the Board of Directors of the Bank (the "Board") and the Risk Management Committee (the "RMC"). The ALCO identifies, evaluates and mitigates financial risks in close co-operation with the Group's operating units. The Board and the RMC provide 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 risk and price risk.

Categories of financial instruments

	2017 HK\$'000	2016 HK\$'000
Financial assets		
Fair value through profit or loss	557,058	425,086
Available-for-sale securities	35,450,292	24,164,028
Held-to-maturity securities	3,640,146	5,563,683
Loans and receivables (including cash and cash equivalents)	122,536,230	106,219,426
Financial liabilities		
Fair value through profit or loss	882,279	553,614
Amortised cost (<i>Note</i>)	144,946,083	120,935,322

Note: Loan capital of HK\$4,541,380,000 (2016: HK\$1,792,267,000) was carried at amortised cost with adjustment of fair value hedge as at 31 December 2017.

7. FINANCIAL RISK MANAGEMENT - continued

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 end of the reporting period. 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 end of the reporting period. 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 Hong Kong Banking Ordinance, the Hong Kong Monetary Authority guidelines and other statutory requirements (in the case of branches outside Hong Kong and subsidiaries, the relevant local laws and regulations).

The Group has delegated selected individuals with the credit approval authority. These individuals consist of Chief Risk Officer, Head of Credit Risk Management and experienced credit risk officers of the Group. The Chief Risk Officer has the overall responsibility for the management of credit risk through formulating credit policies, overseeing the credit quality of the Group's loan portfolio, ensuring an independent and objective assessment of credit risk, controlling exposure to selected industries, counterparties, countries and portfolio types etc. and providing advice and guidance to business units on various credit-related issues.

Credit officers perform independent reviews and approvals of credit applications by ensuring that a credit proposal meets underwriting standards of the Group and complies with relevant rules and regulations. Approval from the senior executive approvers, comprising Executive Directors and senior executives of the Group, is required as and when the requested amount of a credit application exceeds the highest delegated authority of a credit officer.

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 management.

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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

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 and commercial 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 losses, the Group will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

Estimates of fair value of collateral are based on the fair value of collateral determined using valuation techniques commonly used for the corresponding assets at the time of borrowing, and also updated at facility reviews. When a loan is identified as impaired, the corresponding fair value of collateral of that loan is updated by reference to market value such as recent transaction price of properties.

(b) Other risk mitigations

The Group uses guarantees 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.

(c) Credit-related commitments

The primary purpose of credit-related commitments (such as guarantee and letters of credit) is to ensure that funds are available to a customer as required, and these commitments carry the same credit risk as loans.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the amount of such loss may be reduced by unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Group monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Risk mitigation policies - continued

(d) Financial markets transactions

The Group maintains strict control limits on net open derivatives positions (i.e. the difference between purchase and sale contracts), by both amount and term. At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favourable to the Group, which in relation to derivatives is only a small fraction of the contract or notional values used to express the volume of instruments outstanding. This credit risk exposure is managed as part of the overall lending limits with customers, together with potential exposures from market movements. Collateral or other security is not usually obtained for credit risk exposures on these instruments, except where the Group requires margin deposits from counterparties.

(e) Master netting arrangements

To mitigate credit risk, the Group enters into master netting arrangements with counterparties whenever possible. Netting arrangements provide that, if an event of default occurs, all outstanding transactions with the counterparty will be terminated and all amounts outstanding will be settled on a net basis. Except for the event of default, all outstanding transaction with the counterparty are settled on a gross basis and generally do not result in offsetting the assets and liabilities in the statement of financial position.

Impairment and provisioning policies

Impairment allowances on individually assessed amounts recognised for financial reporting purposes and only for losses that have been incurred at the end of each reporting period based on objective evidence of impairment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Impairment and provisioning policies - continued

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

	31 December 2017				
	Gross loans and advances	Collective impairment allowances	Individual impairment allowances	Loans and advances secured by collateral	Gross impaired advances
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
				(Note 1)	
Loans for use in Hong Kong					
Industrial, commercial and financial					
– Property development	8,655,602	16,476	–	3,868,090	–
– Property investment	8,469,377	24,066	–	7,238,359	–
– Financial concerns	6,589,728	8,562	200,000	2,302,364	200,000
– Stockbrokers	2,405,034	4,666	–	1,265,898	–
– Wholesale and retail trade	2,666,682	20,358	9,670	2,435,878	9,670
– Manufacturing	1,609,080	55,382	3,023	831,615	3,380
– Transport and transport equipment	1,207,931	17,332	–	982,816	–
– Recreational activities	1,057	–	–	1,057	–
– Information technology	393,723	3,353	–	115,636	–
– Others (Note 2)	8,340,225	77,001	9,165	5,387,101	9,165
Individuals					
– Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	528,700	63	–	528,700	–
– Loans for the purchase of other residential properties	9,038,308	–	–	9,036,821	–
– Credit card advances	104,714	969	603	–	603
– Others (Note 3)	2,344,531	3,681	1,102	1,993,526	1,102
	52,354,692	231,909	223,563	35,987,861	223,920
Trade finance	2,963,400	5,927	20,271	1,133,247	22,533
Loans for use outside Hong Kong	31,380,280	91,803	150,559	10,875,016	151,647
	86,698,372	329,639	394,393	47,996,124	398,100

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Impairment and provisioning policies - continued

	31 December 2016				
	Gross loans and advances <i>HK\$'000</i>	Collective impairment allowances <i>HK\$'000</i>	Individual impairment allowances <i>HK\$'000</i>	Loans and advances secured by collateral <i>HK\$'000</i>	Gross impaired advances <i>HK\$'000</i>
	<i>(Note 1)</i>				
Loans for use in Hong Kong					
Industrial, commercial and financial					
- Property development	4,718,611	16,133	-	1,962,584	-
- Property investment	7,088,653	36,377	-	6,512,554	-
- Financial concerns	2,521,908	7,860	-	1,468,264	-
- Stockbrokers	2,943,866	9,009	-	1,660,372	-
- Wholesale and retail trade	2,827,690	28,426	7,256	2,379,035	7,256
- Manufacturing	2,424,713	24,217	3,899	1,652,931	8,357
- Transport and transport equipment	1,854,325	14,335	-	906,457	-
- Recreational activities	1,135	-	-	1,135	-
- Information technology	136,692	1,486	-	12,572	-
- Others (<i>Note 2</i>)	10,866,348	40,134	5,677	6,434,983	5,677
Individuals					
- Loans for the purchase of flats in the Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	496,907	233	-	496,907	-
- Loans for the purchase of other residential properties	8,506,503	-	-	8,502,916	-
- Credit card advances	111,614	1,720	751	-	751
- Others (<i>Note 3</i>)	3,362,930	5,148	746	2,401,894	746
	47,861,895	185,078	18,329	34,392,604	22,787
Trade finance	2,585,427	8,028	21,408	886,960	25,466
Loans for use outside Hong Kong	20,241,833	58,113	-	4,247,662	-
	70,689,155	251,219	39,737	39,527,226	48,253

Notes: 1. Loans and advances secured by collateral are determined as the lower of the market value of collateral or outstanding loan principal.

2. Major items mainly included loans to businesses in electricity and gas, hotels, catering, margin lending and other business purposes.

3. Major items mainly included loans to professionals and other individuals for various private purposes.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Impairment and provisioning policies - continued

The Group'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 losses at the end of the reporting period on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses the fair value of collateral held and the anticipated receipts for that individual account.

The Group adopted the policy as detailed in note 4 in assessing whether objective evidence of impairment existed.

Collectively assessed impairment allowances are provided for: (i) portfolios of homogeneous assets that are individually below materiality thresholds; and (ii) losses that have been incurred but have not yet been identified by considering the historical loss experience in portfolios of similar credit risk characteristics. The management has also made judgement as to whether the current economic and credit conditions are such that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience.

Concentration of risks of financial assets with credit risk exposure

Concentration of credit risk exists when changes in geographical or industry factors similarly affect 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 that best represent the maximum exposure to credit risk is disclosed below.

The geographical locations of the financial assets are determined by the locations of the counterparties with the ultimate credit exposures.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

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

Geographical locations

	Hong Kong HK\$'000	Asia Pacific excluding Hong Kong HK\$'000 (Note 1)	Others HK\$'000 (Note 2)	Total HK\$'000
At 31 December 2017				
Short-term funds	11,467,508	12,466,310	795,373	24,729,191
Placements with banks	994,907	5,364,097	–	6,359,004
Derivative financial instruments	152,851	138,671	265,271	556,793
Available-for-sale debt securities	7,164,839	17,703,104	10,494,516	35,362,459
Held-to-maturity securities	2,213,362	759,012	667,772	3,640,146
Loan and receivable securities	–	62,798	–	62,798
Advances and other accounts	67,851,957	22,203,129	894,701	90,949,787
	89,845,424	58,697,121	13,117,633	161,660,178
At 31 December 2016				
Short-term funds	4,930,437	22,690,312	2,376,696	29,997,445
Placements with banks	11,569	1,604,971	–	1,616,540
Derivative financial instruments	196,302	98,090	130,453	424,845
Available-for-sale debt securities	5,877,797	9,585,972	8,608,499	24,072,268
Held-to-maturity securities	2,480,165	1,549,961	1,533,557	5,563,683
Loan and receivable securities	–	–	–	–
Advances and other accounts	58,169,313	15,563,510	348,782	74,081,605
	71,665,583	51,092,816	12,997,987	135,756,386

Notes: 1. The countries reported in "Asia Pacific excluding Hong Kong" mainly included the Mainland China, Japan, Australia and other Asian countries.

2. The countries reported in "Others" mainly included Canada, United States and other European countries.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

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

Industry sectors

	Banks and other financial institutions HK\$'000	Central governments and central banks HK\$'000	Public sector entities HK\$'000	Corporate entities HK\$'000	Others HK\$'000	Total HK\$'000
At 31 December 2017						
Short-term funds	12,923,203	11,805,988	-	-	-	24,729,191
Placements with banks	6,359,004	-	-	-	-	6,359,004
Derivative financial instruments	359,033	-	-	197,760	-	556,793
Available-for-sale debt securities	14,571,099	4,101,191	-	16,690,169	-	35,362,459
Held-to-maturity securities	915,151	-	-	2,724,995	-	3,640,146
Loan and receivable securities	62,798	-	-	-	-	62,798
Advances and other accounts	6,094,110	1,413,256	377,100	65,840,109	17,225,212	90,949,787
	41,284,398	17,320,435	377,100	85,453,033	17,225,212	161,660,178
At 31 December 2016						
Short-term funds	24,780,764	5,216,681	-	-	-	29,997,445
Placements with banks	1,616,540	-	-	-	-	1,616,540
Derivative financial instruments	365,779	-	-	59,066	-	424,845
Available-for-sale debt securities	7,702,819	4,006,693	-	12,362,756	-	24,072,268
Held-to-maturity securities	941,530	4,645	39,234	4,578,274	-	5,563,683
Loan and receivable securities	-	-	-	-	-	-
Advances and other accounts	2,441,605	738,069	125	53,684,467	17,217,339	74,081,605
	37,849,037	9,966,088	39,359	70,684,563	17,217,339	135,756,386

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

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

Maximum exposure to credit risk relating to assets in the statements of financial position are as follows:

	2017 HK\$'000	2016 HK\$'000
Short-term funds	24,729,191	29,997,445
Placements with banks	6,359,004	1,616,540
Derivative financial instruments	556,793	424,845
Available-for-sale debt securities	35,362,459	24,072,268
Held-to-maturity securities	3,640,146	5,563,683
Loan and receivable securities	62,798	–
Advances and other accounts	90,949,787	74,081,605
	161,660,178	135,756,386

Maximum exposure to credit risk relating to items unrecorded in the statements of financial position are as follows:

	2017 HK\$'000	2016 HK\$'000
Direct credit substitutes	1,315,865	805,429
Trade-related contingencies	1,995,688	596,068
Undrawn formal standby facilities, credit lines and other commitments excluding those that are unconditionally cancellable without prior notice	10,917,633	17,277,667
	14,229,186	18,679,164

The above tables represent a worst case scenario of credit risk exposures to the Group as at 31 December 2017 and 31 December 2016, without taking account of any collateral held or other credit enhancements attached. For on-balance sheet assets, the exposures set out above are based on net carrying amounts.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Credit quality

Credit quality of loans and advances to customers, excluding interest receivable, are summarised as follows:

	2017 HK\$'000	2016 HK\$'000
Neither past due nor impaired	86,096,362	70,490,490
Past due but not impaired	203,910	150,412
Impaired	398,100	48,253
	86,698,372	70,689,155
Less: Allowances for impairment	(724,032)	(290,956)
	85,974,340	70,398,199

(i) Loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the internal rating system adopted by the Group which is also the classification system required to be adopted for reporting to the Hong Kong Monetary Authority.

	Overdrafts	Instalment loans	Term loans	Syndication loans	Foreign currency loans	Trade finance	Personal loans and tax loans	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2017									
GRADES:									
Pass	1,218,990	22,712,229	30,295,850	20,743,653	6,135,529	2,782,727	202,890	1,033,504	85,125,372
Special mention	39,570	64,110	81,518	703,233	-	33,940	891	-	923,262
Substandard or below	2,493	17,164	27,100	-	-	971	-	-	47,728
Total	1,261,053	22,793,503	30,404,468	21,446,886	6,135,529	2,817,638	203,781	1,033,504	86,096,362
At 31 December 2016									
GRADES:									
Pass	1,222,787	22,125,983	26,522,250	14,372,740	2,062,018	2,373,736	278,244	875,850	69,833,608
Special mention	69,362	77,614	71,053	-	34,118	63,315	34	-	315,496
Substandard or below	6,303	325,083	10,000	-	-	-	-	-	341,386
Total	1,298,452	22,528,680	26,603,303	14,372,740	2,096,136	2,437,051	278,278	875,850	70,490,490

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

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 of customers that were past due but not impaired were as follows:

	Overdrafts	Instalment loans	Term loans	Trade finance	Personal loans and tax loans	Others	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2017							
Past due up to 30 days	10,662	979	-	56,969	-	-	68,610
Past due from 31 to 90 days	2,387	17,229	-	6,563	295	1,724	28,198
Past due more than 90 days	8,066	9,767	80,000	9,269	-	-	107,102
Total	21,115	27,975	80,000	72,801	295	1,724	203,910
Fair value of collateral	38,941	74,845	163,050	67,372	-	-	344,208
Loans and advances secured by collateral (Note)	21,113	27,913	80,000	63,276	-	-	192,302
At 31 December 2016							
Past due up to 30 days	2,457	7,944	-	73,381	141	-	83,923
Past due from 31 to 90 days	-	28,704	21,970	-	629	1,924	53,227
Past due more than 90 days	6,267	6,995	-	-	-	-	13,262
Total	8,724	43,643	21,970	73,381	770	1,924	150,412
Fair value of collateral	32,522	168,232	28,978	77,888	-	-	307,620
Loans and advances secured by collateral (Note)	8,725	43,412	21,970	66,903	-	-	141,010

Collateral mainly consists of properties and fixed deposits.

Note: The amount of loans and advances secured by collateral is determined as the lower of the market value of collateral or outstanding loan principal.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk – continued

Credit quality – continued

- (iii) Loans and advances individually impaired

Loans and advances to customers

The breakdown of the gross amount of individually impaired loans and advances by class of customers are as follows:

	Overdrafts HK\$'000	Instalment loans HK\$'000	Term loans HK\$'000	Syndication loans HK\$'000	Foreign currency loan HK\$'000	Trade finance HK\$'000	Personal loans and tax loans HK\$'000	Others HK\$'000	Total HK\$'000
At 31 December 2017									
Individually impaired loans	8,446	10,538	207,949	149,859	244	20,834	112	118	398,100
Fair value of collateral	-	1,520	-	-	-	2,353	-	-	3,873
Loans and advances secured by collateral (Note)	-	1,520	-	-	-	2,353	-	-	3,873
At 31 December 2016									
Individually impaired loans	10,584	11,836	2,300	-	-	23,167	97	269	48,253
Fair value of collateral	3,097	1,682	-	-	-	4,371	-	-	9,150
Loans and advances secured by collateral (Note)	3,097	1,682	-	-	-	4,371	-	-	9,150

Collateral mainly consists of properties and fixed deposits.

Note: The amount of loans and advances secured by collateral is determined as the lower of the market value of collateral or outstanding loan principal.

- (iv) Placements with and advances to banks

As at 31 December 2017 and 31 December 2016, the advances to banks are neither past due nor impaired and unsecured.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Credit risk - continued

Debt securities

Financial investments by rating agency designation

The following tables present analysis of financial securities, other than loans and advances, held by the Group and the Bank by rating agency designation at the end of the reporting period, based on Moody's ratings. Financial securities not rated by Moody's are treated as unrated ones.

	Available-for-sale debt securities HK\$'000	Held-to- maturity securities HK\$'000	Loan and receivable securities HK\$'000	Total HK\$'000
At 31 December 2017				
Aaa	3,853,067	–	–	3,853,067
Aa1 to Aa3	1,066,978	61,045	–	1,128,023
A1 to A3	20,805,591	1,345,056	–	22,150,647
Lower than A3	7,048,076	1,021,854	–	8,069,930
Unrated	2,588,747	1,212,191	62,798	3,863,736
Total	35,362,459	3,640,146	62,798	39,065,403
At 31 December 2016				
Aaa	3,774,980	–	–	3,774,980
Aa1 to Aa3	3,640,615	1,059,526	–	4,700,141
A1 to A3	9,352,816	845,536	–	10,198,352
Lower than A3	4,065,312	1,096,508	–	5,161,820
Unrated	3,238,545	2,562,113	–	5,800,658
Total	24,072,268	5,563,683	–	29,635,951

Repossessed collateral

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

	2017 HK\$'000	2016 HK\$'000
Types of assets		
Others	10,250	2,500

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Market risk

Market risk is the risk of losses in assets, liabilities and off-balance sheet positions arising from movements in market rates and prices, including foreign exchange rates, interest rates, commodity prices, and equity prices etc.

Market risk exposures are separated into trading and non-trading portfolios. Trading portfolios comprise positions arising from market-making and warehousing of customer derived positions. Market risk arising from trading portfolio is at acceptable level, as the Group maintains controllable positions of financial instruments leading to foreign exchange and interest rate exposures.

Non-trading portfolios comprise positions that primarily arise from the interest rate management of our retail and commercial banking assets and liabilities, financial investments designated as available-for-sale and held-to-maturity, and exposures arising from our daily risk management operations.

Market risk management

Market risk is measured in terms of value at risk ("VaR"), which is used to estimate potential losses on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence;

It is monitored using measures including the net interest income and the sensitivity of foreign exchange which are applied to the market risk positions within each risk type; and

It is managed using risk limits approved by the Group. These limits are allocated across business lines and to the Group's legal entities.

The Group has established standards, policies and procedures to control and monitor the market risk and Risk Management Committee provides management oversight for the risk.

The Group uses derivatives to mitigate market risk caused by price fluctuation in interest rate and foreign exchange rate.

Stress tests are carried out to provide an indication of the potential losses under extreme market conditions. The stress test results are regularly reviewed by senior management and the Board. The Bank adopts scenario-based approach in stress-testing.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Currency risk

The assets and liabilities of the Group are mainly denominated in United States dollars (“US\$”), Renminbi (“RMB”) and Hong Kong dollars (“HK\$”). The Group adopts a policy of predominately matching the assets with liabilities in the same currency, effectively reducing the foreign currency exchange rate exposure. Limits are set to ensure that the net foreign currency exposure is kept to an acceptable level. The Group uses foreign exchange spot and forward contracts to manage its foreign currency risk.

The following tables indicate the concentration of currency risk at the end of each reporting periods:

	HK\$ HK\$'000	US\$ HK\$'000	RMB HK\$'000	Others HK\$'000 (Note)	Total HK\$'000
At 31 December 2017					
Assets					
Cash and short-term funds	17,302,870	325,818	6,506,653	1,029,300	25,164,641
Placements with banks	3,179,719	–	2,711,165	468,120	6,359,004
Derivative financial instruments	294,312	188,370	743	73,368	556,793
Financial assets at fair value through profit or loss	265	–	–	–	265
Available-for-sale securities	6,886,539	21,199,681	2,855,693	4,508,379	35,450,292
Held-to-maturity securities	520,238	2,597,116	409,525	113,267	3,640,146
Loan and receivable securities	–	–	62,798	–	62,798
Advances to customers	63,524,888	13,012,439	9,483,564	677,481	86,698,372
Advances to banks	–	107,829	–	–	107,829
Other financial assets	344,217	1,202,374	2,550,707	46,288	4,143,586
Total financial assets	92,053,048	38,633,627	24,580,848	6,916,203	162,183,726
Liabilities					
Deposits and balances of banks	466,251	1,236,071	1,128,007	221,603	3,051,932
Financial assets sold under repurchase agreements	–	11,137,481	–	865,508	12,002,989
Deposits from customers	77,888,784	14,821,953	20,473,818	5,574,119	118,758,674
Derivative financial instruments	436,005	359,757	724	85,793	882,279
Certificates of deposit	985,759	1,959,397	227,772	44,523	3,217,451
Debt securities issued	–	–	1,796,069	–	1,796,069
Loan capital	–	4,541,380	–	–	4,541,380
Other financial liabilities	975,611	360,403	219,386	22,188	1,577,588
Total financial liabilities	80,752,410	34,416,442	23,845,776	6,813,734	145,828,362
Net position – total financial assets and liabilities	11,300,638	4,217,185	735,072	102,469	16,355,364

Note: Currencies included in “Others” mainly represented Australian dollars and New Zealand dollars.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Currency risk - continued

	HK\$ HK\$'000	US\$ HK\$'000	RMB HK\$'000	Others HK\$'000 (Note)	Total HK\$'000
At 31 December 2016					
Assets					
Cash and short-term funds	7,958,188	12,679,708	9,078,151	805,234	30,521,281
Placements with banks	503,215	–	1,113,325	–	1,616,540
Derivative financial instruments	240,806	180,264	3,775	–	424,845
Financial assets at fair value through profit or loss	241	–	–	–	241
Available-for-sale securities	78,333	16,091,125	4,574,307	3,420,263	24,164,028
Held-to-maturity securities	945,501	3,087,342	1,246,322	284,518	5,563,683
Loan and receivable securities	–	–	–	–	–
Advances to customers	55,144,510	9,313,483	6,180,648	50,514	70,689,155
Advances to banks	–	496,256	–	–	496,256
Other financial assets	505,131	829,882	1,542,668	18,513	2,896,194
Total financial assets	65,375,925	42,678,060	23,739,196	4,579,042	136,372,223
Liabilities					
Deposits and balances of banks	991,886	699,559	1,001,767	3,469	2,696,681
Financial assets sold under repurchase agreements	–	8,307,200	–	1,538,553	9,845,753
Deposits from customers	67,400,777	11,946,482	18,295,979	5,237,391	102,880,629
Derivative financial instruments	174,721	375,155	3,738	–	553,614
Certificates of deposit	580,325	232,004	–	–	812,329
Debt securities issued	–	–	1,663,774	–	1,663,774
Loan capital	–	1,792,267	–	–	1,792,267
Other financial liabilities	779,482	320,494	120,769	23,144	1,243,889
Total financial liabilities	69,927,191	23,673,161	21,086,027	6,802,557	121,488,936
Net position – total financial assets and liabilities	(4,551,266)	19,004,899	2,653,169	(2,223,515)	14,883,287

Note: Currencies included in "Others" mainly represented Australian dollars and New Zealand dollars.

The Group entered into a number of foreign currency forward contracts to manage the currency risk exposure, details of which are set out in note 18.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Currency risk - continued

Foreign currency sensitivity analysis

The Group mainly exposes to US dollars and Renminbi. The following table illustrates sensitivity measure of the currency risk exposure given ± 1 and ± 5 (2016: ± 1 and ± 5) per cent change in exchange rate of US dollars/Renminbi against Hong Kong dollars.

	Change in currency rate			
	US Dollars		Renminbi	
	Appreciate	Depreciate	Appreciate	Depreciate
	+1%	-1%	+ 5%	-5%
Hong Kong dollars equivalents (HK\$'000)				
2017				
Profit after tax	33,527	(33,527)	(95,940)	95,940
Other comprehensive income (after tax)	-	-	134,096	(134,096)

	Change in currency rate			
	US Dollars		Renminbi	
	Appreciate	Depreciate	Appreciate	Depreciate
	+1%	-1%	+ 5%	-5%
Hong Kong dollars equivalents (HK\$'000)				
2016				
Profit after tax	21,456	(21,456)	(96,812)	96,812
Other comprehensive income (after tax)	-	-	141,517	(141,517)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Interest rate risk

Interest rate risk is referred to the risk to the Bank's financial condition resulting from adverse movements in interest rates. This consists of repricing risk, basis risk, option risk and yield curve risk. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movement arises.

Interest rate risks comprise those originating from both trading and non-trading portfolio. The Group's interest rate risk exposure is mainly contributed by non-trading portfolio. The Group manages interest rate risks within the limits approved by the RMC and under the monitoring of both ALCO and RMC. Limits are set on the level of mismatch of interest rate repricing that may be undertaken, which is monitored regularly. For trading portfolio, additional limits on interest rate sensitivities (also known as DV01) and stop loss are being enforced on daily basis.

The Group maintains controllable interest rate positions on its trading portfolio, in addition to certain interest rate contracts entered into for the management of Group's own risk with securities that are classified as trading. Interest rate risk arises primarily from the timing differences in the re-pricing of and the different bases of pricing interest-bearing assets, liabilities and off-balance-sheet positions. Interest rate risk is regularly monitored by regular sensitivity analysis of the net re-pricing gap and of different scenarios of pricing bases of assets and liabilities grouped with reference to their next contractual repricing date or maturity date.

The tables below summarise the Group's interest rate risk exposure by the earlier of contractual repricing or maturity dates of its assets and liabilities. For debt securities designated as available-for-sale, the exposure shown below has considered the interest rate swaps entered by the Group to manage interest rate risk of the debt securities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Interest rate risk - continued

	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	Total HK\$'000
At 31 December 2017						
Assets						
Cash and short-term funds	24,198,211	386,835	-	-	579,595	25,164,641
Placements with banks	4,222,802	2,136,202	-	-	-	6,359,004
Derivative financial instruments	168,394	100,897	-	-	287,502	556,793
Financial assets at fair value through profit or loss	-	-	-	-	265	265
Available-for-sale securities	25,389,403	9,928,906	9,125	35,026	87,832	35,450,292
Held-to-maturity securities	1,873,930	1,744,932	19,284	-	2,000	3,640,146
Loan and receivable securities	-	62,798	-	-	-	62,798
Advances to customers	72,775,699	2,487,099	8,615,501	2,511,269	308,804	86,698,372
Advances to banks	-	107,829	-	-	-	107,829
Other financial assets	1,943,410	523,779	-	79	1,676,318	4,143,586
Total financial assets	130,571,849	17,479,277	8,643,910	2,546,374	2,942,316	162,183,726
Liabilities						
Deposits and balances of banks	2,387,031	629,249	-	-	35,652	3,051,932
Financial assets sold under repurchase agreements	11,078,800	924,189	-	-	-	12,002,989
Deposits from customers	102,327,247	13,008,980	3,392,480	-	29,967	118,758,674
Derivative financial instruments	187,088	264,851	-	-	430,340	882,279
Certificates of deposit	1,539,806	1,677,645	-	-	-	3,217,451
Debt securities issued	-	1,796,069	-	-	-	1,796,069
Loan capital	-	-	4,541,380	-	-	4,541,380
Other financial liabilities	119,253	81,552	-	-	1,376,783	1,577,588
Total financial liabilities	117,639,225	18,382,535	7,933,860	-	1,872,742	145,828,362
Net position – total financial assets and liabilities	12,932,624	(903,258)	710,050	2,546,374	1,069,574	16,355,364

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Market risk - continued

Interest rate risk - continued

	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	Total HK\$'000
At 31 December 2016						
Assets						
Cash and short-term funds	28,480,703	1,446,576	–	–	594,002	30,521,281
Placements with banks	799,236	817,304	–	–	–	1,616,540
Derivative financial instruments	127,267	58,779	–	–	238,799	424,845
Financial assets at fair value						
through profit or loss	–	–	–	–	241	241
Available-for-sale securities	16,893,455	7,164,230	14,583	–	91,760	24,164,028
Held-to-maturity securities	2,925,453	2,606,094	30,136	–	2,000	5,563,683
Loan and receivable securities	–	–	–	–	–	–
Advances to customers	65,294,378	3,448,346	999,597	444,880	501,954	70,689,155
Advances to banks	496,256	–	–	–	–	496,256
Other financial assets	870,767	828,795	–	–	1,196,632	2,896,194
Total financial assets	115,887,515	16,370,124	1,044,316	444,880	2,625,388	136,372,223
Liabilities						
Deposits and balances of banks	1,849,097	833,238	–	–	14,346	2,696,681
Financial assets sold under						
repurchase agreements	8,677,987	1,167,766	–	–	–	9,845,753
Deposits from customers	80,189,211	12,272,947	56,707	–	10,361,764	102,880,629
Derivative financial instruments	236,259	144,301	–	–	173,054	553,614
Certificates of deposit	422,089	390,240	–	–	–	812,329
Debt securities issued	–	1,663,774	–	–	–	1,663,774
Loan capital	–	1,792,267	–	–	–	1,792,267
Other financial liabilities	95,262	48,207	–	–	1,100,420	1,243,889
Total financial liabilities	91,469,905	18,312,740	56,707	–	11,649,584	121,488,936
Net position – total financial assets and liabilities	24,417,610	(1,942,616)	987,609	444,880	(9,024,196)	14,883,287

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

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 floating interest rates at the end of the reporting period and the stipulated change taking place at the beginning of the financial year and held constant throughout the reporting period. A 100 basis points change in upwards and 10 basis points change in downwards are used when reporting interest rate risk internally to key management personnel and represents management's assessment of the possible change in interest rates.

	2017		2016	
	Change in basis points		Change in basis points	
	+100	-10	+100	-10
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Profit after tax	91,790	(8,262)	134,056	(28,807)

Price risk

The Group is exposed to price risk arising from its listed investments in equity securities. Except for those classified as held for trading, the Group does not actively trade these investments. The sensitivity analysis below is determined based on 10% changes in the price of the underlying investments.

Price sensitivity

	2017		2016	
	Change in price		Change in price	
	+10%	-10%	+10%	-10%
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Profit after tax	22	(22)	20	(20)
Other comprehensive income (after tax)	4,434	(4,434)	4,943	(4,943)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk

Liquidity risk is the risk that the Group may not be able to fund increases in assets or meet obligations as they fall due, without incurring unacceptable losses. Liquidity problems can have an adverse impact to the Group's earnings and capital and, in extreme circumstances, may even lead to the collapse of the Group which is otherwise solvent.

Management of liquidity risk

Principal objective

The principal objective of the Group's liquidity risk management framework is to maintain a conservative level of liquid funds on a daily basis so that the Group has sufficient cash flows to meet its current obligations when they fall due in the ordinary course of business, to make new loans and investments as opportunities arise and to satisfy statutory liquidity maintenance ratio requirements. The Group has enhanced its liquidity risk management framework by conducting cash flow analysis to ensure that the Group has adequate liquidity and funding capacity to meet its normal business operations and to withstand a prolonged period of liquidity stress in accordance with the requirements set out in the Supervisory Policy Manual LM-2 "Sound Systems and Controls for Liquidity Risk Management" ("SPM LM-2") revised by the HKMA in November 2016. This also provides a foundation to other risk management tools including stress-testing and contingency funding plan.

Organisation structure

The Group adopts a liquidity risk management model that incorporates both centralised and decentralised elements based on thorough consideration of the organisational structure and major business characteristics of the Group as well as regulatory policies. The Head Office is ultimately responsible for managing the Group's overall liquidity risk, while the branches outside Hong Kong in Macau and Mainland China manage their own liquidity risk pursuant to the Head Office's policies within authorised scope through submission of monthly management accounts and daily cash flow positions to Head Office.

Risk management functions are carried out by the ALCO and the RMC established by the EXCO. The ALCO identifies, evaluates and mitigates liquidity risk in close co-operation with the Group's operating units. The Board and the RMC provide written principles for overall risk management, as well as written policies covering specific areas, including liquidity risk. In addition, the Internal Audit Department performs independent reviews periodically to ensure the risk management functions are carried out effectively.

The management of the Group's liquidity risk is governed by the Liquidity Risk Management Policy which is reviewed by the ALCO and approved by the EXCO. Key features of liquidity position, appropriate limits and triggers are set in the Liquidity Risk Management Policy. The ALCO is delegated by the EXCO to oversee the Group's day-to-day liquidity risk management, responsible for monitoring and controlling of the Group's liquidity position through ongoing and periodic review of different liquidity metrics, including but not limited to the statutory liquidity maintenance ratios, the maturity mismatch of assets and liabilities, loan-to-deposit ratios, normal and stressed cash flow projections and inter-bank transactions. The Group uses various management information systems developed in-house to prepare and compile regular management reports to facilitate the liquidity risk management duties.

Treasury Department is responsible for the Group's intraday and day-to-day management of cash flow and liquidity positions while Finance Division is responsible for the identification, measurement and monitoring of liquidity risk exposures, conducting liquidity cost analysis and stress-testing, handling regulatory reporting in relation to liquidity risk and coordinating the regular forecast of loans and deposits, liquidity maintenance ratio, liquidity and funding statements. Depending on the level of severity, any breach in policies will be reported by these units to the ALCO and/or the EXCO, whilst seeking their advices or instructions on mitigating measures.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Management of liquidity risk - continued

The following tables detail the Group'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, with reference to their respective contractual interest rate, and for those variable rate instruments, by using the appropriate prevailing market rates as at the end of the reporting period as stated in their contracts.

	Repayable on demand HK\$'000	Repayable within 1 month HK\$'000	Repayable after 1 month but within 3 months HK\$'000	Repayable after 3 months but within 1 year HK\$'000	Repayable after 1 year but within 5 years HK\$'000	Over 5 years HK\$'000	Undated HK\$'000	Total HK\$'000
Liabilities adjusted with interest payable								
At 31 December 2017								
Deposits and balances of banks	6,290	791,419	1,635,363	630,956	-	-	-	3,064,028
Financial assets sold under repurchase agreements	-	3,568,616	7,534,952	930,745	-	-	-	12,034,313
Deposits from customers	51,642,610	25,398,229	25,764,039	13,301,812	3,429,934	-	6,544	119,543,168
Certificates of deposit	-	983,648	326,485	1,704,199	235,822	-	-	3,250,154
Debt securities issued	-	-	-	-	1,863,401	-	-	1,863,401
Loan capital	-	-	-	211,635	2,249,254	3,572,622	-	6,033,511
Other financial liabilities	634,341	57,731	189,331	198,366	12,960	-	18,846	1,111,575
Total undiscounted financial liabilities	52,283,241	30,799,643	35,450,170	16,977,713	7,791,371	3,572,622	25,390	146,900,150
Liabilities adjusted with interest payable								
At 31 December 2016								
Deposits and balances of banks	9,033	1,022,328	841,581	835,044	-	-	-	2,707,986
Financial assets sold under repurchase agreements	-	43,412	8,652,452	1,177,071	-	-	-	9,872,935
Deposits from customers	45,383,453	23,329,408	23,520,134	10,852,003	55,439	-	-	103,140,437
Certificates of deposit	-	192,692	232,620	394,320	-	-	-	819,632
Debt securities issued	-	-	-	-	1,728,629	-	-	1,728,629
Loan capital	-	-	-	104,679	2,058,687	-	-	2,163,366
Other financial liabilities	458,917	102,904	145,283	297,284	13,970	-	-	1,018,358
Total undiscounted financial liabilities	45,851,403	24,690,744	33,392,070	13,660,401	3,856,725	-	-	121,451,343

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Management of liquidity risk - continued

The following tables detail the Group's expected maturity for its derivative financial instruments. The tables have been drawn up based on the undiscounted net cash inflows (outflows) on the derivative financial instruments 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 end of the reporting period.

	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 2017						
Derivatives settled net						
Interest rate contracts						
– (Outflows)/inflows	17,192	(2,897)	(173,689)	(593,358)	(368,148)	(1,120,900)
Derivatives settled gross						
Exchange rate contracts						
– Inflows	52,242,666	41,704,574	49,511,651	858,097	–	144,316,988
– Outflows	(52,326,612)	(41,765,222)	(49,513,793)	(858,519)	–	(144,464,146)
	(83,946)	(60,648)	(2,142)	(422)	–	(147,158)
At 31 December 2016						
Derivatives settled net						
Interest rate contracts						
– Outflows	(33,260)	(22,205)	(120,466)	(653,501)	(308,312)	(1,137,744)
Derivatives settled gross						
Exchange rate contracts						
– Inflows	22,231,243	12,246,793	12,474,202	–	–	46,952,238
– Outflows	(22,211,203)	(12,247,625)	(12,483,180)	–	–	(46,942,008)
	20,040	(832)	(8,978)	–	–	10,230

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Management of liquidity risk - continued

The dates of the contractual amounts of the Group's commitments and contingencies unrecorded in the statements of financial position that commit them to extending credit to customers and other facilities and financial guarantees are set out in note 37 to the consolidated financial statements and summarised in the table below:

	No later than 1 year HK\$'000
At 31 December 2017	
Direct credit substitutes	1,315,865
Trade-related contingencies	1,995,688
Undrawn formal standby facilities, credit lines and other commitments excluding those that are unconditionally cancellable without prior notice	10,917,633
	14,229,186
At 31 December 2016	
Direct credit substitutes	805,429
Trade-related contingencies	596,068
Undrawn formal standby facilities, credit lines and other commitments excluding those that are unconditionally cancellable without prior notice	17,277,667
	18,679,164

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Sources of liquidity risk

Liquidity risk can arise from both sides of the on-balance sheet and the off-balance sheet transactions. The major sources of liquidity risk include the maturity mismatches between the Group's assets and liabilities, withdrawal of customers' deposits and drawing of loans by customers. The Group manages liquidity risk by conducting cash flow analysis arising from on-and off-balance sheet items over an appropriate set of time horizons under normal business conditions and stress scenarios on a daily and monthly basis respectively to identify liquidity needs.

The Group's liquidity risk management process also includes the use of liquidity metrics against which statutory and internal limits are set and observed, the design and implementation of early warning indicators of which exceptions should be reported, and the allocation of liquidity costs. The last line of defense is to ensure that the Group has funding capacity supported by good reputation and liquidity cushion.

The Group also measures and manages liquidity risk arising from off-balance sheet exposures and contingent funding obligations such as loan commitments, derivatives and contingent liabilities. Such exposures are subject to the limits set and are also factored into the Group's stress-testing. The Group does not engage in any transactions, such as securitisation, which give rise to the need of providing liquidity support.

Funding strategies

The Group has strong capital base and stable customer deposits which form its main funding sources. Funding diversification is achieved internally through surveillance on large depositors and externally by maintaining its access to the interbank market, issuance of certificates of deposit and through financial assets sold under repurchase agreements and swap markets. All of these are parts of the Group's funding strategy.

The Group's branches outside Hong Kong are mainly self-funded through acquiring customer deposits and maintaining its access to the local interbank market. Nevertheless, it is the Group's policy that the Head Office is to support their liquidity needs when necessary. The funding to branches outside Hong Kong is subject to preset limits so as to encourage them to source their own funding in the local markets.

Liquidity cushion

In order to address and mitigate market liquidity risk, the Group maintains a sufficient portfolio of liquidity cushion which can be sold or used as collateral to provide liquidity even under periods of stress. The Group deploys funds in good credit quality debt securities with deep and liquid markets to ensure short term funding requirements can be covered within prudent limits. The Group periodically obtains liquidity from a proportion of the liquidity cushion through secured borrowing to test the usability of these assets. Liquidity sources and contingency funding plan are maintained to identify early warning indicators of stress conditions, provide strategic liquidity to meet unexpected and material cash outflows and to describe remedial actions to be taken under crisis scenarios.

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Liquidity cushion - continued

The eligible assets as liquidity cushion are mainly debt securities which are unencumbered, low risk, simple structure and traded in active and sizable market with low volatility. Structured products and concentrated positions are not allowed in order to ensure the ease and certainty of valuation. For the liquidity cushion as a whole, there is an appropriate mix of eligible assets to ensure a high degree of diversification by limiting the exposure to each single credit. The liquidity cushion also contains a significant proportion of government issued debt securities with 0% risk-weight for credit risk to minimise risks.

The size of the liquidity cushion should be sufficient for the Group to meet its intraday payment obligations and to cover the day-to-day liquidity needs under both normal and stress market conditions. The Group is not subject to particular collateral arrangements or requirements in contracts if there is a credit rating downgrade of entities within the Group.

The table below shows the estimated value (nominal amount before assumed haircuts) of the liquid assets used for the purposes of liquidity cushion.

Internal Categorisation	Cash to be Recognised	Asset Classes	Eligibility Criteria
Level 1	Within one month	Debt securities issued by central governments or central banks	0% Risk-weight
Level 2A	Within one month	Debt securities issued by public sector entities or non-financial corporate entities	20% Risk-weight
Level 2B	Within one month	Debt securities issued by non-financial corporate entities which are single-A rated	50% Risk-weight

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Liquid assets of the Group

Internal Categorisation	At 31 December 2017 HK\$'000	At 31 December 2016 HK\$'000
Level 1	4,612,548	5,273,589
Level 2A	238,021	1,171,583
Level 2B	4,199,051	4,537,060

The Group's liquidity framework defines the asset classes that can be assessed locally as high quality and realisable within one month. ALCO approves the size and composition of the liquidity cushion in accordance with the Liquidity Risk Management Policy.

Details of liquidity cushion are set out in the Liquidity Risk Management Policy which is reviewed by the ALCO and approved by the EXCO, and reported to the Board on an annual basis.

Stress-testing

The Group supplements the analysis of various types of risks with stress-testing. Stress-testing is a risk management tool for estimating risk exposures under stress conditions arising from extreme but plausible market or macroeconomic movements. Finance Division performs stress-testing on a monthly basis in accordance with the principles stated in the supervisory policy manual LM-2 and IC-5, and when necessary, may carry out special stress-testing in accordance with regulatory requirements and changes in the external operating environment. The stress-test results are regularly reviewed by the ALCO and the RMC, approved by the EXCO and reported to the Board.

In performing the stress-testing on liquidity risk, the Group adopts the cash flow analysis which has taken into consideration of various macroscopic and microscopic factors in line with the characteristics and complexity of the Group's businesses. Both on- and off-balance sheet items with applicable hypothetical, historical and behavioral assumptions are considered to address both funding and market liquidity risks. Four stress scenarios, namely the institution-specific crisis, the modified institution-specific crisis, the general market crisis and the combined crisis are adopted with minimum survival periods defined according to SPM LM-2. With reference to the stress-testing results, the Group identifies potential vulnerabilities on its liquidity position under stress market conditions and formulates the contingency funding plan that sets out remedial actions for dealing with liquidity problems (e.g. conducting repo transactions or liquidation of assets held for liquidity risk management purpose).

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Stress-testing - continued

The Group also performs reverse stress-testing in accordance with SPM IC-5. Reverse stress-testing is an iterative process assisting the Group to identify and assess extreme stress scenarios that can cause business failures (e.g. breaches of regulatory capital ratios, illiquidity and severe negative profitability). It is a process of working backwards from the event causing business failures and involves a mix of qualitative and quantitative analyses. The Group uses results of reverse stress-testing to strengthen resilience to liquidity stress and serve as early-warning triggers for the formulation of management actions and contingency funding plan to mitigate potential stresses and vulnerabilities which the Group might face.

Contingency funding plan

The Group distinguishes between different stages of a liquidity crisis that the Group may face, namely: Funding Stress, Liquidity Drain, Bank Run and recovery zone. The escalation is to reflect the worsening liquidity conditions. This includes the liquidity shortfalls estimated from stress- testing performed.

The Group's contingency funding plan, as stipulated in the Liquidity Risk Management Policy and the Procedures Manual for Contingency Funding Plan, details the Group's immediate action in order to react to emergency. It covers three major components: (1) Predefined conditions to activate the plan; (2) The Group's strategy and potential funding options to deal with different crisis scenarios; and (3) Practical action plans and procedures with clear responsibilities of management and its supporting teams. The ALCO would be called during liquidity crisis to ensure business continuity of the Group.

The Liquidity Risk Management Policy and the Procedures Manual for Contingency Funding Plan are reviewed and updated at least annually to cope with required changes and improvements.

To ensure the contingency funding plan remains practical and effective, drill test is conducted by the Group on an annual basis.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

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 on the statements of financial position, based on the remaining period at the end of the reporting period to the contractual maturity date is shown below:

	Repayable on demand HK\$'000	Repayable within 1 month (except those on demand) HK\$'000	Repayable after 1 month but within 3 months 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	Undated HK\$'000	Total HK\$'000
At 31 December 2017								
Assets								
Cash and short-term funds	9,184,243	12,701,567	2,891,996	386,835	-	-	-	25,164,641
Placements with banks	-	-	4,222,802	2,136,202	-	-	-	6,359,004
Derivative financial instruments	-	86,759	117,664	86,605	137,091	128,674	-	556,793
Financial assets at fair value through profit or loss	-	-	-	-	-	-	265	265
Available-for-sale securities	-	1,081,040	1,239,594	7,142,326	11,303,800	14,595,698	87,834	35,450,292
Held-to-maturity securities	-	61,045	-	124,100	3,455,001	-	-	3,640,146
Loan and receivable securities	-	-	-	62,798	-	-	-	62,798
Advances to customers	1,403,473	3,221,935	9,532,838	14,986,516	39,652,060	17,686,431	215,119	86,698,372
Advances to banks	-	-	-	107,829	-	-	-	107,829
Other financial assets	1,337,148	325,035	1,778,121	616,464	53,835	6,364	26,619	4,143,586
Total financial assets	11,924,864	17,477,381	19,783,015	25,649,675	54,601,787	32,417,167	329,837	162,183,726

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk – continued

Analysis of assets and liabilities by remaining maturity – continued

	Repayable within 1 month	Repayable after 1 month but within 3 months	Repayable after 3 months but within 1 year	Repayable after 1 year but within 5 years	Repayable after 5 years	Undated	Total
	Repayable on demand	(except those on demand)	but within 3 months	but within 1 year	but within 5 years	5 years	HK\$'000
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2017							
Liabilities							
Deposits and balances of banks	6,290	790,916	1,625,477	629,249	-	-	3,051,932
Financial assets sold under repurchase agreements	-	3,566,353	7,512,447	924,189	-	-	12,002,989
Deposits from customers	51,629,989	25,194,216	25,525,257	13,016,732	3,392,480	-	118,758,674
Derivative financial instruments	-	164,583	187,369	82,716	186,234	261,377	882,279
Certificates of deposit	-	980,066	325,248	1,677,645	234,492	-	3,217,451
Debt securities issued	-	-	-	-	1,796,069	-	1,796,069
Loan capital	-	-	-	-	1,615,531	2,925,849	4,541,380
Other financial liabilities	644,967	201,598	320,840	334,379	50,414	-	1,577,588
Total financial liabilities	52,281,246	30,897,732	35,496,638	16,664,910	7,275,220	3,187,226	145,828,362
Net position – total financial assets and liabilities	(40,356,382)	(13,420,351)	(15,713,623)	8,984,765	47,326,567	29,229,941	304,447
Of which debt securities included in:							
Available-for-sale securities	-	1,081,041	1,239,594	7,142,326	11,303,800	14,595,698	35,362,459
Held-to-maturity securities	-	61,045	-	124,100	3,455,001	-	3,640,146
Loan and receivable securities	-	-	-	62,798	-	-	62,798
	-	1,142,086	1,239,594	7,329,224	14,758,801	14,595,698	39,065,403

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Analysis of assets and liabilities by remaining maturity - continued

	Repayable within 1 month Repayable on demand HK\$'000	Repayable (except those on demand) HK\$'000	Repayable after 1 month but within 3 months 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	Undated HK\$'000	Total HK\$'000
At 31 December 2016								
Assets								
Cash and short-term funds	4,001,611	24,396,062	677,032	1,446,576	-	-	-	30,521,281
Placements with banks	-	-	799,236	817,304	-	-	-	1,616,540
Derivative financial instruments	-	67,031	43,512	128,548	73,176	112,578	-	424,845
Financial assets at fair value through profit or loss	-	-	-	-	-	-	241	241
Available-for-sale securities	-	1,421,255	155,517	2,921,618	9,413,411	10,160,467	91,760	24,164,028
Held-to-maturity securities	-	852	366,795	1,409,437	3,287,859	498,740	-	5,563,683
Loan and receivable securities	-	-	-	-	-	-	-	-
Advances to customers	1,516,946	4,257,061	5,215,821	15,551,836	26,561,615	17,405,078	180,798	70,689,155
Advances to banks	-	-	-	389,251	107,005	-	-	496,256
Other financial assets	1,601,690	387,131	203,189	982,696	17,672	-	(296,184)	2,896,194
Total financial assets	7,120,247	30,529,392	7,461,102	23,647,266	39,460,738	28,176,863	(23,385)	136,372,223

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Liquidity risk - continued

Analysis of assets and liabilities by remaining maturity - continued

	Repayable within 1 month Repayable on demand HK\$'000	Repayable within 1 month (except those repayable on demand) HK\$'000	Repayable after 1 month but within 3 months 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	Undated HK\$'000	Total HK\$'000
At 31 December 2016								
Liabilities								
Deposits and balances of banks	9,033	1,013,858	840,552	833,238	-	-	-	2,696,681
Financial assets sold under repurchase agreements	-	43,391	8,634,596	1,167,766	-	-	-	9,845,753
Deposits from customers	45,381,760	23,271,126	23,428,186	10,744,118	55,439	-	-	102,880,629
Derivative financial instruments	-	41,774	29,086	103,717	115,615	263,422	-	553,614
Certificates of deposit	-	190,085	232,004	390,240	-	-	-	812,329
Debt securities issued	-	-	-	-	1,663,774	-	-	1,663,774
Loan capital	-	-	-	-	1,792,267	-	-	1,792,267
Other financial liabilities	464,667	165,098	211,109	389,040	13,975	-	-	1,243,889
Total financial liabilities	45,855,460	24,725,332	33,375,533	13,628,119	3,641,070	263,422	-	121,488,936
Net position - total financial assets and liabilities	(38,735,213)	5,804,060	(25,914,431)	10,019,147	35,819,668	27,913,441	(23,385)	14,883,287
Of which debt securities included in:								
Available-for-sale securities	-	1,421,255	155,517	2,921,618	9,413,411	10,160,467	-	24,072,268
Held-to-maturity securities	-	852	366,795	1,409,437	3,287,859	498,740	-	5,563,683
Loan and receivable securities	-	-	-	-	-	-	-	-
	-	1,422,107	522,312	4,331,055	12,701,270	10,659,207	-	29,635,951

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Fair value of financial assets and financial liabilities

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

	Carrying amount		Fair value	
	2017	2016	2017	2016
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Financial assets				
– Held-to-maturity securities	3,640,146	5,563,683	3,681,149	5,645,930
Financial liabilities				
– Loan capital	4,541,380	1,792,267	4,667,114	1,735,717
– Debt securities issued	1,796,069	1,663,774	1,762,600	1,663,099

The following tables give information about financial assets and financial liabilities which are not measured at fair values at the end of each reporting period, but for which the fair values are disclosed.

	Level 1	Level 2	Level 3	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2017				
Held-to-maturity securities				
Debt securities	–	3,681,149	–	3,681,149
Loan capital	–	4,667,114	–	4,667,114
Debt securities issued	–	1,762,600	–	1,762,600
At 31 December 2016				
Held-to-maturity securities				
Debt securities	–	5,645,930	–	5,645,930
Loan capital	–	1,735,717	–	1,735,717
Debt securities issued	–	1,663,099	–	1,663,099

7. FINANCIAL RISK MANAGEMENT - continued

Fair value of financial assets and financial liabilities – continued

Please refer to next section for the definition of fair value hierarchy.

The fair values of listed securities are determined with reference to quoted market bid prices from relevant stock exchanges.

The fair values of debt securities classified as available-for-sale securities, debt securities classified as held-to-maturity securities and loan capital are determined based on indicative prices provided by the dealers and brokers. In addition, the Group makes comparison of the indicative prices with the prices obtained from pricing service providers and other service providers and with the values calculated using valuation models such as discounted cash flows method to substantiate the indicative prices of the debt securities. The key inputs used in the valuation models are the interest rate data, which are observable at the end of the reporting period. The objective of valuation models is to arrive at a fair value estimation that reflects the price of the financial instrument at the reporting date, which would have been determined by market participants acting at arm's length.

The fair values of foreign currency forward contracts are measured by comparing the contracted forward rates and the quoted forward exchange rates, which are observable at the end of the reporting period.

The fair values of interest rate swaps and cross-currency interest rate swaps are measured by the present value of future cash flows estimated and discounted based on the applicable yield curves derived from quoted interest rates, which are observable at the end of the reporting period.

There were no changes in the Group's valuation techniques during the year.

Fair value measurements recognised in the statements of financial position

Some of the Group's financial assets and financial liabilities are measured at fair values at the end of each reporting period. The following table and paragraph give information about how the fair values of these financial assets and financial liabilities are determined (in particular, the valuation techniques and inputs used), as well as the level of the fair value hierarchy into which the fair value measurements are categorised (Levels 1 to 3) based on the degree to which the inputs to the fair value measurements is observable.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Fair value measurements recognised in the statements of financial position - continued

	Fair value hierarchy			Total HK\$'000
	Level 1 HK\$'000	Level 2 HK\$'000	Level 3 HK\$'000	
At 31 December 2017				
Financial assets at fair value through profit or loss – Held for trading	265	–	–	265
Available-for-sale securities				
Equity securities	53,098	–	277	53,375
Debt securities	–	35,362,459	–	35,362,459
Derivative financial assets not used for hedging	–	374,572	–	374,572
Derivative financial assets used for hedging	–	182,221	–	182,221
Derivative financial liabilities not used for hedging	–	(513,819)	–	(513,819)
Derivative financial liabilities used for hedging	–	(368,460)	–	(368,460)
Total	53,363	35,036,973	277	35,090,613
At 31 December 2016				
Financial assets at fair value through profit or loss – Held for trading	241	–	–	241
Available-for-sale securities				
Equity securities	59,199	–	275	59,474
Debt securities	–	24,072,268	–	24,072,268
Derivative financial assets not used for hedging	–	250,026	–	250,026
Derivative financial assets used for hedging	–	174,819	–	174,819
Derivative financial liabilities not used for hedging	–	(183,762)	–	(183,762)
Derivative financial liabilities used for hedging	–	(369,852)	–	(369,852)
Total	59,440	23,943,499	275	24,003,214

There were no transfers between Levels 1, 2 and 3 in both years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

7. FINANCIAL RISK MANAGEMENT - continued

Fair value measurements recognised in the statements of financial position – continued Reconciliation of Level 3 fair value measurements of financial assets

	Available- for-sale securities HK\$'000	Total HK\$'000
Balance at 1 January 2016	23,331	23,331
Total net losses recognised in the investment revaluation reserve	(84)	(84)
Disposals	(22,972)	(22,972)
Balance at 31 December 2016 and 1 January 2017	275	275
Total net gains recognised in the investment revaluation reserve	2	2
Balance at 31 December 2017	277	277

The majority of the Group's investments are valued based on quoted market information or observable market data. A small percentage, less than 0.01% (2016: 0.01%), of total assets recorded at fair values, are based on estimates and recorded as Level 3 investments. If the carrying amount of these investments would be increased (decreased) by 5%, the impact on other comprehensive income would be increased (decreased) by HK\$14,000 (2016: HK\$14,000) respectively.

Of the total net gains or losses for the year included in other comprehensive income, an amount of HK\$2,000 gains (2016: HK\$84,000 losses) relate to available-for-sale securities held at the end of the reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES SUBJECT TO OFFSETTING, ENFORCEABLE MASTER NETTING ARRANGEMENTS AND SIMILAR AGREEMENTS

The disclosures set out in the tables below include financial assets and financial liabilities that:

- are offset in the Group's statements of financial position; or
- are subject to an enforceable master netting arrangement or similar agreement that covers similar financial instruments, irrespective of whether they are offset in the statements of financial position.

The Group entered into International Swaps and Derivatives Association ("ISDA") Master Agreements and Global Master Repurchase Agreements ("GMRA") for derivatives and sale and repurchase agreements.

The Group's derivative transactions that are not transacted on an exchange are entered into under ISDA Master Agreements. The Group's sale and repurchase transactions are covered by GMRA with netting terms similar to those of ISDA Master Agreements. The ISDA Master Agreements and GMRA do not meet the criteria for offsetting in the statements of financial position. However, they create a right of set off of different contracts that is enforceable only following an event of default, insolvency and bankruptcy of the Group or the counterparties. In such circumstances, all outstanding contracts under the agreements are terminated, the termination value is assessed and only a single net amount is due or payable in settlement of all contracts.

In addition, the Group received and pledged collateral in the form of cash in respect of its derivative transactions and sale and repurchase agreements. Such collateral is subject to the standard industry terms of ISDA Credit Support Annex or GMRA. Collateral received or pledged must be returned on maturity of the transactions.

Under the agreement of Continuous Net Settlement made between the Group and Hong Kong Securities Clearing Company Limited ("HKSCC"), money obligations receivable and payable with HKSCC on the same settlement date are settled on net basis.

The Group has a legally enforceable right to set off the trades receivable and payable with brokerage clients that are due to be settled on the same date and the Group intends to settle these balances on a net basis.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES SUBJECT TO OFFSETTING, ENFORCEABLE MASTER NETTING ARRANGEMENTS AND SIMILAR AGREEMENTS - continued

Types of financial assets	Gross	Gross	Net	Related amounts		Net
	amounts of recognised financial liabilities	amounts of recognised financial liabilities offset in the consolidated statement of financial position	amounts of financial assets presented in the consolidated statement of financial position	not offset in the consolidated statement of financial position		
	Gross amounts of recognised financial assets	offset in the consolidated statement of financial position	consolidated financial position	Financial instruments	Cash/ financial collateral received	amounts
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
					(Note)	
At 31 December 2017						
Derivatives – interest rate swaps	152,612	–	152,612	(149,827)	(1,494)	1,291
Derivatives – foreign currency forward contracts	265,829	–	265,829	(231,859)	(25,901)	8,069
Available-for-sale debt securities	11,203,718	–	11,203,718	(10,500,958)	–	702,760
Held-to-maturity debt securities	1,614,402	–	1,614,402	(1,502,031)	–	112,371
Amounts due from HKSCC and brokerage clients	484,501	(63,896)	420,605	–	–	420,605
Total	13,721,062	(63,896)	13,657,166	(12,384,675)	(27,395)	1,245,096

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES SUBJECT TO OFFSETTING, ENFORCEABLE MASTER NETTING ARRANGEMENTS AND SIMILAR AGREEMENTS - continued

Types of financial liabilities	Gross		Net	Related amounts		
	amounts of recognised financial assets	offset in the consolidated statement of financial position	amounts of financial liabilities presented in the consolidated statement of financial position	not offset in the consolidated statement of financial position	Cash/ financial collateral pledged	Net amounts
	Gross amounts of recognised financial liabilities	offset in the consolidated statement of financial position	amounts of financial liabilities presented in the consolidated statement of financial position	Financial instruments	Cash/ financial collateral pledged	Net amounts
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
At 31 December 2017						
Derivatives – interest rate swaps	335,482	-	335,482	(149,827)	(195,615)	(9,960)
Derivatives – foreign currency forward contracts	408,517	-	408,517	(231,859)	(194,132)	(17,474)
Financial assets sold under repurchase agreements	12,002,989	-	12,002,989	(12,002,989)	(200,171)	(200,171)
Amounts due to HKSCC and brokerage clients	307,647	(63,896)	243,751	-	-	243,751
Total	13,054,635	(63,896)	12,990,739	(12,384,675)	(589,918)	16,146

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES SUBJECT TO OFFSETTING, ENFORCEABLE MASTER NETTING ARRANGEMENTS AND SIMILAR AGREEMENTS - continued

Types of financial assets	Gross amounts of recognised financial assets	Gross amounts of recognised financial liabilities offset in the consolidated statement of financial position	Net amounts of financial assets presented in the consolidated statement of financial position	Related amounts not offset in the consolidated statement of financial position	Cash/financial collateral received	Net amounts
	HK\$'000	HK\$'000	HK\$'000	Financial instruments HK\$'000	HK\$'000 (Note)	HK\$'000
At 31 December 2016						
Derivatives – interest rate swaps	184,632	–	184,632	(165,567)	(26,086)	(7,021)
Derivatives – foreign currency forward contracts	221,802	–	221,802	(103,189)	(117,465)	1,148
Available-for-sale debt securities	8,737,811	–	8,737,811	(8,158,443)	–	579,368
Held-to-maturity debt securities	1,656,879	–	1,656,879	(1,463,104)	–	193,775
Amounts due from HKSCC and brokerage clients	284,413	(24,845)	259,568	–	–	259,568
Total	11,085,537	(24,845)	11,060,692	(9,890,303)	(143,551)	1,026,838

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES SUBJECT TO OFFSETTING, ENFORCEABLE MASTER NETTING ARRANGEMENTS AND SIMILAR AGREEMENTS - continued

Types of financial liabilities	Gross		Net	Related amounts		
	amounts of recognised financial assets	offset in the consolidated statement of financial position	amounts of financial liabilities presented in the consolidated statement of financial position	not offset in the consolidated statement of financial position	Cash/ financial collateral pledged	Net amounts
	HK\$'000	HK\$'000	HK\$'000	Financial instruments	HK\$'000	HK\$'000
<i>(Note)</i>						
At 31 December 2016						
Derivatives – interest rate swaps	376,536	–	376,536	(165,567)	(246,185)	(35,216)
Derivatives – foreign currency forward contracts	152,767	–	152,767	(103,189)	(82,642)	(33,064)
Financial assets sold under repurchase agreements	9,621,547	–	9,621,547	(9,621,547)	(235,736)	(235,736)
Amounts due to HKSCC and brokerage clients	159,521	(24,845)	134,676	–	–	134,676
Total	10,310,371	(24,845)	10,285,526	(9,890,303)	(564,563)	(169,340)

Note: The cash and financial collateral received/pledged as at 31 December 2017 and 31 December 2016 represent in fair value.

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES SUBJECT TO OFFSETTING, ENFORCEABLE MASTER NETTING ARRANGEMENTS AND SIMILAR AGREEMENTS - continued

The gross amounts of financial assets and financial liabilities and their net amounts as presented in the statements of financial position that are disclosed in the above tables are measured in the statements of financial position on the following basis:

- derivative financial assets and liabilities – fair value;
- financial assets sold under repurchase agreements – amortised cost;
- available-for-sale debt securities – fair value;
- held-to-maturity debt securities – amortised cost; and
- amounts due from or due to HKSCC and brokerage clients – amortised cost

The amounts which have been offset against the related recognised financial assets and financial liabilities in the Group's statements of financial position or subject to enforceable master netting arrangements or similar agreements are measured on the same basis as the recognised financial assets and financial liabilities except for available-for-sale debt securities, which are measured on different basis as the related financial assets sold under repurchase agreements. The directors of the Bank consider there are no material differences arising from the measuring differences.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES SUBJECT TO OFFSETTING, ENFORCEABLE MASTER NETTING ARRANGEMENTS AND SIMILAR AGREEMENTS - continued

The tables below reconcile the net amounts of financial assets and financial liabilities presented in the Group's statements of financial position, as set out above, to the line items presented in the Group's statements of financial position.

Types of financial assets	2017 HK\$'000	2016 HK\$'000
Derivatives – interest rate swaps as stated above	152,612	184,632
Derivatives – foreign currency forward contracts as stated above	265,829	221,802
Derivative financial assets not in scope of offsetting disclosures	418,441	406,434
Total derivative financial assets stated in note 18	556,793	424,845
Available-for-sale debt securities as stated above	11,203,718	8,737,811
Available-for-sale securities not in scope of offsetting disclosures	24,246,574	15,426,217
Total available-for-sale securities stated in note 19	35,450,292	24,164,028
Held-to-maturity debt securities as stated above	1,614,402	1,656,879
Held-to-maturity securities not in scope of offsetting disclosures	2,025,744	3,906,804
Total held-to-maturity securities stated in note 19	3,640,146	5,563,683
Amount due from HKSCC and brokerage clients as stated above	420,665	259,568
Other accounts not in scope of offsetting disclosures	3,802,585	2,446,503
Total other accounts stated in note 21	4,223,250	2,706,071

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

8. FINANCIAL ASSETS AND FINANCIAL LIABILITIES SUBJECT TO OFFSETTING, ENFORCEABLE MASTER NETTING ARRANGEMENTS AND SIMILAR AGREEMENTS - continued

Types of financial liabilities	2017 HK\$'000	2016 HK\$'000
Derivatives – interest rate swaps as stated above	335,482	376,536
Derivatives – foreign currency forward contracts as stated above	408,517	152,767
	743,999	529,303
Derivative financial liabilities not in scope of offsetting disclosures	138,280	24,311
Total derivative financial liabilities stated in note 18	882,279	553,614
Financial assets sold under repurchase agreements as stated above	12,002,989	9,621,547
Financial assets sold under repurchase agreements not in scope of offsetting disclosures	–	224,206
Financial assets sold under repurchase agreements stated in note 28	12,002,989	9,845,753
Amounts due to HKSCC and brokerage clients as stated above and included in other accounts	243,751	134,676
Total other accounts and accruals not in scope of offsetting disclosures	1,333,837	1,109,213
Total other accounts and accruals as stated in the Group's statements of financial position	1,577,588	1,243,889

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

9. NET INTEREST INCOME

	2017 HK\$'000	2016 HK\$'000
Interest income		
Balances and placements with central bank and banks	523,975	294,803
Investments in securities	977,210	910,983
Loans and advances	2,299,206	1,780,671
Interest rate swaps	–	14,713
	3,800,391	3,001,170
Interest expense		
Deposits and balances of banks	(125,068)	(75,103)
Deposits from customers	(989,745)	(686,118)
Financial assets sold under repurchase agreements	(162,557)	(66,275)
Certificates of deposit	(20,243)	(6,668)
Debt securities issued	(63,161)	(38,961)
Loan capital in issue	(122,489)	(71,018)
Interest rate swaps	–	(12,227)
	(1,483,263)	(956,370)
Net interest income	2,317,128	2,044,800
Included within interest income		
Interest income on impaired loans and advances	1,701	704

Included within interest income and interest expense are HK\$3,800,391,000 (2016: HK\$2,986,457,000) and HK\$1,483,263,000 (2016: HK\$944,143,000) earned and incurred from financial assets and financial liabilities that are not at fair value through profit or loss, respectively.

Included above is interest income from unlisted investments in debt securities of HK\$977,210,000 (2016: HK\$910,983,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

10. NET FEE AND COMMISSION INCOME

	2017 <i>HK\$'000</i>	2016 <i>HK\$'000</i>
Fee and commission income		
Securities dealings	145,356	109,234
Credit lines	48,282	26,972
Trade finance	16,261	13,962
Credit card services	101,567	91,610
Agency services	85,780	85,780
Others	27,299	16,936
Total fee and commission income	424,545	344,494
Less: Fee and commission expenses	(97,074)	(84,910)
Net fee and commission income	327,471	259,584
of which:		
Net fee and commission, 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 through profit or loss		
– Fee income	172,967	139,879
– Fee expenses	(92,218)	(83,138)
	80,749	56,741

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

11. NET (LOSS) INCOME FROM TRADING AND INVESTMENTS

	Note	2017 HK\$'000	2016 HK\$'000
Foreign exchange		(216,314)	201,704
Net gains from financial assets designated at fair value		964	919
Net gains on financial instruments at fair value through profit or loss		6,052	2,867
Net gains (losses) on fair value hedge:			
– Net losses on hedged items attributable to the hedged risk		(113,864)	(312,858)
– Net gains on hedging instruments		115,287	319,847
Net gains on disposal of available-for-sale securities	19		
– Debt securities		106,435	17,580
– Equity securities		7,502	–
		(93,938)	230,059

“Net (loss) income from trading and investments – foreign exchange” includes gains and losses from spots and forward contracts, swaps and translated foreign currency assets and liabilities, which are not designated as qualifying hedging relationship.

The Group entered into foreign exchange swaps for its liquidity management and funding activities. It involves swapping a currency (“original currency”) into another currency (“swap currency”) at the spot exchange rate for short-term placement and simultaneously entering into a forward contract to convert the funds back to the original currency on maturity of the placement. The exchange difference between the spot and forward contracts is recognised as a gain or loss in “net (loss) income from trading and investments – foreign exchange”, while the corresponding interest differential between the surplus funds in the original currency and swap currency is reflected in net interest income.

“Net (loss) income from trading and investments – foreign exchange” also includes certain translation gains and losses reported in accordance with Hong Kong Accounting Standard 21 “The Effects of Changes in Foreign Exchange Rates” in relation to the Group’s Mainland Operation. There were translation losses of approximately HK\$56 million (2016: gains of HK\$56 million) arising from translation of non-Renminbi net monetary assets maintained in the Mainland branches and there were translation losses of approximately HK\$139 million (2016: gains of HK\$70 million) arising from the translation of Renminbi net monetary liabilities at Head Office level in relation to the working capital provided to the Mainland branches. These translation losses from monetary items had been reported as “net (loss) income from trading and investments – foreign exchange” whereas the corresponding translation gains from the consolidation of the Mainland branches had been reported as part of exchange differences arising on translation under other comprehensive income.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

12. OTHER OPERATING INCOME

	2017 HK\$'000	2016 HK\$'000
Dividend income		
– Listed investments	2,092	5,922
– Unlisted investments	6,119	5,868
	8,211	11,790
Gross rents from investment properties	8,432	7,399
Less: Outgoings	17	(1,640)
Net rental income	8,449	5,759
Safe deposit box rentals	53,567	51,088
Insurance underwriting premiums less claims and commission expenses	14,269	13,158
Other banking services income	55,734	51,082
Gain on retirement benefit	323	–
Others	18,342	6,976
	158,895	139,853

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

13. OPERATING EXPENSES

	2017 HK\$'000	2016 HK\$'000
Auditor's remuneration		
– Audit services – current year	6,263	5,134
– Audit services – under provision in prior year	–	615
– Non-audit services	917	2,985
Total auditor's remuneration	7,180	8,734
Staff costs (including directors' emoluments)		
– Salaries and other costs	789,341	709,038
– Retirement benefits scheme contributions	48,937	41,615
– Capitalised to intangible assets	(34,697)	(30,693)
Total staff costs	803,581	719,960
Depreciation	84,137	62,629
– Capitalised to intangible assets	(4,168)	(4,182)
	79,969	58,447
Release of prepaid lease payments for land	66	66
Premises and equipment expenses, excluding depreciation and release of prepaid lease payments for land		
– Rentals and rates for premises	147,038	136,303
– Capitalised to intangible assets	(3,623)	(5,025)
	143,415	131,278
– Others	33,987	29,675
Other operating expenses	287,004	281,518
– Capitalised to intangible assets	(1,569)	(2,126)
	285,435	279,392
	1,353,633	1,227,552

Included in the premises and equipment expenses are minimum lease payments under operating lease of HK\$138,286,000 (2016: HK\$127,072,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

14. TAXATION

	2017 HK\$'000	2016 HK\$'000
The tax charge comprises:		
Hong Kong Profits Tax		
– Current year	109,377	235,009
– Under (over) provision in prior years	312	(133)
Overseas taxation		
– Current year	34,557	26,632
– Over provision in prior years	–	(509)
Deferred tax (Note 34)	152	3,297
	144,398	264,296

Hong Kong Profits Tax is calculated at 16.5% (2016: 16.5%) 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 before taxation per the consolidated income statement as follows:

	2017 HK\$'000	2016 HK\$'000
Profit before taxation	1,709,265	1,684,000
Tax at the domestic income tax rate of 16.5% (2016: 16.5%)	282,029	277,859
Tax effect of share of profits of associates	(9,194)	(5,217)
Tax effect of expenses not deductible for tax purpose	17,852	1,719
Tax effect of income not taxable for tax purpose	(120,921)	(9,752)
Under (over) provision in prior years	312	(642)
Effect of different tax rates of subsidiaries and branches operating in other jurisdictions	3,828	472
Others	(29,508)	(143)
Tax charge for the year	144,398	264,296

Included in the "Others" is mainly the tax effect on deductibility of additional tier 1 capital distribution of HK\$151,974,000 (2016: Nil).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

15. DIVIDENDS

	2017 HK\$'000	2016 HK\$'000
Dividends recognised as distribution to ordinary shareholders during the year:		
2017 Interim – HK\$0.15 (2016: Interim – HK\$0.15) per share	97,875	97,875
2016 Final – HK\$0.39 (2015: Final – HK\$0.37) per share	254,475	241,425
	352,350	339,300

The final dividend of HK\$0.39 per share, totalling HK\$254,475,000, in respect of the current financial year (2016: HK\$0.39 per share, totalling HK\$254,475,000) has been proposed by the Board and is subject to approval by the shareholders in the forthcoming annual general meeting of the shareholders.

At the board meeting on 25 August 2017, the Board declared a total amount of interim dividend of HK\$97,875,000 (2016: HK\$97,875,000) at a rate of HK\$0.15 (2016: HK\$0.15) per share. The interim dividend was paid on 25 September 2017.

16. EARNINGS PER SHARE – BASIC AND DILUTED

The calculation of basic earnings per share is based on the profit attributable to equity owners of the Bank of HK\$1,564,867,000 (2016: HK\$1,419,704,000) with deduction of distribution payment for additional equity instruments of HK\$151,974,000 (2016: HK\$151,425,000) on 652,500,000 (2016: 652,500,000) weighted average ordinary shares in issue during the year.

As at 31 December 2017 and 31 December 2016, there were no potential dilutive instrument in issue.

17. CASH AND SHORT-TERM FUNDS

	2017 HK\$'000	2016 HK\$'000
Cash and balances with central bank and banks	9,593,548	4,009,869
Money at call and short notice	11,170,870	23,415,448
Exchange fund bills	4,400,223	3,095,964
	25,164,641	30,521,281

Included in the “Cash and balances with central bank and banks” are surplus reserve deposits placed with People’s Bank of China by the Mainland branches of HK\$378,234,000 (2016: HK\$376,287,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

18. DERIVATIVE FINANCIAL INSTRUMENTS

	2017			2016		
	Notional amount HK\$'000	Fair value		Notional amount HK\$'000	Fair value	
		Assets HK\$'000	Liabilities HK\$'000		Assets HK\$'000	Liabilities HK\$'000
Derivatives held for trading						
– Foreign currency forward contracts	148,149,348	361,561	500,892	46,805,949	238,799	173,054
– Foreign currency options	4,490,336	898	898	–	–	–
– Interest rate swaps	5,314,612	12,113	12,029	567,520	11,227	10,708
Derivatives designated as hedging instruments						
– Interest rate swaps	24,642,872	182,221	368,460	16,284,175	174,819	369,852
		556,793	882,279		424,845	553,614

As at 31 December 2017 and 31 December 2016, all foreign currency forward contracts have settlement dates within four years (2016: one year) from the end of the reporting period.

The remaining maturity of interest rate swaps held for trading is within 10 years (2016: within 10 years).

The credit risk-weighted amounts of derivative exposures calculated based on the Banking (Capital) Rules of the Hong Kong Banking Ordinance are as follows:

	2017			2016		
	Notional amount HK\$'000	Replacement cost HK\$'000	Credit risk- weighted amount HK\$'000	Notional amount HK\$'000	Replacement cost HK\$'000	Credit risk- weighted amount HK\$'000
Exchange rate contracts	152,639,684	362,459	699,625	46,805,949	238,799	222,385
Interest rate contracts	29,957,484	194,334	167,938	16,851,695	186,046	113,171
		556,793	867,563		424,845	335,556

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

18. DERIVATIVE FINANCIAL INSTRUMENTS - continued

Replacement cost is the cost which would be incurred by the Group if it was required to enter into another contract to replace the existing transaction or existing contract with another counterparty with substantially the same economic consequences for the Group and is calculated by marking-to-market the existing transaction or existing contract. If the resultant value is positive for the Group, the replacement cost shall be the resultant value of the existing transaction or existing contract. If the resultant value is negative for the Group, the replacement cost shall be zero. Replacement cost is a close approximation of the credit risk for these contracts at the end of the reporting period.

The derivative financial instruments including exchange rate contracts and interest rate contracts have been recognised in the statements of financial position at fair values.

The fair values of the derivative financial instruments do not take into account the effect of any bilateral netting agreements.

Fair value hedge of fixed-rate bonds

The Group designates certain interest rate swaps as fair value hedges of available-for-sale debt securities with carrying amount of HK\$20,591,803,000 (2016: HK\$15,011,658,000) as at 31 December 2017. The purpose is to minimise its exposure to fair value changes of its fixed-rate bonds by swapping these fixed-rate bonds from fixed rates to floating rates. The interest rate swaps and the corresponding fixed-rate bonds have the same terms. The management of the Group considers that the interest rate swaps are highly effective hedging instruments. The remaining maturity of these interest rate swaps and debt securities ranged from 3 months to 10 years (2016: 5 months to 9 years).

During the years ended 31 December 2017 and 31 December 2016, the above fair value hedges were effective in hedging the fair value exposures to interest rate movements and as a result, both the losses in fair value of the bonds of HK\$184,159,000 (2016: losses of HK\$342,602,000) and gains in fair value of the interest rate swaps of HK\$183,949,000 (2016: gain of HK\$346,203,000) were included in the consolidated income statement.

Fair value hedge of subordinated note issued

The Group designates an interest rate swap as fair value hedge of the interest rate movement of the US\$587 million (2016: US\$225 million) subordinated note issued (see note 31). The purpose is to minimise its exposure to fair value changes of its fixed-rate note by swapping fixed-rate note from fixed rate to floating rate. The interest rate swap and the hedged subordinated note have the same terms and the management of the Group considers that the interest rate swap is a highly effective hedging instrument.

The hedge was effective in hedging the fair value exposure to interest rate movements and as a result, both the increase in fair value of the note of HK\$70,295,000 (2016: decrease in fair value of HK\$29,744,000) and gains in fair value of the interest rate swap of HK\$68,662,000 (2016: losses of HK\$26,356,000) were included in the consolidated income statement.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

19. INVESTMENTS IN SECURITIES

	Financial assets at fair value through profit or loss – Held for trading HK\$'000	Available- for-sale securities HK\$'000	Held-to- maturity securities HK\$'000	Loan and receivable securities HK\$'000	Total HK\$'000
2017					
Equity securities:					
Listed in Hong Kong	265	49,166	–	–	49,431
Listed overseas	–	3,932	–	–	3,932
	265	53,098	–	–	53,363
Unlisted	–	34,735	–	–	34,735
	265	87,833	–	–	88,098
Debt securities:					
Unlisted	–	35,362,459	3,640,146	62,798	39,065,403
Total:					
Listed in Hong Kong	265	49,166	–	–	49,431
Listed overseas	–	3,932	–	–	3,932
Unlisted	–	35,397,194	3,640,146	62,798	39,100,138
	265	35,450,292	3,640,146	62,798	39,153,501
As analysed by issuing entities:					
Central governments and central banks	–	4,101,191	–	–	4,101,191
Public sector entities	–	–	–	–	–
Banks	–	13,024,732	836,787	62,798	13,924,317
Corporate entities	265	18,324,369	2,803,359	–	21,127,993
	265	35,450,292	3,640,146	62,798	39,153,501

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

19. INVESTMENTS IN SECURITIES - continued

	Financial assets at fair value through profit or loss – Held for trading HK\$'000	Available- for-sale securities HK\$'000	Held-to- maturity securities HK\$'000	Loan and receivable securities HK\$'000	Total HK\$'000
2016					
Equity securities:					
Listed in Hong Kong	241	56,882	–	–	57,123
Listed overseas	–	2,317	–	–	2,317
	241	59,199	–	–	59,440
Unlisted	–	32,561	–	–	32,561
	241	91,760	–	–	92,001
Debt securities:					
Unlisted	–	24,072,268	5,563,683	–	29,635,951
Total:					
Listed in Hong Kong	241	56,882	–	–	57,123
Listed overseas	–	2,317	–	–	2,317
Unlisted	–	24,104,829	5,563,683	–	29,668,512
	241	24,164,028	5,563,683	–	29,727,952
As analysed by issuing entities:					
Central governments and central banks	–	4,006,693	4,645	–	4,011,338
Public sector entities	–	26	39,234	–	39,260
Banks	–	7,314,551	941,530	–	8,256,081
Corporate entities	241	12,842,758	4,578,274	–	17,421,273
	241	24,164,028	5,563,683	–	29,727,952

19. INVESTMENTS IN SECURITIES - continued

For the equity securities classified as available-for-sale financial instruments, impairment losses accumulated through the years of HK\$18,022,400 (2016: HK\$14,978,000) have been provided by the Group.

Unlisted equity securities classified as available-for-sale held by the Group amounting to HK\$34,735,000 (2016: HK\$32,286,000) are measured at cost less impairment. No impairment has been recognised for these equity securities.

No held-to-maturity certificates of deposit (2016: HK\$775,000) held by the San Francisco representative office of the Bank has been pledged to the State of California of the United States of America in compliance with the requirements of the California Financial Code.

Debt securities classified as available-for-sale and held-to-maturity amounting to HK\$238,061,000 (2016: HK\$231,712,000) and HK\$Nil (2016: HK\$4,645,000) respectively were issued by the Government of Hong Kong Special Administrative Region and the Mainland.

The debt securities classified as available-for-sale and held-to-maturity held by the Group are mainly guaranteed or issued by corporates and financial institutions from the Mainland and Hong Kong.

The Group has disposed certain securities classified as available-for-sale financial instruments during the year ended 31 December 2017 and 31 December 2016. Net gains on disposal of available-for-sale securities included in net (loss) income from trading and investments (note 11) (refers to the gains on the disposal of securities which form part of the business operation). Net gains on disposal of other investments refers to the gains on the disposal of equity investments and structured investment vehicles which were held for capital appreciation.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

20. TRANSFER OF FINANCIAL ASSETS

The following were the Group's debt securities classified as held-to-maturity and available-for-sale as at 31 December 2017 and 31 December 2016 that were transferred to an entity with terms to repurchase these debt securities at agreed dates and prices. As the Group has retained substantially all the risks and rewards relating to these debt securities, the full carrying amount of these debt securities continued to be recognised. The cash received on the transfer was reported as liabilities under "Financial assets sold under repurchase agreements" (see note 28). The transferred debt securities serve as collateral to secure these liabilities. During the covered period, the legal title of the debt securities are transferred to the counterparty entity and there is no restriction for the counterparty entity to sell or repledge the collateral. These debt securities are either measured at amortised cost or carried at fair value in the consolidated statement of financial position.

	31 December 2017		
	Available- for-sale debt securities HK\$'000	Held-to- maturity debt securities HK\$'000	Total HK\$'000
Carrying amount of transferred assets	11,743,378	1,929,075	13,672,453
Carrying amount of associated liabilities (Note 28)	10,840,377	1,162,612	12,002,989

	31 December 2016		
	Available- for-sale debt securities HK\$'000	Held-to- maturity debt securities HK\$'000	Total HK\$'000
Carrying amount of transferred assets	8,967,269	1,656,879	10,624,148
Carrying amount of associated liabilities (Note 28)	8,382,649	1,463,104	9,845,753

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

21. ADVANCES AND OTHER ACCOUNTS

	2017 HK\$'000	2016 HK\$'000
Advances to customers		
Bills receivable	845,295	564,206
Trade bills	283,588	801,981
Other advances to customers	85,569,489	69,322,968
	86,698,372	70,689,155
Interest receivable	644,368	481,079
Impairment allowances		
– Individually assessed	(394,393)	(39,737)
– Collectively assessed	(329,639)	(251,219)
	86,618,708	70,879,278
Advances to banks	107,829	496,256
Other accounts	4,223,250	2,706,071
	90,949,787	74,081,605

Included in the “Other accounts” is initial and variation margin of HK\$849,906,000 (2016: HK\$538,331,000) deposited in banks for certain interest rate swaps, foreign currency forward contracts and repurchase agreements and an amount of approximately HK\$2,657,492,000 (2016: HK\$1,548,577,000) placed as reserve funds with banks in the Mainland by the Mainland branches. Among which, HK\$1,776,005,000 (2016: HK\$716,623,000) are the mandatory reserve deposits placed with the People’s Bank of China. The mandatory reserve deposits are not available for the Group’s daily operation; HK\$881,487,000 (2016: HK\$831,954,000) are the fixed deposits placed with financial institutions in the Mainland in compliance with the requirements of Regulations Governing Foreign Financial Institutions of the Mainland.

The remaining balance of “Other accounts” amounting to HK\$715,852,000 (2016: HK\$619,163,000) mainly included account receivables from Hong Kong Securities Clearing Company Limited, Hong Kong Futures Exchange Clearing Corporation Limited and brokerage clients in relation to securities dealing of HK\$420,605,000 (2016: HK\$259,568,000).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

21. ADVANCES AND OTHER ACCOUNTS - continued

Impairment allowances on advances:

	Individual assessment HK\$'000	Collective assessment HK\$'000	Total HK\$'000
Balance 1 January 2017	39,737	251,219	290,956
– Increase in impairment allowances	366,022	74,543	440,565
– Amounts reversed	(68,974)	–	(68,974)
Net charge of impairment allowances	297,048	74,543	371,591
Amounts written off	(4,487)	–	(4,487)
Recoveries of advances written off in previous years	63,796	–	63,796
Unwinding effect of discount rate	(1,701)	–	(1,701)
Exchange difference	–	3,877	3,877
Balance 31 December 2017	394,393	329,639	724,032
Balance 1 January 2016	23,688	250,494	274,182
– Increase in impairment allowances	27,070	2,167	29,237
– Amounts reversed	(69,435)	–	(69,435)
Net charge (reversal) of impairment allowances	(42,365)	2,167	(40,198)
Amounts written off	(5,758)	–	(5,758)
Recoveries of advances written off in previous years	64,876	–	64,876
Unwinding effect of discount rate	(704)	–	(704)
Exchange difference	–	(1,442)	(1,442)
Balance 31 December 2016	39,737	251,219	290,956

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

21. ADVANCES AND OTHER ACCOUNTS - continued

Details of the impaired loans are as follows:

	2017 HK\$'000	2016 HK\$'000
Gross impaired loans	398,100	48,253
Less: Impairment allowances under individual assessment	(394,393)	(39,737)
Net impaired loans	3,707	8,516
Gross impaired loans as a percentage of gross advances to customers	0.46%	0.07%
Market value of collateral pledged	3,873	9,150

Details of the non-performing loans are as follows:

	2017 HK\$'000	2016 HK\$'000
Gross non-performing loans (<i>Note</i>)	485,492	449,772
Less: Impairment allowances under individual assessment	(394,393)	(39,737)
Net non-performing loans	91,099	410,035
Gross non-performing loans as a percentage of gross advances to customers	0.56%	0.64%
Market value of collateral pledged	200,716	760,420

Note: Non-performing loans represent advances which are either classified as “substandard”, “doubtful” or “loss” under the Group’s classification of loan quality. The occurrence of loss event(s) may not necessarily result in impairment loss where the advances are fully collateralised. While such advances are of “substandard” or lower grades, they are regarded as not being impaired.

In accordance with HKAS 39, 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 increase in impairment allowances under individual allowances for the year ended 31 December 2017 was mainly due to one corporate credit relationship, which is engaged in various business segments including food production based in Mainland China, and is undergoing winding up proceedings. The exposure was fully provided for individual impairment allowances as at 31 December 2017.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

22. SUBSIDIARIES

Name of company	Place of incorporation and kind of legal entity	Issued share capital	Percentage of issued share capital held by the Group	Principal activities and place of operation
Chong Hing (Nominees) Limited	Hong Kong, limited liability company	HK\$ 100,000	100%	Provision of nominee services in Hong Kong
Chong Hing Finance Limited	Hong Kong, limited liability company	HK\$ 25,000,000	100%	Deposit-taking and lending in Hong Kong
Chong Hing Information Technology Limited	Hong Kong, limited liability company	HK\$ 100,000	100%	Provision of electronic data processing services in Hong Kong
Chong Hing Securities Limited	Hong Kong, limited liability company	HK\$ 10,000,000	100%	Stockbroking in Hong Kong
Chong Hing Commodities and Futures Limited	Hong Kong, limited liability company	HK\$ 5,000,000	100%	Investment holding and commodities and futures broking in Hong Kong
Gallbraith Limited	Hong Kong, limited liability company	HK\$ 16,550,000	100%	Property investment in Mainland China
Top Benefit Enterprise Limited	Hong Kong, limited liability company	HK\$ 100,000	100%	Property investment in Hong Kong
Card Alliance Company Limited	Hong Kong, limited liability company	HK\$ 18,000,000	100%	Credit card management in Hong Kong
Chong Hing Insurance Company Limited	Hong Kong, limited liability company	HK\$ 85,000,000	100%	Insurance underwriting in Hong Kong
Hero Marker Limited	Hong Kong, limited liability company	HK\$ 100,000	100%	Property investment in Hong Kong

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

22. SUBSIDIARIES - continued

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

The above table lists the subsidiaries of the Group which, in the opinion of the directors, principally affected the results of the year or form a substantial portion of the net assets of the Group. In the opinion of the directors, listing details of other subsidiaries would result in particulars of excessive length.

23. INTERESTS IN ASSOCIATES

	2017 HK\$'000	2016 HK\$'000
Share of post-acquisition profits and other comprehensive income net of dividends received	301,337	262,565

The directors consider the Group have significant influence over these entities.

As at 31 December 2017 and 2016, the Group had interests in the following associates:

Name of company	Place of incorporation and operation	Class of share held	Ownership interest	Proportion of voting power (Note)	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 (Dissolved on 8 February 2018)	Hong Kong	Ordinary	17.6%	17.6%	Provision of internet services

Note: The Group is able to exercise significant influence over all of these entities because it has the power to appoint one out of twelve to two out of eight directors of these companies.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

23. INTERESTS IN ASSOCIATES - continued

All of these associates are accounted for using the equity method in these consolidated financial statements.

The summarised financial information below represent the aggregate amount of the Group's share of its interests in associates which are not individually material:

	2017 HK\$'000	2016 HK\$'000
Other comprehensive income	4,647	497
Profit after tax	55,723	31,617
Total comprehensive income	60,370	32,114

There are no significant restrictions on the ability of the associates to transfer funds to the Group in the form of cash dividends, except for Hong Kong Life Insurance Limited ("HKLI") which has to maintain net assets of not less than 150% of the required margin of solvency which is determined in accordance with the Hong Kong Insurance Companies (Margin of Solvency) Regulations and which may trigger restrictions to fund transfer.

On 20 March 2017, the Group entered into a Share Sale Agreement (the "Agreement") to sell the Group's stake in HKLI to First Origin International Limited (the "Purchaser") for a consideration of approximately HK\$1,183,333,000 (the "Disposal"). Under the Agreement, the closing of the Disposal is subject to the satisfaction of certain conditions. As at 31 December 2017, the Group's interest in HKLI is accounted for using the equity method as the Disposal was not completed. On 15 March 2018, the Group and the Purchaser agreed to extend the long stop date to 30 September 2018 or to a date falling no later than 24 months after the date of the Agreement.

24. ASSETS HELD FOR SALE

The carrying amount of assets held for sale comprises:

	2017 HK\$'000	2016 HK\$'000
Leasehold land and buildings in Hong Kong Held on medium-term lease (10-50 years expired)	-	2

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

25. INVESTMENT PROPERTIES

	2017 <i>HK\$'000</i>	2016 <i>HK\$'000</i>
At 1 January	282,927	264,222
Transfer from land and buildings	–	19,000
Net increase in fair value recognised in the profit or loss	12,632	2,026
Exchange adjustments	3,206	(2,321)
At 31 December	298,765	282,927

All of the Group's property interests held under operating leases to earn rentals and/or for capital appreciation purposes are measured using the fair value model and are classified and accounted for as investment properties.

Investment properties owned by the Group were revalued at 31 December 2017 by adopting the direct comparison approach (2016: direct comparison approach) and with reference to the recent transactions for similar premises by Vigers Appraisal and Consulting Limited (2016: Vigers Appraisal and Consulting Limited), independent professionally qualified valuers. The fair value is mainly arrived at by reference to comparable market transactions for similar properties.

In estimating the fair value of the properties, the highest and best use of the properties is their current use.

One of the key inputs used in valuing the investment properties was the unit sale rate taking into account of time, location and individual factors such as size and levels of building, which ranged from HK\$3,300 to HK\$49,400 (2016: HK\$3,000 to HK\$47,900) per square feet. A decrease in the unit sale rate would result in decrease in fair value measurement of the investment properties by the same percentage decrease and vice versa.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

25. INVESTMENT PROPERTIES - continued

In estimating the fair value of the Group's investment properties, the management of the Group uses market-observable data to the extent it is available. Where Level 1 inputs are not available, the management of the Group engages third party qualified valuers to perform the valuation of the Group's investment properties. At the end of each reporting period, the management of the Group works closely with the qualified external valuers to establish and determine the appropriate valuation techniques and inputs for Level 2 and Level 3 fair value measurement. The management of the Group will first consider and adopt Level 2 inputs where inputs can be derived from observable quoted prices in the active market. When Level 2 inputs are not available, the management of the Group will adopt valuation techniques that include Level 3 inputs. Where there is a material change in the fair value of the assets, the causes of the fluctuations will be reported to the directors of the Bank.

Information about the valuation techniques and inputs in determining the fair value of the Group's investment properties are disclosed above.

Investment properties are classified as Level 3 under fair value hierarchy as at 31 December 2017 and 31 December 2016. There were no transfers into or out of Level 3 during the year.

The investment properties are rented out under operating leases or are held for capital appreciation purposes.

The carrying amount of investment properties of the Group comprises:

	2017 HK\$'000	2016 HK\$'000
Leasehold properties		
Held in Hong Kong on long-term lease (over 50 years unexpired)	164,500	159,700
Held in Hong Kong on medium-term lease (10 – 50 years unexpired)	87,500	84,300
Held outside Hong Kong on medium-term lease (10 – 50 years unexpired)	46,765	38,927
	298,765	282,927

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

26. PROPERTY AND EQUIPMENT

	Leasehold land HK\$'000	Buildings HK\$'000	Equipment HK\$'000	Total HK\$'000
COST				
At 1 January 2017	478,312	161,440	705,814	1,345,566
Additions	–	–	133,276	133,276
Disposals	(133,055)	(49,048)	(24,078)	(206,181)
Exchange adjustments	–	825	10,172	10,997
At 31 December 2017	345,257	113,217	825,184	1,283,658
ACCUMULATED DEPRECIATION				
At 1 January 2017	140,206	51,501	520,255	711,962
Depreciation	9,863	3,604	70,670	84,137
Eliminated on disposals	(66,790)	(22,150)	(18,059)	(106,999)
Exchange adjustments	–	32	3,780	3,812
At 31 December 2017	83,279	32,987	576,646	692,912
CARRYING AMOUNTS				
At 31 December 2017	261,978	80,230	248,538	590,746
At 1 January 2017	338,106	109,939	185,559	633,604

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

26. PROPERTY AND EQUIPMENT - continued

	Leasehold land HK\$'000	Buildings HK\$'000	Equipment HK\$'000	Total HK\$'000
COST				
At 1 January 2016	486,181	163,595	641,040	1,290,816
Additions	–	–	82,389	82,389
Disposals	(3,661)	(814)	(13,356)	(17,831)
Transfer to assets held for sale	(6)	(20)	–	(26)
Transfer to investment properties	(4,202)	(1,070)	–	(5,272)
Exchange adjustments	–	(251)	(4,259)	(4,510)
At 31 December 2016	478,312	161,440	705,814	1,345,566
ACCUMULATED DEPRECIATION				
At 1 January 2016	131,429	48,663	482,947	663,039
Depreciation	10,805	4,072	47,752	62,629
Eliminated on disposals	(93)	(534)	(8,795)	(9,422)
Transfer to assets held for sale	(4)	(20)	–	(24)
Transfer to investment properties	(1,931)	(570)	–	(2,501)
Exchange adjustments	–	(110)	(1,649)	(1,759)
At 31 December 2016	140,206	51,501	520,255	711,962
CARRYING AMOUNTS				
At 31 December 2016	338,106	109,939	185,559	633,604
At 1 January 2016	354,752	114,932	158,093	627,777

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

26. PROPERTY AND EQUIPMENT - continued

The carrying amounts of leasehold land shown above comprise:

	2017 HK\$'000	2016 HK\$'000
Leasehold land in Hong Kong:		
Held on long-term lease (over 50 years unexpired)	28,881	33,507
Held on medium-term lease (10 – 50 years unexpired)	232,236	303,775
Leasehold land outside Hong Kong:		
Held on medium-term lease (10 – 50 years unexpired)	861	824
	261,978	338,106

The carrying amounts of buildings shown above comprise:

	2017 HK\$'000	2016 HK\$'000
Building		
Held in Hong Kong on long-term lease (over 50 years unexpired)	5,493	7,959
Held in Hong Kong on medium-term lease (10-50 years unexpired)	68,334	96,031
Held outside Hong Kong on medium-term lease (10-50 years unexpired)	6,403	5,949
	80,230	109,939

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

27. PREPAID LEASE PAYMENTS FOR LAND

The Group's prepaid lease payments for land comprise:

	2017 HK\$'000	2016 HK\$'000
COST		
Outside Hong Kong held on:		
Leases of between 10-50 years	2,850	2,850
Net book value at 1 January	2,201	2,269
Release of prepaid operating lease payments	(66)	(66)
Exchange adjustments	(1)	(2)
Net book value at 31 December	2,134	2,201
Analysed as:		
Current portion	66	66
Non-current portion	2,068	2,135
Total	2,134	2,201

28. FINANCIAL ASSETS SOLD UNDER REPURCHASE AGREEMENTS

	2017 HK\$'000	2016 HK\$'000
Analysed by collateral type:		
Debt securities classified as:		
Available-for-sale (Note 20)	10,840,377	8,382,649
Held-to-maturity (Note 20)	1,162,612	1,463,104
	12,002,989	9,845,753

As at 31 December 2017, debt securities which are classified as available-for-sale and held-to-maturity with carrying amount of HK\$11,743,378,000 (2016: HK\$8,967,269,000) and HK\$1,929,075,000 (2016: HK\$1,656,879,000) respectively were sold under repurchase agreements with other banks. All repurchase agreements are due within 12 months from the end of the reporting period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

29. DEPOSITS FROM CUSTOMERS

	2017 HK\$'000	2016 HK\$'000
Demand deposits and current accounts	12,624,082	9,508,384
Savings deposits	37,667,095	35,751,109
Time, call and notice deposits	68,467,497	57,621,136
	118,758,674	102,880,629

30. CERTIFICATES OF DEPOSIT AND DEBT SECURITIES ISSUED

The Group has issued certificates of deposit which are measured at amortised cost with a total carrying amount of HK\$3,217,451,000 as at 31 December 2017 (2016: HK\$812,329,000). Certificates of deposit bear contractual interest rates between 0.95% to 4.65% (2016: 1.10% to 1.41%) per annum and will mature within 3 years (2016: 1 year). All certificates of deposit issued are not secured by any collateral.

The Group has issued debt securities which are measured at amortised cost with a total carrying amount of HK\$1,796,069,000 as at 31 December 2017 (2016: HK\$1,663,774,000). The debt securities issued bear contractual interest rate at 3.6% per annum (2016: 3.6% per annum) and will mature in May 2019. The debt securities issued are not secured by any collateral.

Analysis of changes in financing cash flows of debt securities issued during the year

	2017 HK\$'000
At 1 January 2017	1,663,774
Changes from financing cash flows:	
Interest paid on debt securities issued	(58,349)
	1,605,425
Exchange adjustments	130,350
Other changes	
Interest expense	63,161
Other non-cash movements	(2,867)
Total other changes	60,294
At 31 December 2017	1,796,069

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

31. LOAN CAPITAL

	2017 HK\$'000	2016 HK\$'000
Subordinated notes, at amortised cost with fair value hedge adjustments		
US\$204 million (2016: US\$225 million) fixed rate subordinated note due 2020 (Notes (a) & (c))	1,615,531	1,792,267
US\$383 million fixed rate subordinated note due 2027 (Notes (b) & (c))	2,925,849	-
	4,541,380	1,792,267

Notes:

- (a) This represented a subordinated note qualifying as tier 2 capital under Basel II accord with face value of US\$225,000,000 issued on 5 November 2010 (the "Existing Notes"). The note will mature on 4 November 2020. If at any time on or after 1 January 2013, the note no longer fully qualifies as term subordinated debt for inclusion in Category II – Supplementary Capital of the Bank upon changes to regulatory requirements, the Bank may, at its option and subject to the prior written approval of the HKMA, exercise a change of the status of the note by serving the "Change in Status Notice" to the noteholders. Upon a "Change in Status Notice" becoming effective, the note shall thereafter constitute unsubordinated obligations and the rate of interest on the note shall be reduced from 6% per annum to 5.5% per annum. As "Change in Status Notice" has not been served, the rate of interest on the note remains at 6% per annum. Pursuant to the exchange offer by the Bank, the Bank settled and exchanged US\$20,976,000 of the Existing Notes for new tier 2 subordinated note due 2027 (Note(b)). Following the settlement of the exchange offer, US\$204,024,000 in aggregate principal amount of the Existing Notes remains outstanding.
- (b) This represented a subordinated note qualifying as tier 2 capital under Basel III accord with face value of US\$382,903,000 tier 2 subordinated notes issued on 26 July 2017 (the "New Notes"). The New Notes are 10-year non-call 5-year fixed rate notes, with a fixed coupon rate of 3.876% per annum, payable semi-annually for the first five years; the interest rate will be reset on 26 July 2022. This includes US\$22,903,000 of "New Exchange Notes" (being the New Notes issued pursuant to the exchange offer by the Bank to the holders of its US\$225 million 6.000% Subordinated Notes due 2020) and US\$360 million of "New Money Notes". The New Notes have been listed on the Stock Exchange of Hong Kong under Stock Code of 05249 on 27 July 2017.
- (c) The subordinated notes issued are not secured by any collateral.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

31. LOAN CAPITAL - continued

Analysis of changes in financing cash flows of loan capital during the year

	2017 HK\$'000
At 1 January 2017	1,792,267
Changes from financing cash flows:	
Net proceeds from issue of loan capital	2,816,997
Interest paid on loan capital	(102,471)
	4,506,793
Exchange adjustments	748
Fair value hedge adjustments	(70,295)
Other changes	
Interest expense	122,489
Other non-cash movements	(18,355)
Total other changes	104,134
At 31 December 2017	4,541,380

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

32. SHARE CAPITAL

	2017		2016	
	Number of shares (thousands)	Share capital HK\$'000	Number of shares (thousands)	Share capital HK\$'000
At 1 January and 31 December	652,500	5,435,904	652,500	5,435,904

33. ADDITIONAL EQUITY INSTRUMENTS

	2017 HK\$'000	2016 HK\$'000
US\$300 million undated non-cumulative subordinated additional tier 1 capital securities	2,312,030	2,312,030

On 25 September 2014, the Bank issued undated non-cumulative subordinated additional tier 1 capital securities ("Additional Tier 1 Capital Securities") with a face value of US\$300 million (equivalent to HK\$2,312,030,000 net of related issuance costs). The Additional Tier 1 Capital Securities are undated and bear a 6.50% coupon until the first call date on 25 September 2019. The coupon will be reset every five years if the Additional Tier 1 Capital Securities are not redeemed to a fixed rate equivalent to the then-prevailing five-year US Treasury rate plus 4.628% per annum.

The coupon shall be payable semi-annually. The Bank has the right to cancel coupon payment (subject to the requirement as set out in the terms and conditions of the Additional Tier 1 Capital Securities) and the coupon cancelled shall not be cumulative. However, the Bank is stopped from declaring dividend to its ordinary shareholders unless the next scheduled coupon payment is paid.

The principal of the Additional Tier 1 Capital Securities will be written off up to the amount as directed or agreed with the HKMA if the HKMA notifies the Bank that in the opinion of the HKMA, the Bank would become non-viable if there is no written off of the principal.

The Bank has a call option to redeem all the outstanding capital securities from 25 September 2019 or any subsequent coupon payment date, but subject to restriction as set out in the terms and conditions.

During the year, a distribution of US\$19,500,000 (2016: US\$19,500,000) (equivalent to HK\$151,974,000 (2016: HK\$151,425,000)) was paid to the securities holders.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

34. DEFERRED TAXATION

For the purpose of presentation in the statements of financial position, certain deferred tax assets and liabilities have been offset. The following is the analysis of the deferred tax balances for financial reporting purposes:

	2017 HK\$'000	2016 HK\$'000
Deferred tax assets	–	4,672
Deferred tax liabilities	(50,136)	(13,245)
	(50,136)	(8,573)

The following are the major deferred tax assets (liabilities) 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	Remeasurement of retirement benefits HK\$'000	Total HK\$'000
At 1 January 2017	(2,899)	35,365	(8,473)	(29,074)	(3,492)	(8,573)
Credit (charge) to income statement for the year (Note 14)	3,039	632	(3,823)	–	–	(152)
Charge to other comprehensive income for the year	–	–	–	(39,619)	(932)	(40,551)
Exchange adjustments	–	–	(860)	–	–	(860)
At 31 December 2017	140	35,997	(13,156)	(68,693)	(4,424)	(50,136)
At 1 January 2016	(3,881)	38,327	(7,653)	(22,626)	(3,492)	675
Credit (charge) to income statement for the year (Note 14)	982	(2,962)	(1,317)	–	–	(3,297)
Charge to other comprehensive income for the year	–	–	–	(6,448)	–	(6,448)
Exchange adjustments	–	–	497	–	–	497
At 31 December 2016	(2,899)	35,365	(8,473)	(29,074)	(3,492)	(8,573)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

34. DEFERRED TAXATION – continued

Under the Enterprise Income Tax Law of the People's Republic of China, withholding tax is imposed on profits distributed by the Bank's Mainland branches from 1 January 2008 onwards. Deferred taxation has not been provided in the consolidated financial statements in respect of temporary differences attributable to accumulated profits of the Mainland branches amounting to HK\$561,562,000 (2016: HK\$455,797,000) as the Group is able to control the timing of the reversal of the temporary differences and it is probable that the temporary differences will not reverse in the foreseeable future.

35. SHARE OPTION SCHEME

The Bank adopted a share option scheme (the "Scheme") pursuant to a resolution passed on 9 May 2012 for the primary purpose of providing incentives to directors and eligible employees and to replace the share option scheme (the "Expired Scheme") which expired on 24 April 2012. The terms of the Scheme are similar to those of the Expired Scheme. Under the Scheme, the Board of Directors of the Bank may grant options to eligible persons, including directors and employees of the Bank and its subsidiaries, to subscribe for shares in 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. No option may be granted to any person which, if exercised in full, would result in the total number of shares issued and to be issued upon exercise of the option already granted and to be granted to such person (including exercised, cancelled and outstanding options but excluding lapsed options) in the 12-month period up to and including the date of such new grant exceeding 1% of the shares in issue as at the date of such new grant, provided that options may be issued in excess of such limit if, among other things, such grant shall have been separately approved by shareholders of the Bank in a general meeting at which that proposed grantee and his associates (as defined in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited) shall have abstained for voting.

Options granted must be taken up within 28 days of the date of offer, upon payment of HK\$10 per option, and the exercise period shall not in any event be longer than 10 years from the date of grant of the relevant options. 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 business days immediately preceding the date of offer and the nominal value of the shares.

No options have been granted under the Scheme since it was adopted.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

36. INTANGIBLE ASSETS

	Goodwill	Internally developed software	Total
Cost:			
At 1 January 2017	110,606	171,123	281,729
Addition through internal development	–	159,677	159,677
At 31 December 2017	110,606	330,800	441,406
At 1 January 2016	110,606	–	110,606
Addition through internal development	–	171,123	171,123
At 31 December 2016	110,606	171,123	281,729
Accumulated impairment			
At 1 January and 31 December 2017	71,000	–	71,000
At 1 January 2016	60,000	–	60,000
Impairment	11,000	–	11,000
At 31 December 2016	71,000	–	71,000
Net book value			
At 31 December 2017	39,606	330,800	370,406
At 31 December 2016	39,606	171,123	210,729

The Group acquired 100% of issued share capital of Chong Hing Insurance Company Limited (“CHI”). The amount of goodwill arising as a result of acquisition was HK\$110,606,000.

For the year ended 31 December 2017, the management has reviewed goodwill for impairment testing purpose. The review comprised a comparison of the carrying amount and the fair value less cost to sell, 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 fair value of CHI as at 31 December 2017 was estimated by applying market approach based on a price-to-book ratio of 1.

The management of the Group determines no impairment loss on the goodwill for the year ended 31 December 2017 (2016: HK\$ 11,000,000).

During the year, there was an addition of HK\$159,677,000 to internally developed software, which is a computer software currently under internal development. Included in the balance as at 31 December 2017, HK\$86,083,000 (2016: HK\$42,026,000) is capitalised from expenditures that directly attributable to the development of the software.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

37. CONTINGENT LIABILITIES AND COMMITMENTS

	2017 HK\$'000	2016 HK\$'000
Contingent liabilities and commitments		
– contractual amounts		
Direct credit substitutes	1,315,865	805,429
Trade-related contingencies	1,995,688	596,068
Forward asset purchases	82,323	161,609
Undrawn formal standby facilities, credit lines and other commitments		
Which are unconditionally cancellable without prior notice	23,797,922	6,489,024
With an original maturity of one year and under	3,738,747	8,880,273
With an original maturity of over one year	7,178,886	8,397,394
Lease commitments	199,560	258,360
	38,308,991	25,588,157

The credit risk-weighted amount of contingent liabilities and commitments is HK\$5,604,792,000 (2016: HK\$6,103,286,000).

The credit risk-weighted amount is calculated based on “standardised approach”. The risk-weights used in the computation of credit risk-weighted amounts range from 0% to 100% (2016: 0% to 100%) which is assessed in accordance with the Banking (Capital) Rules.

Direct credit substitutes include financial guarantees given by the Group.

Most of the contingent liabilities and commitments are denominated in Hong Kong dollars.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

37. CONTINGENT LIABILITIES AND COMMITMENTS – continued

At the end of the reporting period, the Group had commitments for future minimum lease payments under non-cancellable operating leases which fall due as follows:

	2017 HK\$'000	2016 HK\$'000
Within one year	128,470	120,932
In the second to fifth years, inclusive	71,090	137,428
	199,560	258,360

Operating lease payments represent rentals 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 end of the reporting period are as follows:

	2017 HK\$'000	2016 HK\$'000
Capital expenditure contracted for but not provided in the consolidated financial statements in respect of property and equipment	82,323	161,609

At the end of the reporting period, the Group as lessor had contracted with tenants for the following future minimum lease payments:

	2017 HK\$'000	2016 HK\$'000
Within one year	5,312	7,409
In the second to fifth years, inclusive	6,853	10,764
After five years	–	632
	12,165	18,805

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

38. RETIREMENT BENEFITS SCHEME

At the end of the reporting period, the Group had two retirement schemes in operation including a defined benefit scheme (the “ORSO Scheme”), which was registered under the Occupational Retirement Scheme Ordinance 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 in defined contribution segment prior to the establishment of the MPF Scheme could stay within the ORSO Scheme or switch 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 Scheme for qualifying employees. Under the ORSO Scheme, the employees are entitled to retirement benefits varying between 0 and 100 percent of total contributions on attainment of a retirement age of 60. 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 defined benefit segment of the ORSO Scheme was carried out as at 31 December 2017 by the qualified actuaries of Towers Watson Hong Kong Limited. The actuarial valuation is carried out periodically, but at least triennially. The present value of the defined benefit obligation and the current service cost have been measured using the Projected Unit Credit method. At the date of the latest formal independent actuarial valuation made on 31 December 2017, the net retirement asset of the defined benefit segment was HK\$27,696,000.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

38. RETIREMENT BENEFITS SCHEME – continued

	2017 HK\$'000
Amounts recognised in the consolidated income statement in respect of the defined benefit plans are as follow:	
Interest cost on benefit obligation	(403)
Interest income on plan assets	815
Net interest income	412
Current service cost	(89)
	323
Amount recognised in the consolidated income statement and other comprehensive income in respect of the defined benefit plans is as follow:	
Difference between actual return on plan assets and interest, and actuarial losses	5,647

The amount included in the consolidated statement of financial position arising from the Group's defined benefit retirement benefit plan is as follows:

	2017 HK\$'000
Present value of defined benefit obligation	(17,682)
Fair value of plan assets	45,378
	27,696

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

	2017 HK\$'000
Opening defined benefit obligation	22,221
Interest cost	403
Current service cost	89
Actuarial gain	(3,377)
Benefits paid	(1,654)
Closing defined benefit obligation	17,682

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

38. RETIREMENT BENEFITS SCHEME – continued

Changes in fair value of plan assets are as follow:

	2017 HK\$'000
Opening fair value of plan assets	43,947
Interest income	815
Return on plan assets	2,270
Benefits paid	(1,654)
Closing fair value of plan assets	45,378

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

	2017 %
Cash	32
Equities (Note)	68

Note: The equities represented investments in three equity securities which are securities of The Hong Kong & China Gas Limited, Liu Chong Hing Investment Limited and Chong Hing Bank Limited which are all listed on the Hong Kong Stock Exchange.

The fair value of the plan assets as at 31 December 2017 for each category, are as follow:

	2017 HK\$'000
Deposits with the Bank	14,661
Interest receivable	25
Equity securities listed in Hong Kong:	
The Hong Kong & China Gas Limited	22,684
Liu Chong Hing Investment Limited	6,750
Chong Hing Bank Limited	1,258
	45,378

The fair values of the equity instruments are determined based on quoted market prices in active markets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

38. RETIREMENT BENEFITS SCHEME – continued

The amounts of assets of the ORSO Scheme's defined benefit segment invested in the Bank's own deposit account as at 31 December 2017 were:

	2017 HK\$'000
Deposits with the Bank	14,661

The ORSO Scheme's defined benefit segment exposes the Group to the interest rate risk, longevity risk and price risk as at 31 December 2017.

Interest rate risk

The present value of the defined benefit plan liability is calculated using a discount rate determined by reference to the yields of the Hong Kong Government Exchange Fund Notes. A decrease in the discount rate would increase the plan liability.

Longevity risk

The present value of the defined benefit plan liability is calculated by reference to the best estimate of the mortality of qualifying employees both during and after their employment. An increase in the life expectancy of the qualifying employees will increase the plan's liability.

Price risk

As stated above, 68% of the assets were invested into three equity securities as at 31 December 2017. Such high concentration may expose to the Group to price risk when the equity prices fluctuate.

The significant assumptions used in determining the defined benefit obligations are shown below:

	2017 %
Discount rate (per annum)	1.8
Expected rate of salary increase (per annum)	4.0
Expected rate of pension increase (per annum)	0.0

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

38. RETIREMENT BENEFITS SCHEME – continued

The table below indicates the potential effect of change of the significant assumptions on the defined benefit obligation:

	2017	
	Change in assumption	
	+0.25%	-0.25%
	HK\$'000	HK\$'000
Discount rate	(401)	420
Expected rate of salary increase	51	(50)
	Age +1 year	Age -1 year
	HK\$'000	HK\$'000
Pensioner mortality	(709)	724

As at 31 December 2017, the weighted average duration of the defined benefit obligation is approximately 8.7 years.

The costs for providing benefits to the members of the ORSO Scheme's defined benefit segment are funded by the Group. The contributions required by the Group to fund the costs are determined by periodic funding valuations in accordance with the Occupational Retirement Scheme Ordinance.

As of 31 December 2017, the Group is not required to contribute to the ORSO Scheme's defined benefit segment with respect to the members of the ORSO Scheme's defined benefit segment according to the results of the last statutory funding valuation of the ORSO Scheme's defined benefit segment as at 31 December 2017. The Group's contribution rate may be subject to change when the results of the next statutory funding valuation of the ORSO Scheme's defined benefit segment as at 31 December 2020 become available.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

39. RELATED PARTY TRANSACTIONS

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

	Interest, commission and rental income		Interest, rental and other operating expenses	
	2017 HK\$'000	2016 HK\$'000	2017 HK\$'000	2016 HK\$'000
Ultimate holding company	12	2	18,285	3,505
Intermediate holding company	7,526	1,528	13,953	17,518
Fellow subsidiaries	4,784	11,579	47,555	14,068
Associates	48,848	62,115	1,783	5,393
Key management personnel (Note)	1,962	1,202	1,644	1,219

During the year, the Group had net trading income with intermediate holding company and fellow subsidiary of HK\$6,674,000 (2016: HK\$8,921,000).

At the end of reporting period, the Group had the following material outstanding balances with related parties:

	Amounts due from related parties		Amounts due to related parties	
	2017 HK\$'000	2016 HK\$'000	2017 HK\$'000	2016 HK\$'000
Ultimate holding company	–	–	426,430	1,453,839
Intermediate holding company	298,008	295,792	53,704	2,140
Fellow subsidiaries	835,733	2,507	1,766,326	1,842,204
Associates	–	–	213,367	152,867
Key management personnel (Note)	572,376	55,754	201,155	211,290

Note: Includes key management personnel, close family members of key management personnel and entities that are controlled or jointly controlled, directly or indirectly, by key management personnel.

The above outstanding balances bear interest at rates similar to those made available to non-related parties. A portion of the loans to related parties are secured with properties, securities and fixed deposits.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

39. RELATED PARTY TRANSACTIONS – continued

As at 31 December 2017, the Group had operating lease commitments with fellow subsidiaries of HK\$18,411,000 (31 December 2016: HK\$19,183,000).

Amounts due from related parties are included in advances and other accounts on the statements of financial position.

Amounts due to related parties are included in deposits from customers on the statements of financial position.

Compensation of key management personnel

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

	2017 HK\$'000	2016 HK\$'000
Short-term benefits	160,161	139,331
Post employment benefits	10,015	8,739
	170,176	148,070

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

As of 31 December 2017, the Group accrued a bonus for the Group's senior management and employees. The accrued bonus was approved by the Remuneration Committee on 9 February 2018. The Group has not completed the allocation of the bonus to individual senior management. The allocation of accrued bonus included under short-term benefits above represents the best estimate of management for the bonus to be distributed to key management personnel as of the date of approval of the financial statements.

40. CAPITAL MANAGEMENT

The Group's policy is to maintain a strong capital base to support the development of the Group's business and to ensure compliance with the statutory capital adequacy ratio requirement, a requirement used to assess the capital adequacy of banks. Capital is allocated to the various activities of the Group depending on the risk taken by each business division. Where the subsidiaries or branches are directly regulated by other regulators, they are required to maintain capital according to the rules of those regulators.

The Group's objective when managing capital are:

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

Capital adequacy and the use of regulatory capital are monitored regularly by the Group's management, employing techniques based on the Banking (Capital) Rules of the Hong Kong Banking Ordinance. The required information is filed with the Hong Kong Monetary Authority (the "HKMA") on a quarterly basis.

The HKMA requires each bank or banking group to maintain a ratio of total regulatory capital to the risk-weighted asset (the capital adequacy ratio) at or above the minimum as stipulated in the Banking (Capital) Rules. In addition, branches outside Hong Kong of the Bank are also directly regulated and supervised by their local banking supervisors, which may differ from country to country. Subsidiaries of the Group are also subject to statutory capital requirements from other regulatory authorities, such as the Securities and Futures Commission and the Insurance Authority.

The capital adequacy ratios are computed on the consolidated basis, which includes the Bank and certain of its subsidiaries as specified by the HKMA for its regulatory purposes, and are in accordance with the Banking (Capital) Rules of the Hong Kong Banking Ordinance.

The Group has established a capital planning process to assess the adequacy of its capital to support current and future activities and to set 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 including additional capital required for future expansion, results of the stress test programme regularly conducted, dividend policy, income recognition and provisioning policies.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

41. STATEMENT OF FINANCIAL POSITION AND RESERVE MOVEMENT OF THE BANK

	2017 HK\$'000	2016 HK\$'000
Assets		
Cash and short-term funds	25,156,970	30,510,775
Placements with banks maturing between one to twelve months	6,347,359	1,604,971
Derivative financial instruments	556,793	424,845
Investments in securities	39,088,758	29,643,981
Advances and other accounts	90,500,982	73,799,209
Investments in subsidiaries	250,984	250,984
Amounts due from subsidiaries	404,600	221,629
Assets held for sale	–	2
Interests in associates	20,000	21,500
Investment properties	252,000	244,000
Property and equipment	385,386	410,516
Prepaid lease payments for land	2,134	2,201
Deferred tax assets	–	4,672
Intangible assets	330,800	171,123
Total assets	163,296,766	137,310,408
Liabilities		
Deposits and balances of banks	3,051,932	2,696,681
Financial assets sold under repurchase agreements	12,002,989	9,845,753
Deposits from customers	118,841,329	102,880,629
Amounts due to subsidiaries	623,285	676,870
Derivative financial instruments	882,279	553,614
Other accounts and accruals	1,081,427	975,407
Current tax liabilities	429,098	353,945
Certificates of deposit	3,217,451	812,329
Debt securities issued	1,796,069	1,663,774
Loan capital	4,541,380	1,792,267
Deferred tax liabilities	35,232	2,927
Total liabilities	146,502,471	122,254,196
Equity attributable to owners of the Bank		
Share capital	5,435,904	5,435,904
Additional equity instruments	2,312,030	2,312,030
Reserves (Note (a))	9,046,361	7,308,278
Total equity	16,794,295	15,056,212
Total liabilities and equity	163,296,766	137,310,408

Approved and authorised for issue by the Board of Directors on 29 March 2018 and signed on its behalf by:

Zhang Zhaoxing
Chairman

Leung Ko May Yee Margaret
Deputy Chairman and Managing Director

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

41. STATEMENT OF FINANCIAL POSITION AND RESERVE MOVEMENT OF THE BANK – continued

Note (a):

	Investment revaluation reserve HK\$'000	Land and building 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 2017	136,530	174,247	1,378,500	(185,204)	739,000	5,065,205	7,308,278
Profit for the year	-	-	-	-	-	1,791,853	1,791,853
Exchange differences arising on translation	-	-	-	246,324	-	-	246,324
Surplus on remeasurement of retirement benefit	-	-	-	-	-	5,647	5,647
Income tax charge relating to retirement benefit	-	-	-	-	-	(932)	(932)
Fair value gains of available-for-sale securities arising during the year	345,265	-	-	-	-	-	345,265
Amount reclassified to the profit or loss upon disposal of available-for-sale securities	(106,435)	-	-	-	-	-	(106,435)
Income tax effect relating to disposal of available-for-sale securities	17,562	-	-	-	-	-	17,562
Income tax effect relating to fair value change of available-for-sale securities	(56,877)	-	-	-	-	-	(56,877)
Other comprehensive income	199,515	-	-	246,324	-	4,715	450,554
Total comprehensive income for the year	199,515	-	-	246,324	-	1,796,568	2,242,407
Distribution payment for additional equity instruments	-	-	-	-	-	(151,974)	(151,974)
Interim dividend paid	-	-	-	-	-	(97,875)	(97,875)
Final dividend paid	-	-	-	-	-	(254,475)	(254,475)
Earmark of retained profits as regulatory reserve	-	-	-	-	77,000	(77,000)	-
At 31 December 2017	336,045	174,247	1,378,500	61,120	816,000	6,280,449	9,046,361

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

41. STATEMENT OF FINANCIAL POSITION AND RESERVE MOVEMENT OF THE BANK – continued

Note (a): – continued

	Investment revaluation reserve HK\$'000	Land and building 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 2016	100,258	158,018	1,378,500	(19,242)	663,000	4,272,337	6,552,871
Profit for the year	-	-	-	-	-	1,359,593	1,359,593
Exchange differences arising on translation	-	-	-	(165,962)	-	-	(165,962)
Surplus on transfer of land and buildings to investment properties	-	16,229	-	-	-	-	16,229
Fair value gains of available-for-sale securities arising during the year	184,427	-	-	-	-	-	184,427
Amount reclassified to the profit or loss upon disposal of available-for-sale securities	(140,914)	-	-	-	-	-	(140,914)
Income tax effect relating to disposal of available-for-sale securities	23,251	-	-	-	-	-	23,251
Income tax effect relating to fair value change of available-for-sale securities	(30,492)	-	-	-	-	-	(30,492)
Other comprehensive income	36,272	16,229	-	(165,962)	-	-	(113,461)
Total comprehensive income for the year	36,272	16,229	-	(165,962)	-	1,359,593	1,246,132
Distribution payment for additional equity instruments	-	-	-	-	-	(151,425)	(151,425)
Interim dividend paid	-	-	-	-	-	(97,875)	(97,875)
Final dividend paid	-	-	-	-	-	(241,425)	(241,425)
Earmark of retained profits as regulatory reserve	-	-	-	-	76,000	(76,000)	-
At 31 December 2016	136,530	174,247	1,378,500	(185,204)	739,000	5,065,205	7,308,278

41. STATEMENT OF FINANCIAL POSITION AND RESERVE MOVEMENT OF THE BANK – continued

Note (a): – continued

The Bank's reserves available for distribution to owners as at 31 December 2017 comprised retained profits of HK\$6,066,080,000 (2016: HK\$4,929,131,000) and general reserve of HK\$1,378,500,000 (2016: HK\$1,378,500,000).

The regulatory reserve is set up in compliance with the HKMA's requirements and is distributable to owners of the Bank subject to consultation with the HKMA.

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

The investment revaluation reserve represents cumulative gains and losses arising on the revaluation of available-for-sale investments that have been recognised in other comprehensive income, net of amounts reclassified to the income statement when those available-for sale investments are disposed of or are determined to be impaired.

The land and building revaluation reserve represents difference between fair value and carrying value of the properties transferred from owner-occupied properties to investment properties during the year.

Exchange differences relating to the translation of the net assets of the Bank's foreign operations from their functional currencies to the Bank's presentation currency (i.e. Hong Kong dollars) are recognised directly in other comprehensive income and accumulated in the translation reserve. Such exchange differences accumulated in the translation reserve are reclassified to the income statement on the disposal of the foreign operations.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

42. BENEFITS AND INTERESTS OF DIRECTORS

(Disclosures required by section 383 of the Hong Kong Companies Ordinance (Cap 622) and Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap 622G)) and Listing Rules

The emoluments of the Directors and the Chief Executive of the Bank were as follows:

(A) Directors' emoluments

	2017						Total HK\$'000
	Fees HK\$'000	Salaries HK\$'000	Bonus HK\$'000	Housing allowance HK\$'000	Estimated value of other benefits HK\$'000	Employer's contribution to retirement scheme HK\$'000	
Executive Directors and Chief Executive							
Leung Ko May Yee Margaret (Note 1)	180	12,661	-	-	-	818	13,659
Zong Jianxin (Note 2)	180	7,235	-	-	-	422	7,837
Lau Wai Man	180	5,282	-	-	-	528	5,990
Total Executive Directors' and Chief Executive's emoluments	540	25,178	-	-	-	1,768	27,486
Non-executive Directors							
Zhang Zhaoxing	450	-	-	-	-	-	450
Chow Cheuk Yu Alfred	450	-	-	-	-	-	450
Li Feng	400	-	-	-	-	-	400
Wang Shuhui	400	-	-	-	-	-	400
Zhu Chunxiu	400	-	-	-	-	-	400
Total Non-executive Directors' emoluments	2,100	-	-	-	-	-	2,100
Independent Non-executive Directors							
Cheng Yuk Wo	515	-	-	-	-	-	515
Lee Ka Lun	515	-	-	-	-	-	515
Chiranakhorn Wanchai (Note 4)	18	-	-	-	-	-	18
Ma Chiu Cheung Andrew	435	-	-	-	-	-	435
Yu Lup Fat Joseph	475	-	-	-	-	-	475
Total Independent Non-executive Directors' emoluments	1,958	-	-	-	-	-	1,958
Total	4,598	25,178	-	-	-	1,768	31,544

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

42. BENEFITS AND INTERESTS OF DIRECTORS – continued

(Disclosures required by section 383 of the Hong Kong Companies Ordinance (Cap 622) and Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap 622G)) and Listing Rules – continued

The emoluments of the Directors and the Chief Executive of the Bank were as follows:– continued

(A) Directors' emoluments – continued

	2016						Total HK\$'000
	Fees HK\$'000	Salaries HK\$'000	Bonus HK\$'000	Housing allowance HK\$'000	Estimated value of other benefits HK\$'000	Employer's contribution to retirement benefits scheme HK\$'000	
Executive Directors and Chief Executive							
Leung Ko May Yee Margaret (Note 1)	180	11,648	3,800	–	–	694	16,322
Zong Jianxin (Note 2)	180	7,002	1,800	–	–	373	9,355
Lau Wai Man	180	5,212	1,000	–	–	521	6,913
Liu Tit Shing Don	66	1,996	–	–	–	158	2,220
Total Executive Directors' and Chief Executive's emoluments	606	25,858	6,600	–	–	1,746	34,810
Non-executive Directors							
Zhang Zhaoxing	350	–	–	–	–	–	350
Chow Cheuk Yu Alfred	309	–	–	–	–	–	309
Li Feng	300	–	–	–	–	–	300
Wang Shuhui	300	–	–	–	–	–	300
Zhu Chunxiu	300	–	–	–	–	–	300
Total Non-executive Directors' emoluments	1,559	–	–	–	–	–	1,559
Independent Non-executive Directors							
Cheng Yuk Wo	420	–	–	–	–	–	420
Lee Ka Lun	380	–	–	–	–	–	380
Chiranakhorn Wanchai (Note 4)	300	–	–	–	–	–	300
Ma Chiu Cheung Andrew	300	–	–	–	–	–	300
Yu Lup Fat Joseph	331	–	–	–	–	–	331
Total Independent Non-executive Directors' emoluments	1,731	–	–	–	–	–	1,731
Total	3,896	25,858	6,600	–	–	1,746	38,100

Notes:

1. Ceased to act as Chief Executive of the Bank with effect from 19 April 2017.
2. Being the Deputy Managing Director of the Bank and assumed the role of Chief Executive of the Bank with effect from 19 April 2017.
3. For the year ended 31 December 2017, no directors have waived any emoluments (2016: Nil).
4. Passed away on 23 January 2017.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

42. BENEFITS AND INTERESTS OF DIRECTORS – continued

(Disclosures required by section 383 of the Hong Kong Companies Ordinance (Cap 622) and Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap 622G) and Listing Rules – continued)

(B) Information about loans, quasi-loans and other dealings in favour of directors, controlled bodies corporate by and connected entities with such directors

The information about loans, quasi-loans and other dealings entered into by the company or subsidiary undertaking of the company, where applicable, in favour of directors is as follows:

	Aggregate balance of all relevant loans outstanding		Maximum aggregate balance of relevant loans during the year
	at January 1 HK\$'000	at December 31 HK\$'000	HK\$'000
2017	3,703	3,560	5,879
2016	5,348	3,703	6,318

The loans bear interest at rates ranging from 0% to prime rate plus 10%. Included in the loans to officers are loans of HK\$3,510,000 (2016: HK\$3,688,000) secured by collateral. The collateral consists mainly of properties, securities and fixed deposits.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2017

42. BENEFITS AND INTERESTS OF DIRECTORS – continued

(Disclosures required by section 383 of the Hong Kong Companies Ordinance (Cap 622) and Companies (Disclosure of Information about Benefits of Directors) Regulation (Cap 622G) and Listing Rules – continued)

(C) Five Highest Paid Individuals

The five highest paid individuals in the Group in 2017 included three (2016: three) directors whose emoluments are set out in 42(A) above. The emoluments of the remaining two (2016: two) highest paid individuals are as follows:

	2017 HK\$'M	2016 HK\$'M
Salary and other emoluments	9.0	6.7
Contributions to pension scheme	0.2	0.5
Discretionary bonuses	1.3	1.3
	10.5	8.5

Their emoluments are within the following bands:

HK\$	2017 Number of individuals	2016 Number of individuals
3,500,001 – 4,000,000	1	–
4,000,001 – 4,500,000	–	2
6,500,001 – 7,000,000	1	–

43. IMMEDIATE AND ULTIMATE HOLDING COMPANIES

As at 31 December 2017 and 31 December 2016, the immediate holding company of the Bank was Yuexiu Financial Holdings Limited, which is incorporated in Hong Kong. Its ultimate holding company was Guangzhou Yue Xiu Holdings Limited, which is incorporated in the People's Republic of China.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

The following information is disclosed as part of the accompanying information to the financial statements and does not form part of the audited financial statements.

The preparation of supplementary financial information is in accordance with the Banking (Disclosure) Rules and consolidated supervision arrangement approved by the HKMA.

1. MAJOR SPECIALISED COMMITTEES

The Board is constituted in accordance with the Bank's Articles of Association and is ultimately responsible for the sustainable performance of the Group. The Board has established the following specialised committees and delegated its authorities and power to enable them to operate under defined terms of reference. The Board reviews and updates the committees' Terms of Reference on a regular basis.

These specialised committees are:

- (i) Audit Committee**
- (ii) Connected Party Transactions Committee**
- (iii) Executive Committee**
- (iv) Nomination Committee**
- (v) Remuneration Committee**
- (vi) Risk Committee**

The Terms of Reference and the composition of each of the above committees are set out in the "Corporate Governance Report" of this Annual Report.

The Executive Committee has established the Asset and Liability Management Committee (the "ALCO") and the Risk Management Committee (the "RMC"). The roles and functions of these committees are as follows:

(vii) ALCO

Members of the ALCO are appointed by the Executive Committee, comprising senior executives 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 funding and 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 statement of financial position, and the formulation of the corresponding strategies and plans also come under other key functions of the ALCO.

(viii) RMC

Members of the RMC are appointed by the Executive Committee. It comprises the Chief Risk Officer with other senior executives who are responsible for risk management, compliance issues and daily operations of the Bank.

The RMC is responsible for the oversight of risk management of the Group, within the framework of the Group's policies, its Terms of Reference and such other directives as the Executive Committee may determine from time to time.

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, divisions and departments of the Group and are regularly reviewed by the Board. Internal auditors also play an important role in risk management process by performing regular, as well as conducting sporadic compliance audits.

The management of assets and liabilities of the Group is conducted under guidance of the ALCO. The ALCO holds meetings every two weeks, and more frequent meetings when required, to review and direct the relevant policies, the business strategies and to monitor the bank-wide positions. The day-to-day management of the funding and liquidity, foreign exchange, interest rate and other market risks, and the compliance with the ALCO and the RMC policies are monitored by the Finance and Capital Management Division, the Financial Markets Division, the Market Risk Management Department and the Finance Department with the assistance of various qualitative and quantitative analyses.

Complementing with the ALCO in its management of assets and liabilities, the RMC also oversees the implementation of the policies and procedures established for managing the Group's credit, strategic, 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, frauds, or inadequate internal controls and procedures.

Executive Directors, division heads, 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 the Bank's normal operations are restored effectively and efficiently in the event of business interruption.

(ii) Reputation risk

Reputation risk is the risk that the Group's reputation is damaged by one or more than one reputation event that results in negative publicity about the Group's business practices, conduct or financial condition.

Reputation risk is managed by every member of staff ensuring proper and adequate communications and public relation efforts to foster the reputation of the Group. A reputation risk management mechanism guided by the senior management including executive directors has been established to manage including, without limitation, media exposure, handle customers' and other stakeholders' complaints and suggestions, and to ensure that business activities and agents and/or bodies acting on the Group's behalf do not jeopardise its 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 2017

3. CAPITAL ADEQUACY RATIOS, LEVERAGE RATIO AND LIQUIDITY RATIOS

	2017 %	2016 %
Total capital ratio	17.60	16.32
Tier 1 capital ratio	13.30	14.16
Common Equity Tier 1 ("CET 1") capital ratio	11.30	11.81
	31 December 2017 %	31 December 2016 %
Capital buffers (as a percentage of risk-weighted assets)		
Capital conservation buffer ratio	1.25	0.63
Countercyclical capital buffer ratio	0.91	0.49
	2.16	1.12
	2017 %	2016 %
Leverage ratio	8.85	9.57
	Year ended 31 December 2017 %	Year ended 31 December 2016 %
Average liquidity maintenance ratio for the year	40.73	40.59

3. CAPITAL ADEQUACY RATIOS, LEVERAGE RATIO AND LIQUIDITY RATIOS - continued

Capital adequacy ratios are compiled in accordance with the Banking (Capital) Rules under Hong Kong Banking Ordinance for the implementation of the “Basel III” capital accord, which became effective on 1 January 2013. In accordance with the Banking (Capital) Rules, the Bank has adopted the “standardised approach” for the calculation of the risk-weighted assets for credit risk, “standardised (market risk) approach” for the calculation of market 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, Right Way Investments Limited, Gallbraith Limited, Chong Hing Information Technology Limited, Card Alliance Company Limited, Top Benefit Enterprise Limited and Hero Marker Limited.

Leverage ratio is disclosed in accordance with the Banking (Disclosure) Rules under Hong Kong Banking Ordinance. The leverage ratio is consolidated with reference to the financial information of the Bank, Chong Hing Finance Limited, Right Way Investments Limited, Gallbraith Limited, Chong Hing Information Technology Limited, Card Alliance Company Limited, Top Benefit Enterprise Limited and Hero Marker Limited.

Liquidity maintenance ratio (“LMR”) is compiled in accordance with the Banking (Liquidity) Rules under Hong Kong Banking Ordinance, which became effective on 1 January 2015. The LMR is calculated on an unconsolidated basis. The average liquidity maintenance ratio is calculated based on the arithmetic mean of the average value of the LMR of the Bank reported in the liquidity position return of the Bank for each month during the reporting period.

4. OTHER FINANCIAL INFORMATION

The Bank has set up a “Regulatory Disclosure” section on its website to house all of information relating to the disclosure of regulatory capital to comply with Banking (Disclosure) Rules.

The “Regulatory Disclosure” will be available on the Bank’s website: www.chbank.com/en/regulatory-disclosures/index.shtml in the “Regulatory Disclosure” section in accordance with the Banking (Disclosure) Rules.

5. 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.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

6. ADVANCES TO CUSTOMERS – BY INDUSTRY SECTORS

The Group's gross advances to customers (including advances booked in branches outside Hong Kong and subsidiaries) are analysed and reported by industry sectors according to the usage of the loans or business activities of the borrowers. Details are set out in note 7 (credit risk) to the consolidated financial statements.

The Group's advances to customers overdue for over three months, and new impairment allowances and advances written off during the year ended 31 December 2017 and 2016 in respect of industry sectors which constitute not less than 10 per cent of gross advances to customers are analysed as follows:

	2017		
	Advances overdue for over three months as at 31 December HK\$'000	New impairment allowances during the year HK\$'000	Advances written-off during the year HK\$'000
Loans for use in Hong Kong			
Individuals			
– Loans for the purchase of other residential properties	5,780	–	–
Loans for use outside Hong Kong	151,647	150,579	–
	2016		
	Advances overdue for over three months as at 31 December HK\$'000	New impairment allowances during the year HK\$'000	Advances written-off during the year HK\$'000
Loans for use in Hong Kong			
Individuals			
– Loans for the purchase of other residential properties	5,780	472	472
Loans for use outside Hong Kong	–	135	–

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

7. 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:

	2017				
	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	66,635,650	347,802	246,453	243,834	241,053
Mainland China	16,697,292	149,859	149,859	149,859	77,567
Macau	3,342,965	1,788	1,788	700	11,019
Others	22,465	-	-	-	-
	86,698,372	499,449	398,100	394,393	329,639

	2016				
	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	56,974,017	55,448	48,253	39,737	202,120
Mainland China	10,670,402	-	-	-	40,052
Macau	2,517,063	-	-	-	9,047
Others	527,673	-	-	-	-
	70,689,155	55,448	48,253	39,737	251,219

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

8. INTERNATIONAL CLAIMS

The Group's international claims by countries or geographical areas which constitute 10% or more of the relevant disclosure items after taking into account any risk transfers are as follows:

	At 31 December 2017				Total HK\$'000
	Non-bank private sector				
	Banks HK\$'000	Official sector HK\$'000	Non-bank financial institutions HK\$'000	Non- financial private sector HK\$'000	
Offshore centres	1,531,449	4,200	16,666,358	15,301,720	33,503,727
of which					
– Hong Kong	1,531,206	4,200	4,403,559	8,026,365	13,965,330
Developing Asia-Pacific	13,510,809	233,157	948,894	7,437,270	22,130,130
of which					
– Mainland China	12,534,009	233,157	948,894	7,431,108	21,147,168
Developed countries	6,192,052	3,860,788	1,435,606	107,354	11,595,800

	At 31 December 2016				Total HK\$'000
	Non-bank private sector				
	Banks HK\$'000	Official sector HK\$'000	Non-bank financial institutions HK\$'000	Non- financial private sector HK\$'000	
Offshore centres	4,939,083	2,957	7,782,051	13,070,152	25,794,243
of which					
– Hong Kong	1,899,423	2,957	2,672,304	5,131,784	9,706,468
Developing Asia-Pacific	16,365,527	215,778	2,568,047	9,036,914	28,186,266
of which					
– Mainland China	14,646,785	215,778	2,167,612	8,787,682	25,817,857
Developed countries	9,744,648	3,780,272	1,043,634	715,024	15,283,578

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

9. 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:

	US\$	2017 RMB	Total
Equivalent in thousand of HK\$			
Spot assets	38,794,996	27,732,363	66,527,359
Spot liabilities	(37,371,492)	(27,256,003)	(64,627,495)
Forward purchases	70,397,765	4,855,330	75,253,095
Forward sales	(71,262,225)	(4,859,242)	(76,121,467)
Net long position	559,044	472,448	1,031,492

	MOP	RMB	Total
Net structural position	48,545	351,377	399,922

	US\$	2016 RMB	Total
Equivalent in thousand of HK\$			
Spot assets	43,198,586	25,692,734	68,891,320
Spot liabilities	(26,518,744)	(23,225,764)	(49,744,508)
Forward purchases	14,816,584	5,446,876	20,263,460
Forward sales	(31,251,838)	(7,627,195)	(38,879,033)
Net long position	244,588	286,651	531,239

	MOP	RMB	Total
Net structural position	48,545	351,377	399,922

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

10. OVERDUE AND RESCHEDULED ASSETS

	2017	
	Gross amount of advances HK\$'000	Percentage to total advances %
Advances overdue for		
– 6 months or less but over 3 months	12,656	0.0
– 1 year or less but over 6 months	432,113	0.5
– Over 1 year	54,680	0.1
Total overdue advances	499,449	0.6
Rescheduled advances	18,353	0.0
Individual impairment allowances made in respect of overdue loans and advances	388,641	
	2016	
	Gross amount of advances HK\$'000	Percentage to total advances %
Advances overdue for		
– 6 months or less but over 3 months	1,429	0.0
– 1 year or less but over 6 months	27,448	0.0
– Over 1 year	26,571	0.0
Total overdue advances	55,448	0.1
Rescheduled advances	265,023	0.4
Individual impairment allowances made in respect of overdue loans and advances	33,630	

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

10. OVERDUE AND RESCHEDULED ASSETS – continued

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

	2017 HK\$'000	2016 HK\$'000
Covered portion of overdue loans and advances	110,975	22,412
Uncovered portion of overdue loans and advances	388,474	33,036
	499,449	55,448
Market value of collateral held against covered portion of overdue loans and advances	229,255	89,224

There were no advances to banks or other assets which were overdue for over three months as at 31 December 2017 and 31 December 2016, nor were there any rescheduled advances to banks and other financial institutions.

Repossessed assets held by the Group as at 31 December 2017 amounted to HK\$10,250,000 (2016: HK\$2,500,000).

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

11. MAINLAND ACTIVITIES EXPOSURES

The table below summarizes the non-bank Mainland China exposures of the Bank's Hong Kong banking operations and the Bank's Mainland branches and sub-branches categorized by types of counterparties:

	31 December 2017		Total HK\$'000
	On-balance sheet exposure HK\$'000	Off-balance sheet exposure HK\$'000	
Type by counterparties			
1. Central government, central government-owned entities and their subsidiaries and joint ventures (JVs)	16,733,076	1,928,809	18,661,885
2. Local government, local government-owned entities and their subsidiaries and JVs	2,226,715	1,252,874	3,479,589
3. Mainland China nationals residing in Mainland China or other entities incorporated in Mainland China and their subsidiaries and JVs	14,510,630	3,229,129	17,739,759
4. Other entities of central government not reported in item 1 above	5,739,266	1,006,372	6,745,638
5. Other entities of local government not reported in item 2 above	474,243	45,000	519,243
6. Mainland China nationals residing outside Mainland China or entities incorporated outside Mainland China where the credit is granted for use in Mainland China	9,719,331	1,546,041	11,265,372
7. Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	6,585,223	2,432,079	9,017,302
Total	55,988,484	11,440,304	67,428,788
Total assets after provision (Note)	162,810,827		
On-balance sheet exposures as percentage of total assets (Note)	34%		

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

11. MAINLAND ACTIVITIES EXPOSURES – continued

	31 December 2016		Total HK\$'000
	On-balance sheet exposure HK\$'000	Off-balance sheet exposure HK\$'000	
Type by counterparties			
1. Central government, central government-owned entities and their subsidiaries and joint ventures (JVs)	11,885,965	1,136,390	13,022,355
2. Local government, local government-owned entities and their subsidiaries and JVs	3,123,582	247,363	3,370,945
3. Mainland China nationals residing in Mainland China or other entities incorporated in Mainland China and their subsidiaries and JVs	8,081,232	1,432,214	9,513,446
4. Other entities of central government not reported in item 1 above	3,279,271	554,276	3,833,547
5. Other entities of local government not reported in item 2 above	250,068	-	250,068
6. Mainland China nationals residing outside Mainland China or entities incorporated outside Mainland China where the credit is granted for use in Mainland China	7,656,328	1,975,802	9,632,130
7. Other counterparties where the exposures are considered by the reporting institution to be non-bank Mainland China exposures	402,801	406,500	809,301
Total	34,679,247	5,752,545	40,431,792
Total assets after provision (Note)	136,919,757		
On-balance sheet exposures as percentage of total assets (Note)	25%		

The categories of non-bank counterparties and type of direct exposures are disclosed in accordance with Banking (Disclosure) Rules with reference to the Return of Mainland Activities of the HKMA.

Note: Include total assets after provisions of the Bank's Hong Kong banking operations and the Bank's Mainland branches and sub-branches.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

12. CAPITAL CHARGE FOR CREDIT, MARKET AND OPERATIONAL RISKS

The capital requirements for each class of exposures are summarised 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	
	2017 HK\$'000	2016 HK\$'000
Sovereign exposures	43,950	–
Public sector entity exposures	8,548	8,660
Bank exposures	975,386	984,270
Securities firm exposures	87,017	66,920
Corporate exposures	5,999,273	4,668,720
Collective investment scheme exposures	5,075	–
Cash items	29,068	5,451
Regulatory retail exposures	20,118	7,731
Residential mortgage loans	431,414	507,058
Other exposures which are not past due exposures	576,441	646,351
Past due exposures	10,252	20,562
Total capital charge for on-balance sheet exposures	8,186,542	6,915,723
Direct credit substitutes	94,557	54,936
Trade-related contingencies	16,149	9,126
Forward asset purchases	7,585	12,836
Other commitments	331,092	411,366
Exchange rate contracts	55,970	17,791
Interest rate contracts	12,828	9,054
Securities financing transaction	26,141	27,234
Total capital charge for off-balance sheet exposures	544,322	542,343
Total capital charge for securitisation exposures	–	–
Total central counterparty default risk exposures	607	–
Total capital charge for credit valuation adjustment	35,579	18,202
Total capital charge for credit risk	8,767,050	7,476,268

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

12. CAPITAL CHARGE FOR CREDIT, MARKET AND OPERATIONAL RISKS – continued

(ii) Capital charge for market risk

The market risk capital charge set out below relates to interest rate risk and foreign exchange risk. The net open positions of the Group's foreign exchange exposures amounted to HK\$915,675,000 as at 31 December 2017 (2016: HK\$726,050,000). There are no other market risk exposures as at that date.

	Capital charge 2017 HK\$'000	2016 <i>HK\$'000</i> (Restated)
Interest rate risk exposures	72,358	4,766
Foreign exchange exposures (including gold and options)	73,254	58,084
Capital charge for market risk	145,612	62,850

The Group uses the standardised (market risk) approach for calculating market risk.

(iii) Capital charge for operational risk

	Capital charge 2017 HK\$'000	2016 <i>HK\$'000</i>
Capital charge for operational risk	387,173	342,124

The Group uses the basic indicator approach for calculating operational risk.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

13. 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.

	2017							
	Class of credit risk exposures							
	Total exposures HK\$'000	Exposures after recognised credit		Risk-weighted amounts		Total risk-weighted amounts HK\$'000	Total exposures covered by recognised collateral HK\$'000	Total exposures covered by recognised guarantees HK\$'000
	Rated HK\$'000	Unrated HK\$'000	Rated HK\$'000	Unrated HK\$'000				
A. On-balance Sheet								
1. Sovereign	18,020,797	18,020,797	-	549,377	-	549,377	-	-
2. Public sector entity	-	-	534,270	-	106,854	106,854	-	-
3. Bank	36,405,780	35,192,822	1,526,492	11,887,021	305,299	12,192,320	-	-
4. Securities firm	2,177,115	468,847	1,706,569	234,423	853,285	1,087,708	1,699	-
5. Corporate	84,098,144	20,670,959	59,828,146	15,180,274	59,810,633	74,990,907	3,285,506	761,851
6. Collective Investment Scheme	63,432	-	63,432	-	63,432	63,432	-	-
7. Cash items	435,870	-	3,855,081	-	363,351	363,351	-	-
8. Regulatory retail	354,944	-	335,306	-	251,479	251,479	19,638	-
9. Residential mortgage loan	13,818,820	-	13,252,249	-	5,392,679	5,392,679	32,301	534,270
10. Other exposures which are not past due exposures	6,964,477	-	6,884,409	-	7,205,512	7,205,512	80,068	-
11. Past due exposures	122,218	-	122,218	-	128,156	128,156	108,491	-
B. Off-balance Sheet								
1. Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	6,147,013	440,629	5,706,384	275,720	5,341,567	5,617,287	1,128,735	504,851
2. OTC derivative transactions	2,357,824	2,312,158	45,666	814,305	45,667	859,972	-	-
3. Securities financing transactions	12,916,553	939,415	11,977,138	326,767	-	326,767	11,977,137	-
	183,882,987	78,045,627	105,837,360	29,267,887	79,867,914	109,135,801	16,633,575	1,800,972
C. Securitisation Exposures								
	-	-	-	-	-	-	-	-
D. Central Counterparties Default Risk Exposure								
	379,546	379,546	-	7,591	-	7,591	-	-
E. Credit Valuation Adjustment								
	2,357,824	-	2,357,824	-	444,738	444,738	-	-

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

13. RISK MANAGEMENT – continued

(i) Credit risk – continued

(a) Credit risk exposures – continued

	2016							
	Class of credit risk exposures						Total exposures covered by recognised collateral	Total exposures covered by recognised guarantees
	Total exposures	Exposures after recognised credit		Risk-weighted amounts		Total risk-weighted amounts		
HK\$'000	Rated	Unrated	Rated	Unrated	HK\$'000	HK\$'000	HK\$'000	HK\$'000
A. On-balance Sheet								
1. Sovereign	9,960,292	9,960,292	-	-	-	-	-	-
2. Public sector entity	39,359	39,359	501,914	7,872	100,383	108,255	-	-
3. Bank	38,682,342	36,833,739	2,447,450	11,338,394	964,985	12,303,379	-	-
4. Securities firm	1,675,818	-	1,673,001	-	836,501	836,501	2,816	-
5. Corporate	64,443,276	16,030,835	47,224,106	11,134,901	47,224,105	58,359,006	589,488	1,442,267
6. Cash items	524,089	-	1,228,414	-	68,143	68,143	-	-
7. Regulatory retail	136,073	-	128,848	-	96,636	96,636	7,225	-
8. Residential mortgage loan	13,350,322	-	12,793,261	-	6,338,220	6,338,220	55,147	501,914
9. Other exposures which are not past due exposures	7,807,930	-	7,758,280	-	8,079,384	8,079,384	49,649	-
10. Past due exposures	283,430	-	283,430	-	257,019	257,019	275,739	156
B. Off-balance Sheet								
1. Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	7,059,840	1,999,888	5,059,952	1,192,225	4,911,061	6,103,286	151,498	753,010
2. OTC derivative transactions	1,070,870	1,067,869	3,001	333,174	2,381	335,555	-	-
3. Securities financing transactions	10,693,972	902,886	9,791,086	340,426	-	340,426	9,791,086	-
	155,727,613	66,834,868	88,892,743	24,346,992	68,878,818	93,225,810	10,922,648	2,697,347
C. Securitisation Exposures								
	-	-	-	-	-	-	-	-
D. Credit Valuation Adjustment								
	1,070,870	-	1,070,870	-	227,519	227,519	-	-

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

13. 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, corporates and the Government of the HKSAR. The Group has also taken properties and listed shares as collateral pledged as security against loans totalling HK\$36,176,683,000 (2016: HK\$35,556,881,000) and HK\$1,714,823,000 (2016: HK\$2,631,322,000) respectively.

(b) Counterparty credit risk exposures

The Group enters into Over-The-Counter (“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 counterparty credit exposures is based on Banking (Capital) Rules. Counterparties 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 is no credit derivative contract outstanding as at 31 December 2017 and 31 December 2016.

	OTC derivative transactions	
	2017	2016
	HK\$'000	HK\$'000
OTC derivative		
Gross total positive fair value	556,793	424,845
Credit equivalent amounts	2,357,824	1,070,870
Risk-weighted amounts	867,563	335,556

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

13. RISK MANAGEMENT – continued

(i) Credit risk – continued

(b) Counterparty credit risk exposures – continued

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

	OTC derivative transactions	
	2017 HK\$'000	2016 HK\$'000
Notional amounts:		
– Banks	159,356,785	57,072,120
– Corporates	23,222,060	6,585,524
– Public Sector	18,323	–
– Other	–	–
	182,597,168	63,657,644
Credit equivalent amounts:		
– Banks	1,998,836	935,747
– Corporates	358,805	135,123
– Public Sector	183	–
– Other	–	–
	2,357,824	1,070,870
Risk-weighted amounts:		
– Banks	600,369	266,880
– Corporates	267,157	68,676
– Public Sector	37	–
– Other	–	–
	867,563	335,556

(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, corporates and the Government of the HKSAR.

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

13. RISK MANAGEMENT – continued

(i) Credit risk – continued

(c) Credit risk mitigation – continued

The Group only accepts collateral pledged as security:

- when it is readily realisable;
- 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) Securitisation exposures

There was no securitisation exposures as at 31 December 2017 (2016: Nil).

13. RISK MANAGEMENT – continued

(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 associate operations that complement directly the Group's banking 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 consolidated financial statements. At the statement of financial position 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.

	2017	2016
	HK\$'000	HK\$'000
Net realised gains from sales	7,502	94,577
Net unrealised revaluation gains:		
– Amount included in available-for-sale securities	8,292	6,105
– Amount included in disclosed reserves	7,374	5,300

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

13. RISK MANAGEMENT – continued

(iv) Interest rate exposures in banking book

Note 7 to the consolidated financial statements 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:

	2017 Currency			Total
	HK\$	US\$	Others	
Interest rate risk shock				
Equivalents of HK\$'000				
– Variations in earnings (+100 basis points)	108,542	(2,824)	(13,928)	91,790
– Variations in earnings (-10 basis points)	(9,650)	293	1,095	(8,262)
	2016 Currency			Total
	HK\$	US\$	Others	Total
Interest rate risk shock				
Equivalents of HK\$'000				
– Variations in earnings (+100 basis points)	52,047	122,790	(40,781)	134,056
– Variations in earnings (-10 basis points)	(18,285)	(13,651)	3,129	(28,807)

UNAUDITED SUPPLEMENTARY FINANCIAL INFORMATION

for the year ended 31 December 2017

14. BASIS OF CONSOLIDATION

The consolidated financial statements cover the consolidated financial information of the Bank and all its subsidiaries and include the attributable share of interest in the Group's associates.

In preparing the capital adequacy ratio and liquidity ratio of the Group, they are prepared according to the basis of consolidation determined by the Hong Kong Monetary Authority 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 associates whereas the latter includes the Bank and only some of the Group's subsidiaries which mainly conduct banking business or other business incidental to banking business. The LMR is prepared on an unconsolidated basis which includes the Bank only.

Subsidiaries that are included within the accounting scope of consolidation but are not included within the regulatory scope of consolidation are as follows:

Name of company	Principal activities	Total assets		Total equity	
		2017 HK\$'000	2016 HK\$'000	2017 HK\$'000	2016 HK\$'000
Chong Hing (Nominees) Limited	Provision of nominee services	100	100	100	100
Chong Hing Securities Limited	Stockbroking	780,812	680,437	376,854	565,335
Chong Hing Commodities and Futures Limited	Investment holding and commodities and futures broking	68,652	66,779	65,186	63,102
Chong Hing Insurance Company Limited	Insurance underwriting	445,869	351,924	133,824	211,312
Chong Hing (Management) Limited	Provision of management services	273	173	99	100

HEAD OFFICE, BRANCHES, SUB-BRANCHES, REPRESENTATIVE OFFICES, PRINCIPAL SUBSIDIARIES AND ASSOCIATES

as of 29 March 2018

		Telephone
HONG KONG MAIN BRANCH	Chong Hing Bank Centre 24 Des Voeux Road Central	3768 1111
HONG KONG ISLAND BRANCHES		
Aberdeen	166-168 Aberdeen Main Road	3768 6210
Causeway Bay	488 Jaffe Road	3768 6290
North Point	376 King's Road	3768 6200
Sai Ying Pun	81-85 Des Voeux Road West	3768 6340
Shau Kei Wan	203-205 Shau Kei Wan Road	3768 6330
Sheung Wan	163 Wing Lok Street	3768 6220
Wan Chai	265-267 Hennessy Road	3768 6350
Western	347-349 Des Voeux Road West	3768 6280
KOWLOON BRANCHES		
Castle Peak Road	285-287 Castle Peak Road, Cheung Sha Wan	3768 6320
How Ming Street	114 How Ming Street, Kwun Tong	3768 6480
Jordan	G/F, No. 120 Woosung Street	3768 6720
Kowloon Bay	Shop Unit 8, G/F, Chevalier Commercial Centre No. 8 Wang Hoi Road	3768 6740
Kowloon City	31-33 Nga Tsin Wai Road	3768 6300
Kwun Tong	31-33 Mut Wah Street	3768 6410
Lai Chi Kok Road	139 Lai Chi Kok Road, Tai Kok Tsui	3768 6380
Lei Yue Mun	Shop No. LG1, Lower Ground Floor Lei Yue Mun Plaza, Yau Tong	3768 6530

HEAD OFFICE, BRANCHES, SUB-BRANCHES, REPRESENTATIVE OFFICES, PRINCIPAL SUBSIDIARIES AND ASSOCIATES

as of 29 March 2018

		Telephone
KOWLOON BRANCHES – continued		
Mongkok	591 Nathan Road	3768 0001
San Po Kong	55-57 Yin Hing Street	3768 6360
Sham Shui Po	144-148 Tai Po Road	3768 6310
Shun Lee Estate	Lee Yat House, Shun Lee Estate	3768 6420
Tak Tin Estate	No. 207, Tak Tin Plaza, Tak Tin Estate, Lam Tin	3768 6470
To Kwa Wan	34-34A Tam Kung Road	3768 6370
Tsim Sha Tsui	16 Granville Road	3768 6240
Tsz Wan Shan	60-64 Sheung Fung Street	3768 6390
NEW TERRITORIES BRANCHES		
Cheung Fat Estate	Shop No. 206A, 2/F Cheung Fat Plaza, Cheung Fat Estate, Tsing Yi	3768 6560
Cho Yiu Chuen	G/F, Block C, King Cho Road, Cho Yiu Chuen, Lai King	3768 6250
Fanling	2 Wo Lung Street, Luen Wo Market	3768 6260
Glorious Garden	Shop No. 82, Glorious Garden, 45 Lung Mun Road Tuen Mun	3768 6520
Heng On Estate	Level 3, Commercial Centre, Heng On Estate Ma On Shan, Shatin	3768 6450
Lek Yuen Estate	Shop No. 212, Lek Yuen Plaza, Lek Yuen Estate, Shatin	3768 6400
Sheung Shui	71 San Fung Avenue	3768 6270

HEAD OFFICE, BRANCHES, SUB-BRANCHES, REPRESENTATIVE OFFICES, PRINCIPAL SUBSIDIARIES AND ASSOCIATES

as of 29 March 2018

Telephone

NEW TERRITORIES BRANCHES – continued

Sheung Tak Estate	Shop No. 237, Sheung Tak Plaza, Sheung Tak Estate Tseung Kwan O	3768 6510
Tai Wo Plaza	Shop No. 101 I, Level 1, Tai Wo Plaza No. 12 Tai Wo Road, Tai Po	3768 6900
Tin Chak Estate	Shop No. 218, 2/F, Tin Chak Shopping Centre Tin Chak Estate, Tin Shui Wai	3768 6570
Tsuen Wan	298 Sha Tsui Road	3768 6440
Tuen Mun Hong Lai Garden	G/F, Hong Lai Garden, 117 Heung Sze Wui Road Tuen Mun	3768 6580
Yat Tung Estate	Shop Nos. 1 & 2, G/F, Yat Tung Shopping Centre Yat Tung Estate, Tung Chung	3768 6710
Yuen Long	99-109 Castle Peak Road	3768 6230

GUANGZHOU BRANCH

Guangzhou	50/F, Yuexiu Financial Tower, No. 28 Zhujiang East Road Tianhe District, Guangzhou, Guangdong, China	(86-20) 2213 7988
-----------	--	-------------------

SHENZHEN BRANCH

Shenzhen	Unit 17, 18 & 19 of 1 Floor Unit 39 of 2 Floor & 13 Floor, T2 Tower, Ali Center No. 3331 Keyuan South Road (Shenzhen Bay) Nanshan District, Shenzhen, China	(86-755) 3352 9099
----------	--	--------------------

SHANTOU BRANCH

Shantou	Lanbao International Mansion No. 103-105, Block One, Fenggezhuang No. 162 Jinsha Road, Shantou Guangdong, China	(86-754) 8890 3222
---------	---	--------------------

GUANGZHOU TIANHE SUB-BRANCH

Guangzhou Tianhe	Room 160 & Room 260 Guangzhou International Finance Centre No. 5 Zhujiang West Road, Tianhe District Guangzhou, Guangdong, China	(86-20) 2338 7386
------------------	---	-------------------

HEAD OFFICE, BRANCHES, SUB-BRANCHES, REPRESENTATIVE OFFICES, PRINCIPAL SUBSIDIARIES AND ASSOCIATES

as of 29 March 2018

Telephone

GUANGDONG PILOT FREE TRADE ZONE

NANSHA SUB-BRANCH

Nansha	Room 801-805, Building No. 1 No. 106 Fengze Road East, Nansha District Guangzhou, Guangdong, China	(86-20) 3226 0620
--------	--	-------------------

FOSHAN SUB-BRANCH

Foshan	P6, P7, Part of P27, G/F, No. 127 North Lingnan Avenue Chancheng District, Foshan, Guangdong, China	(86-757) 6352 2888
--------	--	--------------------

GUANGDONG PILOT FREE TRADE ZONE

HENGQIN SUB-BRANCH

Hengqin	Area B, Block 10, Hengqin Financial Industry Service Base, Shizimen Central Business District Hengqin New Area, Zhuhai, Guangdong, China	(86-756) 3833 039
---------	---	-------------------

SHANGHAI REPRESENTATIVE OFFICE

Shanghai	Room 1807, Yue Xiu Tower, No. 388 Fushan Road Pudong, Shanghai, China	(86-21) 6031 0138
----------	--	-------------------

MACAU BRANCH

Macau	No. 693, Avenida da Praia Grande Edificio Tai Wah, R/C, Macau	(853) 2833 9982
-------	--	-----------------

SAN FRANCISCO REPRESENTATIVE OFFICE

San Francisco	Suite 810, 601 California Street, San Francisco California 94108-2823, USA	(1-415) 433 6404
---------------	---	------------------

HEAD OFFICE, BRANCHES, SUB-BRANCHES, REPRESENTATIVE OFFICES, PRINCIPAL SUBSIDIARIES AND ASSOCIATES

as of 29 March 2018

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 (Management) Limited

Chong Hing (Nominees) Limited

Chong Hing Securities Limited

Gallbraith Limited

Hero Marker Limited

Top Benefit Enterprise Limited

ASSOCIATES

Bank Consortium Holding Limited

BC Reinsurance Limited

Hong Kong Life Insurance Limited

www.chbank.com



 **創興銀行有限公司**
Chong Hing Bank Limited